



Audit of Land Acquisition and Management Processes

Report # 10-01

Prepared By

Office of Inspector General

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SOUTH FLORIDA WATER MANAGEMENT DISTRICT

September 1, 2010

Audit and Finance Committee Members:

Mr. Charles J. Dauray, Chair
Eric Buermann, Esq., Member
Mr. Joe Collins, Member
Glenn J. Waldman, Esq., Member

Re: Audit of the Land Acquisition
and Management Processes –
Project No 10-01

This audit was performed pursuant to the Inspector General's authority set forth in Chapter 20.055, F.S. The audit examined the land acquisition and appraisal processes for the period October 1, 2007 through December 31, 2009. This report was prepared by Dan Sooker.

Sincerely,

A handwritten signature in black ink, appearing to read "John W. Williams", is written over a faint, large, stylized signature graphic that spans across the signature line and extends upwards and to the right.

John W. Williams, Esq.
Inspector General

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BACKGROUND

In accordance with our FY09 Audit Plan, the Office of Inspector General completed an Audit of the District's Land Acquisition and Management Processes. As a part of our audit, we reviewed Palm Beach County's investigation of various operational aspects including its land acquisition program to determine whether the District's land acquisition program could benefit from recommendations made in this investigative report.

Function	Employees
Acquisition and Negotiation	6
Closing and Title	10
Survey	11
Geography	7
Appraisers	2
Environmental Assessment	2
Management Directors	2
Administrative	3
Total	43

For the period October 1, 2007 through December 31, 2009, the District spent \$349 million on land acquisitions. The Land Acquisition program is managed by the Land Acquisition Department which is under the Everglades Restoration and Capital Projects Resource Area. The Land Acquisition program consists of forty-three employees, who are responsible for the entire acquisition process from negotiations to closing. The adjacent table lists the Land Acquisition employees by function.

Land acquisitions are based on fair market value, which is defined by Florida law as the amount of money that a purchaser willing but not obligated to buy the property would pay an owner willing but not obligated to sell, taking into consideration all uses to which the property is adapted and might be applied in reason. Inherent in the willing buyer-willing seller test of the fair market value are the following:

1. A fair sale resulting from fair negotiations.
2. Neither party is acting under compulsion of necessity (this eliminates forced liquidation or sale at auction). Economic pressure may be enough to preclude a sale's use.
3. Both parties having knowledge of all relevant facts.

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4. A sale without peculiar or special circumstances.
 5. A reasonable time to find a buyer.

Fair market value is determined through the appraisal process. The appraisal process is governed by District policies and procedures and State statutes as well as by standards promulgated by the Federal Government and the Appraisal Foundation. The Appraisal Foundation is authorized by Congress as the source of appraisal standards and appraiser qualifications. Such standards include the Uniform Standards of Professional Appraisal Practices (USPAP) and Uniform Appraisal Standards for Federal Acquisitions (Yellow Book). The intent of these Standards is to create a uniform methodology of land valuation that is consistent, unbiased, and thorough.

The District's appraisal function serves as a vital internal control in protecting the integrity of the land acquisition process. Through the appraisal process, market valuations for potential acquisitions are determined and are the basis for negotiations with landowners. Appraisal assignments are typically outsourced to outside independent appraisers. In-house appraisal staff usually is responsible for conducting quality control reviews of completed appraisals to verify technical compliance with professional appraisal standards and regulations. On occasion, both the appraisal and review appraisal assignment is outsourced to outside appraisers.

OBJECTIVE SCOPE AND METHODOLOGY

The objective of the audit was to examine the land acquisition process which included the process used to prioritize, budget and purchase land for projects and conservation. This included examining the appraisal process which entailed focusing on the outside appraiser selection process and compliance with District policies and procedures for the period October 1, 2007 through December 31, 2009. In addition, we reviewed Palm Beach County's investigation of its land program to determine whether the District could benefit from recommendations made in this investigative report. In order to accomplish our objectives, we performed the following:

- Conducted interviews of appropriate staff
- Selected and examined land acquisition packages
- Determined whether District appraisers and outside appraisers are adhering to statutes and District policies and procedures

Our audit was conducted in accordance with Generally Accepted Government Auditing Standards. These standards require that we plan and perform the audit to obtain sufficient, appropriate evidence to provide a reasonable basis for our findings and conclusions based on our audit objectives. We believe that the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit objectives.

