



UNITED STATES DEPARTMENT OF AGRICULTURE

OFFICE OF INSPECTOR GENERAL

Washington D.C. 20250



DATE: **July 14, 2000**

REPLY TO  
ATTN OF: 08003-6-SF

SUBJECT: Zephyr Cove Land Exchange, Lake Tahoe Basin Management Unit

TO: Mike Dombek  
Chief  
Forest Service

This report presents the results of our audit of the Zephyr Cove land exchange at Lake Tahoe, Nevada. Our objective was to review all aspects of the land exchange to determine if it complied with Federal laws and regulations, as well as Forest Service (FS) policies and procedures. Our audit identified improprieties committed by FS staff which compromised the integrity of the land exchange, and recommended specific actions to correct the deficiencies noted.

Your written response to the draft report is included in its entirety as exhibit D. Based on your response, we have accepted management decision on all audit recommendations. We appreciate the prompt corrective actions initiated by FS regional staff to address the conditions noted in the report.

The Office of the Chief Financial Officer (OCFO), U.S. Department of Agriculture, has responsibility for monitoring and tracking final action for the findings and recommendations. Please note that final action on the findings and recommendations should be completed within 1 year to preclude listing in the Semiannual Report to Congress. Please follow your agency's internal procedures for forwarding final action correspondence to OCFO.

ROGER C. VIADERO  
Inspector General

Attachment





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

FOREST SERVICE  
PACIFIC SOUTHWEST REGION  
ZEPHYR COVE LAND EXCHANGE  
LAKE TAHOE BASIN MANAGEMENT UNIT  
SOUTH LAKE TAHOE, CA

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Report No.  
08003-6-SF  
July 2000

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# EXECUTIVE SUMMARY

FOREST SERVICE  
PACIFIC SOUTHWEST REGION  
ZEPHYR COVE LAND EXCHANGE  
LAKE TAHOE BASIN MANAGEMENT UNIT  
SOUTH LAKE TAHOE, CALIFORNIA

REPORT NO. 08003-6-SF

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## RESULTS IN BRIEF

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This report presents the results of the U.S. Department of Agriculture, Office of Inspector General's (OIG) audit of the Zephyr Cove land exchange administered by the Lake Tahoe

Basin Management Unit (LTBMU) at Lake Tahoe, Nevada. Zephyr Cove's appraised value of \$38 million makes it one of the most expensive land exchanges in Forest Service (FS) history. A previously issued OIG report (Evaluation Report No. 08003-4-SF) focused on the ownership of the physical improvements on Zephyr Cove. This report covers our review of all aspects of the Zephyr Cove land exchange to determine if it complied with Federal laws and regulations as well as FS policies and procedures.

The Zephyr Cove exchange was completed in two phases: the first phase involved 35.4 acres of unimproved land, and the second phase involved 11.8 acres of land that included an 11,000-square-foot mansion. The exchange was completed with the cooperation of the Department of Interior's Bureau of Land Management (BLM), whose land outside of Las Vegas, Nevada, was given in exchange for the Zephyr Cove properties. The FS, as recipient of the properties, helped BLM process the transaction in conjunction with the landowner of the Zephyr Cove estate, Olympic Group, Inc.

The FS failed to obtain for the American public clear title to this unique and remarkable lakeshore property that so precisely accomplished the intent of the Federal Land Exchange Facilitation Act. The FS' interest in seeking to acquire Zephyr Cove was to broaden public access to Lake Tahoe's beaches, protect sensitive wildlife species, and improve hiking activities by joining separate parcels of land the FS already owned. However, Zephyr Cove currently satisfies none of these interests. What was to be a prize acquisition for the FS is instead a fenced-off area with a title encumbered by claims of private ownership, with access by the public restricted by a private operation that has taken constructive possession of the property, and with a total cost to the government (\$38 million) that is potentially in excess of twice the actual value of the land when it was conveyed to the FS.

We concluded that the Zephyr Cove land exchange was seriously compromised and that the Pacific Southwest regional office (RO) should have exercised greater control over the transaction. We concluded that improprieties occurred because the RO staff

- did not communicate FS levels of authority and responsibility to BLM staff before the land exchange began,
- allowed the LTBMU to create an interagency agreement with BLM without reviewing the agreement to ensure it identified the limited authority of the LTBMU and the specific role of the RO, and
- did not monitor the actions of the LTBMU employee responsible for completing the exchange.

The absence of RO oversight and the conduct of the LTBMU employee, who did not exercise due professional care in fulfilling land acquisition responsibilities, resulted in the following inappropriate actions:

- Material information was not provided to a FS appraiser, and some of the data that was provided by the LTBMU employee was misleading, resulting in an overvaluation of the Zephyr Cove property,
- The LTBMU authorized BLM to process the second phase of the land exchange with the mansion and other structures in place even though this contradicted FS policy,
- The LTBMU employee drafted an agreement with Olympic Group, Inc., that allowed Olympic to sell the Government-owned mansion and allied structures and keep the profits,
- Letters of approval were drafted by the LTBMU employee and signed by the forest supervisor, that allowed a private operation unknown to the FS (Park Cattle Company) to claim title to the mansion and allied structures on FS lands,
- The LTBMU employee created an improvement reservation to the Zephyr Cove deed after the land exchange had closed, that clouded FS' title to the mansion and may have strengthened Park Cattle's claim to it,
- The FS failed to review the deeds, which has allowed Park Cattle to exert control over perpetual and exclusive rights-of-way on specific portions of the FS Zephyr Cove lands, and
- The LTBMU employee did not inform the RO or the Office of the General Counsel (OGC) of his actions in a timely manner. The RO and OGC

became aware of the problems months after the transaction had been settled with Olympic.

The LTBMU employee felt that FS policy and procedures did not apply to the Zephyr Cove land exchange because it was a BLM transaction. However, no instructions were given to the LTBMU employee by the RO to suggest that FS policy did not apply.

We also questioned the appraisal of the Zephyr Cove estate. Our review found that the appraisals did not comply with Federal regulations or appraisal policy and were based on speculative events. In effect, the \$38 million appraised value assigned to the Zephyr Cove property and approved by a FS appraiser did not reflect the property actually acquired by the FS. We estimated that the questionable appraisal procedures might have overvalued the land by as much as \$20 million. We concluded that in accepting the valuations made by Olympic's appraiser, the FS appraiser failed to uphold the standards required of a Federal appraiser.

To date, the OGC has not issued a final title opinion on the transaction. Our audit identified several key areas that need to be covered by the OGC opinion, such as ownership interests in the mansion and other structures, access easements, water rights, and development rights. Park Cattle Company has also not compensated the FS for its use of public property. The FS needs to take action to collect a fee for the period of Park Cattle's unauthorized occupancy.

In its early attempt to convince Park Cattle to relinquish the mansion, the RO emphasized that it would likely not issue Park Cattle a special-use permit to occupy Zephyr Cove and that such a permit, if issued, would require a fee of nearly a half million dollars a year. Park Cattle refused to leave Zephyr Cove and threatened litigation if the FS did not give it a special-use permit at a low rate.

It is in the public's interest for the FS to achieve the opportunities it expected from the Zephyr Cove land exchange. Once a final title opinion is issued, the FS should resolve Park Cattle's unauthorized occupancy of Zephyr Cove. The FS should assert its rights to the improvements, if so stipulated in the title opinion, or resolve Park Cattle's unauthorized occupancy through legal options available to it that serve the general public's best interest.

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## **KEY RECOMMENDATIONS**

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We recommend that the FS Washington Office ensure that the Pacific Southwest Region RO obtain a final title opinion on the Zephyr Cove lands and structures from OGC, after OGC evaluates all aspects of the Zephyr Cove land exchange transaction. On the basis of OGC's title opinion, the FS should either assert FS' rights to the

improvements, if so stipulated in the opinion, or resolve Park Cattle's unauthorized occupancy through legal options available to it that serve the general public's best interest.

We also recommend that the Washington Office ensure that the Pacific Southwest Region (1) refer the actions of the LTBMU employee to the Human Resources Division for the appropriate action, and (2) conduct a peer review of the appraisals performed on the Zephyr Cove lands and take corrective action.

For future land exchanges, we recommend that the FS create a memorandum of understanding with BLM specifying the roles and responsibilities on FS-BLM land exchanges, and we recommend that the Pacific Southwest Region clarify the responsibilities between the Zone land adjustment teams and the RO.

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**AGENCY RESPONSE**

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The FS concurred with all the audit recommendations. The complete text of the FS response is shown in exhibit D.

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**OIG POSITION**

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Based on FS written response, OIG accepted FS management decision for all the audit report recommendations.

## PICTORIAL ADDENDUM TO EXECUTIVE SUMMARY

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**The following pages illustrate, in map and photographs, the history and results of the Zephyr Cove land exchange, as described in the Executive Summary.**

Zephyr Cove is located on the southeast shore of Lake Tahoe, on the Nevada side of the Lake. It is forested with fir, pine, and other evergreens, has a half-mile stretch of pristine shoreline, and commands a panoramic view of the California mountains, looking west toward Squaw Valley. A gated driveway marks the entrance to the property and winds towards an 11,000-square-foot mansion located by the lake's edge (See Figure 1).

With National Forest lands adjacent to it on both the north and south, the acquisition of the Zephyr Cove lands could greatly enhance public recreation opportunities and provide much needed public access to sandy beaches, a setting in short supply around the lake. It was with the goal of enhancing public access to Lake Tahoe and its beaches that the Forest Service entered into a land exchange with the owner of Zephyr Cove, a real estate investment firm known as Olympic Group, that bought the property with such an exchange in mind.

Crucial to the \$38-million value paid by the public for Zephyr Cove was the assumption that the property would be conveyed to the Forest Service without encumbrances—that is, with the Forest Service having a clear title to all of the land. Any reservation to the title, withholding ownership rights to anyone else, would diminish the value of the property and restrict full recreational use by the public. When the property was appraised at \$38 million, the land had no reservations, and the property was conveyed to the Forest Service in two phases with no reservation in either deed. However, a written agreement between the LTBMU and Olympic Group, Inc., purported to give ownership of the lakefront mansion to Olympic, even though ownership of the structure had already been conveyed to the Government.

# PICTORIAL ADDENDUM TO EXECUTIVE SUMMARY

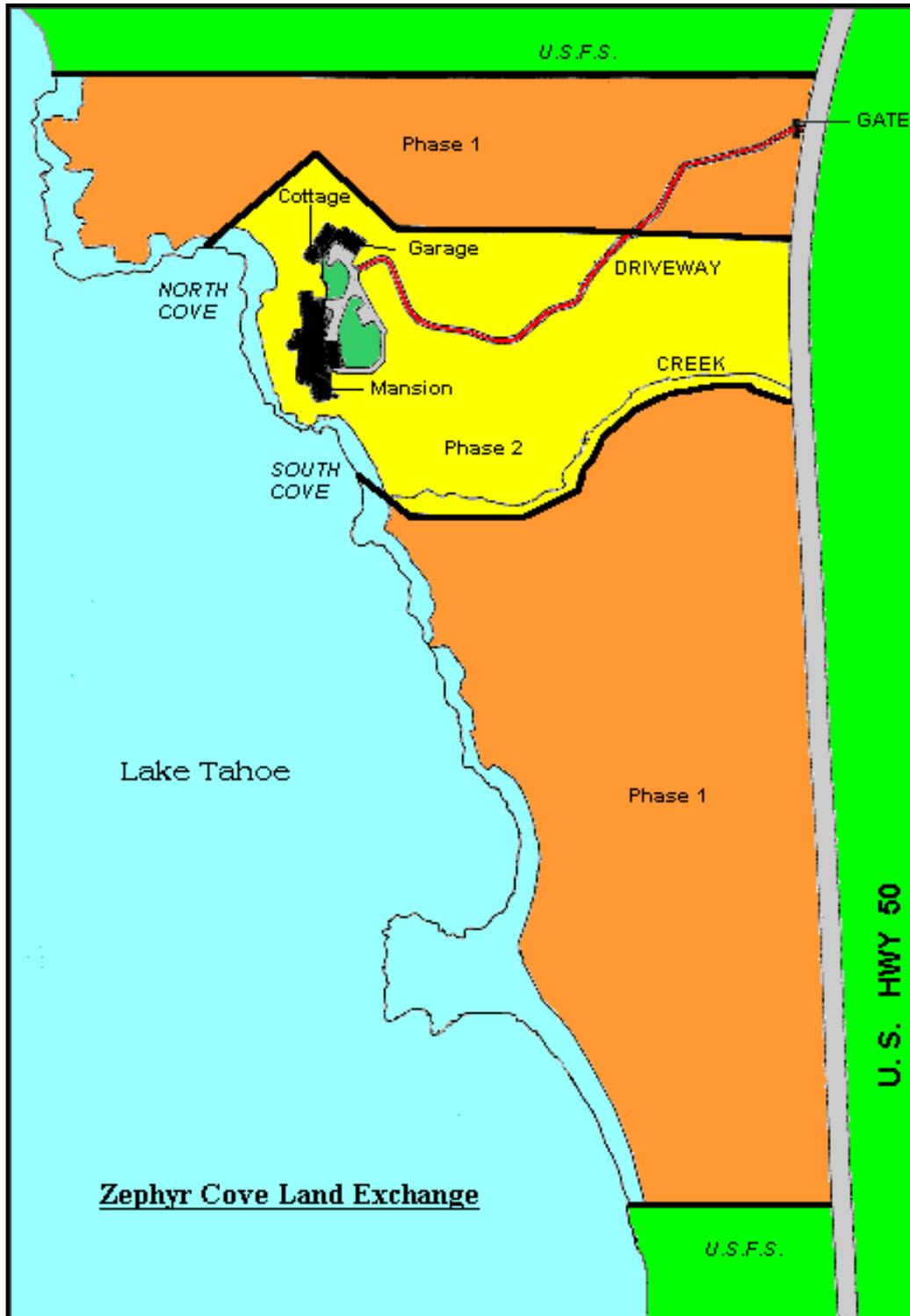


Figure 1: Layout of the Zephyr Cove lands (Phase 1 and 2) showing the location of the lakefront mansion, gated driveway and sandy coves. This property was acquired at a cost to taxpayers of \$38 million.

## PICTORIAL ADDENDUM TO EXECUTIVE SUMMARY

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Within 2 months of the completion of the Zephyr Cove exchange, Olympic Group sold the mansion it claimed to own to Park Cattle Company for \$300,000 cash and certain potential future benefits.

As the following photographs show, the gate to the Zephyr Cove property is now padlocked and the driveway itself reserved for the exclusive use of Park Cattle. "Private" signs are posted along the driveway to deter the public from entering the property, and approaching the mansion and caretaker's cottage. To further discourage a public presence on the land, Park Cattle fronted the buildings with signs warning against trespassing and posted the beaches with markers announcing that no hiking trails crossed the property. The public is restricted from accessing the beaches that the Forest Service specifically acquired for public enjoyment, and is effectively stopped from traversing the land it owns.



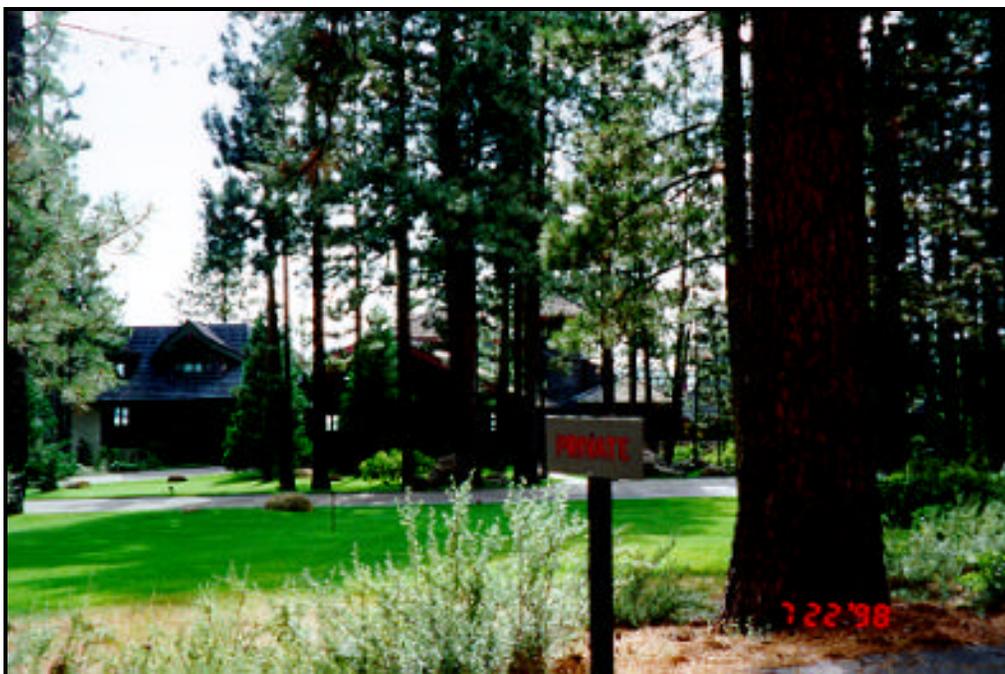
**Photo 1: Main gate to the Zephyr Cove property. Park Cattle Company has locked the main gate accessing the property in order to restrict public access to the lake front lands acquired by the FS almost 3 years ago.**

## PICTORIAL ADDENDUM TO EXECUTIVE SUMMARY

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**Photo 2:** Park Cattle Company claims it has an exclusive, perpetual right to the driveway leading to the Zephyr Cove improvements and the lakefront. Park Cattle has barred the public from walking or driving on the road.



