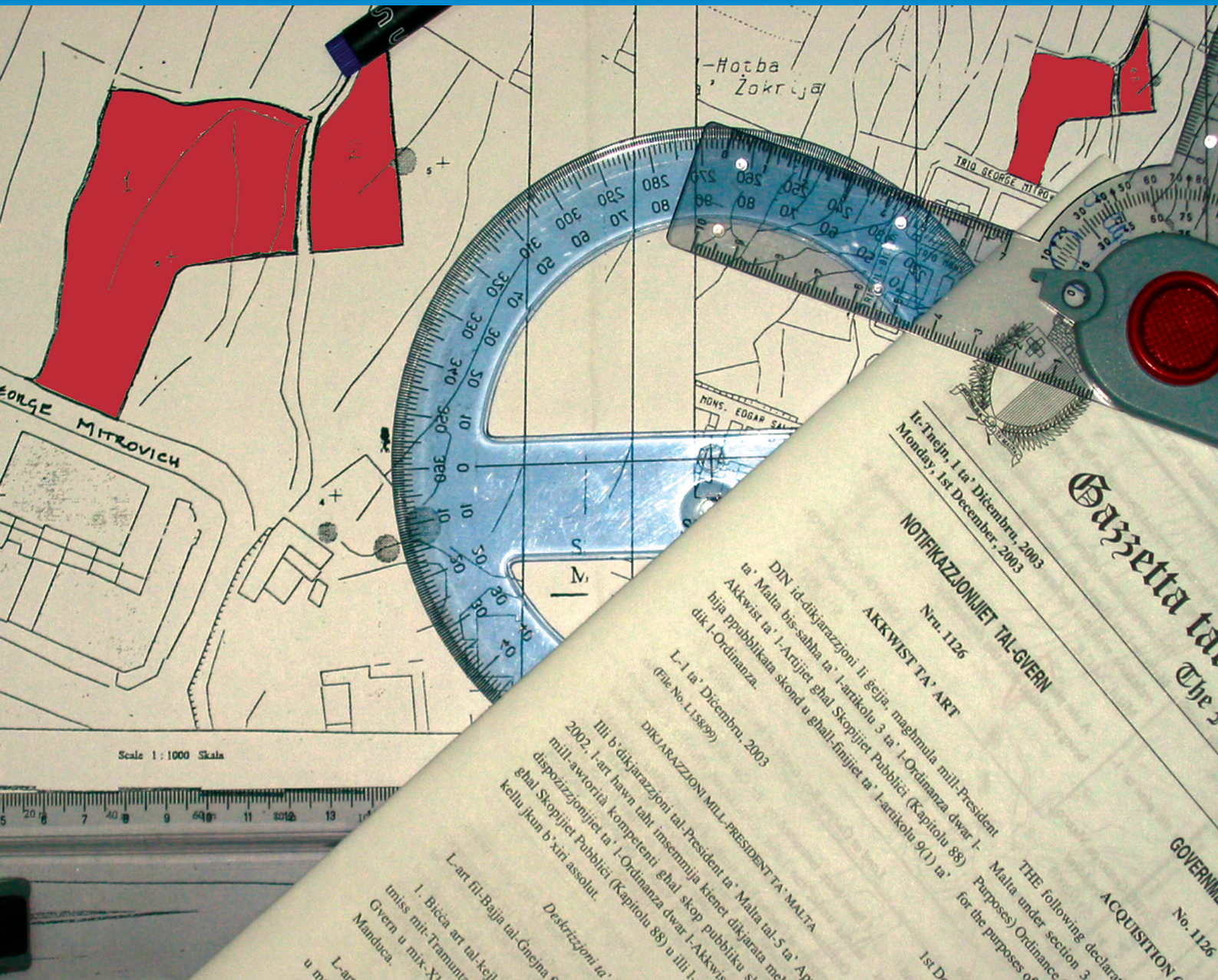




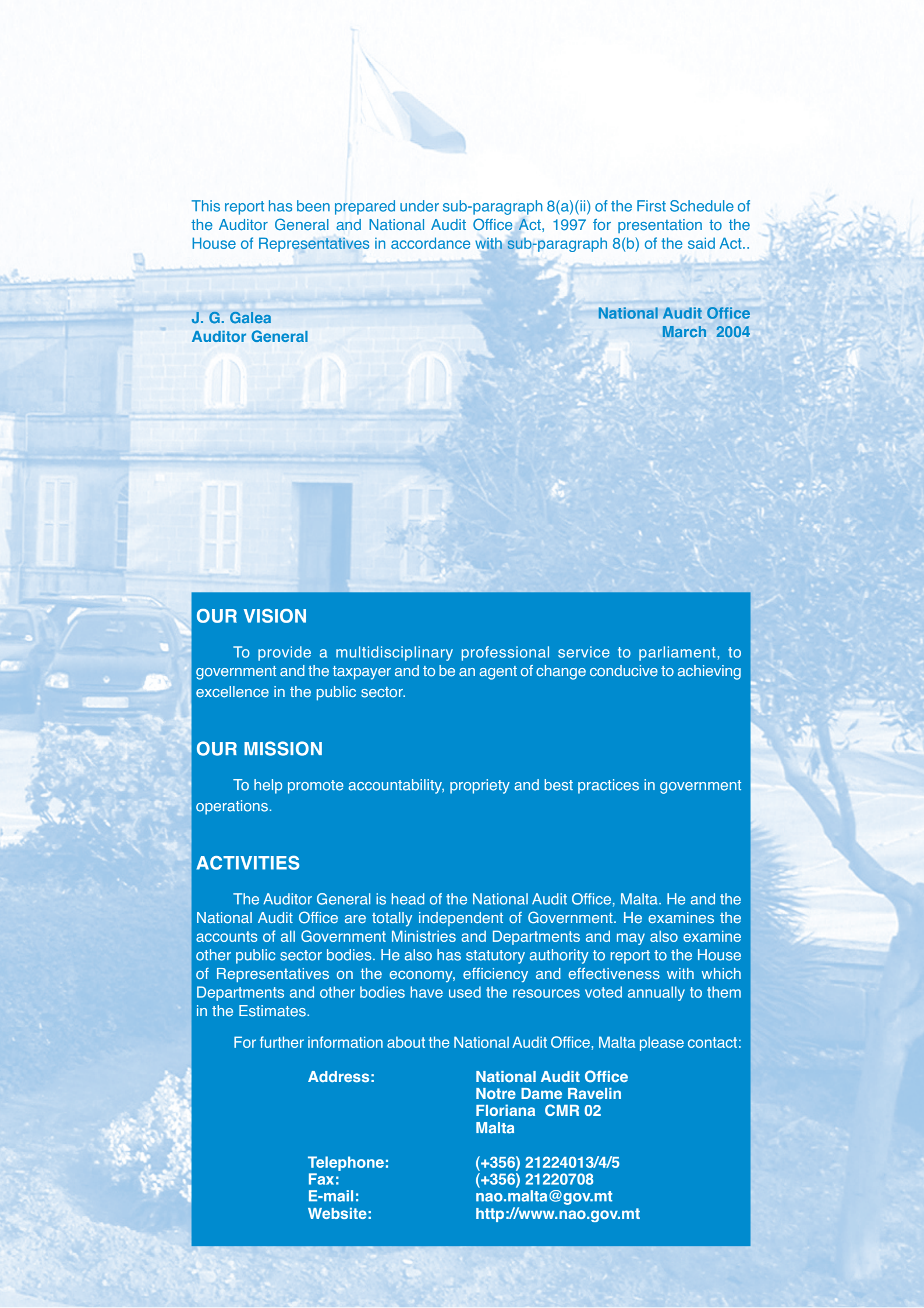
**N A O**  
National Audit Office  
Malta

# Performance Audit Acquisition of Property by Government

## Report by the Auditor General







This report has been prepared under sub-paragraph 8(a)(ii) of the First Schedule of the Auditor General and National Audit Office Act, 1997 for presentation to the House of Representatives in accordance with sub-paragraph 8(b) of the said Act..