AUDIT RESULTS

Executive Summary

The District's land acquisition program average spending was over \$100 million annually but new forecasts project expenditures for land to be reduced to approximately \$30 million. Due to the expected decrease in land acquisition activities, and uncertain state revenue from the state of Florida for the Save Our Everglades and Florida Forever Trust Funds, management should consider staff redirections commensurate with the anticipated work plan.

One staff redirection option is to outsource appraisal reviews but we recommend that this function remain in-house. A strong review appraiser with authority to challenge appraisal valuations is crucial to the system of internal controls over the land acquisition process.

To improve the internal control framework over the land acquisition and appraisal processes and enhance accountability and transparency, we recommend that District management establish a Land Oversight Committee. The Committee's composition could include an Attorney from Office of Counsel, Outside Board Counsel, the Director of Land Acquisitions, the Chief Appraiser and/or the Senior Review Appraisers. The Committee could monitor the land acquisition strategy, solicit and select appraisers for appraisal assignments, and review appraisal instructions.

Five years ago, our Office completed an audit of the appraisal process. Recommendations in Report 03-15, *Audit of the District's Real Estate Appraisal Process*, centered on the need to improve internal controls over the appraisal process by establishing an appraisal function that was independent of the land negotiation and acquisition processes. Management concurred with the recommendations and made the organizational change to create an independent appraisal unit that was separate from the Land Acquisition Department.

However, through a series of District reorganizations, the once independent appraisal section has been merged into the Land Acquisition Division according to the

most recent organizational chart. The Chief Appraiser now reports directly to the Director of the Land Acquisitions and also serves the role of Division Director. Best practices recommend that the appraisal function and the land acquisition process should be separate to remove any perception of bias or independence issues.

The Palm Beach County investigation of its land program recommended that the practice of using extraordinary assumptions to determine market value be discontinued. We reviewed nine appraisals related to District land acquisitions and found that in four of them, the appraisals contained extraordinary assumptions¹. Management may also want to consider discontinuing the use of hypothetical and/or extraordinary assumptions, special instructions, but if deemed appropriate in rare circumstances, the hypothetical and/or extraordinary appraisal condition should be approved by the Deputy Executive Director of the Everglades Restoration and Capital Projects and/or the Land Oversight Committee.

In addition, the Palm Beach County investigation recommended that all land transaction appraisals be published on the Palm Beach County website at least two weeks before being scheduled for Board of County Commissioner approval. District management may also want to consider similar action and post appraisals on the District's website prior to land acquisition approval by the Governing Board in accordance with Section 373.139(3)(a), Florida Statutes, regarding appraisal disclosure to the public.

¹ The Uniformed Standards of Professional Appraisal Practice defines an Extraordinary Assumption as an assumption which, if found to be false, could alter the appraiser's opinions or conclusions. Extraordinary assumptions presume as fact otherwise uncertain information about physical, legal, or economic characteristics of the subject property; or about conditions external to the property, such as market conditions or trends; or about the integrity of data.

Align Land Acquisition Program Staffing Needs with the Anticipated Work Plan

During the audit period, the District purchased 80,727 acres for thirty-two projects. Executive management in collaboration with the Projects and Lands Committee determined the planned acquisitions based on funding projections, priority projects and opportunity. The majority of land purchases were for priority projects, Picayune Strand, Biscayne Bay Coastal Wetlands, Loxahatchee Slough and C-23/C-24 Storage Reservoirs.

In the past, the land acquisition program spent over \$100 million annually but new forecasts project expenditures for land to be reduced to approximately \$30 million. The five-year work plan anticipates minimal acquisitions but may require unanticipated acquisitions in the Picayune Strand, C-111, Herbert Hoover Dike, and Kissimmee River. Inverse condemnation cases in the Kissimmee River basin could prove costly when finally adjudicated. Management may want to consider establishing a reserve for the probable inverse condemnation loss as estimated by Office of Counsel, The Deputy Executive Director of Everglades Restoration and Capital Projects, and the Director of the Land Acquisition Department.

State of Florida budget shortfalls have also resulted in uncertain revenue contributions from the state for the Save Our Everglades and Florida Forever Trust Funds. The projected state and ad valorem revenue reductions will have a substantial economic effect on the District's land acquisition program. Accordingly, management needs to align staffing needs with future demands of the land acquisition program.

Management should evaluate staffing levels and consider staff redirections commensurate with the anticipated work plan. A major benefit of retaining these staff would be that the District keeps the skills set and experience of the redirected employees which could be useful at a future time.