**Photo 3:** Park Cattle Company has posted “private” signs on the public lands surrounding the mansion, improperly restricting public access to the sandy coves and lakefront.

## PICTORIAL ADDENDUM TO EXECUTIVE SUMMARY

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**Photo 4:** 11,000-square-foot lakefront mansion at Zephyr Cove. Park Cattle Company has constructively occupied this residence and used the surrounding FS lands since July 1997, without FS authorization and without compensating the public.



**Photo 5:** “No Trespassing” sign posted by Park Cattle Company without FS authorization. This is one of numerous signs posted on FS land to restrict public use of the property.

## PICTORIAL ADDENDUM TO EXECUTIVE SUMMARY

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**Photo 6: View of Lake Tahoe from Zephyr Cove. Public enjoyment of this unique vista is jeopardized by Park Cattle Company's unauthorized occupancy of the FS lands.**



**Photo 7: Sandy cove north of the Zephyr Cove mansion. Although the FS acquired this rare sandy beach to enhance recreational opportunities, Park Cattle Company has restricted public access by posting "No Trespassing" signs on the public land.**

## PICTORIAL ADDENDUM TO EXECUTIVE SUMMARY

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**Photo 8: “No Trail” sign posted by Park Cattle Company on the sandy cove south of the mansion (background). Park Cattle used signs that mimic official Forest Service trail markers to direct the public away from the sandy beaches adjacent to the Zephyr Cove mansion.**

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# INTRODUCTION

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## BACKGROUND

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To acquire land that meets the FS' land management needs, the FS is authorized to carry out land exchanges with private landowners or their representatives. Land

exchanges between the National Forest System and other ownerships are needed to protect key resources, eliminate conflicting use, and reduce fragmented ownership. Much of the non-Federal land acquired through land exchanges lies within classified wilderness areas, national recreation areas, wild and scenic river corridors, national trails, and other congressionally designated areas. The Code of Federal Regulations (CFR) specifies that the FS may only complete land exchanges if the public's interest is well served. The CFR defines the public's interest as achieving better management of Federal lands and resources, and securing objectives such as protection of fish and wildlife habitats and the enhancement of recreation opportunities.

Private parties that exchange land with the FS are known as "proponents." In many cases, proponents are not the original owners of the property but acquire the right to sell it or negotiate its exchange either by entering into an agreement with the true owner or by purchasing it outright for the purpose of exchange.

In the fall of 1995, a proponent, Olympic Group, Inc., proposed a land exchange with the BLM to acquire Federal lands in the Las Vegas valley in exchange for non-Federal lands throughout Nevada. The non-Federal lands offered for exchange included a 47.2-acre parcel in the Lake Tahoe Basin known as Zephyr Cove. This property is located on the shore of Lake Tahoe, with approximately 3,000 feet of sandy beach, a small wetland area, meadow, creek, and an 11,000-square-foot mansion and other buildings. The property supports a variety of sensitive plant and wildlife species, as well as four distinctive micro-ecosystems. Because this land met the land management needs of the FS, the Federal Government agreed to exchange BLM land in Las Vegas to acquire the Zephyr Cove land for the FS.

The LTBMU considered the acquisition of the quarter mile of sandy beach to be a great public benefit because public beach access to Lake Tahoe was extremely limited. FS staff wished to acquire the Zephyr Cove property in an unimproved, natural state.

The Olympic Group optioned the entire 47.2-acre parcel, including all improvements, for \$28 million in the fall of 1995. About 14 months later the FS approved appraisals totaling \$38 million for the same acreage; an increase of \$10 million. Because the FS did not want to acquire land with improvements, the land was separated into two parcels, one comprising 35.4 acres of unimproved land, and the other, with the improvements, comprising 11.8 acres. Ultimately the FS received both parcels of land in two separate phases.

The FS acquired the 35.4 unimproved acres, valued at about \$24¼million, in the first phase of Olympic's exchange with BLM. Title to this portion of the property was transferred to the FS in the fall of 1996. The FS then agreed to acquire the remaining 11.8 acres in the second phase of Olympic's land exchange with BLM. The \$13¼million value assigned to the 11.8-acre parcel assumed that the existing improvements on the property had been removed and that the land was unencumbered and free to be developed. It was later decided by LTBMU staff, BLM management and Olympic Group that the improvements would not be removed as originally planned. Instead, Olympic would retain private ownership of the improvements and sell them to a private party after the land exchange was completed.

When the FS acquires land with improvements and the proponent or owner wishes to retain rights to the improvements, the CFR requires that a reservation be added to the deed with language that is prescribed by the CFR. The reservation language reserves the right of the proponent to hold and use the improvements and a specified piece of FS land, for a specific purpose, for a specific period of time, after which time the property reverts to the FS. When the Phase 2 parcel of Zephyr Cove was transferred to the FS on April 25, 1997, the CFR reservation was not in the deed.

According to OGC, because Olympic did not reserve the improvements in the title closing, ownership of the parcel and the improvements passed to the FS on April 25, 1997. Nevertheless, Olympic claimed it had control of the improvements as well as a perpetual, exclusive right-of-way (called an "easement") to the property's driveway leading to the improvements. By claiming the exclusive easement, Olympic claimed the perpetual right to restrict the public from using specific portions of the Zephyr Cove property.

On July 2, 1997, Olympic sold the publicly owned improvements, and the exclusive easement, to Park Cattle Company for \$300,000 cash, plus future amenities conditioned on Park Cattle's receipt of a FS special-use permit. These future amenities included two memberships to the Edgewood Tahoe Golf Course for 20 years and exclusive use of the Zephyr Cove improvements for 7 weeks during the spring and summer months for the next 25 years. The total amenities provided by Park Cattle to Olympic were estimated at \$2.7 million. The USDA OIG questioned the sale of the Zephyr

Cove improvements in a previous report (Evaluation Report No. 08003-4-SF).

While Olympic realized a profit of up to \$10 million from the sale of the Zephyr Cove land without the CFR reservation, as well as approximately \$3 million more in cash and conditional amenities from the sale of the improvements, the Federal Government, by contrast, now finds itself negotiating with Park Cattle for control over the property that it spent \$38 million to acquire. Park Cattle has locked the entrance gates to the property, has denied public access to the easement road, and has posted "Private" signs and restrictive trail markers on the Zephyr Cove grounds surrounding the improvements. Public access to Zephyr Cove's sandy beaches fronting the improvements has also been severely curtailed.

In comparison to the Zephyr Cove transaction, FS staff successfully processed a similar lakefront land exchange during the same period. This exchange, known as the Thunderbird Lodge, was valued at \$50 million and consisted of 140 acres of lakefront property with extensive improvements, including a historic stone mansion. Unlike the Zephyr Cove exchange, the FS relied on the expertise of its Washington Office and RO staff as well as recommendations from an evaluation by the OIG (Evaluation Report No. 08801-5-SF) and OGC in ensuring that the FS' property rights were protected, and that use of the improvements and public access to the property was controlled and authorized under terms developed by the FS.

The table on the following page outlines the major differences between the Zephyr Cove exchange and the Thunderbird Lodge exchange.

<b>ZEPHYR COVE</b>	<b>THUNDERBIRD LODGE</b>
<p><b>The FS did not include an improvement reservation in the deed.</b> Even though the proponent claimed private ownership of the improvements, the value paid by the Government was not reduced to reflect the encumbrance of privately owned improvements on FS land.</p>	<p><b>The FS included a reservation in the deed.</b> Consequently, the value paid to proponent was reduced by about \$10 million due to privately owned improvements on FS lands.</p>
<p><b>The FS did not control the use of the improvements.</b> The proponent entered into an agreement with a private party without FS knowledge or approval. The private party plans to use the improvements and surrounding FS lands for an upscale bed &amp; breakfast resort. The private party has also guaranteed the proponent <i>exclusive</i> use of the facilities for 7 weeks of the year, with no public presence allowed.</p>	<p><b>The FS reservation restricts the use of improvements</b> to research-related facilities and public tours. The reservation also guarantees <i>full public access</i>. FS also approved the private party prior to the transfer of the improvements.</p>
<p><b>The public's investment in the land was not protected.</b> The proponent sold property on the land for \$3 million in cash and amenities. The private party is now using the FS land and water without compensating the Government.</p>	<p><b>The proponent had to spend an additional \$1.5 million to pay for additional water rights and other legal expenses</b> to meet the terms of the FS agreement. The proponent also paid for a performance bond of \$2.3 million to ensure compliance with the terms of the FS reservation agreement.</p>
<p><b>Now that the private party has taken constructive possession of the Zephyr Cove improvements, the FS may not be able to</b> enforce its authority over the private party and compel it to remove the unnecessary improvements from FS land.</p>	<p><b>If the private party does not comply with the terms of the FS reservation, the reservation will be terminated</b> and all improvements, including all development and water rights, revert to FS ownership at no additional cost. The FS is also protected from future maintenance expenses via the performance bond.</p>
<p><b>The private party has restricted public access to the FS land and claimed an exclusive easement</b> by locking the main gates and placing "private" signs on the driveway leading to the property and on the surrounding FS land.</p>	<p><b>There are no easements and encumbrances on the property.</b> The public has full access.</p>
<p><b>The LTBMU staff relied on attorneys employed by the proponent.</b> The staff also failed to consult OGC when it created agreements with the proponent and when it drafted reservations for the Zephyr Cove deed.</p>	<p><b>Government lawyers were consulted in all phases of the exchange</b>, including reviewing the reservation agreement and drafting the legal reservations to the deed.</p>

For a more detailed comparison of the Zephyr Cove exchange with the Thunderbird Lodge exchange, see exhibit C.

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## **OBJECTIVES**

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Our audit objective was to review all aspects of the Zephyr Cove land exchange to determine if the land exchange transaction complied with Federal laws and regulations as well as FS policies and procedures. In addition, we planned to identify specific actions that the FS needs to take to correct any deficiencies identified and develop recommendations to improve future land exchanges at the LTBMU.

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## **SCOPE**

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This report covers the Zephyr Cove land exchange from its inception in October 1995 to the title closure on April 25, 1997. We also reviewed subsequent activity from June 1997, when the Olympic Group, Inc., transferred the improvements to Park Cattle Company, to the current issues relating to the unauthorized occupancy and proposed use of the improvements by Park Cattle Company.

OIG previously issued an evaluation report (Evaluation Report No. 08003-4-SF) in August 1998 on the title issues relating to the Zephyr Cove improvements. OIG also released a report of investigations (Report of Investigation No. SF-899-83) dated June 8, 1999, concerning issues relating to the transfer and sale of the improvements.

The audit was conducted in accordance with generally accepted Government auditing standards.

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## **METHODOLOGY**

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To accomplish our review concerning the processing of the Zephyr Cove land exchange, we performed the following steps and procedures.

- We interviewed the Washington Office staff concerning issues relating to the Zephyr Cove appraisals.
- At the FS RO, we interviewed staff members to discuss the exchange process and their understanding of what was being communicated at the time. We reviewed all documents relating to the processing and appraisal of the Zephyr Cove land exchange. We obtained signed statements from members of the regional staff who were knowledgeable of the events relating to the land exchange. We also obtained a signed statement from a FS appraiser responding to our questions concerning the approval of the Zephyr Cove appraisals.
- At the LTBMU, we met with forest staff to discuss the processing of the Zephyr Cove land exchange. We also reviewed documents and correspondence relating to that transaction. In addition, we obtained a

signed, sworn statement from the LTBMU employee responding to our questions relating to the Zephyr Cove land exchange.

- We met with regional staff attorneys at OGC to discuss legal issues pertaining to the Zephyr Cove land exchange transaction and the current status of the Zephyr Cove improvements. We also discussed any current legal actions needed by the FS to preserve their rights to the Zephyr Cove property.
- We also reviewed certain evidence files from the OIG Investigation of Zephyr Cove.

## CHRONOLOGY OF EVENTS

Fall of 1995	The Olympic Group, Inc., options to buy the 47.2-acre Zephyr Cove property from its original owner for \$28 million. Olympic indicates to the FS that it is interested in exchanging 35.4 acres of undeveloped land but will keep the 11.8 acres of land with the improvements.
February 26, 1996	Olympic's appraiser values the 35.4 acres of unimproved land for exchange with the FS at \$24¼million.
July 17, 1996	LTBMU employee notes that Olympic is now willing to exchange the other 11.8 acres at Zephyr Cove to the FS. Although this information will affect the total land's fair market value, the LTBMU employee does not tell the FS appraiser, who must approve Olympic's appraisal. The LTBMU employee lets the appraiser approve the \$24¼million value placed on what is now Phase 1 of the Zephyr Cove exchange.
July 26, 1996	Olympic exercises its option to buy Zephyr Cove from the original owner for \$28 million.
October 3, 1996	Olympic exchanges the Phase 1 land with the FS. The deed is recorded. Although not noted in the appraisal, the deed contains a perpetual, exclusive easement, granting Olympic exclusive rights-of-way to the land.
November 26, 1996	Olympic's appraiser values the remaining 11.8 acres of the Zephyr Cove land at \$13¼million, based on the land being free of all encumbrances and outstanding interests.
Early 1997	The FS appraiser becomes aware for the first time that the Zephyr Cove exchange involves two parcels of land. Because Phase 1 has already been completed, the appraiser reviews the appraisal of the Phase 2 exchange as a separate parcel. Dividing the land into two parcels potentially overstates the land's total appraised value by almost \$9 million.
Early 1997	OGC informs the LTBMU employee that any privately owned improvements remaining on land transferred to the FS <i>must</i> be reserved by a CFR reservation in the deed. The LTBMU employee is told specifically that a special-use permit cannot supplant the CFR requirement.

## CHRONOLOGY OF EVENTS (continued)

March 5, 1997	The LTBMU employee and Olympic create an unauthorized agreement that allows Olympic to convey Zephyr Cove improvements to a third party after the land exchange is completed. According to the agreement, a special-use permit, not a CFR reservation, will authorize occupancy and use of the improvements. This overstates the fair market value of the Phase 2 exchange by up to \$10 million. A FS specialist approves the document even though the specialist is told that there is no statutory authority to support the agreement.
April 25, 1997	Olympic exchanges the Phase 2 land with the FS. When the deed is recorded, it grants a perpetual, exclusive easement to Olympic. All land and improvements at Zephyr Cove are conveyed to the FS. BLM land is conveyed to Olympic.
June 30, 1997	Olympic advises the LTBMU of its intention to sell the Zephyr Cove improvements to a third party. The LTBMU acknowledges this action but tells Olympic that the third party has no guarantee of being able to operate a FS concession.
July 2, 1997	Using a quitclaim deed, Olympic sells the improvements at Zephyr Cove to Park Cattle Company, a party not known to the FS. Olympic receives \$300,000 plus \$2.7 million in conditional amenities for the sale of FS property. Park Cattle takes constructive possession of Zephyr Cove and restricts public access to the land.
July 11, 1997	The LTBMU employee advises BLM to add a CFR reservation to the recorded Phase 2 deed in an attempt to reserve Olympic's ownership rights to the Zephyr Cove improvements after the land exchange has closed. The CFR reservation is inserted and the deed is re-recorded.
January 21, 1998	Park Cattle requests a special-use permit for expanded, urban development of Zephyr Cove. Park Cattle tells FS staff that if a permit is approved, Park is unwilling to pay the FS a concessionaire fee based on the fair market value of the land.

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## FINDINGS AND RECOMMENDATIONS

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CHAPTER 1	<b>ACTIONS OF FS STAFF COMPROMISED THE INTEGRITY OF THE ZEPHYR COVE LAND EXCHANGE AND DID NOT PROTECT THE PUBLIC'S INTEREST</b>
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Because of a number of improprieties committed during the Zephyr Cove exchange, the FS failed to obtain for the American public clear title to a unique and remarkable lakeshore property that so precisely accomplished the intent of the Federal Land Exchange Facilitation Act. The FS' interest in seeking to acquire Zephyr Cove was to broaden public access to Lake Tahoe's beaches, protect sensitive wildlife species, and improve hiking activities by joining separate parcels of land the FS already owned. However, Zephyr Cove currently satisfies none of these interests. What was to be a prize acquisition for the FS is instead a fenced-off area whose title is encumbered by private claims of ownership, whose access by the public is restricted by a private operator that has taken constructive possession of the property, and whose \$38-million cost to the Government may be in excess of twice the actual value of the land when it was conveyed to the FS.

We concluded that the Pacific Southwest regional office (RO) should have exercised greater control over the Zephyr Cove land exchange. The improprieties in the exchange occurred largely because the RO staff

- did not communicate FS levels of authority and responsibility to BLM staff before the land exchange began,
- allowed the LTBMU to create an interagency agreement with BLM without reviewing the agreement to ensure it identified the limited authority of the LTBMU and the oversight role of the RO, and
- did not monitor the actions of the LTBMU employee responsible for completing the exchange.

In the absence of adequate oversight, the LTBMU employee did not exercise due professional care in fulfilling land acquisition responsibilities to protect the public's interest. He<sup>1</sup> exceeded his authority, withheld information from the Federal staffs normally overseeing land exchanges, failed to inform a FS

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<sup>1</sup> To protect personal privacy, we will hereafter refer to all persons as "he".

appraiser about the total acreage being acquired in the land exchange and misled the FS appraiser about the future uses to which the land would be put.