**J. G. Galea**  
**Auditor General**

**National Audit Office**  
**March 2004**

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# **Performance Audit**

## **Acquisition of Property by Government**



**Report by the Auditor General**

**March 2004**



# Table of Contents

<b>Executive Summary of Findings .....</b>	<b>5</b>
<i>Executive Summary .....</i>	6
<i>Conclusions and Recommendations .....</i>	8
<b>Introduction .....</b>	<b>9</b>
<i>Audit concerns .....</i>	10
<i>Background .....</i>	10
<i>Audit objectives .....</i>	12
<i>Audit scope .....</i>	12
<i>Methodology .....</i>	12
<i>Structure of the report .....</i>	13
<b>Part 2: The Role of User Departments .....</b>	<b>15</b>
<i>Introduction .....</i>	16
<i>Minimising the Cost of Land Acquisition .....</i>	16
<i>Taking Possession of Land prior to Publication of the President's Declaration .....</i>	17
<i>Land Acquisition outside the provisions of the LAO .....</i>	17
<i>Land Acquired Surplus to Requirements .....</i>	17
<i>The Need for Guidelines and Control Structures in the Role of User Departments .....</i>	18
<b>Part 3: The Land Acquisition Process .....</b>	<b>19</b>
<i>Introduction .....</i>	20
<i>Inadequate management information .....</i>	20
<i>The Acquisition Process .....</i>	21
<i>Implications of the Delay in Determining Prices of Land Acquisitions .....</i>	25
<b>Part 4: Compensation Issues .....</b>	<b>27</b>
<i>Introduction .....</i>	28
<i>Availability of Funds .....</i>	28
<i>Land Valuations .....</i>	29
<i>Financial Implications of the Delay in Determining the Value of Land Acquisitions .....</i>	32
<b>Part 5: Conclusions And Recommendations .....</b>	<b>35</b>
<i>Conclusions .....</i>	36
<i>Recommendations .....</i>	37
<b>Appendices .....</b>	<b>39</b>
<i>Appendix I - Report on Procedures for Valuation of Compulsorily Acquired Land .....</i>	41
<i>Appendix II - Estimating Government's additional cost as a result of delaying determination of compensation .....</i>	47



## List of Charts

<i>Chart 1 - Cumulative Average Time-Intervals between the Key Stages of Concluded Acquisitions</i> .....	22
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## List of Tables

<i>Table 1 - Key stages within the land acquisition process</i> .....	11
<i>Table 2 - Delay in the Pre-acquisition process</i> .....	21
<i>Table 3 - Position of Outstanding Sampled Acquisitions at end 2002</i> .....	22
<i>Table 4 - Notices to Treat issued between 1998 and 2002 referred to the LAB</i> .....	24
<i>Table 5 - Comparison between NAO and GPD Valuations</i> .....	30
<i>Table 6 - Cases referred to the LAB between 1998 and 2002 - Differences between GPD Valuations and Owners' Counterclaims</i> .....	31
<i>Table 7 - Cases concluded by the LAB between 1998 and 2002 - Differences between Valuations by the GPD and the LAB</i> .....	31
<i>Table 8 - Additional Costs Incurred - The Intrinsic Growth in the Value of Land</i> .....	33



## Abbreviations used in this Report

<b>GPD</b>	Government Property Division
<b>LAB</b>	Land Arbitration Board
<b>LAO</b>	Land Acquisition (Public Purposes) Ordinance
<b>LEMIS</b>	Land and Estate Management Department Information System
<b>NAO</b>	National Audit Office
<b>NTT</b>	Notice to Treat



An aerial photograph of an industrial facility, possibly a water treatment plant, with a large blue overlay. The facility includes several large rectangular basins, various buildings, and piping. A road is visible on the left side. A central blue rounded rectangle contains the text "Executive Summary of Findings".

# Executive Summary of Findings



## Executive Summary of Findings

### Executive Summary

1. The Value for Money Section of the National Audit Office (NAO) carried out the performance audit: *'Acquisition of Property by Government'* during the period July 2002 – August 2003. The Land Department and the Estate Management Department are the principal units involved in the process to acquire property on behalf of government departments. Both departments fall within the remit of the Government Property Division (GPD) of the Ministry for Justice and Home Affairs. The main legislation regulating the acquisition of property by Government is the Land Acquisition (Public Purposes) Ordinance (LAO), which empowers the Commissioner of Land to acquire land<sup>1</sup> that may be required for a public purpose.

2. The objectives of the audit were to establish whether:

- i. policies and procedures related to land acquisition are clearly defined and implemented;
- ii. government departments (i.e. user departments) explore opportunities to minimise costs associated with land acquisition;
- iii. management of the land acquisition function by the GPD safeguards the interests of government, third parties and society in general;
- iv. management information related to acquired property is adequate.

3. The audit entailed the review of the acquisition process related to 30 government projects. These projects involved a total of 226 separate acquisitions of property from third parties.

4. User departments requesting land acquisition were not fully exploring opportunities to minimise land acquisition costs, in liaison with the GPD, for example, by considering alternative sites. Guidelines to this effect were not in place.

5. In the case of 107 out of the acquisitions sampled by the NAO, possession of the land was taken by the user department concerned before the legal acquisition process began. Such action may expose the Government to avoidable risks. Most of these acquisitions related to road construction.

6. There was no laid down procedure whereby, on completion of public projects and works, government departments were to inform the GPD of any land that remained surplus to their requirements. This diminished the GPD's control over land at its disposal.

7. Due to a lack of resources, the GPD was not in a position to maintain adequate management information to support the land acquisition process, including such critical information as the estimated value of funds owed to land owners by way of compensation. Outstanding cases were not readily identifiable. A major project to implement comprehensive IT facilities had fallen far behind schedule. Policies and procedures were either lacking or not documented.

<sup>1</sup> In the context of the LAO, the term 'land' includes any immovable property and related rights.

**8.** The processing of land acquisitions at the GPD was characterised by the lengthy delays to reach conclusive settlement. Out of the 226 acquisitions sampled, 114 were not yet concluded. 76 of them had been outstanding for more than 5 years; these included 40 acquisitions that had been outstanding for over twenty years, with the oldest cases dating back to 1951. Concluded acquisitions in the sample took an average of 5.6 years to reach settlement.