We also recommend that appraisal reviews remain an in-house function. A strong review appraiser with the authority to challenge appraisal valuations is crucial to the system of internal controls over the valuation process. In light of the reduced level of

land acquisition and funding activity, management should reassess staffing needs regarding the review appraisal function.

Management should also finalize a surplus land policy to establish criteria to identify surplus properties. Most of the 1.4 million acres of District owned and managed properties are used or will be used for improvements and the Department expects only a small percentage of land will be deemed surplus. The Department's preliminary review of District land inventory identified only 10 parcels consisting of 1,100 acres as surplus. However, a thorough initial review of District property inventory is needed to determine whether the land is surplus or needed for restoration, conservation or water resources.

Recommendations

- 1. Align Land Acquisition Program staffing needs with the anticipated work plan.**

Management Response: Agree
Responsible Department: Real Estate Department
Estimated Completion Date: January, 2011

- 2. Consider establishing a designated reserve for probable inverse condemnation losses.**

Management Response: The Budget Office has established a reserve that may be used for inverse condemnations.
Responsible Department: Office of Management and Budget
Estimated Completion Date: Complete

- 3. Complete a surplus land policy that establishes criteria to identify surplus properties.**

Management Response: Agree. A surplus land process was approved by the WRAC, the Projects and Land Committee and the Governing Board.

Responsible Department: Real Estate Department

Estimated Completion Date: Complete

4. Management should reassess staffing needs regarding the review appraisal function.

Management Response: Agree

Responsible Department: Real Estate Department

Estimated Completion Date: January, 2011

**Improvements to the Appraisal Process Control Framework
Would Enhance Accountability**

To enhance accountability and transparency over the land acquisition and appraisal processes, management should establish a Land Oversight Committee. In the past, the District once had an Appraisal Review Committee whose primary function was appraiser selection but it was disbanded in July of 2002 because of committee member's limited availability and time constraints.

The newly established Land Oversight Committee could monitor land acquisition strategies, solicit and select appraisers for appraisal assignments and review appraisal instructions. The Committee's composition could include an Office of Counsel Attorney, Outside Board Counsel, Director of Land Acquisitions, Chief Appraiser and/or the Senior Review Appraisers.

One of the key recommendations in our Audit Report of the Real Estate Appraisal Process dated November 18, 2003, was to separate the District's appraisal function from the Land Acquisition Department. At the time of the audit, the Chief Appraiser reported to the Director of Land Acquisition. We recommended an organizational change which

management made to create an independent appraisal unit and separated the Appraisal Section from the Acquisition Department.

However, through a series of District reorganizations, the once independent Appraisal section has been merged into the Land Acquisition Division according to the most recent organizational chart. This Division is lead by the Chief Appraiser and consists of the appraisal function, Land Acquisition, the Title and Closings Section and the Surveying and Mapping Section. The Chief Appraiser again reports directly to the Director of the Land Acquisitions. We discussed the organizational changes relating to the appraisal function with the Chief Appraiser. Although this may appear to create a perceived independence problem, the Chief Appraiser stated that at no time was the appraisal process compromised adding that the Appraisal Section has always ensured that appraisals reflect fair market value. Nevertheless, the Appraisal Foundation recommends that the appraisal function should be independent of the acquisition process. Accordingly, they recommend that the appraisal function and the land acquisition process be separate to remove any perception of bias. In addition, both contract and internal appraisers may perceive more authority to challenge appraisal valuations when these processes are independent of each other.

For the audit period, the Appraisal Section conducted forty-four appraisal assignments which included the large and complex proposed acquisition of United States Sugar Corporation (US Sugar) land for the River of Grass project. The District's process to become an approved appraiser requires the outside appraiser to fill out an application through an internet portal. The process is continually open. Minimum qualifications for inclusion on the District's approved appraiser database list include State of Florida certification, senior level designation (MAI, ASA or other appraisal foundation membership) and relevant work experience. Currently, there are 184 appraisers on the District's approved appraiser list.

Even though District appraisal services are exempt from competition, the Appraisal Policy promotes a competitive process. However, in practice the appraiser selection process did not consistently use competition. We found that of the forty-four

outsourced appraisal assignments which were completed during the period, five were competitively solicited, eight were appraisal updates that were completed by the original appraiser, and the remaining thirty assignments were completed by appraisers that were short listed or previously approved as the most qualified for the projects. A best practice to ensure economical and equitable distribution of appraisal services is competition.