Similarly, a FS appraiser did not exercise due professional care in the review of the Zephyr Cove valuations made by Olympic's appraiser. The FS appraiser approved values that did not comply with Federal law or appraisal standards, allowed the Zephyr Cove land to be artificially subdivided and its value increased, and accepted values that were based on speculative assumptions.

BLM lands personnel assumed the LTBMU and its employee had full authority to make decisions regarding the exchange. The RO staff relied on the professionalism and expertise of the LTBMU employee and assumed the employee would comply with FS land exchange policies and procedures. The LTBMU employee's actions went undetected by the RO until it was too late for them to act.

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**FINDING NO. 1**  
**REGIONAL OFFICE OVERSIGHT  
OF THE ZEPHYR COVE LAND  
EXCHANGE WAS INADEQUATE**

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The RO staff did not communicate FS levels of authority and responsibility to BLM staff before the land exchange began, and it did not adequately monitor the actions of the LTBMU employee during the exchange. RO staff also allowed the LTBMU to create an interagency agreement with BLM without reviewing the agreement to ensure it identified the limited authority of the LTBMU and the oversight role of the RO. Finally, RO staff did not specifically direct the LTBMU to submit the Zephyr Cove land exchange documents to a required FS review before allowing BLM to finalize the land exchange. The RO staff relied on the professionalism and expertise of the LTBMU employee and assumed he would comply with FS land exchange policies and procedures. The LTBMU employee's improper actions went undetected by the RO until it was too late for them to act.

Standards for Internal Controls in the Federal Government<sup>2</sup> specify that key duties and responsibilities need to be divided or segregated among different people to reduce the risk of error or fraud. This should include separating the responsibilities for authorizing transactions, processing and recording them, reviewing them, and handling any related assets. No one individual should control all key aspects of a transaction or event.

**a. The ESRO Inappropriately Allowed the LTBMU to Act as the Primary Contact Between FS and BLM Staff**

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<sup>2</sup> These standards were issued by the Comptroller General in 1983 and updated in 1999.

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The RO's acceptance of the LTBMU employee as the primary contact between FS and BLM staffs contributed to the errors in the Zephyr Cove land exchange. The BLM staff communicated exclusively with the LTBMU employee and did not contact the RO during any part of the case processing. Believing that the LTBMU employee had the authority to approve changes in the Zephyr Cove land exchange, the BLM staff accepted instructions from the LTBMU employee that were inappropriate and did not comply with FS policy and procedures.

A RO lands employee told us that in a typical FS land exchange, the LTBMU had limited land exchange authority. LTBMU staff could prepare land exchange documents at the forest level, but had to submit all documents to the RO staff for final review and approval. The RO lands employee said that he

- considered the LTBMU employee to be an appropriate point of contact between the FS and BLM because he had over 7 years of experience, and
- specifically instructed the LTBMU employee to keep the RO informed of any changes in the Zephyr Cove transaction.

Although the land exchange authority of the LTBMU employee was limited, the RO did not communicate this information directly to BLM before BLM began processing the Zephyr Cove land exchange. The RO staff did not consider it necessary because they assumed that the LTBMU employee would comply with normal FS review and approval procedures and delegations of authority.

BLM staffers said they assumed that the LTBMU employee spoke for the FS. When changes to the Zephyr Cove exchange occurred (see Finding No. 2), the BLM staffers assumed the LTBMU employee had the delegated authority to approve these changes or that he had obtained prerequisite approvals from FS upper management.

**b. RO Staff Did Not Participate in the Development of an Interagency Agreement Between LTBMU and BLM**

The RO staff allowed the LTBMU and a BLM district office to create an interagency agreement that defined FS and BLM staff roles and responsibilities in the processing of the Zephyr Cove land exchange. This agreement was inappropriate because (1) it involved a level of FS management (LTBMU) that did not have the delegated authority to approve changes in the Zephyr Cove land exchange and (2) it did not specify RO oversight responsibilities.

The LTBMU employee contacted the RO and suggested that the FS and BLM create an interagency agreement that specified the roles and responsibilities of each agency during the Zephyr Cove case processing.

The RO staff agreed to the development of the interagency agreement, but instead of creating an agreement between themselves and upper levels of BLM management, the RO allowed the LTBMU to create an agreement between itself and the BLM district office processing the Zephyr Cove exchange. The RO was not involved in the development of the interagency agreement or its contents. The RO also did not review the agreement before BLM began processing the exchange to ensure that the agreement specified the limited land exchange authority of the LTBMU, that the transaction would be processed in compliance with FS policies and procedures, and that any significant changes to the land exchange would be approved by the RO and/or OGC.

We reviewed the interagency agreement and determined that it involved inappropriate levels of authority, did not specify any oversight role for RO lands management, and lacked important internal controls.

- The agreement gave the LTBMU apparent authority to approve changes in the land exchange, when the LTBMU had no such authority.
- The agreement did not direct the LTBMU or BLM staff to consult with and obtain the approvals of RO staff when significant changes occurred in the Zephyr Cove land exchange. The agreement also did not direct the LTBMU to subject the Zephyr Cove land exchange to the same FS reviews and approvals required in a typical FS land adjustment transaction.
- The agreement did not require BLM to provide the FS and OGC with draft copies of the final title documents before the Zephyr Cove land exchange was finalized by BLM staff.

The interagency agreement between the LTBMU and the BLM district office was to remain in effect until all Zephyr Cove operations had been completed or 30 days after receiving written notice from one of the participating agencies. Since the FS still has not received a final title opinion on the Zephyr Cove land exchange from OGC (see Finding No. 4) the agreement may still be in force. The FS should send a written notice to BLM and terminate this interagency agreement.

**c. RO Staff Did Not Ensure LTBMU Employee Submitted Zephyr Cove Documents to Required FS Review**

RO staff did not ensure that the LTBMU employee submitted the Zephyr Cove land exchange documents to the Central Zone Landownership

Adjustment Team for their review and approval before BLM finalized the land exchange. Consequently, the LTBMU employee did not subject any of the Zephyr Cove documents to FS review. This resulted in land exchange documents that contained multiple errors and did not comply with FS policy or Federal regulations.

In the Pacific Southwest Region, landownership adjustment teams are responsible for reviewing and approving all land exchange documents. These three teams, located in the north, south and central zones of the region, are staffed with FS title specialists who review and cure land title problems, assist in the preparation of all land conveyance documents and ensure that titles to the non-Federal lands being transferred to the USA are acceptable to the FS before land adjustments are finalized. Under regional direction, each forest in the region must submit all land adjustment cases to the zone teams for their review and approval. The zone teams then forward the land exchange documents to the RO for final review and approval.

The RO staff did not specifically direct the LTBMU employee to submit the Zephyr Cove documents to the Central Zone Landownership Adjustment Team for their technical review and approval. RO staffers told us that they assumed the LTBMU employee would comply with normal FS review and approval procedures. The staffers added that there was no reason for the LTBMU employee to believe that FS internal control procedures, such as the zone's technical review of the title documents, did not apply to the Zephyr Cove transaction.

The LTBMU employee told us that Zephyr Cove documents were not submitted to the Central Zone because the employee assumed the BLM staff would review the Zephyr Cove documents to ensure they complied with FS policies and procedures. The employee did not determine if anyone on the BLM staff was familiar with FS policies and procedures, did not discuss this review process with BLM during the land exchange, and did not ensure that BLM had actually reviewed the documents for compliance with FS policy.

The RO staff needs to establish clear lines of authority and responsibility when processing land exchanges with other Federal agencies. For exchanges involving the Pacific Southwest Region and BLM, the RO staff should create a formal Memorandum of Understanding between the region and BLM that specifies the roles and responsibilities of each of these staffs. This memorandum should ensure that any FS personnel designated as the principal contact between FS and BLM have the delegated authority to approve changes that may occur during the land exchange. It should also ensure that appropriate FS personnel receive draft copies of final title documents prior to BLM's closure of any land exchange involving the FS.

This would give the RO and zone staffs an opportunity to correct any provisions that do not comply with FS policy and procedure.

The RO should also reiterate the FS policy regarding the review and approval responsibilities of the landownership adjustment teams. The RO should specifically direct FS staffs to submit all documents associated with FS/BLM land transactions to zone review and approval to ensure that these transactions comply with FS policy and procedures and meet management expectations.

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**RECOMMENDATION NO. 1**

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Send written notice to the BLM staff and terminate the interagency agreement between the LTBMU and BLM.

**ES Response**

By letter dated June 15, 2000, the Regional Forester of Region 5 formally terminated the 1996 interagency agreement between the LTBMU and BLM.

**OIG Position**

We accept management decision on this recommendation.

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**RECOMMENDATION NO. 2**

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Create a Memorandum of Understanding between the Pacific Southwest Region and BLM that specifies the roles and responsibilities of the FS and BLM staffs when processing land

exchanges involving both agencies. Ensure that principal contacts cited in the agreement have sufficient delegated authority to approve changes that may occur during the land exchange.

**ES Response**

A Memorandum of Understanding (MOU) between the Pacific Southwest Region and the BLM has been signed by the R-5 Regional Forester and the Nevada State Office BLM Director and became effective on June 14, 2000. The MOU outlines the work to be performed and specifies the roles and responsibilities of the Forest Service and BLM lands staffs when processing land exchanges involving both agencies.

**OIG Position**

We accept management decision on this recommendation.

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**RECOMMENDATION NO. 3**

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Ensure that appropriate FS personnel at the RO and zone levels receive draft copies of final title documents prior to BLM's closure of any land exchanges involving the FS.

**ES Response**

The Regional Director of Lands mailed copies of the executed MOU to all relevant forest, zone, and RO personnel on June 15, 2000. Follow-up will be made by the Regional Director of Lands to ensure receipt of these documents by the appropriate parties by July 1, 2000. Attachment "A" to the MOU specifies that the Forest Service will review and concur on final title opinions to non-Federal lands before BLM accepts title.

**OIG Position**

We accept management decision on this recommendation.

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**RECOMMENDATION NO. 4**

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Clarify RO policy relating to the review and approval function of zone landownership adjustment teams for land exchanges involving BLM.

**ES Response**

We agree that the RO policy relating to the review and approval function of zone land ownership adjustment teams for land exchanges involving BLM needs to be clarified. The Regional Forester will develop written policy, which will be reviewed by the WO Director of Lands. The final policy will be incorporated into the Forest Service Region 5 directives no later than December 31, 2000.

**OIG Position**

We accept management decision on this recommendation.

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**FINDING NO. 2**  
**ACTIONS BY LTBMU STAFF**  
**OVERVALUED THE LAND**  
**ACQUIRED IN THE EXCHANGE**  
**AND ENCUMBERED THE**  
**GOVERNMENT'S OWNERSHIP**  
**INTEREST**

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As a result of actions taken by LTBMU staff during the Zephyr Cove land exchange, the FS has acquired, at a cost to the taxpayer of \$38 million, a property in which a private party, Park Cattle Company, has asserted the exclusive right to control public access to the main gate and driveway existing on the Zephyr Cove land. Park Cattle Company also currently occupies improvements on the property and has imposed exclusive use of the surrounding public land

contrary to FS policy. In addition, the proponent who initiated the Zephyr Cove land exchange, the Olympic Group, Inc., not only received a potential profit of \$10 million from the transaction but also was subsequently allowed by the LTBMU staff to receive an additional \$300,000 in cash and approximately \$2.7 million in conditional amenities from the unauthorized sale of the Zephyr Cove improvements to Park Cattle.

In completing the Zephyr Cove land exchange, the LTBMU employee failed to protect the public's interest. Although he was directed by the FS regional staff to keep the RO office informed of any significant changes relating to the land exchange, the LTBMU employee proceeded with the transaction regardless of significant issues concerning the value of the property, the use of the property, the improvements on the property, and the ownership rights to the property. The employee took inappropriate and unauthorized actions that benefited Olympic Group, Inc. and did not protect the taxpayer's interest.

Title 36 CFR 254.15(cii) states that the FS shall not accept title to lands in which there are reserved or outstanding interests that would interfere with the use and management of the land by the FS, or would otherwise be inconsistent with the purpose for which the lands are to be acquired. The section further specifies that any reserved interests by the landowner are subject to Secretary of Agriculture regulations, cited in 36 CFR 251.

Responsibility for land exchanges is set forth in Forest Service Manual (FSM) 5404.14 (March 1995). The FSM specifies that the RO director of lands is responsible for approving land exchange documents and consummating all land exchanges subject to any required approval of the Secretary. The RO director of lands is also responsible for executing deeds, accepting title to non-Federal lands, and authorizing delivery of other considerations after approval of the land exchange. The Forest Supervisor, or designee (such as the LTBMU employee), has no such land exchange authorities unless specifically designated by the RO. Rather, the Forest Supervisor is responsible for informing the Regional Forester of all land acquisitions that may have policy implications or be precedent-setting and that may attract congressional or media attention.

When the Zephyr Cove land exchange was first proposed to the FS, the Pacific Southwest Regional Forester made it known that the FS was interested only in acquiring the Zephyr Cove land, not the improvements that resided on it. Olympic Group, Inc., which would receive BLM land in exchange for Zephyr Cove, agreed to remove the improvements. The RO staff agreed to the exchange on these terms, and BLM began processing the case. The LTBMU forest supervisor designated the LTBMU employee as the primary contact between the FS and BLM. RO staff directed the LTBMU employee to keep them informed of any significant changes to the approved land exchange and turned the case processing over to BLM and the LTBMU.

RO lands staff did not communicate further with BLM or the LTBMU and assumed that the Zephyr Cove land exchange was proceeding as planned.

However, this was not the case. We determined that the LTBMU employee took several actions to the detriment of the public's interest:

1. Withheld information from a FS appraiser that affected the overall value of the property, benefiting Olympic,
2. Authorized the acquisition of the Zephyr Cove property with the improvements in place, contrary to RO direction,
3. Overstated the value of the property by avoiding a deed reservation, benefiting Olympic,
4. Created an agreement with Olympic that was not supported by Federal law,
5. Misinformed a FS appraiser about the future use of the Phase 2 property,
6. Did not review the Zephyr Cove deeds to ensure they did not contain unacceptable easements, benefiting both Olympic and Park Cattle Company,
7. Attempted to significantly modify the Zephyr Cove title documents after the land exchange was completed, and
8. Allowed Olympic to sell Government-owned improvements to Park Cattle Company.

The LTBMU employee pursued these actions without notifying RO staff of the changing status of the Zephyr Cove land exchange and without having OGC review the title documents.

#### **APPRAISING ZEPHYR COVE AS TWO SEPARATE EXCHANGES INCREASED ITS OVERALL COST TO THE TAXPAYER**

The LTBMU employee failed to advise a FS appraiser that the Zephyr Cove property was going to be conveyed to the USA in its entirety, even though the LTBMU employee knew during the first phase of the exchange that Olympic intended to convey additional Zephyr Cove acreage to the FS at a later date.

The employee's failure to communicate this information to the FS appraiser overstated the total value of the Zephyr Cove property by several million dollars.

Olympic initially proposed exchanging the entire 47.2-acre Zephyr Cove estate to the FS, but later reduced the offer to 35.4 acres of unimproved land after the FS stated that they did not want to acquire the Zephyr Cove improvements. Olympic purportedly intended to sell the remaining 11.8-acre parcel containing the mansion and guest cottage on the open market. However, during the processing of the 35.4-acre land exchange, the LTBMU employee learned that Olympic had changed its plans and wanted to give the remaining Zephyr Cove acreage to the FS in the second phase of its land exchange with BLM.

Notes written by the LTBMU employee show that he knew about Olympic's plans as early as July 1996, four months before Phase 1 of the Zephyr Cove land exchange was completed and before its appraised value had been approved by the FS appraiser. However, the LTBMU employee did not notify the FS appraiser or RO staff about the Phase 2 acreage until after the first land exchange had been completed.

The Uniform Appraisal Standards for Federal Land Acquisitions (UASFLA), which governs all Federal appraisals, as well as FS appraisal procedures both require contiguous parcels under the same ownership to be appraised as a single transaction, if possible. These appraisal instructions are designed to prevent a landowner from dividing one large parcel into multiple smaller parcels in order to increase the land's total appraised value.

The LTBMU employee responded to our questions about his actions in a signed sworn statement. When we asked the LTBMU employee why Olympic's plans were not communicated to the FS appraiser in a timely manner, the employee stated that he did not think about how the acquisition of additional Zephyr Cove acreage in Phase 2 would impact the property's total appraised value.

The FS appraiser told us that he did not know Olympic intended to transfer the Phase 2 acreage to the FS until the LTBMU employee sent him a completed appraisal report for the 11.8-acre parcel a few months after Phase 1 of the Zephyr Cove land exchange closed. The FS appraiser stated that if he had known there was going to be a second phase in the Zephyr Cove land exchange, he would have required the entire 47.2-acre property to be appraised as a single parcel, rather than as two separate parcels. According to the FS appraiser, the employee's delay in communicating Olympic's plans potentially overstated the total appraised value of the Zephyr Cove property by several million dollars.