**9.** The most significant delay occurred in the course of identifying land owners. The 226 sampled acquisitions included 80 cases where the owners had not yet been identified.

**10.** Besides preventing owners from receiving timely compensation, the lengthy delays in the land acquisition process was proving to be financially burdensome to Government. The 83 acquisitions in the sample, where the relative values had not yet been determined, are particularly significant.

**11.** In such cases, the rate of appreciation of the value of land over time has a critical impact on the price that Government must eventually pay by way of compensation. An analysis of nine concluded acquisitions in the sample revealed that the lengthy delays to issue the Notice to Treat were proving to be costly to Government as higher prices than anticipated were being paid. Infact, Government incurred Lm165,000 more in a payment bill of more than Lm329,000 due to delay in determining prices. This was due to the increase in the value of land over time, arising out of an increase due to inflation, the cost of tied up funds, and a higher demand for an increasingly scarcer resource. In these nine instances, the percentage average change in the value of land ranged from 1.23 per cent to 21.29 per cent per annum.

**12.** The high proportion of land acquisitions occurring in the sample where the relative prices had not yet been determined, if extended to the entire population of unpaid acquisitions at the GPD,

could have a serious impact on Government funding requirements in future.

**13.** As a result of the amendments to the LAO, which came in force in March 2003, the price of expropriated land is determined, and ownership passes to Government, on publication of the President's Declaration. All outstanding acquisitions must henceforth be processed in terms of the updated legislation.

**14.** It is observed that the GPD was not maintaining reliable records of outstanding dues. The NAO was informed that the total debt stood at a book value of about Lm26 million. The book value neither includes possible damages/interest payable on settlement in view of delayed payment, nor takes into account potentially substantial increases in the value of land where prices had not been determined by the issue of Notices to Treat.

**15.** The GPD has been aware of the unreliability of its records as far back as 1995. In the circumstances, the NAO was not in a position to audit the GPD's debt records. This situation is a serious handicap in any initiative to establish an effective debt management programme.

**16.** Between 1998 and 2002, on average circa Lm2.64 million were being paid annually in reduction of outstanding dues. At this rate, it would take many years to settle all outstanding land acquisition debts.

**17.** The GPD's practice of settling the relatively smaller debts as a priority is not considered to be equitable and transparent.

**18.** The GPD's land valuation approaches and practices were not documented, and architect's reports on file stated only valuation figures. Verification of the GPD's valuations on the basis of set criteria was not possible.

**19.** Nevertheless, the NAO sought to analyse the GPD's valuations through various approaches:

- i. An independent architect was engaged to value a small number



of properties in the sample. There were significant variations between the two sets of valuations, however, the NAO's valuations were generally higher (range: between four and 156 per cent higher).

- ii. The NAO analysed the gap between the GPD's valuations and the owners' expectations of compensation, as evidenced by their counterclaims, in the case of 118 acquisitions that were referred to the LAB between 1998 and 2002. It was revealed that on average, owners' counterclaims were roughly three times higher than the valuations applied by the GPD.
- iii. The NAO compared LAB and GPD valuations in 12 relevant cases concluded between 1998 and 2002. Whilst the LAB agreed with the GPD's valuations in four instances and reduced the price in

one case by about four per cent, in the remaining seven cases the Board made upward revisions of GPD valuations, ranging from *circa* 67 to 396 per cent.

### Conclusions and Recommendations

**20.** The accumulation of outstanding dues by way of compensation payable to owners of land acquired by Government has been building up over time. Various factors contributed to the current situation, in particular the lack of reliable management information and accounting records, the lack of funds allocated for the acquisition of land, and costly delays in the acquisition process. Notwithstanding this scenario, a debt management strategy was not in place.

**21.** The NAO proposes several recommendations mainly targeted to achieve efficient management control of the land acquisition process, with a view to protect the interests of Government and land owners.





# Introduction

## Introduction

**1.1** The Value for Money Section in the National Audit Office carried out the performance audit: Acquisition of Property by Government. The Land Department and the Estate Management Department are the principal units involved in the process to acquire property on behalf of government departments, hereafter referred to as user departments,<sup>1</sup> unless otherwise stated. Both Directorates fall within the remit of the Government Property Division (GPD) of the Ministry for Justice and Home Affairs. This audit reviewed records up to December 2002.

### Audit concerns

**1.2** The delay to conclude land acquisition proceedings, the owners' right to the timely payment of compensation, and outstanding payments, are the basic concerns of this report.

### Background

#### Government policy

**1.3** The acquisition of property is one aspect of Government's overall management of its immovable property, which also includes maintenance, rent collection and disposal. The objective of the acquisition of private property is to enable Government to implement infrastructural works and other projects to the benefit of Maltese society. To this end, the GPD aims to ensure an equitable process for the acquisition of property that may be required for a public purpose.<sup>2</sup>

<sup>1</sup> For the purpose of this report, a user department includes any Government entity that requests the GPD's services for land acquisition.

<sup>2</sup> Source: GPD mission statement.

**1.4** The main legislation regulating the acquisition of property by Government is the Land Acquisition (Public Purposes) Ordinance (LAO). The LAO empowers the Commissioner of Land to acquire land that may be required for a public purpose. In the context of the LAO, the term '*land*' includes any immovable property and related rights.<sup>3</sup> The LAO stipulates procedures, which include compensation to third parties, that are to be followed in respect of the various types of acquisitions. Government can acquire property either by absolute purchase, or for possession and use for a stated period of time, or on public tenure.

**1.5** Occasionally, Government also acquired property from third parties by amicable agreement. Such acquisitions fall outside the scope of the LAO, which primarily regulates expropriation (forced acquisition) of property. In such cases, negotiations are carried out by the user department concerned. However, the Commissioner of Land appears on the contract as the buyer of the property.

**1.6** The large majority of property acquisitions in the past were of the type regulated by the LAO.

**1.7** The Administration of Lands Act 2002 introduced various amendments to the LAO. The main amendments are aimed to avoid the implications of the often lengthy and costly delay between the start of the acquisition process and the deed of purchase; ownership now passes to Government, and the value of compensation is determined, at the outset.

<sup>3</sup> Vide: Land Acquisition (Public Purposes) Ordinance, Paragraph 2 (Definitions).



### The land acquisition process

**1.8** The Land Department is mainly responsible for the acquisition of private property for a public purpose, in accordance with the provisions of the LAO, acting as agent for other government departments.<sup>4</sup> The relevant duties are carried out by the Legal team within its Enforcement section, and its Contracts section.

**1.9** The process consists of a series of stages leading to a deed of contract,

whereby ownership of the land acquired passes to Government against payment of compensation to the owner(s). Table 1 below lists the key stages in the chronological order generally followed, and indicates the departments that carried out each stage.