Further review of the appraiser selection process revealed that certain appraisers were selected for multiple assignments and only fourteen of the 184 approved appraisers were given an opportunity to compete for appraisal work. We were told that all 184 approved appraisers may not be capable and available for District work. Accordingly, the District's approved appraiser listing should be scrubbed and/or re-solicited every two years.

We selected nine appraisal assignments to verify compliance with attributes of District policies and procedures related to the appraisal selection process. We also reviewed the sample of nine appraisals for the assumptions used by outside appraisers to determine market value. The Palm Beach County investigation of its land program recommended that the practice of using extraordinary assumptions to determine market value be discontinued (See definition of extraordinary assumptions in the footnote on page 5). In addition, the report recommended that all land transaction appraisals be published on the Palm Beach County website at least two weeks before being scheduled for Board of County Commissioner approval.

We found that, without exception, the assigned appraisers were on the approved appraisal list and two appraisers were assigned for property with an estimated value of over \$1 million. We also found that in four of the nine appraisals reviewed, the appraisals contained extraordinary assumptions. Management may want to consider discontinuing the use of hypothetical and/or extraordinary assumptions, special instructions, but if deemed appropriate in rare circumstances, the hypothetical and/or extraordinary appraisal condition should be approved by the Deputy Executive Director of the Everglades Restoration and Capital Projects or the land Committee overseeing the appraisal process. Management should also consider posting appraisals on the District's

website prior to Governing Board meetings.

Recommendations

5. Separate the appraisal process from the land acquisition process.

Management Response: Agree. ERCP Business Services will recommend an alternative.

Responsible Department: ERCP Business Services

Estimated Completion Date: March 2011

6. Compete appraisal services except in rare circumstances. Document reasons for sole sourcing appraisal services.

Management Response: Agree.

Responsible Departments: Real Estate Department and ERCP Business Services

Estimated Completion Date: March 2011

7. Establish a Land Oversight Committee to oversee the acquisition and appraisal processes.

Management Response: Agree.

Responsible Departments: Real Estate Department and ERCP Business Services

Estimated Completion Date: March 2011

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- 8. Adopt the recommendations made in the Palm Beach County investigative report in regards to discontinuing the use of extraordinary/hypothetical assumptions in the appraisal process and follow Section 373.139(3)(a), Florida Statutes, regarding appraisal disclosure to the public.**

Management Response: Hypothetical assumptions have never been allowed in appraisal assignments for the District. However, the use of extraordinary assumptions will on occasion be necessary. For example, if the appraisal must be initiated prior to a determination that an environmental assessment may be required, an appraisal would likely require an extraordinary assumption that the property does not contain excessive environmental contaminations. As an alternative to complete discontinuation, it is recommended that the Real Estate Department first must receive review approval from the Deputy Executive Director and/or the Real Estate Team before an extraordinary exception is written into an appraisal request. This will ensure that management is fully aware of the circumstances and the negotiator has not influenced the process.

Responsible Department: Real Estate Department

Estimated Completion Date: March 2011

- 9. Scrub and/or re-solicit the District's approved appraiser listing every two years.**

Management Response: Agree. However, it is recommended that the list be approved every three years with potential for renewals. This is consistent with Procurement standards.

Responsible Departments: ERCP Business Services, Real Estate and Procurement Departments.

Estimated Completion Date: March 2011

Addendum 1

Regulations and Standards Relevant to the Land Acquisition Process

Regulations	Descriptions
Public law 91-646	Establishes uniform and equitable land acquisition policies for federal or federally assisted programs.
49CFRpart 24	Section 24.104 requires that a qualified reviewing appraiser examine all appraisals to assure they meet applicable appraisal requirements.
Chapter 373.139(3)(c)F.S.	Requires two appraisals for parcels in which estimated value exceeds \$1 million.
District Appraisal Policies and Procedures	These policies and procedures provide broad, high-level guidance that embody the many directives applicable to the appraisal function. They require compliance with applicable regulations and USPAP standards. District policy requires two appraisals when a parcel's value is estimated at over \$1 million.
Uniform Appraisal Standards for Federal Acquisitions	Establishes standards for land acquisitions for federal programs. Requires a detailed review of the appraisal to determine that the opinions of value are adequately supported and the appraisal complies with applicable standards.
Uniform Standards of Professional Appraisal Practices	Establishes minimum standards for the appraisal practice.