**ACQUIRING ZEPHYR COVE WITH IMPROVEMENTS DEFIED REGIONAL DIRECTION AND FS POLICY**

The Pacific Southwest Region RO agreed to proceed with the Zephyr Cove land exchange under the expectation that the FS would acquire only unimproved lakefront property. However, during the processing of the Zephyr Cove land exchange, the LTBMU employee improperly instructed BLM to proceed with the land exchange even though the improvements on the Zephyr Cove property would remain in place. These actions directly contradicted RO direction and exceeded the LTBMU employee's delegated authority.

Knowing that the FS did not want to acquire the Zephyr Cove improvements, Olympic initially volunteered to remove all structures from the land before transferring it to the FS. FS staff agreed to this proposal and BLM began processing Phase 2 of the Zephyr Cove land exchange. However, approximately 2 months before the second phase of the Zephyr Cove land exchange was scheduled to close, the LTBMU employee drafted an agreement with Olympic that allowed Olympic to choose between demolishing the improvements at its own expense, or selling the improvements to a third party to operate as a FS concession. Soon after, BLM lands management became concerned that demolition of a lakefront mansion might generate negative public reaction. They told the LTBMU employee that removal of the improvements was not an option if the FS wished to proceed with the land exchange.

In response, the LTBMU employee chose to modify the LTBMU draft agreement with Olympic. Under the new terms of the agreement, Olympic could either sell the Zephyr Cove improvements to a private party to operate as a FS concession, or it could quitclaim the improvements to the FS and pay the FS \$42,500 for annual maintenance expenses. In March 1997, the LTBMU forest supervisor and Olympic signed the agreement. The forest supervisor told us that he thought the LTBMU employee had submitted the agreement to the RO and OGC for their review and approval. However, the employee had not. (Our concerns about this agreement are detailed in the following two sections.)

The LTBMU employee sent the signed agreement to the BLM staff processing the Zephyr Cove exchange. According to a BLM lands employee, the BLM staff assumed the LTBMU had the authority to approve the Zephyr Cove exchange with the improvements in place, had followed FS policy and procedure and had received the appropriate approvals to proceed. Consequently, after BLM received the signed agreement from the LTBMU, it finalized the Zephyr Cove land exchange with the improvements in place on the land.

Even though the RO had specifically prohibited any Zephyr Cove acquisition with improvements, the LTBMU employee did not tell RO staff that the LTBMU and the BLM had decided not to remove the structures or that the

LTBMU had created a special agreement with Olympic. RO staff did not learn that the Zephyr Cove improvements had remained on the lakefront parcel until June 1997, about 3 months after Phase 2 of the Zephyr Cove land exchange closed.

A RO lands employee told us that the LTBMU employee exceeded his delegated authorities when he told BLM to process the Zephyr Cove land exchange with the improvements in place. The RO lands employee said that the LTBMU employee knew that the RO did not want to acquire the improvements and had agreed to the exchange only after Olympic arranged to remove the improvements from the land. The RO lands employee told us that any decision to keep the Zephyr Cove improvements on FS land would have clearly required the involvement of the RO, the Washington Office, and the OGC. He stated that the LTBMU employee had many years of land adjustment experience and should have known that he did not have the authority to significantly change the terms of the Zephyr Cove land exchange without the approval of higher management.

**OMISSION OF THE CFR DEED RESERVATION VIOLATED FEDERAL REGULATIONS AND OVERSTATED THE VALUE OF THE ZEPHYR COVE LAND**

The agreement created by the LTBMU and Olympic purportedly allowed Olympic to retain ownership of the Zephyr Cove improvements after the land was transferred to the USA. The reservation of privately owned improvements on public land is specifically controlled by Federal regulation and FS procedures. However, the LTBMU employee did not comply with these requirements. Instead, the employee once again exceeded his delegated authority and chose to omit the required reservation language. The employee's actions violated Federal regulations and overstated the Zephyr Cove appraised value by as much as \$10 million (see Finding No. 3 for details of appraisal values).

Privately owned improvements remaining on land being transferred to the Federal Government must be reserved in conformance with Title 36 CFR 251. The use of this reservation is required without exception. Under Federal regulations, the landowner must identify the improvements reserved, the type of intended use, and the amount of Federal land that will be encumbered by that use. The reservation of improvements decreases the amount of usable land being transferred to the USA and reduces the property's appraised value. The landowner's improvement reservation must be specified in the deed used in the appraisal analysis and in the deed used to convey the land to the USA.

When we asked the LTBMU employee about his familiarity with the use of reservations and their impact on land values, the employee indicated a complete familiarity in his signed sworn statement.

*I have always used the occupancy and use reservation in the past. This was the first time I did not use [it]. I don't know why I did not use [it]...The impact on value depends on how the reservation affects the new owner's ability to use the land. In the case of road or utility easements, that type of reservation would probably not affect the appraised value. However, in a case like the Zephyr Cove improvements, such a reservation would impact the appraised value because the presence of the house would affect the new owner's use of the land.<sup>3</sup>*

The LTBMU employee told us that he thought the LTBMU could authorize the landowner's occupancy and use of the Zephyr Cove improvements by issuing a special-use permit rather than using the CFR reservation. However, FS special-use permits are used to authorize commercial development on land already owned by the FS and are issued only after the public has commented on and approved commercial development of public land. Special-use permits are not used to authorize private ownership of improvements remaining on land being transferred to the FS.

The LTBMU employee said that he did not consult with RO staff or OGC when he made the decision to omit the CFR reservation and substitute a special-use permit. The employee told us that he did not have to get RO and OGC approval because the LTBMU had the delegated authority to issue special-use permits. The LTBMU employee said that he did not know why he thought the CFR reservation did not apply to the Zephyr Cove land exchange. However, the LTBMU employee wrote in an earlier FS document that Olympic did not want a reservation.

OGC and RO staff learned of the omitted CFR reservation after Phase 2 of the Zephyr Cove land exchange was completed. OGC told us that the LTBMU employee exceeded his delegated authority when he omitted the CFR reservation. OGC said that the LTBMU employee did not have the authority to decide that the CFR reservation would not be used and that a special-use permit could be substituted. Further, OGC counsel had specifically informed the LTBMU employee of the CFR requirement a few months before the employee omitted the required reservation. OGC staff discussed the use of the CFR reservation with the LTBMU employee in early 1997 in connection with the Thunderbird land exchange. In that conversation, the LTBMU employee and OGC discussed the fact that the Thunderbird land

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<sup>3</sup> This and all quotes from the LTBMU employee were taken from the officer's signed sworn statement, obtained by OIG on October 6, 1999.

exchange proponent wanted to transfer the underlying land to the FS but retain ownership of the Thunderbird Lodge and other structures. However, the exchange proponent did not want to use the CFR reservation because it would reduce the land's appraised value.

In that conversation, the LTBMU employee suggested that the CFR reservation might not be required. He thought that if the Thunderbird improvements could somehow be "severed" from the underlying land, the CFR reservation would not apply. The LTBMU employee suggested that the occupancy and use of the Thunderbird Lodge (one of the improvements) could be authorized through a special-use permit issued by the LTBMU, rather than by the CFR reservation.

According to OGC, the LTBMU employee's concept was flawed because it presumed that the improvements could be artificially "severed" from the underlying land, when in fact the improvements remained on the land and used the land. OGC told the LTBMU employee that a special-use permit could not be used to replace the CFR reservation, and that the CFR reservation was the only legal way a landowner could retain privately owned improvements on Federal land.

A RO lands employee also remembered this discussion with OGC. He recalled OGC telling the LTBMU employee that the CFR reservation was mandatory. The lands employee stated that this discussion occurred at the same time the Zephyr Cove land exchange was being processed and that the implication for the Zephyr Cove improvements was clear. He added that the LTBMU employee never discussed plans to omit the CFR reservation in the Zephyr Cove land exchange with him.

The LTBMU employee's decision to omit the CFR reservation was a direct violation of the instructions the employee received from RO staff and OGC. By omitting the CFR reservation, the employee caused the appraised value of the Zephyr Cove land to be greatly overstated. According to appraiser estimates, if Olympic had properly reserved 6 acres of land immediately surrounding the improvements (the minimum reasonable amount), the appraised value of the property would have been reduced by up to \$10 million. (See Finding No. 3 for details of appraisal values).

**LTBMU'S UNAUTHORIZED AGREEMENT GAVE OLYMPIC THE APPARENT RIGHT TO SELL GOVERNMENT-OWNED PROPERTY WITHOUT COMPENSATING THE PUBLIC**

As noted above, the LTBMU and Olympic entered into an agreement that intended to allow Olympic to convey the Zephyr Cove improvements to a third party after Phase 2 of the land exchange was completed. Execution of this agreement exceeded the LTBMU's delegated authority and was not supported by Federal law.

According to the March 1997 agreement between the LTBMU and Olympic, Olympic would "sever" the Zephyr Cove improvements from the FS land and "convey only the improvements" to a private party who would operate them as a FS concession. However, as stated earlier, the LTBMU employee did not use a required CFR improvement reservation. Without this reservation in the deed, Olympic did not legally reserve ownership of the Zephyr Cove improvements. Consequently, the agreement created by the LTBMU purported to authorize Olympic to sell Government-owned improvements to a private party.

The LTBMU employee and Olympic created this agreement without notifying or consulting RO staff or OGC. The LTBMU employee told us that he did not think RO or OGC approval was necessary. The LTBMU employee stated that since the LTBMU had the authority to approve FS concessions, he thought the LTBMU also had the authority to direct Olympic to convey the improvements to a private party to operate as a FS concession. The LTBMU employee stated that a FS specialist had reviewed the agreement and approved it. The employee considered this review and approval to be sufficient. However, when we interviewed the specialist, he told us that he had approved the agreement even though the LTBMU employee told him there was no statutory authority to support it.

At our request, OGC reviewed the agreement between the LTBMU and Olympic. OGC concluded that the LTBMU had no authority to create such an agreement with Olympic, no authority to agree that Government-owned improvements could be "severed" from public land, and no authority to direct Olympic to convey the Government-owned improvements to a third party.

A RO lands employee stated that the LTBMU employee had enough experience to know that OGC's legal opinion was required when dealing with structures and improvements on FS land.

**FUTURE USE OF THE ZEPHYR COVE IMPROVEMENTS WAS MISREPRESENTED TO A FS APPRAISER**

The LTBMU employee told a FS appraiser that the Zephyr Cove improvements would be operated as a FS concession when in fact no concession had been approved by the LTBMU. Although appraisers may

not estimate values enhanced by Government permits<sup>4</sup> or based on speculative future events, the FS appraiser relied on the LTBMU employee's information, and recommended approval of a \$13½million value for Phase 2 of the Zephyr Cove land exchange (See Finding No. 3 for details of appraisal values).

The LTBMU employee told the FS appraiser that the LTBMU would issue a special-use permit to the private party taking control of the Zephyr Cove improvements, and allowed the appraiser to believe that the LTBMU would collect a concessionaire fee based on a percentage of the land's fair market value. Such a fee would amount to \$450,000 to \$500,000 per year.

We determined that the information communicated to the FS appraiser was incorrect. No need for a concession had been demonstrated on the Zephyr Cove property, no concession had been approved or evaluated by LTBMU staff, and no potential purchaser of the improvements had applied for a special-use permit. Further, the LTBMU employee knew the LTBMU would probably not charge the concessionaire a fee based on the land's fair market value if/when the concession was approved. The LTBMU employee told us the LTBMU planned to charge the concessionaire a much smaller fee, based on a percentage of operating revenue. A RO special-use officer told us such a fee would have been "miniscule."

The FS appraiser stated that the Zephyr Cove improvements encumbered the public land and that he only approved the \$13½million value because he thought the LTBMU intended to charge a concessionaire fee that would fairly compensate the public. The appraiser told us that if he had known the Zephyr Cove concession had not been approved, or that the prerequisite fee would not be charged, he probably would not have approved the \$13½million value. He added that the Zephyr Cove value, approved with the expectations of an approved FS concession and an explicit fee, might have become invalid when the expectations did not occur.

### **ZEPHYR COVE DEEDS CONTAINED EXCLUSIVE EASEMENTS THAT COULD RESTRICT PUBLIC ACCESS TO THE LAND**

The LTBMU employee did not review the Zephyr Cove conveyance documents before the land exchange closed. As a result, the FS acquired land that may be subject to an exclusive, perpetual easement (i.e., right-of-way) controlled by Park Cattle Company. (See Chapter 2)

The deeds used to convey the Zephyr Cove land to the USA for both Phase 1 and Phase 2 cited an exclusive, perpetual easement reserved by Olympic. This easement, if enforceable, would restrict the public's use of the land and

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<sup>4</sup> See Forest Service Handbook 5409.12(1.15).

is not allowed under FS policy. In addition, the presence of an exclusive easement on FS land would further complicate FS management of the Zephyr Cove property.

It was the responsibility of the LTBMU employee to review the Zephyr Cove deeds before the land exchange closed, to ensure that the land being transferred to the FS was in acceptable condition. The LTBMU employee did not review the deeds prepared for Phase 1 or Phase 2 of the land exchange until the land exchange had been closed by BLM. At that point in the transaction, title to the Zephyr Cove lands had already passed to the USA and nothing could be done about the exclusive easements.

The LTBMU employee stated that he did not review the Zephyr Cove deeds prior to closing because he assumed BLM staff had performed the review and had removed any easements or encumbrances objectionable to the FS.

When asked to explain his actions specifically concerning the presence of an exclusive easement in the Phase 2 warranty deed, the LTBMU employee stated that he had never noticed the exclusive easement until the day of our interview, more than 2 years after the land exchange closed.

*I never noticed that the exclusive easement was also in the Phase 2 warranty deed. I did notice the exclusive easement in the Phase 1 warranty deed. I received the warranty deed for Phase 1 after BLM had finalized the land exchange, so I did not have an opportunity to change the language. When I noticed the exclusive easement in the Phase 1 warranty deed, I did not talk to anyone at BLM about it, or notify BLM staff that exclusive easements were unacceptable to the FS.*

#### **BELATED DEED RESERVATION ENCUMBERED THE ZEPHYR COVE LAND AND RESULTED IN CONFLICTING CLAIMS OF OWNERSHIP**

After Phase 2 of the Zephyr Cove land exchange had been completed and the \$13½million value had been approved without the CFR reservation, the LTBMU employee tried to belatedly insert a CFR reservation into the recorded Zephyr Cove deed. The LTBMU employee exceeded his delegated authority and took this action without informing or consulting RO staff or OGC and without considering the potential impact to Zephyr Cove's approved value.

In June 1997, the LTBMU employee directed BLM staff to insert a CFR reservation into the Zephyr Cove deed. This direction occurred about 2 months after the land exchange closed and after Olympic had received Federal land valued at \$13½million. In the employee's signed sworn statement, he offered little explanation why, if he thought a special-use permit could authorize occupancy and use of the improvements before the land

exchange closed, a CFR reservation became necessary after the land exchange was finalized.

*Earlier in the land exchange, I did not think the CFR's applied so I did not send any of the information to BLM. However, later, after the land exchange was completed, I somehow realized that the CFR's did apply ... It somehow came to me that occupancy and use had to be specified in the reservation and that the occupancy and use reservation had to be used. I cannot recall why I reached that conclusion.*

The LTBMU employee contacted BLM staff and told them to add the CFR reservation and re-record the document. Even though the Zephyr Cove property had already passed into FS ownership, the LTBMU employee did not contact either RO staff or OGC to discuss the propriety of asserting an improvement reservation onto land already owned by the FS.

We determined that the LTBMU employee did not have the delegated authority to create a CFR reservation or to decide that the reservation could, and should, be inserted into a revised deed after title to the Zephyr Cove land had transferred to the FS. Such legal decisions are the responsibility of OGC, which drafts and finalizes all FS reservations. When questioned about these actions, the LTBMU employee told us that he knew he did not have the authority to create CFR reservations in normal FS land adjustments. He said that he did not think OGC approval was necessary in this case because he still considered the Zephyr Cove transaction to be a BLM land exchange, even though the Zephyr Cove land had transferred to the FS approximately 2 months earlier.

OGC learned about the inserted CFR reservation in the summer of 1997, about 3 months after Phase 2 closed and shortly after BLM recorded the CFR reservation in a revised deed. OGC reviewed the Zephyr Cove title documents and determined that the original deed, recorded in April 1997, conveyed the Zephyr Cove land to the USA with no reservation for improvements. Consequently, title to the Zephyr Cove land, and to the improvements, passed to the USA at that time. OGC then reviewed the later deed, with the inserted reservation, and concluded that it appeared to be an attempt to reserve Olympic's ownership of the Zephyr Cove improvements after title had passed to the USA. OGC stated that the inserted reservation was void because significant terms, such as area encumbered, purpose of use, and duration were not specified. OGC also noted that any reservation of the Zephyr Cove improvements would require that the \$13½million appraisal be redone to reflect the fact that the land transferred to the USA was encumbered by private use.

The LTBMU employee told us that he had intended to specify the area encumbered by the Zephyr Cove improvements, purpose of use and duration of occupancy, but had been unable to do so because BLM staff recorded the vaguely worded reservation before he could further refine it. The LTBMU employee stated that a properly worded reservation would have authorized the presence of the Zephyr Cove improvements on the FS land and removed the need for a special-use permit.