**1.10** Between 1998 and 2002, 179,666 square metres of land and 259 buildings were scheduled for acquisition. The relative properties were initially valued by the GPD at Lm5.9 million.<sup>5</sup>

Table 1 - Key stages within the land acquisition process

Key Stages	User department requiring acquisition	Ministry for Justice and Home Affairs	
		Government Property Division	
		Estate Management Department	Land Department
Submit official request for land acquisition	√		
Draw up plan and obtain initial valuation; seek to establish apparent ownership		√	
Submit up-front funds to the GPD <sup>6</sup>	√		
Arrange to publish the President's Declaration			√
Take possession of the acquired land, not before 14 days after the President's Declaration	√		
Confirm ownership			√
Issue Notice to Treat based on the current value of the acquired land, effectively freezing the value of compensation due <sup>7</sup>			√
Publish the deed of contract and pay compensation to owner(s)			√

Note: The last two stages in Table 1 are no longer applicable under the LAO as amended.

<sup>4</sup> The Land Department is also responsible for enforcement measures related to government property, including control inspections, lease termination, evictions, and the collection of ground rents.

<sup>5</sup> This figure excludes the value of 896 square metres of land and 71 buildings, as they had previously been acquired for possession and use on a rental basis, which rent was then being capitalised in order to obtain absolute purchase.

<sup>6</sup> Since 1994; vide paragraph 1.11.

<sup>7</sup> Subject to appeal before the Land Arbitration Board; excluding eventual payment of damages/interest, as applicable.

## Financial implications of land acquisition

**1.11** Since 1994, the Land Department has sought to limit the growth of the acquisition debt by requiring user departments that originate the need for acquisition to provide up-front the estimated value of the relative property as at the initial stage of the process.<sup>8</sup>

**1.12** In recent years, more funds were being made available in order to reduce outstanding dues, mainly in respect of acquisitions prior to 1994. Payments in respect of pre-1994 acquisitions amounted to Lm600,000 in 1998; payments in the following years ranged between Lm1 million and Lm3.2 million.

**1.13** Matters related to compensation issues, including outstanding dues to owners, are discussed in detail in Part 4.

## Audit objectives

**1.14** The audit examined whether:

- i. policies and procedures related to land acquisition are clearly defined and implemented;
- ii. user departments explore opportunities to minimise costs associated with land acquisition;
- iii. management of the land acquisition process by the GPD safeguards the interests of Government, third parties and society in general;
- iv. management information related to acquired property is adequate.

## Audit scope

**1.15** The audit scope included:

- i. the GPD's documented policies and objectives, in relation to the acquisition of government property;
- ii. the GPD's management structures and controls;

- iii. the GPD's systems and procedures;
- iv. the Estate Management Department's inventory system of acquired property;
- v. land acquisition files.

**1.16** In order to realise its objectives, the NAO reviewed the acquisition process related to 30 government projects selected at random from files at the GPD. These projects involved a total of 226 separate acquisitions of property from third parties. Land required by government acquisition often consists of various properties owned by different individuals; in such circumstances, the acquisition of each property is a separate process, which is undertaken for each specifically identifiable plot.

**1.17** In view of the significant policy change in respect of funding with effect from 1994 (vide paragraph 1.11), half of the cases were selected from projects prior to that date.

**1.18** The NAO was constrained to adopt this audit approach in the absence of reliable population sizes of acquisition projects and the relative parcels of lands and buildings, besides inadequate management information. Whilst the NAO did not carry out a statistically representative sample, the conclusions in this report apply for the cases examined, and results presented are considered to be indicative for the purposes of this audit.

## Methodology

**1.19** The audit objectives and scope were achieved through the following:

- i. review of the Division's documented policies and objectives;
- ii. review of the Division's systems, procedures and internal controls, in terms of the relevant property acquisition legislation;
- iii. collection and analysis of information relating to property

<sup>8</sup> Circular MF 9/93.



acquisitions from available manual, computerised and/or other electronic records;

- iv. interviews of key Division personnel responsible for, and involved in, the property acquisition process;
- v. land valuations by a consultant architect.

**1.20** The audit team utilised the services of:

- a legal consultant in connection with the interpretation of the LAO;
- an architect to carry out independent land valuations;
- a mathematician in connection with the analysis of value of land over time.

### Structure of the report

**1.21** The following chapters cover the primary issues addressed by the audit:

- Part 2 discusses the land acquisition process from the requesting user department's perspective, focusing on:

- whether user departments were exploring available opportunities to minimise acquisition costs;
- the timeliness whereby user departments took possession of land earmarked for acquisition;
- the acquisition of property by user departments outside the provisions of the LAO;
- the identification of land acquired surplus to requirements.

- Part 3 discusses management information available at the GPD, and the delay in time frames for completing the various stages of the acquisition process.

- Part 4 discusses the financial aspects of the acquisition function, including the availability of funds, valuation practices and the financial implications of delaying payment of compensation.

**1.22** The NAO's recommendations emerging from the audit are listed in Part 5: Conclusions and Recommendations, pages 36 to 38.





## The Role of User Departments

MINISTERU għall-POLITIKA SOĊJALI  
AWTORITA' TAD-DJAR HOUSING AUTHORITY  
Djar tal-Gvern favur l-Ambjent  
www.msp.gov.mt  
10 Appartamenti

## Part 2: The Role of User Departments

### Introduction

**2.1** In the course of its project plans, a user department would have identified land required for public use. If such land is not government-owned, the user department submits a formal request to the Government Property Division (GPD) for its acquisition. The user department can then take possession of the land in accordance with the provisions of the Land Acquisition (Public Purposes) Ordinance (LAO).

**2.2** The NAO review in this report included:

- The extent to which user departments were exploring alternative available options to meet their needs, in order to minimise acquisition costs.
- The timeliness whereby user departments took possession of the lands, in relation to the formal commencement of their acquisition.
- The implications of land acquisition by user departments outside the provisions of the LAO.
- The incidence of acquired land surplus to requirements.

**2.3** The 226 sampled land acquisitions (vide paragraph 1.16), involving six user departments, formed the basis of the NAO's review. These acquisitions were required for the construction of roads, schools, housing, administrative centres, waste management sites, a radar station and a public garden.

### Minimising the Cost of Land Acquisition

**2.4** User departments were not in a position to confirm that, where possible, opportunities to minimise costs, in connection with land acquisition, were fully explored, for example by considering less costly alternative project sites. Cost considerations in respect of land acquisition were given a low or no priority, in project plans carried out by or on behalf of user departments.

**2.5** According to the GPD, user departments, or planning organisations, where applicable, rarely consulted with it as the Government's estate manager, when selecting sites which would be utilised for their projects.

**2.6** There were no guidelines to the effect that such consultation with the GPD should take place. On its part, the GPD was evidently reluctant to bring its views on potential alternative sites to the attention of user departments. In a report to the Parliamentary Secretary dated 5 April 1995, the Land Department's Chief Architect and Civil Engineer stated that *'very few, if any, questions/suggestions regarding the location and/or extent of the project were referred back to the requesting body, on the assumption that the latter knows best....'* This situation prevailed at the time of the audit.

**2.7** According to the GPD, this resulted in the location of certain projects on more expensive sites than others that would have been available, and on sites larger than actually required.<sup>1</sup>

<sup>1</sup> Source: Letter to Parliamentary Secretary from the Land Department's Chief Architect and Civil Engineer dated 5 April 1995.



### Taking Possession of Land prior to Publication of the President's Declaration

**2.8** The audit revealed that in the case of 107 out of the 226 sampled acquisitions, possession of the land was taken by the user department before the legal acquisition process began, that is, prior to the issue of the relative President's Declaration, and, hence, in breach of the provisions of the LAO.

**2.9** 84 of these acquisitions were related to road construction projects and possession was taken between 0.5 and 98 months prior to publication of the President's Declaration. The Roads Department stated that works began prior to the publication of the President's Declaration in order to avoid delaying implementation of the Department's projects.<sup>2</sup>

**2.10** Whilst acknowledging the need for efficient implementation of projects, taking possession of private property prior to commencing the legal acquisition process exposed the Government to avoidable risks consequent to breaking the law.

**2.11** 23 acquisitions were related to housing projects. The taking of possession in these cases preceded publication of the President's Declaration by a range of between 14 and 96 months. In 22 cases, urgency due to dangerous buildings was given as the reason for premature possession.

### Land Acquisition outside the provisions of the LAO

**2.12** In exceptional cases, the price of land acquired or to be acquired was agreed upon between the owner and the user department, outside the provisions of the LAO (i.e. by amicable agreement, dispensing with the normal acquisition process, such as publication of a President's Declaration and issue of a Notice to Treat). The NAO sample included two such cases.<sup>3</sup>

<sup>2</sup> Delay in the pre-acquisition process, that is, between submission of an official request and publication of the President's Declaration, are discussed in Part 3.

<sup>3</sup> In one of these cases, negotiations were not concluded, and the land was acquired in accordance with expropriation procedures.

**2.13** In such instances, there is no laid down procedure whereby the agreed price would be confirmed as reasonable, independently from the user department. The GPD, which includes the Government's Estate Management Department, is not necessarily involved in the negotiations, even though the Commissioner of Land appears on the deed of contract.

**2.14** Section 13 of the LAO already provides for amicable agreement – between owners and the GPD - on the price of acquired land. The NAO feels that negotiation between a user department and an owner(s) that is not subject to independent supervision or control, for the purpose of acquiring land outside the provisions of the LAO, could lead to conflict of interests or abuse.

### Land Acquired Surplus to Requirements

**2.15** There was no evidence that, on completion of public projects and works, user departments were informing the GPD of any acquired land that was not utilised, and therefore remained surplus to requirements.

**2.16** User departments confirmed that they did not always include the identification of surplus land obtained through the acquisition process.

**2.17** Out of the 30 sampled projects covering 226 separate lands, two remained with surplus land.

**2.18** Out of 14 land acquisitions related to a road construction project, 11 properties, totalling 3379 square metres (55.8 per cent) were released by a President's Declaration in March 1996. These 11 parcels of land were returned to their owners 26 years after having been taken over by the Public Works Department, following a request by some of the owners. In this instance, the owners waived their rights to damages or any other form of compensation. The other case, also related to road construction, involved one small parcel of land.

**2.19** The possible existence of surplus land could not be determined in the case of 22 land acquisitions related to two projects.

These were very old projects (1957 and 1964), and the relative files, including site plans, could not be traced at the user departments concerned.

### **The Need for Guidelines and Control Structures in the Role of User Departments**

**2.20** User departments did not attach great importance to certain aspects of land acquisition. The user departments' conduct

in this respect could have been conditioned by a lack of guidelines and control structures. On several occasions, this attitude may have led to an outright breach of the law when possession of land earmarked for acquisition was taken prior to commencement of the due process of the law.

**2.21** The next section of this report will discuss the processing by the GPD of the user departments' requests for the acquisition of land by Government.

# The Land Acquisition Process

NOTIFIKAZZJONIJET TAL-GVERN  
Nru. 1126  
AKKWIST TA' ART

DIN iddikjarazzjoni li joġġa, magħmula mill-President ta' Malta bis-saħħa ta' l-Artikolu 3 ta' l-Ordinanza dwar l-Akkwist ta' l-Artijiet għal Skopijiet Pubbliċi (Kapitolu 88) lija rrapreżentata skond u għall-finejiet ta' l-Artikolu 9(1) ta' dik l-Ordinanza.

L-1 ta' Diċembru, 2003  
DIN iddikjarazzjoni tal-President ta' Malta tal-5 ta' April, 2002, liet liwien taħt imsejkenja kienet dikjarata madurja mill-awtorità kompetenti għal skop pubblika skond ta' disposizzjonijiet ta' l-Ordinanza dwar l-Akkwist ta' Artijiet għal Skopijiet Pubbliċi (Kapitolu 88) u li l-Akkwist tagħha kienet jkun b'raġi sħiħ.

ACQUISITION  
THE following declaration, made by Malta under section 3 of the Land Acquisition (Purpose) Ordinance (Chapter 88), is published for the purpose of section 9(1) thereof.

L-1 ta' Diċembru, 2003  
Dikjarazzjoni ta' l-ART

L-1 ta' Diċembru, 2003  
Dikjarazzjoni ta' l-ART



## Part 3: The Land Acquisition Process

### Introduction

**3.1** This section of the report discusses the various stages of the acquisition process. The NAO audit utilised the GPD's records and available management information.

**3.2** Prior to the recent amendments to the LAO, as stipulated in the Administration of Lands Act 2002, the process at the GPD consisted of five steps, generally in the following chronological order: *pre-acquisition work* (request from the user department to President's Declaration); *publication of the President's Declaration*; *confirmation of ownership*; *issue of the Notice to Treat to land owners*; and *payment of compensation*. As a result of the amendments, which came in force in March 2003, the price of the land is now determined upon publication of the President's Declaration, and, therefore, the Notice to Treat (NTT) has become obsolete.

**3.3** The issues raised in this section of the report are:

- the inadequacy of management information at the GPD, and its impact on the Division's operations;
- delay in the various stages of the acquisition process, focusing on:
  - concluded acquisitions;
  - outstanding acquisitions;
  - acquisitions referred to the Land Arbitration Board.

### Inadequate management information

**3.4** Key information relating to the acquisition process was not easily accessible. The GPD's files did not contain history sheets that would enable a quick assessment of the current status of individual property acquisitions. An IT database recording the history and current status of all acquisitions was not maintained.<sup>1</sup> This meant that the NAO had to generate its own indicators from information found in the hard files.

**3.5** Manual records held by the GPD were incomplete. Two files from the NAO sample of 226 acquisitions could not be found at the time of the audit. A number of documents were missing: in 27 cases, there were no documents to evidence that ownership was confirmed, whilst 35 Notices to Treat were not traced. These missing documents mainly related to files over 40 years old. In addition, documents in many of the older files, some of which were still outstanding, were in poor physical condition.

**3.6** The GPD's voluminous records were not properly safeguarded, particularly against the risks of fire and unauthorised access. At the time of the NAO audit, there were no measures to detect and deal with a potential fire.