We explained to the LTBMU employee that if he had been able to insert a legal reservation into the Phase 2 deed as he intended, the approved \$13½ million value would have become invalid because the appraisal assumed the Phase 2 property had no outstanding reservations. We also explained that, because the Zephyr Cove land exchange had already been completed, and Olympic had already received title to \$13½million worth of BLM lands, the Zephyr Cove appraisal could not have been corrected. Further, insertion of a reservation into the deed after the land exchange closed would have authorized Olympic's payment-free use of the Zephyr Cove improvements and surrounding FS land. In his signed sworn statement, the LTBMU employee stated:

*I did not think about how the occupancy and use reservation would impact the appraised value. Now, in retrospect, I realize that if occupancy and use had been specified and imposed, it would have affected the fair market value of the Zephyr Cove land.<sup>5</sup>*

The LTBMU employee acknowledged that, in retrospect, inserting a CFR reservation into the recorded Zephyr Cove deed was not the right solution.

**LTBMU ALLOWED PARK CATTLE COMPANY TO TAKE CONSTRUCTIVE POSSESSION OF THE IMPROVEMENTS ON FS LANDS WITHOUT ENSURING THAT PARK CATTLE WOULD ABIDE BY FS JURISDICTION AND CONTROL**

The LTBMU allowed Olympic to sell the Zephyr Cove improvements to Park Cattle Company, a private operator with whom the FS had no prior understanding. Prior to the sale, the LTBMU employee had no direct communication with Park Cattle, no written agreement on how the Zephyr Cove improvements residing on the public land would be operated, and no assurance that Park Cattle would comply with FS land use policies and procedures. The LTBMU also allowed the sale to occur without ensuring that Park Cattle would allow public access to the FS land surrounding the improvements and would fairly compensate the public.

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<sup>5</sup> This contradicts the LTBMU employee's earlier statement (on page 21) that he knew the CFR reservation would have reduced the value of the Phase 2 property.

On June 30, 1997, the acting LTBMU forest supervisor signed a letter, prepared by the LTBMU employee, that acknowledged Olympic's plan to sell the Zephyr Cove improvements to Park Cattle. Park Cattle, a Nevada Corporation, had never operated as a FS concessionaire, and had a reputation for catering to "upper-end clientele." The LTBMU could have directed Olympic to convey the improvements to the FS, but it did not do so. We questioned the rationale of the forest supervisor's decision, because his action undermined the property rights of the FS and allowed Park Cattle to assert claims on the newly acquired Zephyr Cove lands. The LTBMU forest supervisor stated that when he signed the acknowledgement letter, he did not know the agreement between the LTBMU and Olympic had not been approved by OGC, that the Government owned the improvements, or that the terms of the agreement allowed the FS to direct Olympic to transfer the improvements to the FS. The supervisor told us that he thought Olympic had the right to sell the Zephyr Cove improvements and that he sent the authorizing letter to Olympic after receiving numerous phone calls from Olympic, local county commissioners, and Park Cattle.

On July 2, 1997, Olympic sold the Zephyr Cove improvements to Park Cattle Company for \$300,000 cash and other amenities. After the purchase, Park Cattle locked the gates to the Zephyr Cove property, employed a caretaker to guard the grounds surrounding the Zephyr Cove improvements, and installed private property signs and trail markers on the lakefront property designed to restrict the public's use of the FS land. Park Cattle also submitted a special-use application to the LTBMU requesting approval to use the entire 47.2-acre Zephyr Cove property surrounding the improvements for non-natural, urban development. Included in Park Cattle's request were plans for tennis courts, gazebos, and swimming pools for paying guests staying at the mansion or attending meetings at the proposed conference center. Park Cattle's application did not provide for general public access and use of the FS land and lakefront. In addition, Park Cattle arranged, as part of its sale agreement, to give Olympic exclusive use of the Zephyr Cove improvements in the months of February, March, July, August and September for 25 years. Park Cattle's proposed urban development of the Zephyr Cove land, the lack of public access, and the exclusive use by Olympic, were all contrary to FS land use policies and procedures.

When we questioned the LTBMU employee as to why he had not met with Park Cattle prior to the sale of the improvements, the LTBMU employee said that he assumed Olympic would inform Park Cattle of FS land use policies and procedures before selling them the Zephyr Cove improvements. We questioned the land staff officer's reliance on Olympic to communicate specific FS regulatory information to a private party when Olympic was not a FS representative, had no experience as a FS concessionaire, and had a vested interest in selling the Zephyr Cove improvements for the highest possible price.

The LTBMU's decision to let Park Cattle control the Zephyr Cove improvements is now the source of the current legal dilemma faced by the FS. In early 1998, RO staff determined there was no demonstrated need for a concession at Zephyr Cove, but that there was a critical need for unrestricted public access to Lake Tahoe. In an effort to resolve the situation, RO staff suggested that Park Cattle sell the Zephyr Cove improvements back to Olympic, and that the FS and Olympic would resolve the improvement issue without any financial hardship to Park Cattle. However, Park Cattle refused to divest itself of the Zephyr Cove improvements and instead, threatened litigation if the FS did not issue it a special-use permit at a low fee. The FS is now negotiating with Park Cattle to resolve the situation. (See Finding No. 4)

Our audit concluded that the LTBMU employee did not act prudently or in the public's best interest when he processed the Zephyr Cove land exchange. He took actions that were inappropriate, unauthorized, and irresponsible. As a result, the public paid \$38 million to acquire the Zephyr Cove property that is now encumbered by unauthorized, private use. In addition, the proponent, Olympic Group, Inc., was overpaid by as much as \$10.3 million as a result of the LTBMU employee's decision to omit the CFR reservation and authorize the sale of the Government-owned Zephyr Cove improvements.

The original intent of the Zephyr Cove land exchange--to protect sensitive species and to increase public access to Lake Tahoe--is no longer feasible due to the unauthorized occupancy by Park Cattle. RO staff responsible for evaluating the performance of the LTBMU employee should review his performance in the Zephyr Cove land exchange and take the appropriate personnel action commensurate with his actions.

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**RECOMMENDATION NO. 5**

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Review the actions of the LTBMU employee and refer the matter to the Human Resources Department for the appropriate action.

**ES Response**

Human Resource personnel at the Region and Washington office levels are currently reviewing the actions of the R-5 employees. The complete record will be reviewed and any appropriate action taken by October 1, 2000. While this matter is under review, both individuals have been given details to other duties.

### **OIG Position**

We accept management decision on this recommendation.

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### **RECOMMENDATION NO. 6**

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In future land exchanges, ensure that any concessionaire operation proposed for FS lands meets the forest's long-range management plan, satisfies a public need, and has concurrence from appropriate FS groups and upper management.

### **FS Response**

This is existing Forest Service policy and it was not violated by the LTBMU in this transaction. In the Forest Service letter of June 30, 1997, to Olympic Group, the Forest Supervisor states, "The Park Cattle Company is not currently an operating permittee and therefore must go through the Forest Service's permittee approval process. This could take several months and will require in-depth financial information. Once this process is complete, Park Cattle Company must understand there is no guarantee of being able to operate."

Further guidance was given to the Regional Foresters in a letter dated October 14, 1999, which states "The competitive land exchanges need to be given major consideration when land exchanges involve Federal properties that are atypical, influenced by escalating markets, or that have broad market appeal and interest...In all cases where structural improvements are being acquired, the Feasibility Analysis (FA) and Agreement to Initiate should document the type and size of the structure(s). The FA needs to also document the purpose of acquiring the structure(s) and how their acquisition would aid in achieving the goals and objectives of the Forest Land and Resource Management Plan. The Decision Document approving acquisition of any structure(s) needs to document how the acquisition serves the public's interest and disclose the disposition of said structure(s) and the funding source for future maintenance costs and/or disposition costs; i.e. sale or demolition (letter enclosed)." The above excerpts taken from the enclosed letter will be included where appropriate in the Forest Service Manuals and Handbooks by July 31, 2001.

### **OIG Position**

We accept management decision on this recommendation.

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### **RECOMMENDATION NO. 7**

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Direct FS staff to communicate directly to all parties involved in FS land adjustments rather than relying on proponents and/or facilitators to convey the necessary information to third

parties.

### **ES Response**

Forest Service policy concerning the use of third party facilitators in land ownership adjustments is clearly stated in a letter dated October 15, 1998, to Regional Foresters from the Deputy Chief of the NFS, and in the draft FSH 5409.13 – Land Acquisition Handbook.

The Region's Lands Officers, RO Lands Staff and Zone Landownership Adjustment Teams will receive training on the draft Land Acquisition Handbook FSH 5409.13 on June 28-30, 2000, by the National Lands Oversight Team. Continual monitoring will occur during subsequent National Team Review of proposed and pending land exchange proposals.

### **OIG Position**

We accept management decision on this recommendation.

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**FINDING NO. 3**

**ZEPHYR COVE APPRAISALS  
OVERSTATED THE LAND'S  
VALUE BY AS MUCH AS \$20  
MILLION**

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A FS appraiser approved values for the Zephyr Cove land exchange that were based on speculative events and that did not reflect the property actually acquired by the USA. In performing his review, the FS appraiser did not comply with FS policy and appraisal standards and did not exercise due professional care. As a result, the value of the Zephyr Cove land acquired by the public was overstated by as

much as \$20 million.

The Uniform Appraisal Standards for Federal Land Acquisitions (UASFLA) were prepared to promote uniformity in the appraisal of lands being acquired by the United States. Appraisers must comply with these standards when valuing lands involved in a Federal land exchange. UASFLA states that it is the review appraiser's responsibility to ensure that the appraisal under review is adequately supported, complies with recognized appraisal standards, and conforms to governing legal premises. In addition, FS Appraisal Handbook 5409.12 (7.31) directs the FS review appraiser to approve an appraisal only if it is prepared to existing standards.

Olympic group optioned the entire 47.2-acre Zephyr Cove property, including the lakefront mansion, for \$28 million in the fall of 1995. Within a year, Olympic's appraiser had valued this same property, in two parcels and without the mansion, at \$38 million. We estimate that the actual value of the Zephyr Cove property, as it was conveyed to the United States, with third-party occupancy of the improvements, may only have been \$18 million.

	Per OIG	Per appraiser
Purchase price of land and improvements	\$28 million	
Appraised value of Phase 1; 35.4 acres of unimproved land. Speculative event: subdivided lots. Ignored presence of exclusive easement		\$24¼million
Appraised Value of Phase 2; remaining 11.8 acres: Violation of Federal Law: Ignored presence of privately owned improvements Ignored presence of exclusive easement		\$13½million
Loss of value through outstanding ownership interest and 3 <sup>rd</sup> party occupancy:	- \$10 million	0
<b>TOTALS</b>	<b>\$18 million</b>	<b>\$38 million</b>
<b>Difference</b>		<b>\$20 million</b>

A FS appraiser reviewed and approved Olympic's appraisal of the Phase 1 parcel of Zephyr Cove before he was aware that Olympic also planned to exchange the Phase 2 parcel to the FS. He subsequently reviewed and approved Olympic's appraisal of the Phase 2 parcel. We concluded that three flaws in Olympic's appraisals overstated the value of the Zephyr Cove land and obligated the FS appraiser to require a revaluation. Specifically—

- appraisal values of both phases of land were based on the assumption that the land was fully developable, even though such development was impeded by alleged private ownership and the presence of exclusive, perpetual easements,
- appraisal values of Phase 1 were based on an assumption that the land could be subdivided, even though there was a strong risk that zoning authorities would not allow the presumed subdivision, and
- appraisal values of Phase 2 valued the land as a separate tract, creating an artificial division of Zephyr Cove into two parcels, an unacceptable practice in FS land exchanges.

**Appraisal Values Did Not Take Privately Owned Improvements and Exclusive Easements into Account**

As noted in Finding No. 2, the appraisal of Zephyr Cove, Phase 2, did not include an improvement reservation, required under Federal regulations, which would have legally reserved Olympic's right to continue to own and use the improvements. Instead, the \$13½million appraisal valued the land as though it were free of all encumbrances, with no reservations or outstanding interests. The FS appraiser approved this value even though it did not

comply with Federal law, did not reflect the property actually being conveyed to the USA, and overstated the land's value by as much as \$10 million.

Valuation Ignored Private Ownership Interest: The \$13½million value assigned to Phase 2 of the Zephyr Cove land exchange was based on the assumption that the existing improvements, a lakefront estate and caretaker's cottage, would be removed from the land. Consequently, Olympic's appraiser valued the parcel as though it was vacant, with full development rights and land coverage available for future development. However, after this appraisal was completed, LTBMU staff, BLM management and Olympic decided the improvements would remain on the land, and in the private ownership of Olympic.

This decision changed the nature of the property being conveyed to the FS, and invalidated the original appraised value of \$13½million. Under UASFLA and FS appraisal procedures, the FS appraiser was required to reject the appraised value and request, in writing, a new description of the property being conveyed; 11.8 acres of land encumbered by privately owned improvements. The FS appraiser was then required to order a new valuation that represented the property actually being acquired by the USA.

Further, it was the FS appraiser's responsibility to ensure that the new appraisal complied with Federal law. Under Federal regulations, Olympic was required to reserve its ownership of the Zephyr Cove improvements through a reservation, subject to specific terms and conditions cited in Title 36 CFR 251. The use of the CFR reservation was a mandatory requirement and would have significantly reduced the fair market value of the Zephyr Cove land being transferred to the FS. According to appraisal estimates, Olympic's reserved use of 6 acres of FS land surrounding the improvements (considered the minimum needed for private ownership) would have reduced the fair market value of the Phase 2 lands by \$8½million to \$10 million.<sup>6</sup> Reservation of a greater area would have reduced the appraised value even further.

The FS appraiser did not reject the \$13½million value, and he did not require a new appraisal. Instead, the FS appraiser approved the Phase 2 value even though he knew

- Olympic had not reserved ownership of the improvements through the required CFR reservation,

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<sup>6</sup> The minimum size of the reserved area and its approximate value are based on a preliminary appraisal estimate performed by a private appraiser in the Lake Tahoe Basin, and do not represent official FS determinations.

- Olympic purportedly intended to retain private ownership of the improvements through some alternate means and sell the improvements to a private party after the land exchange closed, and
- the appraised value of the Phase 2 lands had not been reduced to reflect the encumbrance of privately owned improvements on the land being transferred to the USA.

The FS appraiser told us that he did not think about the CFR reservation requirement when he reviewed the Phase 2 appraisal. He said that the LTBMU employee told him the improvements would be used by a concessionaire under a special-use permit. The FS appraiser added that he did not think the CFR reservation was required because the private use of the improvements on FS land would be authorized by the special-use permit.

We contacted an expert in Federal appraisal standards at the Department of Justice, OGC counsel, and the Washington Office (WO) chief appraiser, who all stated that the CFR reservation was the only legal way for Olympic to retain ownership of the Zephyr Cove improvements when it transferred the land to the USA. The WO chief appraiser told us that the Phase 2 value of \$13½million was specifically predicated on the assumption that the land was free of encumbrances and could be developed. He explained that any private ownership of the improvements encumbered the land and reduced its real fair market value. Private ownership of the improvements without the appropriate price reduction would overstate the fair market value of the land.

Because of the FS appraiser's actions, the public overpaid for a parcel of land that is now encumbered by a lakefront residence that Park Cattle Company claims to own. The value of the land as it was actually conveyed to the USA--encumbered by alleged private ownership and with no development potential--was overstated by as much as \$10 million.

Valuation Ignored Exclusive, Perpetual Easement: The Zephyr Cove property conveyed to the Government also contained an exclusive, perpetual easement that was not reflected in the Phase 1 and Phase 2 values approved by the FS appraiser.

FSH 5409.12 (1.31) (August 1992) directs appraisers to review the property's title and consider all reservations, outstanding rights and other factors that limit or restrict full use of the property. The Handbook states that the appraised interest must agree **exactly** with the interests described in the deed used to convey the land to the USA. FSH 5409.12 (7.11) (August 1992) states that, before approving an appraisal report, the review appraiser must ensure that the estate appraised and the legal description used in the appraisal are identical to the property rights acquired by the Government in the acquisition or exchange.

The Phase 1 and Phase 2 appraisals stated that the Zephyr Cove property was free from any easements or restrictions that would interfere with the land's future use or impact its appraised value. However, the deeds used to convey the Phase 1 and Phase 2 property to the USA described a 40-foot wide "exclusive and perpetual" access easement that began at the property's main gate, bisected the Zephyr Cove property, and terminated at the entrance to the lakefront estate. (See chapter 2 for additional discussion on the easement.)

This type of access easement violated FS policy and significantly impacted the public's use of the land. The nature of an exclusive easement prohibits any other party from using the easement or the land under it. Currently, Park Cattle Company, which has constructively possessed the Zephyr Cove improvements, is enforcing the exclusive easement, now on FS land. Consequently, the public is stopped from walking upon the reserved driveway that bisects the two Zephyr Cove parcels acquired, and must walk up to the highway in order to travel from one end of the Zephyr Cove property to the other.

It was the FS appraiser's responsibility to review the deeds used to convey the property to the Government before he approved the values, and to ensure that those deeds agreed exactly with the property as it was appraised. The FS appraiser did not do this. He did not obtain or review the conveying deeds used for Phase 1 or Phase 2 of the land exchange. He also did not ask LTBMU or BLM staff how the improvements, which he thought were going to be privately owned, would be accessed by the owner, or the nature of that access. Consequently, when the FS appraiser approved the appraised values, he had no assurance that the land, as appraised, was the same as the land that would be conveyed to the USA.

The presence of an exclusive, perpetual easement on the Zephyr Cove property affected the land's fair market value and should have reduced the Phase 1 and Phase 2 appraised values. If the FS appraiser had performed the required review, the presence of the exclusive easement would have been noted before the values had been approved. The appraised values could then have been adjusted downward to reflect this encumbrance, or even removed as unacceptable to the FS and the public.

**Phase 1 Appraisal Values Did Not Reflect the Risk that Subdivision of the Land Might Be Denied**

The FS appraiser approved a value for Phase 1 of the Zephyr Cove land exchange that relied on a series of speculative events and unsupported assumptions. We estimate that the FS appraiser's reliance on these events

may have overstated the actual value of the Phase 1 land by several million dollars.

UASFLA allows landowners fair market value for their property, but does not allow that value to be based on potential uses that are speculative and conjectural. In addition, UASFLA states that it is not appropriate for an appraiser to value property under the *assumption* that the land can be rezoned.

The appraisal of Phase 1 of the Zephyr Cove land exchange valued a 35.4-acre portion of the Zephyr Cove property at \$24¼million. At the time of the valuation, Tahoe Regional Planning Agency (TRPA) recognized the Zephyr Cove property as a single parcel. However, the appraisal assumed that TRPA would allow the Zephyr Cove land to be subdivided into five individual lakefront estates. To support this assumption, Olympic's appraiser relied on a letter issued by TRPA that stated it would be legally possible to subdivide the Zephyr Cove parcel into five separate ownership holdings. However, nine prerequisite conditions had to be met. These conditions included changing the property's current zoning, extending an urban boundary, and maintaining environmental thresholds.

According to the FS appraiser, the conditions cited in the TRPA letter seemed to be routine procedures or typical processing steps. He told us that, to him, none of the conditions seemed difficult to accomplish. The FS appraiser said he consulted with Olympic's appraiser, who told him the TRPA requirements could be easily achieved. The FS appraiser also met with TRPA staff and had the feeling that TRPA would approve the Zephyr Cove subdivision into five individual lakefront lots. Based on the opinion expressed by Olympic's appraiser, and his impression of the TRPA meeting, the FS appraiser concluded that TRPA approval of the project was certain, with no chance of denial. Based on this assumption, the FS appraiser approved the \$24¼million value for Phase 1.

The FS appraiser's assumption that the subdivision would be approved by TRPA, with no chance of denial, was speculative and unsupported. In our discussions with TRPA officials, we determined that TRPA would not have approved the subdivision as assumed by the FS appraiser. TRPA officials told us that it would have been difficult, if not impossible, for the landowner to meet all nine necessary conditions. They said that at the time the TRPA letter was created, no one had ever tried to expand an urban boundary in Lake Tahoe; consequently, the possibility of doing so successfully was completely unknown at the time. They added that another project, submitted to the TRPA board after the Zephyr Cove land exchange was completed, had requested expansion of an urban boundary and had been denied.

The FS appraiser's approval of the \$24¼million value was not based on credible evidence and overstated the value of the Phase 1 parcel. Although the property appeared to have some development potential, there was a strong risk that the subdivision project would have been denied. The FS appraiser did not analyze the risks involved in the hypothetical subdivision and determine its impact on the appraised value. An adequate analysis of risk would have reduced the value, perhaps significantly. Although the effect of the speculative assumption cannot be quantified without another appraisal, it is reasonable to conclude that the FS appraiser's reliance on unsupported assumptions may have overstated the value of the Phase 1 land by several million dollars.

### **Artificial Division of the Zephyr Cove Land Increased the Phase 2 Value**

The FS appraiser allowed the Zephyr Cove property to be appraised as two separate transactions, rather than as a single piece of property. This procedure artificially subdivided the Zephyr Cove land and significantly enhanced the appraised value of the Phase 2 parcel. We estimate that allowing the Zephyr Cove property to be appraised as two separate transactions may have overstated the value of the Phase 2 parcel by as much as \$8.7 million.

The USA acquired the 47.2-acre Zephyr Cove property in two separate phases. As noted, FS appraisal procedures and UASFLA require contiguous parcels of land under the same ownership to be appraised as a single transaction, if possible. This policy prevents a landowner from artificially increasing the value of a single parcel of land by conveying portions of it to the Government, one piece at a time.

In Finding No. 2, we noted that the FS appraiser stated that when he approved the Phase 1 value, he did not know that additional Zephyr Cove acreage was going to be transferred to the FS in Phase 2 of Olympic's land exchange with BLM. The FS appraiser stated that, because the Phase 1 value had already been approved when he learned of the additional Phase 2 acreage, he had no choice but to value the remaining 11.8-acre parcel as a separate transaction.

We determined that the FS appraiser's statement was incorrect. Under FS policy, the FS appraiser could have elected to appraise the entire Zephyr Cove property as one unit, even though Phase 1 of the land exchange had already been completed. When he learned about the Phase 2 acreage, the FS appraiser could have directed Olympic's appraiser to revalue the entire 47.2-acre parcel. He then could have estimated the contributory value of the Phase 2 acreage as the difference between the appraised value of the entire property less the amount already paid to Olympic in Phase 1.

We estimate that the FS appraiser's acceptance of the Phase 2 valuation as a separate piece of land overstated the total value of the Zephyr Cove property by as much as \$8.7 million. The inflated values are shown in the lake frontage measurements,<sup>7</sup> as follows.

- Olympic purchased the entire Zephyr Cove property in July 1996 for \$28 million. The price was about \$6,600 per lineal foot of lake frontage.
- The USA acquired the Phase 1 acreage in October 1996 at a cost of \$24¼million. This price was about \$6,840 per lineal foot of lake frontage, representing a 4-percent increase in a 3-month period.
- The USA acquired the Phase 2 acreage in April 1997 at a cost of \$13½ million. This price was about \$19,369 per lineal foot of lake frontage, representing a 194-percent increase in a 9-month period.

Acquiring the Phase 2 portion of the Zephyr Cove land as a separate piece of lakefront property significantly increased the value of the remaining acreage. If we multiply the amount of lake frontage acquired in Phase 2 (697 linear feet) by the cost difference between the two phases (\$19,369/foot of Phase 2 lake frontage less \$6,840/foot of Phase 1 lake frontage), the estimated increase to Phase 2's value by the artificial subdivision was as much as \$8.7 million.

In our opinion, once the FS appraiser learned that Olympic intended to transfer the remaining Zephyr Cove acreage to the USA, he should have required Olympic's appraiser to re-value the entire Zephyr Cove property as a single parcel. Although FS procedures did not *require* the FS appraiser to take this approach, it would have been prudent to do so and it would have protected the public's interest in the Zephyr Cove land exchange.

The FS appraiser did not exercise due care in his review and approval of the Zephyr Cove values. He did not ensure that the valuation premises complied with Federal law and FS procedures and that the fair market value paid by the public corresponded to the actual property acquired by the USA. He also relied on verbal representations and uninformed assumptions to support the probability of speculative events, rather than actual documentation and analysis. As a result of his actions, the \$38-million value of the Zephyr Cove property may have been overstated by as much as \$20 million.

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<sup>7</sup> Lakefront lineal footage is a principal basis for determining value of land at Lake Tahoe, and was used by both Olympic's appraiser and the FS appraiser.

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**RECOMMENDATION NO. 8**

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Conduct a peer review of the Zephyr Cove appraisals and the actions taken by the FS appraiser. Take any corrective actions recommended by the peer review.

**ES Response**

A peer review of the Zephyr Cove appraisals is currently underway and will be completed by August 1, 2000. The conclusions and recommendations of this review will be provided to the Deputy Chief and WO Director of Lands and any appropriate corrective actions will be initiated by October 1, 2000.

**OIG Position**

We accept management decision on this recommendation.

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**RECOMMENDATION NO. 9**

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Ensure that review appraisers understand and comply with Federal appraisal standards and FS appraisal procedures.

**ES Response**

Policy direction will be provided to the Agency appraisal organization by the Chief Appraiser and WO Director of Lands so as to avoid repetition of these deficient actions prior to January 1, 2001.

A training course has been developed, offered, and is mandatory for all Forest Service staff appraisers. This course deals with transitional properties and appropriate documentation and analysis methods to support values based on potential development. Continual monitoring and oversight will occur through scheduled compliance reviews by the Chief Appraiser and WO Director of Lands.

**OIG Position**

We accept management decision on this recommendation.

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**RECOMMENDATION NO. 10**

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Ensure that any appraisals based on potential actions (e.g. presumed TRPA or FS approvals) are supported by documentation obtained directly from the approving agency.

### **ES Response**

All appraisals based on property zoning or use limitations that are not currently in effect shall be documented not only with local zoning authorities, but also by verification that similar use has been authorized for other similarly situated private property. This market-based verification shall be mandatory in all cases where the assumed zoning for appraisal purposes is different than the actual zoning in effect on the date of value. This is particularly critical as part of the development process for high profile, controversial, and/or complex property appraisals. It is essential that the review appraiser understand the need for a high level of clarity and support for value conclusions in these kinds of actions. Although this requirement is already in effect (see FSH 5409.12-1.33d) as it applies to Federal lands that are being appraised as part of Agency exchange actions, this needs to be further expanded to include valuation of transitional non-Federal properties. This requirement will be underscored in future policy and procedure updates, at the annual appraisers meeting to be held during the week of October 18, 2000, and emphasized in subsequent regional compliance reviews by the Chief Appraiser and WO Director of Lands.

### **OIG Position**

We accept management decision on this recommendation.

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### **RECOMMENDATION NO. 11**

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Reiterate to FS staff and appraisers that improvements remaining on land being transferred to the FS must comply with the provisions of Title 36 CFR 251, and that the reservation may affect the appraised value.

### **ES Response**

Current regulatory requirements provide for a mandatory reservation for structural improvements that are to be retained by the grantor in transactions such as this. The LTBMU employee and FS appraiser should have been aware of this requirement. It is inappropriate to accept title, nor can an appraisal be accepted based on an assumption that a special use permit, authorizing some form of occupancy, is forthcoming subsequent to closure. Special use permits are discretionary actions that require NEPA analysis and conclusions, and are subject to appeal in and of their own right.

Improvements remaining on land being transferred to the Forest Service must comply with the provisions of Title 36 CFR 251.17, and the reservation must be analyzed, as it might affect the estimate of value. This requirement will be highlighted in the draft FSH 5409.13 on Land Exchanges, and

emphasized during upcoming required Handbook training sessions by the National Lands Oversight Team.

**OIG Position**

We accept management decision on this recommendation.

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**FINDING NO. 4**

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The FS has not resolved important legal issues that adversely affect its ability to fully control and manage the Zephyr Cove lands. Because of the improper actions by FS personnel, the FS' ownership of the \$38-million lakefront property is encumbered by the presence of Park Cattle Company. In conjunction with OGC, the FS needs to identify and account for the property rights acquired by the USA, and assess any further legal action or other remedy necessary to preserve FS jurisdiction of the public land and to accomplish the original objectives of the Zephyr Cove land exchange. The FS should first obtain a title opinion from OGC and, on the basis of that opinion, act to resolve the unauthorized occupancy of Zephyr Cove by Park Cattle.

To date, the OGC has not issued a final title opinion on Zephyr Cove. Our audit identified several key areas that need to be covered by the OGC opinion, such as ownership interest of improvements, access easements, water rights, and development rights. Park Cattle has occupied the Zephyr Cove improvements and surrounding FS land since July 1997, without FS authorization and without payment of any fees. It is crucial that a final title opinion, specifying the rights acquired by each party asserting claims to the Zephyr Cove improvements, be completed as soon as possible. The FS also needs to take action to collect a fee for the period of Park Cattle's adverse occupancy.

Forest Service Handbook (FSH) 5409.13 requires OGC to review the evidence of title with related documents and issue a final title opinion. The Handbook states that OGC shall review the title evidence and determine if the title to the non-Federal land is acceptable to the USA. If it is not, OGC will take appropriate action to correct deficiencies, using FS personnel as needed to obtain the data that will support the corrections.

FSH 2709.11(30) states that unauthorized occupancy occurs if an entity uses NFS lands without authorization. Issuance of FS authorization after the unauthorized occupancy has occurred does not authorize the use of NFS lands that took place prior to the authorization date and thus does not cancel or settle the prior occupancy. FS staffs are directed to bill the entity for an amount equal to the fair market value of the NFS lands affected for the entire period of the occupancy.

Because of the improper actions by LTBMU staff (see Finding No. 2), the Zephyr Cove property conveyed to the FS is now significantly encumbered

by the unauthorized presence of Park Cattle Company, which claims ownership rights to the Zephyr Cove lakefront mansion, caretaker's house, main gate and driveway leading to the lakefront estate. Park Cattle has denied the public access to the Zephyr Cove property through the main gate and has prohibited public use of the driveway bisecting the Zephyr Cove parcel. Park Cattle has also restricted public use of several acres of land surrounding the Zephyr Cove improvements, including two sandy beaches, by installing erroneous private property signs, by directing the public away from the beaches with trail markers, and by employing a resident caretaker who physically confronts anyone approaching the improvements and the beaches. In essence, Park Cattle has exerted control over a portion of prime lakefront land acquired in Phase 2 of the Zephyr Cove land exchange at a value of \$13½million.

The FS must resolve Park Cattle's unauthorized occupancy of Zephyr Cove by asserting its rights to the improvements, if so stipulated in the title opinion. If the title opinion stipulates otherwise, the FS should resolve the occupancy through the most effective means at its disposal. One such means is to remove Park Cattle from the land through a Declaration of Taking. Under a Declaration of Taking, the FS would offer Park Cattle the fair market value of whatever interest it may have in the Zephyr Cove improvements and, if Park Cattle refuses the offer, initiate condemnation proceedings against Park Cattle and declare a mandatory acquisition of the Zephyr Cove improvements in the public's interest.

We concluded that it would be in the best interest of the FS as well as the public at large if OGC's research into the title of the Zephyr Cove property included an evaluation of all aspects of the Zephyr Cove land exchange transaction.

### **The FS Needs To Obtain a Final Title Opinion From OGC and Identify Property Rights Acquired in the Zephyr Cove Land Exchange**

The unresolved legal issues associated with Phase 2 of the Zephyr Cove land exchange adversely affect the ability of the FS to manage the land and reduce FS effectiveness in any future negotiations with Park Cattle. RO staff needs to obtain a final title opinion from OGC that identifies ownership of the improvements, water rights, development rights, and exclusive access easement on the Zephyr Cove land.

#### **a. Ownership of the Zephyr Cove Improvements**

In an opinion dated April 8, 1998, OGC stated that ownership of the Zephyr Cove improvements passed to the FS on April 25, 1997, the date Olympic Group, Inc., conveyed the Zephyr Cove property to the USA in exchange for \$13½million worth of BLM lands. However, ownership of the

improvements was encumbered when the LTBMU employee attempted, in June 1997, to retroactively reserve Olympic's ownership of the improvements by inserting a reservation into the deed after the land exchange was completed. (See Finding No. 2.) The legal ownership of the improvements was further confused when the LTBMU forest supervisor allowed Olympic to sell the Government-owned improvements to Park Cattle Company on July 2, 1997.

In response to a request from OGC, the Department of Justice (DOJ) examined copies of the Zephyr Cove deeds and other documentation provided by the FS. DOJ determined that, based on the documentation provided and depending on the facts of the case, Park Cattle may have a stronger claim on the Zephyr Cove improvements than the USA, or in fact a very weak claim. According to DOJ, if it is the case that Olympic and the LTBMU had simply forgotten to put the improvement reservation into the original Zephyr Cove deed when the land was transferred to the FS, then the land staff officer's belated attempt to add an improvement reservation was an effort to correct a simple mistake. However, if it is the case that the CFR reservation was deliberately omitted, then the belated addition could have been an attempt by Olympic and the LTBMU employee to "change the terms of their completed deal in the absence of Federal authority to do so."

DOJ recommended a careful review of the Zephyr Cove land exchange documents and the circumstances surrounding the execution of the deeds. From our conversations with the LTBMU employee (see Finding No. 2), we determined that the improvement reservation was deliberately omitted from the original Zephyr Cove deed, and was not a simple mistake. Furthermore, Nevada taxing officials stated that they do not consider Park Cattle the owners of the Zephyr Cove improvements. Owners of improvements are subject to a possessory interest tax, but the taxing officials said they would not levy the tax on Park Cattle unless the FS, whom they consider the owner of the mansion, grants Park Cattle an authorization to use it.

FS and OGC legal staffs should consider this and all other information relevant to the Zephyr Cove land exchange and determine if it is not the case that the USA has a stronger claim to the Zephyr Cove improvements than Park Cattle. Since the title status of the improvements is a key element to any future negotiations with Park Cattle, a legal resolution to this matter needs to be completed.

b. Ownership of the Zephyr Cove Water Rights

According to the Nevada Water Engineer, the Zephyr Cove property had approximately 73 acre-feet of water rights when it was purchased by the

USA for \$38 million. In the State of Nevada, all water rights associated with a parcel of land are automatically attached to the land and remain with the land when it is sold. The only exceptions to this general rule occur when water rights are specifically identified and transferred off the land via a quitclaim deed or are reserved in a conveyance of title. The USA paid for the Zephyr Cove water rights when it acquired the land. Our review of the land exchange documents showed that Olympic did not reserve or sever the water rights from the Zephyr Cove land prior to transferring the title to the FS. It is our determination that the USA owns all water rights associated with the Zephyr Cove property.