**3.7** Inadequate management information hampered the GPD's decision-making process as regards prioritisation of

<sup>1</sup> The GPD was planning to implement comprehensive IT facilities, and a call for the submission of tenders was advertised in February 2003 in connection with the Land and Estate Management Department Information System (LEMIS) project. This project began in 2000, and was originally targeted for completion in 2004. However, the project has fallen far behind schedule.

its work and to ensure that settlement with owners, given the limited available funds, was transparent and fair. Moreover, valuable assets such as land should be recorded meticulously.

### The Acquisition Process

#### Pre-Acquisition

**3.8** Whilst the President's Declaration marks the legal commencement of the land acquisition process, certain work must be carried out before it can be published. This includes a formal request by the user department, endorsed by the Minister, preparation of plans, and, since 1994, the submission of funds in accordance with the GPD's initial valuation. Delay at this stage can delay projects, as the user department should not legally take possession of land earmarked for acquisition before publication of the President's Declaration, as stipulated in the LAO. However, possession did happen on various occasions (vide paragraphs 2.8 to 2.12).

**3.9** The NAO assessed the lapse of time between the submission of official requests by user departments and the publication of the relative President's Declarations in the case of acquisitions since 1994. Table 2 illustrates the average time frames for acquisitions within the NAO sample, analysed by project type.

**3.10** There were no guidelines to establish and control the timeliness of the pre-acquisition process. The fact that certain cases were processed in as short a time as two months suggests that the time scales indicated in Table 2 can hardly be justified. Delay was generally experienced in the initial work carried out at the GPD, and/or the submission of plans/up-front funds by user departments. The GPD cited a lack of resources as the main contributory factor.

#### Concluded Acquisitions

**3.11** Out of the 226 land acquisitions examined, 101 (44.7 per cent) were concluded.<sup>3</sup> The time frames taken to process these acquisitions appear in Chart 1.

**3.12** On average, the acquisitions took 5.6 years to conclude, between publication of the President's Declaration and payment of compensation to owners; it took 3.6 years to confirm the identity of owners, a further three months for the issue of NTTs and another 1.6 years until final settlement.

**3.13** Chart 1 indicates that the main delay occurred in the process to confirm ownership of the lands being expropriated - on average, 64 per cent of the process time was taken to reach this stage. The result of such delay, in the light of the GPD's practice, determined by prevailing circumstances,<sup>4</sup> not to issue Notices to Treat before confirming

Table 2 – Delay in the Pre-acquisition process

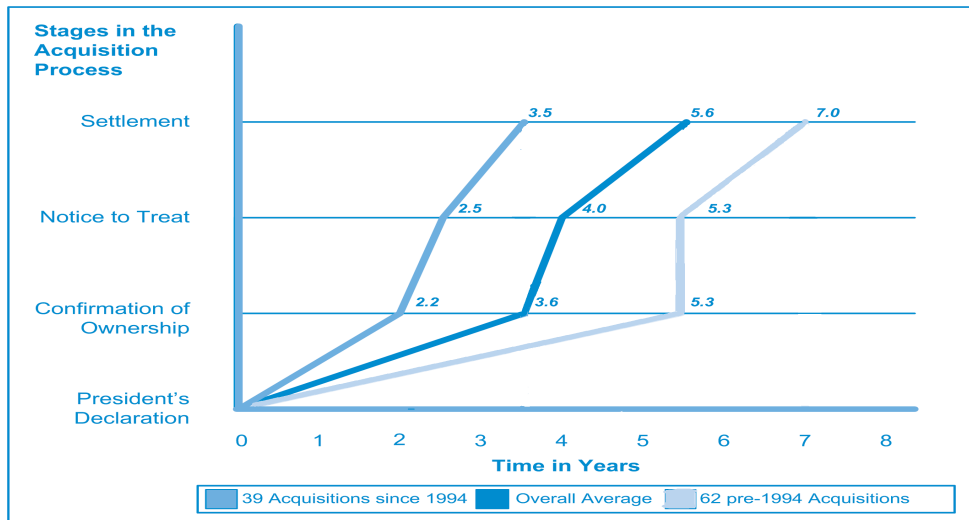
Project type	Number of separate acquisitions involved	Range of time between official request by the user department and publication of the President's Declaration (months)
Education	15	17 – 26
Housing	25	11 – 14
Roads	55	2 – 39
Other <sup>2</sup>	6	11 – 85

<sup>2</sup> Includes a waste management site where the President's Declaration was issued seven years after the user department's request: this accounts for the wide range of elapsed time in the case of the six 'Other' acquisitions.

<sup>3</sup> A further 11 properties were released to the owners prior to the conclusion of the acquisition process.

<sup>4</sup> In this connection, 'circumstances' refer to a lack of resources cited by the GPD.

Chart 1 – Cumulative Average Time-Intervals between the Key Stages of Concluded Acquisitions



the identity of the relative land owners, was to postpone determination of the prices payable to owners, with a consequent negative impact on Government finance, as discussed later in this report. The LAO did not preclude the GPD from determining the prices of the relative lands even if their owners were still not identified. However, some improvement was registered in this stage of the acquisition process since 1994, mainly due to the outsourcing of legal work. Whilst, on average, pre-1994 acquisitions took 5.3 years to establish root of title, the average duration in the case of acquisitions since 1994

was 2.2 years - still considered to be an unreasonably long time.

#### Outstanding Acquisitions

**3.14** Table 3 indicates that by the end of 2002, 114 (50.4 per cent) of the sample were not yet concluded. One of these cases was in the process of acquisition by amicable agreement, which did not require publication of a President's Declaration and issue of a Notice to Treat. The NAO analysed the remaining acquisitions in terms of the relative time scales and stages reached in the process.

Table 3 – Position of Outstanding Sampled Acquisitions at end 2002

Number of years since publication of the President's Declaration	Total number of outstanding acquisitions	Position of Outstanding Acquisitions at end 2002			
		Identification of the land owners not yet confirmed	Land ownership confirmed, but Notices to Treat not yet issued	Pending judgement by the Land Arbitration Board	Awaiting payment of compensation
1 to 5	37	25	0	7	5
6 to 10	30	18	3	6	3
11 to 15	3	2	0	0	1
16 to 20	3	2	0	0	1
Over 20	40	33	0	2	5
<b>Totals</b>	<b>113</b>	<b>80<sup>5</sup></b>	<b>3</b>	<b>15</b>	<b>15</b>

<sup>5</sup> Includes two acquisitions for which the relative files could not be found.



**3.15** 76 (33.6 per cent) acquisitions out of the sample had been outstanding for more than five years, and include 40 acquisitions (17.7 per cent) that had been outstanding for over 20 years. These lengthy periods of elapsed time were due to various factors at each stage of the process.

### Land Owners not Identified

**3.16** In the case of 80 out of the 226 acquisitions sampled (35.4 per cent), the owners of the lands had not yet been identified. The oldest cases dated back to 1951.

**3.17** Given the practice that the GPD was not issuing NTTs prior to the formal identification of the relative land owners, the very high proportion of acquisitions in the NAO sample where the land owners had not yet been identified has serious financial implications in connection with the determination of funds payable for expropriated land.