Currently, Park Cattle is using the Zephyr Cove water rights to support the presence of its caretaker and to maintain the landscaping around the Zephyr Cove improvements. Park Cattle also intends to use the Zephyr Cove water rights for any future residential or commercial development of the improvements it allegedly owns. Park Cattle has used the Zephyr Cove water rights for almost 3 years without FS authorization and without compensating the public for that use. If the FS owns the water rights, as we contend, Park Cattle should cease its unauthorized consumption of that resource and reimburse the public for its use over the last 3 years.

Further, if Park Cattle's claims to the Zephyr Cove improvements prevail, it will have to acquire new water rights, since the existing water rights are owned by the USA. According to Nevada State water engineers, the Lake Tahoe Basin is a fully appropriated site (all available water rights are being used). This means that Park Cattle will have to purchase new water rights on the open market from a willing seller. In May 1998, the Thunderbird land exchange proponent purchased 6 acre-feet of water rights in the Lake Tahoe Basin for about \$9,000 to \$11,000 per acre-foot. Because the price of water rights is negotiated between each buyer and seller, the cost to acquire other water rights in the Lake Tahoe Basin could be more or less.

The FS needs to confirm the amount of the Zephyr Cove waters rights with the Nevada Water Engineer. The FS also needs to assert its ownership rights to the Zephyr Cove water by reporting a "change of conveyance" with the Nevada State Division of Water Resources. In addition, any future negotiation between Park Cattle and the FS should ensure that the public is fairly compensated for any water rights used by or transferred to Park Cattle.

c. Ownership of the Zephyr Cove Development Rights and Coverage

The \$13½million appraised value for Zephyr Cove Phase 2 assumed that the Zephyr Cove land was vacant and could be developed with one or two luxury lakefront home sites. The value ignored the fact that the existing

Zephyr Cove improvements used both development rights and a portion of the land coverage. (See Finding No. 3.) Consequently, the public paid for and owns all development rights and land coverage associated with the Phase 2 parcel.

Development rights and land coverage are valuable assets in the Lake Tahoe Basin because they are required by TRPA regulations in order for new construction to begin or for existing structures to remain on land in the Basin. As such, these assets are sold on the open market, being detached from and transferred to parcels in the area. If the FS determines that Park Cattle has ownership rights to the Zephyr Cove improvements, the FS must ensure that the public is adequately compensated for the improvement's use of the two development rights and portion of land coverage. Park Cattle did not pay for those assets and should not have the right to use them without compensating the public.

d. Ownership of the Exclusive Access Easement

Park Cattle alleges that it has ownership rights to a perpetual, exclusive access easement (i.e., road right-of-way) extending across the FS land to the Zephyr Cove improvements. It has also assumed control of the property's main entrance gate. We discussed this issue with OGC who stated that, in their preliminary review of the Zephyr Cove deeds, it appeared that Park Cattle had no rights to any easement across the FS land or to the property's main gates. OGC explained that Olympic attempted to reserve an exclusive, perpetual easement in the Zephyr Cove deeds but actually transferred the easement to the FS when the land was conveyed to the USA. In addition, Olympic never legally reserved any ownership rights to the property's main gates. However, OGC stated that Park Cattle could challenge the status of the easement and petition the court for the right to access the improvements it allegedly owns.

The FS needs to determine whether Park Cattle has acquired any right to exclusive access across the FS land or to control the property's main entrance gates. If Park Cattle has no such rights, the FS should ensure that Park Cattle immediately relinquishes its control over the property's main gate and the driveway leading to the improvements.

It is crucial that a final title opinion, specifying the property rights acquired by each party asserting claims to the Zephyr Cove lands, be completed as soon as possible. This opinion would resolve the current conflict between Park Cattle and the FS and be the basis for any future negotiations between the two parties.

**FS Staff Needs to Resolve Park Cattle's Unauthorized, Payment-Free Use of the FS Lands at Zephyr Cove.**

Park Cattle has occupied the Zephyr Cove improvements and surrounding property since April 1997, without FS authorization and without payment of any fees. RO management estimates that the USA is owed about \$450,000 per year for Park Cattle's exclusive use of approximately 6 acres of public land. The fee estimate is based on a land value of \$9 million and a minimum land rental rate of 5 percent of market value.

In March 1998, the RO staff met with representatives of Park Cattle to discuss Park Cattle's alleged ownership of the Zephyr Cove improvements. The Park Cattle representatives told RO staff that Park Cattle could not profitably operate the Zephyr Cove improvements if it had to pay a fee based on the land's fair market value.

To date, no special-use permit has been granted to Park Cattle. Without such authorization, Park Cattle has no right to keep the Zephyr Cove improvements on public land and is obligated to remove them at its own expense. However, Park Cattle has not removed the improvements and continues to make exclusive use of approximately 6 acres of public land surrounding the buildings. According to FS management, Park Cattle's installation of a caretaker has also indirectly discouraged the public's use of the entire 47.2-acre parcel. The FS has calculated that Park Cattle owes the FS and the public approximately \$1.35 million for its unauthorized occupancy of 6 acres of FS land for a period of 3 years.<sup>8</sup>

The FS regional staff has started negotiations with Park Cattle to resolve its unauthorized use of the FS lands at Zephyr Cove. We believe that the above issues need to be immediately addressed by the FS in order to determine what property rights may be legitimately claimed by Park Cattle and to ensure that the public is fairly represented in any negotiation process between Park Cattle and the FS.

As one possible way of resolving Park Cattle's unauthorized occupancy of this pristine National Forest lakefront land, and of protecting the general public's interest in this "once in a lifetime" recreational opportunity, the FS could determine the fair market value of the interest, if any, Park Cattle may have in the Zephyr Cove improvements, and offer to purchase the improvements from Park Cattle at that price. The determination of fair market value should occur after the FS has obtained a final title opinion, and should be based on the value of the improvements as allegedly purchased by

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<sup>8</sup> The estimated size of the unauthorized use and the resultant fee are based on preliminary FS estimates and do not represent an official FS determination.

Park Cattle: with no development rights, no land coverage, no water rights and no right to occupy the FS lands on which the improvements reside.

If these negotiations fail, and Park Cattle refuses to sell the improvements to the FS at a fair price, the FS may, as one of the legal options for title resolution, pursue condemnation proceedings and declare a taking of the Zephyr Cove improvements, as authorized by the Condemnation Act of 1888 and the Declaration of Taking Act of 1931.<sup>9</sup> These acquisition authorities are the basis for FSH 5409.13 (71.51), which allows the FS to initiate a condemnation case when mandatory acquisition of real property (such as the improvements) from an unwilling seller serves an important public purpose and protects a valuable National Forest resource. The FS, in consultation with OGC, should investigate such legal action as a way to resolve Park Cattle's unauthorized occupancy of the Zephyr Cove improvements and surrounding FS land.

It is in the public's interest for the FS to achieve the opportunities it expected from the Zephyr Cove land exchange. Once a final title opinion is issued, the FS should resolve Park Cattle's unauthorized occupancy of Zephyr Cove. The FS should assert its rights to the improvements, if so stipulated in the title opinion, or it should resolve Park's unauthorized occupancy of Zephyr Cove through legal means available to it that serve the general public's best interest.

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**RECOMMENDATION NO. 12**

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Consult with OGC to determine what title documents are needed for a final title opinion. Provide the documents to OGC within 60 days.

**FS Response**

The Region, through the Central Zone Land Adjustment Team, is working with OGC to make sure all necessary documents related to water rights, the well, development and coverage rights, etc. are acquired so that a final title opinion can be prepared. The final title opinion will be issued by September 1, 2000.

**OIG Position**

We accept management decision on this recommendation.

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**RECOMMENDATION NO. 13**

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Obtain a final title opinion from OGC which focuses on all aspects of the Zephyr Cove land exchange transaction, including the nonpayment

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<sup>9</sup> See chapter 782, 25 Stat. 357, as amended; 40 U.S.C. 257 for the Condemnation Act, and Public Law 71-736, chapter 307, 46 Stat. 1421; 40 U.S.C. 258a for the Declaration of Taking Act.

of possessory interest tax and the title to (1) improvements, (2) exclusive easements, (3) water rights and (4) development rights and coverage. Consult with OGC on legal actions necessary to preserve the USA's property rights, including determining the nature and quantity of water rights associated with the Zephyr Cove property, and reporting a "change of conveyance" with the Nevada State Division of Water Resources.

**ES Response**

A review of these complex title matters is underway by the Region and OGC. A final opinion will be issued by OGC addressing these and any other relevant title or occupancy issues by September 1, 2000. This will also include the identification of any further actions that need to be taken by the Region to protect any property interests or rights of the United States.

**OIG Position**

We accept management decision on this recommendation.

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**RECOMMENDATION NO. 14**

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In consultation with OGC, take action to collect rental fees owed the FS from Park Cattle for the period of its unauthorized occupancy.

**ES Response**

The fair market rental fee for the occupancy will need to be predicated on an approved appraisal of the land encumbered since 1997. This will be completed by September 1, 2000 and, in consultation with the WO Director of Lands and OGC, the Regional Forester will initiate action to collect the appropriate rental.

**OIG Position**

We accept management decision on this recommendation.

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**RECOMMENDATION NO. 15**

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Initiate legal action, such as a declaration of taking, to resolve Park Cattle's unauthorized occupancy of FS lands.

**ES Response**

Once the title and ownership matters are defined by OGC, the Regional Forester and Director of Lands, in consultation with the WO Director of Lands and OGC, will initiate appropriate action to resolve the ownership and

occupancy issues. The timeline for this action to be initiated is by January 1, 2001.

**OIG Position**

We accept management decision on this recommendation.

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**EXHIBIT A – SUMMARY OF MONETARY RESULTS**

<b>RECOMMENDATION NUMBER</b>	<b>DESCRIPTION</b>	<b>AMOUNT</b>	<b>CATEGORY</b>
9	Estimated value overstated by artificial subdivision of the land.	\$8,700,000	FTBPTBU – Management Or Operating Improvement / Savings
11	Estimated value overstated by lack of CFR reservation in deed conveying land to FS. <sup>10</sup>	\$10,000,000	FTBPTBU – Management Or Operating Improvement / Savings
14	Estimated fee due FS for use of public land. <sup>11</sup>	\$1,350,000	Questioned Costs – Recovery Recommended
<b>TOTAL</b>		<b>\$20,050,000</b>	

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<sup>10</sup> This value is based on preliminary appraisal estimates performed by a private appraiser in the Lake Tahoe Basin, and does not represent official FS determinations.

<sup>11</sup> The estimated fee due is based on preliminary FS estimates. The actual fee will be determined after OGC's final title opinion on the estate conveyed to the FS.

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**EXHIBIT B – LOCATIONS VISITED OR CONTACTED**

ORGANIZATION/ENTITY	LOCATION
Forest Service Pacific Southwest Regional Office (Region 5)	Vallejo, California
Central Zone Landownership Adjustment Team (Region 5)	Placerville, California
Lake Tahoe Basin Management Unit	South Lake Tahoe, California
Office of the General Counsel Regional Office	San Francisco, California
U.S. Department of Interior:	
Bureau of Land Management State Office District Office	Reno, Nevada Las Vegas, Nevada
Office of Inspector General	Sacramento, California
Office of Solicitor General	Sacramento, California
Tahoe Regional Planning Agency	Elks Point, Nevada
State of Nevada, Division of Water Resources	Carson City, Nevada
Douglas County, Assessors Office	Minden, Nevada

**EXHIBIT C – COMPARISON OF ZEPHYR COVE TO THUNDERBIRD LODGE**

TYPE OF COMPARISON	ZEPHYR COVE	THUNDERBIRD LODGE
<b>NUMBER OF ACRES</b>	47.2 lakefront acres	140 lakefront acres
<b>NET COST TO FS</b>	\$38 million	\$40.5 million
<b>TYPE OF IMPROVEMENTS ON FS LANDS</b>	11,000 sq. ft mansion, covered garage, caretakers cottage	16,000 sq. ft mansion, four stone houses and gatekeepers house.
<b>WAS THERE A RESERVATION FOR PRIVATELY OWNED IMPROVEMENTS?</b>	<b>None-</b> LTBMU omits required CFR reservation. Instead, they create unauthorized agreement that allows proponent to sell government owned improvements to private party. Appraised value is not reduced to reflect encumbrance on FS land.	<b>Yes-</b> improvements reserved in conformance with CFR reservation. Value paid to proponent was reduced by about \$10 million to reflect encumbrance on FS land.
<b>WAS THE AGREEMENT ON THE USE OF IMPROVEMENTS APPROVED BY THE FS?</b>	<b>No-</b> proponent enters into agreement with private party without FS knowledge or approval. Private party plans to use the improvements and surrounding FS lands for an exclusive bed & breakfast resort.	<b>Yes-</b> FS develops reservation which restricts the use of improvements for research related facilities and public tours. The reservation also guarantees full public access. FS also approved the private party prior to the transfer of the improvements.
<b>WERE THERE PROVISIONS TO PROTECT THE PUBLIC’S INVESTMENT IN THE LAND?</b>	<b>No-</b> proponent sells property on FS land to a private party for \$300,000 in cash and \$2.7 million in conditional amenities. LTBMU staff does not determine private party's planned use of the improvements and surrounding FS land before allowing the sale to occur.	<b>Yes-</b> proponent had to spend an additional \$1.5 million to pay for additional water rights and other legal expenses to meet the terms of the FS agreement. The proponent also paid for a performance bond of \$2.3 million to ensure compliance to the terms of the FS reservation agreement.
<b>DOES THE FS HAVE RECOURSE IF THE PRIVATE PARTY DOES NOT COMPLY WITH FS MANAGEMENT PLANS?</b>	<b>No-</b> The FS is not enforcing its authority over the private party and may be unable to compel the private party to remove the improvements. The private party has also effectively barred the public from the main road and driveway leading to the property.	<b>Yes-</b> If the private party does not comply with the terms of the FS reservation, the reservation is terminated and all improvements, including all development and water rights, revert to FS ownership at no additional cost. The FS is also protected from future maintenance expenses via the performance bond.

TYPE OF COMPARISON	ZEPHYR COVE	THUNDERBIRD LODGE
<b>DID THE PROPONENT INCLUDE EXCLUSIVE EASEMENTS?</b>	The private party has constructively claimed an exclusive easement by locking the main gates and placing “private” signs on the main driveway leading to the improvements and on surrounding FS land.	<b>No</b> easements and encumbrances on the property – full public access
<b>DID THE APPRAISAL REFLECT FAIR MARKET VALUE?</b>	<b>No</b> – land value was overstated because the appraisal did not address claimed private ownership of the improvements and was based on speculative events and unrealistic assumptions.	<b>Yes</b> - the appraiser reduced the value by \$10 million to reflect the reservation for privately owned improvements on FS lands. The appraisal reflected the property actually acquired by the FS.
<b>WAS THE OFFICE OF THE GENERAL COUNSEL CONSULTED ON ALL LEGAL MATTERS?</b>	<b>No</b> - the FS LTBMU staff relied on attorneys employed by the proponent. FS LTBMU staff also created agreements with the proponent without consulting OGC. Further, they did not consult OGC when drafting reservations in the Zephyr Cove deed.	<b>Yes</b> - OGC was consulted in all phases of the exchange including reviewing the reservation agreement and drafting the legal reservations to the deed.
<b>WAS THE PUBLIC INTEREST SERVED BY THE EXCHANGE?</b>	<b>No</b> – The private party has effectively barred public access to the property’s sandy beaches and from FS lands surrounding the improvements. The private party has also locked the main gate and denied the public access to the main driveway. The private party has stated that it wants to use the property solely for the exclusive use of its paying clients.	<b>Yes</b> – The public is guaranteed access to all the property. Plans are under way to upgrade the facilities to enable public tours as well as to build facilities for the University of Nevada to conduct research on Lake Tahoe.

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## EXHIBIT D – FS RESPONSE TO DRAFT REPORT



United States  
Department of  
Agriculture

Forest  
Service

Washington Office

14<sup>th</sup> & Independence SW  
P.O. Box 96090  
Washington, DC 20090-6090

File Code: 1430  
Route To: 5100

Date: JUN 30 2000

**Subject:** Office of Inspector General Official Draft Report, Review of the Zephyr Cove Land Exchange, Lake Tahoe Basin Management Unit 08003-6-SF, May 24, 2000

**To:** James R. Ebbitt  
Assistant Inspector General for Audit  
Office of Inspector General

We have completed our review of the Office of Inspector General (OIG) Official Draft Audit Report entitled *Review of the Zephyr Cove Land Exchange, Lake Tahoe Basin Management Unit*, Report No. 08003-6-SF.

Enclosed is our response to the OIG report. If you have any questions, please contact Linda Washington, the External Audit Liaison, on (202) 205-3761.

VINCETTE L. GOERL  
Chief Financial Officer  
Deputy Chief, Office of Finance

Enclosure

cc: Deputy Chief, NFS  
Mike William, Lands Staff



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AUDIT REPORT NO. 08003-6-SF

United States Department of Agriculture  
Forest Service

Office of Inspector General (OIG)  
Pacific Southwest Region  
Zephyr Cove Land Exchange, Lake Tahoe Basin Management Unit  
May 24, 2000

Forest Service Review Comments  
June 27, 2000

**GENERAL COMMENTS CONCERNING THIS REPORT:** In order to provide additional background on some of the related concerns noted in this report and in public statements, we offer the following general summary of events, which provides insight into the actions taken by Forest Service officials.

The report deals with the ownership of the physical improvements on the Zephyr Cove property that the Lake Tahoe Basin Management Unit (LTBMU) acquired through a Bureau of Land Management (BLM) land exchange. As originally negotiated, the improvements associated with this property were to be removed by Olympic Group, Inc. (Olympic), the third-party who facilitated the exchange, prior to closing the transaction. Under this scenario, the improvements were not given a contributory value in the appraisal. The determination was later made by the Deputy State Director of BLM that the improvements were to remain on the property; however, the appraiser was instructed by BLM to appraise the property as if the residential dwelling was not there, thus, no consideration was paid for the improvements in this transaction. Title acceptance in this case was made by the BLM and there was no reservation of improvements in the first two deeds. As a result of this situation and latent concerns relative to a potential title claim, the Forest Service entertained preliminary discussions with the third-party and subsequently with Park Cattle Co. (Park) to provide for removal of the improvements. This was not acceptable to Park.

In March 1998, the Regional Forester requested the Office of the General Counsel (OGC) to review the chain of events, including the multiple deeds and side agreements, and to advise the Forest Service as to the ownership status of the improvements. In an opinion dated April 10, 1998, OGC advised that under the first two deeds, the United States acquired title to the land and improvements. The opinion noted the potential basis for a challenge by either Park or Olympic.

The relevant events are as follows:

1. October 21, 1976—Section 206 (c) of FLPMA provides that lands acquired by the Secretary of Interior within the boundaries of any unit of the National Forest System,

- upon acceptance of title by the US shall immediately be reserved for and become a part of the unit within which they are located, without further action by the Secretary.
2. October 31, 1996—The phase 1 deed is recorded.
  3. March 3, 1997—Letter from Deputy State Director, Nevada State Office, BLM, to Forest Staff Officer, stating the offered lands should be appraised as if the residential dwelling was not there.
  4. March 5, 1997—Olympic and Forest Service Agreement signed by the LTBMU Forest Supervisor giving the supervisor the option to choose between two alternatives. Alternative 2 required Olympic to convey the improvements to the Forest Service together with a payment of \$42,500 for expected maintenance costs for 3 years. Alternative 1 would allow Olympic to convey the improvements for the purpose of operating a concession. The alternative 1 option stated that no interest in or to the offered land would go to the concessionaire but rather it would sever the improvements there from. On July 2, 1997, this alternative was conditionally accepted by the acting Forest Supervisor.
  5. March 19, 1997—Staff review of the Johnson-Perkins appraisal prepared for BLM notes that, following BLM instructions and a special assumption, the property was appraised as if the improvements were removed and the site was vacant. At the review appraisers request the appraisers reviewed the BLM instructions to determine if these had an affect on the value of the property.
  6. April 25, 1997—The first deed from Olympic to the US is recorded. The perpetual and exclusive easement reserved to Olympic in phase 1 is conveyed to the US in this deed. There is no reservation of improvements.
  7. June 25, 1997—The deed to the US is re-recorded to add a citation.
  8. June 25, 1997—Olympic records a Memorandum of Interest in Real Property referring to the March 5, 1997 Agreement with the Forest service
  9. June 30, 1997—Olympic letter to Forest Supervisor advising that the improvements will be conveyed to Park as per the Agreement unless Olympic is advised to the contrary.
  10. June 30, 1997—Forest Supervisor writes to Olympic stating that Park must go through the Forest Service permittee approval process and there is no guarantee of being able to operate.
  11. July 1, 1977 Agreement between Olympic and Park for sale of improvements. Park knew of the March 5, 1997 Agreement between the LTBMU and Olympic because it is attached as an exhibit. Olympic made no representation that Park would be successful in ultimately establishing a concession with the USA. Olympic's reserved rights are preconditioned on Park's obtaining necessary approvals for contemplated operation of improvements.
  12. July 2, 1997—Forest Supervisor writes Olympic clarifying his June 30 letter by stating he has selected alternative one.
  13. July 2, 1997—Olympic records a quit claim deed to Park of the real property improvements as created by and defined by the March 5, 1997 Agreement.
  14. July 11, 1997—Olympic records a deed to the US which is to replace the deed recorded April 25, 1997. This deed conveys the Zephyr Cove property plus the phase 1 exclusive and perpetual easement to the US and then accepts and reserves the improvements to Olympic. The deed then quotes the 36 CFR 251.17

conditions without stating the purpose for which the improvements will not be used nor the period after which the reservation of improvements will terminate.

15. January 21, 1998—Park applies for a special use permit on the entire 47.2 acres (phase 1 and 2) with the fee being based on a percentage of income rather than a percentage of the fair market value of the land. This application has been withdrawn and there is no pending application.

The OGC opinion concluded that, the resolution of this issue could necessarily involve protracted litigation, and ongoing disputes over use, management and protection of the property during the litigation. Thus, suggested that the best result would be to negotiate a resolution of the matter through a third-party agreement by which Park and Olympic quit claimed any interest they may have to the United States.

Since the Regional Forester did not think it was in the best interest of the public to authorize use under a special use permit and there was no demonstrated public need for the permit, the Region began discussions on the possibility of a land exchange as means of settling this ownership issue. The proposal discussed involved the potential exchange of approximately 6 acres associated with the Zephyr Cove improvements for other Lake Tahoe frontage property, including a beach for public use.

However, Park Cattle Co. notified the Region on June 1, 2000, that the exchange configuration proposed by the Forest Service was not acceptable. We have now concluded that a land exchange is not in the best interests of the United States and are consulting with OGC and Department of Justice as to what is the appropriate course of action is to pursue to acquire Park Cattle Co.'s interests in the Zephyr Cove improvements.

The Forest Service has exercised Federal ownership of the land and lake frontage (not associated with the improvements) to make them accessible to the public. On April 30, 1998, LTBMU personnel removed approximately 400 feet of the 600 foot chain link fence on the south side of the Zephyr Cove property, removed several pedestrian gates along Highway 50, removed the "no trespassing private" signs, and posted national forest boundary signs approximately 300 feet from each other along the east side of the property, paralleling the highway. Both the north fence and the remainder of the south fence (200) were removed by contract late in 1998. The east fence along the highway was left to prevent indiscriminate vehicle access and an unsafe parking situation and resource damage to environmentally sensitive areas and trampling of native vegetation between the highway and the lakeshore. Similar actions were taken south of the property along Highway 50 at the Zephyr Cove Resort in concert with the State of Nevada. Foot access is available across the property and the beach is accessible from the Zephyr Cove Resort parking area to the south and adjacent National Forest Lands to the north.

As noted in the report, Park Cattle Co. has posted new signs near the Zephyr Cove structures on National Forest System lands, noting that the residences are private property and have erected signs and constructed a trail to direct the public away from the buildings. Park Cattle has also retained a caretaker who confronts members of the public if they walk close to the buildings.

The Funds To Be Put To Better Use appears overstated. The Forest Service does not agree with the dollar amounts indicated as savings to the government. These numbers will be validated once a formal evaluation has been completed.

**Recommendation No. 1**

Send written notice to the BLM lands staff and terminate the interagency agreement between the LTBMU and BLM.

**Response**

By letter dated June 15, 2000, the Regional Forester of R-5 formally terminated the 1996 interagency agreement between the LTBMU and BLM.

**Recommendation No. 2**

Create a Memorandum of Understanding between the Pacific Southwest Region and BLM that specifies the roles and responsibilities of the Forest Service and BLM lands staffs when processing land exchanges involving both agencies. Ensure that principal contacts cited in the agreement have sufficient delegated authority to approve changes that may occur during the land exchange.

**Response**

A Memorandum of Understanding (MOU) between the Pacific Southwest Region and the BLM has been signed by the R-5 Regional Forester and the Nevada State Office BLM Director and became effective on June 14, 2000. The MOU outlines the work to be performed and specifies the roles and responsibilities of the Forest Service and BLM lands staffs when processing land exchanges involving both agencies.

**Recommendation No. 3**

Ensure that appropriate Forest Service personnel at the RO and zone levels receive draft copies of final title documents prior to BLM's closure of any land exchanges involving the Forest Service.

**Response**

The Regional Director of Lands mailed copies of the executed MOU to all relevant forest, zone and RO personnel on June 15, 2000. Follow up will be made by the Regional Director of Lands to ensure receipt of these documents by the appropriate parties by July 1, 2000.

Attachment "A" to the MOU for Forest Service and BLM land exchanges specifies that the Forest Service will review and concur on final title opinions to non-Federal lands before BLM accepts title.

#### **Recommendation No. 4**

Clarify RO policy relating to the review and approval function of zone land ownership adjustment teams for land exchanges involving BLM.

#### **Response**

We agree that the RO policy relating to the review and approval function of zone land ownership adjustment teams for land exchanges involving BLM needs to be clarified. The Regional Forester will develop written policy, which will be reviewed by the WO Director of Lands. The final policy will be incorporated into the Forest Service Region 5 directives no later than December 31, 2000.

#### **Recommendation No. 5**

Review the actions of the two Forest Service employees and refer the matter to the Human Resources Department for the appropriate action.

#### **Response**

Human Resources personnel at the Region and Washington office levels are currently reviewing the actions of the R-5 employees. The complete record will be reviewed and any appropriate action taken by October 1, 2000. While this matter is under review, both individuals have been given details to other duties.

#### **Recommendation No. 6**

In future land exchanges, ensure that any concessionaire operation proposed for Forest Service lands meets the forest's long-range management plan, satisfies a public need, and has concurrence from appropriate Forest Service groups and upper management.

#### **Response**

This is existing Forest Service policy and it was not violated by the LTBMU in this transaction. In the Forest Supervisor letter of June 30, 1997, to Olympic Group, the Forest Supervisor states, "The Park Cattle Company is not currently an operating permittee and therefore must go through the Forest Service's permittee approval process. This could take several months and will require in-depth financial information. Once this process is complete, Park Cattle Company must understand there is no guarantee of being able to operate." Further guidance was given to the Regional Foresters in a letter dated October 14, 1999, which states "The competitive land exchanges need to be given major consideration when land exchanges involves Federal properties that are atypical,

influenced by escalating markets, or that have broad market appeal and interest... In all cases where structural improvements are being acquired, the Feasibility Analysis (FA) and Agreement to Initiate should document the type and size of the structure(s). The FA needs to also document the purpose of acquiring the structure(s) and how their acquisition would aid in achieving the goals and objectives of the Forest Land and Resource Management Plan. The Decision Document approving acquisition of any structure(s) needs to document how the acquisition serves the public interest and disclose the disposition of said structure(s) and the funding source for future maintenance costs and/or the disposition costs; i.e. sale or demolition (letter enclosed)." The above excerpts taken from the enclosed letter will be included where appropriate in the Forest Service Manuals and Handbooks by July 31, 2001.

### **Recommendation No. 7**

Direct Forest Service staff to communicate directly to all parties involved in Forest Service land adjustments rather than relying on proponents and/or facilitators to convey the necessary information to third parties.

### **Response**

Forest Service policy concerning the use of third party facilitators in land ownership adjustments is clearly stated in letter dated October 15, 1998, to Regional Foresters from the Deputy Chief of NFS and in the draft FSH 5409.13 – Land Acquisition Handbook. Under section 32.3 – Third Party Facilitators, Forest Service policy requires that the following items be documented early in the process as follows:

1. After review of title to the non-Federal property, define the estate to be acquired by the United States.
2. Define the respective roles and responsibilities, including responsibilities for accomplishment of action items and responsibility for costs, of both the Federal government and facilitator. Expenses incurred by either party are at their own risk.
3. Schedule timing of actions.

In the case of land exchanges, these items are appropriately documented in an Agreement to Initiate. For purchase and donation cases, these items should be documented in a Letter of Intent, notes of negotiation meetings, challenge cost share agreements, or other adequate form of documentation.

The Region's Lands Officers, RO Lands Staff and Zone Landownership Adjustment Teams will receive training on the draft Land Acquisition Handbook FSH 5409.13, on June 28-30, 2000, by the National Lands Oversight Team. Continual monitoring will occur during subsequent National Team Review of proposed and pending land exchange proposals.

### **Recommendation No. 8**

Conduct a peer review of the Zephyr Cove appraisals and the actions taken by the Forest Service appraiser. Take any corrective actions recommended by the peer review.

**Response**

A peer review of the Zephyr Cove appraisals is currently underway and will be completed by August 1, 2000. The conclusions and recommendations of this review will be provided to the Deputy Chief and WO Director of Lands and any appropriate corrective actions will be initiated by October 1, 2000.

**Recommendation No. 9**

Ensure that review appraisers understand and comply with Federal appraisal standards and Forest Service appraisal procedures.

**Response**

Policy direction will be provided to the Agency appraisal organization by the Chief Appraiser and WO Director of Lands so as to avoid repetition of these deficient actions prior to January 1, 2001.

A training course has been developed, offered, and is mandatory for all Forest Service staff appraisers. This course deals with transitional properties and appropriate documentation and analysis methods to support values based on potential development.

Continual monitoring and oversight will occur through scheduled compliance reviews by the Chief Appraiser and WO Director of Lands.

**Recommendation No. 10**

Ensure that any appraisals based on potential actions (e.g. presumed TRPA or Forest Service approvals) are supported by documentation obtained directly from the approving agency.

**Response**

All appraisals based on property zoning or use limitations that are not currently in effect shall be documented not only with local zoning authorities, but also by verification that similar use has been authorized for other similarly situated private property. This market-based verification shall be mandatory in all cases where the assumed zoning for appraisal purposes is different than the actual zoning in effect on the date of value. This is particularly critical as part of the development process for high profile, controversial, and/or complex property appraisals. It is essential that the review appraiser understand the need for a high level of clarity and support for value conclusions in these kinds of actions. Although this requirement is already in effect (see FSH 5409.12-1.33d) as it applies to Federal lands

that are being appraised as part of Agency exchange actions, this needs to be further expanded to include valuation of transitional non-Federal properties. This requirement will be underscored in future policy and procedure updates, at the annual appraisers meeting to be held during the week of October 18, 2000, and emphasized in subsequent regional compliance reviews by the Chief Appraiser and WO Director of Lands.

### **Recommendation No. 11**

Reiterate to Forest Service Staff and appraisers that improvements remaining on land being transferred to the Forest Service must comply with the provisions of Title 36 CFR 251, and that the reservation may affect the appraised value.

### **Response**

Current regulatory requirements provide for a mandatory reservation for structural improvements that are to be retained by the grantor in transactions such as this. The Forest Staff and appraisers should have been aware of this requirement. It is inappropriate to accept title nor can an appraisal be accepted based on an assumption that a special use permit, authorizing some form of occupancy is forthcoming subsequent to closure. Special use permits are discretionary actions that require NEPA analysis and conclusions, and are subject to appeal in and of their own right.

Improvements remaining on land being transferred to the Forest Service must comply with the provisions of Title 36 CFR 251.17, and the reservation must be analyzed as it might affect the estimate of value.

This requirement will be highlighted in the draft FSH 5409.13 on Land Exchanges and emphasized during upcoming required Handbook training sessions by the National Lands Oversight Team.

### **Recommendation No. 12**

Consult with OGC to determine what title documents are needed for a final title opinion. Provide the documents to OGC within 60 days.

### **Response**

The Region through the Central Zone Land Adjustment Team is working with OGC to make sure all necessary documents related to water rights, the well, development and coverage rights, etc. are acquired so that a final title opinion can be prepared. The final title opinion will be issued by September 1, 2000.

### **Recommendation No. 13**

Obtain a final title opinion from OGC which focuses on all aspects of the Zephyr Cove land exchange transaction, including the nonpayment of possessory interest tax and the title to

(1) improvements, (2) exclusive easements, (3) water rights and (4) development rights and coverage. Consult with OGC on legal actions necessary to preserve the USA's property rights, including determining the nature and quantity of water rights associated with the Zephyr Cove property, and reporting a "change of conveyance" with the Nevada State Division of Water Resources.

### **Response**

A review of these complex title matters is underway by the Region and OGC. A final opinion will be issued by OGC addressing these and any other relevant title or occupancy issues by September 1, 2000. This will also include the identification of any further actions that need to be taken by the Region to protect any property interests or rights of the United States.

### **Recommendation No. 14**

In consultation with OGC, take action to collect rental fees owed the Forest Service from Park Cattle for the period of its unauthorized occupancy.

### **Response**

The fair market rental fee for the occupancy will need to be predicated on an approved appraisal of the land encumbered since 1997. This will be completed by September 1, 2000, and in consultation with the WO Director of Lands and OGC, the Regional Forester will initiate action to collect the appropriate rental.

### **Recommendation No. 15**

Initiate legal action to resolve Park Cattle's unauthorized occupancy of Forest Service lands.

### **Response**

Once the title and ownership matters are defined by OGC, the Regional Forester and Director of Lands, in consultation with the WO Director of Lands and OGC will initiate appropriate action to resolve the ownership and occupancy issues. The timeline for this action to be initiated is by January 1, 2001.

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## ABBREVIATIONS

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BLM	
Bureau of Land Management.....	i
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Director, Planning and Accountability Division (1)