**3.18** Various factors contributed to the delay to confirm the identity of land owners:

- the lack of historic land ownership records/registration;
- inadequate administrative capacity;
- the owners themselves not coming forward;
- further administrative work upon the death of previously identified owners; and
- the incidence of owners living overseas.

**3.19** Since 1997, the GPD has been outsourcing the legal work in connection with the confirmation of land ownership. This strategy resulted in a reduction in the average time scale to conclude this process.

### Issue of the Notice to Treat

**3.20** In the case of acquisitions by absolute purchase from unknown owners, the

GPD could have issued Notices to Treat, and deposited the compensation funds in Court. However, it was the GPD's practice not to issue Notices to Treat before confirming the identity of the relative land owners (vide paragraph 3.13).

**3.21** This practice led to a delay in freezing the relative prices with the issue of Notices to Treat for a total of 83 out of the sample (36.7 per cent). The delay has serious implications for eventual funding requirements, due to the increase in land values over time. This issue is discussed in more detail in Part 4 of this report.

**3.22** The recent amendments to the LAO stipulate that prices are to be frozen immediately upon publication of the President's Declaration, thereby determining the values of lands in the process of acquisition at the outset.

### The Land Arbitration Board

**3.23** The LAO provides for the establishment of a Land Arbitration Board (LAB), which allows owners of land to challenge the value determined by the GPD. The LAB is competent *inter alia* to 'assess the amount of compensation payable under any of the provisions of this Ordinance (the LAO).....'. All the Board's members are appointed by the President of Malta. The Chairman is '... a person who holds or has held the office of judge or a person who holds the office of magistrate;' the other members of the Board are architects and civil engineers.

**3.24** The LAO provides that an owner could decline to accept the GPD's proposed compensation, within 21 days of the date of service of the relative judicial act,<sup>6</sup> The case would then be referred to the LAB by the GPD.

**3.25** Table 4 shows the number of cases, in comparison with NTTs issued between 1998 and 2002, where owners opted to apply for review by the LAB.

<sup>6</sup> Prior to March 2003, the Notice to Treat.

Table 4 – Notices to Treat issued between 1998 and 2002 referred to the LAB

	Number of Notices to Treat issued by the GPD <sup>7</sup>	Number of Notices to Treat referred to the LAB by end 2002	Percentage of cases referred to the LAB
1998	67	32	48%
1999	100	34	34%
2000	165	42	25%
2001	208	53	25%
2002	108	18	17%
Totals	648	179	28%

**3.26** Table 4 indicates that, although in a declining trend, a significant numbers of owners disputed the GPD’s proposed compensation for their lands (or any other aspect of the acquisition process).

**3.27** The NAO examined files at the GPD and the LAB, for the period 1998 – 2002, in order to assess the impact of the LAB process on the time scales leading up to payment of compensation.

**3.28** Between 1998 and 2002, a total of 217<sup>8</sup> new cases were referred to the LAB. Over the same period, the LAB finalised<sup>9</sup> only 81 of the outstanding cases, leaving a running balance of 261 pending cases as at end 2002.

**3.29** 44 out of the 81 finalised cases (54 per cent) were, in fact, abandoned by the LAB, following loss of contact with applicants. On average, these 44 cases had been outstanding at the LAB for over 18 years. A further 12 cases (15 per cent) were abandoned by the applicants themselves. On average, these cases had been outstanding at the LAB for almost six years.

**3.30** The 25 cases decided upon took an average of over six years to reach conclusion.

**3.31** The LAB’s case throughput was creating another bottleneck towards final settlement in the land acquisition process. It is doubtful whether the notion of redress within a reasonable period of time was being fulfilled.

**3.32** The function of the LAB is an integral part of the land acquisition process; the efficiency of its operations has a material bearing on the notion of redress within a reasonable period of time, and the timely payment of compensation.

#### Payment of Compensation

**3.33** Despite the issue of Notices to Treat, and, where applicable, judgement by the LAB, compensation for 15 acquisitions in the sample (6.6 per cent) had not yet been provided to the relative owners (vide Table 3). These acquisitions included:

- Five cases where final procedures were in train.

<sup>7</sup> A Notice to Treat may cover more than one property/owner.

<sup>8</sup> The difference between this figure and the 179 NTTs referred to the LAB as stated in Table 4 mainly relates to NTTs issued prior to 1998.

<sup>9</sup> In this context, ‘finalised’ refers to cases that were either decided upon or abandoned by the LAB, or ceded by the owners.

- Two cases where funds had not yet been provided by the user departments (Lm21,530).
- One case where there was doubt whether the acquisition would be concluded, since possession of the land had not been taken by the relative user department.
- One case which remained outstanding, pending the establishment of a Church Tribunal, in accordance with the provisions of the 1992 Church-State Agreement. (This case involved a claim for Lm604,000).
- Six cases, five of which had been outstanding for over 20 years, where progress stalled mainly due to administrative shortcomings.<sup>10</sup>

### Implications of the Delay in Determining Prices of Land Acquisitions

**3.34** The NAO sample revealed lengthy delay in determining prices of land acquisitions. The delay has a negative impact on the final payment of compensation to land owners, due to the increase in the value of land over time. Financial implications related to delayed land price determination are discussed in the next part of this report.

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<sup>10</sup> Missing or unclear information, and oversight.





An aerial photograph of an industrial facility, possibly a refinery or chemical plant, with a blue overlay. The facility features numerous large storage tanks, processing units, and a complex network of pipes and roads. The surrounding area includes a body of water with several ships and a residential or commercial area with buildings and parking lots. A central blue rounded rectangle contains the text "Compensation Issues".

# Compensation Issues

## Part 4: Compensation Issues

### Introduction

**4.1** This section discusses the financial aspects of the acquisition function. For this purpose, the NAO reviewed issues relating to:

- the availability of funds;
- the GPD's valuation practices;
- the implications of delay in determining the value of acquisitions.

### Availability of Funds

**4.2** Prior to 1994, the practice was that all acquisitions were funded from budgets allocated under a common capital expenditure vote, managed by the Land Department. In 1994, it was decided that user departments would henceforth finance land acquisitions out of their own budgets. Compensation for outstanding acquisitions up to 1994 would continue to be funded through the Land Department's budget. During the last five years, an average of Lm1.75 million were being paid annually in respect of land acquisitions arising before 1994, besides a further annual average of Lm0.89 million for acquisitions since that year.

**4.3** The GPD submitted documents to the NAO indicating an outstanding book value of about Lm26 million.

- The book value was based on records entered manually in a charge book covering the period from 1972 up to 1999, and spreadsheet records in use since year 2000. The entries, however, were not processed in accordance

with generally accepted accounting principles, for instance, individual creditor/property accounts were not maintained, and no periodic accrual of estimated outstanding debts was carried out. The GPD did not have a policy to factor in, periodically, estimated changes in land values. Under these circumstances, the NAO was not in a position to audit the GPD's debt records.

- The GPD was well aware of this situation as far back as 1995, when the then Commissioner of Land, reported that it was almost impossible to quantify the outstanding debt '*...as there exists only a crude register of expropriations carried out, which contains the barest of information, and which might in fact be giving a very wrong impression*'.<sup>1</sup>
- In the same communication, it was stated that '*the collection of relevant data to establish the tens of millions of Maltese Liri involved has to be carried out from each particular Land file; a daunting task to say the least, as this envisages the vetting of a large number of complicated files*'.<sup>2</sup>

The situation which is still prevailing is a serious handicap in any initiative to

<sup>1</sup> Source: Letter to Parliamentary Secretary from the Land Department's Chief Architect and Civil Engineer dated 5 April 1995.

<sup>2</sup> As above.



establish an effective debt management programme.

### Priority of Compensation Payments for Concluded Acquisitions

**4.4** The NAO was informed that, given the limitations on the availability of funds from its Capital Vote to pay outstanding dues in respect of pre-1994 land acquisitions, it was the GPD's practice to settle the relatively smaller debts as a priority. The NAO confirmed that this practice was generally being followed, after sighting records on lists of outstanding debts maintained by the GPD, from which items were being selected for payment.

**4.5** However due to lack of management information, it was not possible to verify the completeness of these lists.

**4.6** The NAO considers that the GPD's practice to give priority to the relatively smaller debts, rather than follow a normal chronological order, was not equitable, as it discriminated against the larger creditors. Neither was this good practice, since it was not formulated as a policy, and creditors had no indication when they would receive payment.

### Land Valuations

#### The GPD's Valuation Practices

**4.7** Valuations of acquisitions are determined by architects, recommended by the Director General and approved by the Permanent Secretary. Architects were recommended on the basis of their experience in the valuation of expropriated land.

**4.8** Various factors are taken into account in a valuation exercise, including land area, topography, configuration and shape, land use designation, surrounding land use, and relevant market prices. Architects' considerations on valuation reports at the GPD were non-existent, and only the value amounts were shown on file. Verifying such valuations, on the basis of tangible criteria determined by the LAO, was not possible.

**4.9** The GPD's valuation methodology and practices were not documented. However, informal meetings of the architects engaged by the Division were held to share experiences and discuss approaches, in order to ensure that consistency is maintained. Minutes of meetings were not kept.

#### Independent Valuations by the NAO

**4.10** The NAO sought to confirm the reasonableness of valuations carried out by the GPD by engaging an architect to examine recent valuations. A small number of land acquisitions in the sample was selected for the exercise.

**4.11** The NAO architect's definition of value, with particular reference to valuations relating to compulsory land acquisition, together with the relative valuation procedures, appear in Appendix I.

**4.12** It results that there is a lack of consistency between the sets of valuations appearing in Table 5. Whilst valuations by the GPD and the NAO in three of the seven cases can be considered to fall within comparable limits, valuations in the remaining four cases exceeded the GPD's valuations by a range of 54 to 156 per cent.

**4.13** During discussions with the GPD, possible reasons for discrepancies emerged as follows:

- Whilst it was confirmed that valuations by the NAO and the GPD architects were based on the same criteria, there is a strong element of subjectivity, which could lead architects to apply different weightings to various factors.
- Section 12 (1) of the LAO provides that the GPD's valuation should reflect what it is '*willing to pay for the land*'. This provision could be interpreted as granting discretion to the GPD when establishing land values. On the other hand, Section 27 (1) (b) provides that '*the value of the land shall ..... be taken to be the amount which the land if sold*

Table 5 - Comparison between NAO and GPD Valuations

Area (sq. m)	Land type <sup>3</sup>	Latest GPD valuation Date	GPD valuation	NAO valuation	Difference in value between the NAO and GPD valuations	Percentage difference between the NAO and GPD valuations
			Lm	Lm	Lm	
591	BS	16-Jan-00	31,150	79,785	48,635	156.13%
528	BS	04-Sep-00	42,600	44,352	1,752	4.11%
240	BS	28-Feb-01	12,900	20,160	7,260	56.28%
410	BS	08-Mar-01	31,770	49,200	17,430	54.86%
165	BS	08-Mar-01	15,540	13,860	-1,680	-10.81%
2886	A+BS	23-Oct-01	125,000	215,196	90,196	72.16%
442	BS	22-Feb-02	53,000	59,670	6,670	12.58%

Note: The NAO is limiting presentation of comparisons to recent GPD valuations in order to avoid potential distortions due to the subjectivity associated with historic land value growth rates.

*in the open market by a willing seller might be expected to realise*, implying that such valuations should be realistically based on prevailing market conditions. The GPD contended that, in case of disagreement, owners can seek redress from the Land Arbitration Board.

- The NAO's legal advisor is of the opinion that land in the process of acquisition by Government should be valued strictly in accordance with the provisions of the LAO, without the influence of any weighting due to its intended use.

#### Valuations by the Land Arbitration Board

**4.14** Owners disagreeing with the GPD's valuations can seek redress from the

LAB. Between 1998 and 2002, an average of 28 per cent of NTT valuations were challenged by owners.

**4.15** On the basis of cases referred to the LAB in the last five years, the NAO sought to determine a general profile of owners that are likely to contest the GPD's valuations of expropriated lands. However, available records were not sufficient to form an opinion.

**4.16** The NAO sought to assess the gap between the GPD's valuations and the owners' expectations of compensation, as evidenced by their counterclaims, in the case of 119 acquisitions<sup>4</sup> that were referred to the LAB between 1998 and 2002, where owners submitted specific counterclaims relating solely to value. This information, as at Table 6, was provided by the GPD.

<sup>3</sup> A = Agricultural Land; BS = Building Site.

<sup>4</sup> 60 cases were excluded from the 179 referred to the LAB between 1998 and 2002 (vide Table 4): 36 cases where owners did not submit specific counterclaims; 11 cases where Government had previously acquired the properties

for public tenure or possession and use; one case where the land area was also being contested; and two cases where reference to the LAB was not related to valuation; the remaining 10 properties were acquired for public tenure/possession and use.

Table 6 – Cases referred to the LAB between 1998 and 2002 – Differences between GPD Valuations and Owners' Counterclaims

Year of issue of the relative NTTs	Number of NTTs referred to the LAB	NTT valuations Lm total	Owners' counterclaims Lm total	Percentage differences
1998	20	248,836	797,250	220.39%
1999	24	860,782	3,169,227	268.18%
2000	29	684,111	3,152,314	360.79%
2001	34	715,726	3,221,805	350.15%
2002	12	253,645	1,029,615	305.93%

 Table 7: Cases concluded by the LAB between 1998 and 2002 – Differences between Valuations by the GPD and the LAB<sup>5</sup>

Year of LAB decision	Land area or Building	GPD valuation for the Notice to Treat Lm	LAB valuation Lm	Percentage difference between LAB and GPD valuations
1999	Building	4,504	16,500	266.34%
2000	Building	6,187	12,850	107.69%
2000	Building	934	2,224.50	138.17%
2000	1120 sq.m	139.47	251	79.97%
2000	Building	72.52 p a	69.65 p a	-3.96%
2001	2846 sq.m	2,558.85	4,861	89.97%
2001	294 sq.m	198	198	-
2001	Building	5.29 p a	26.25 p a	396.22%
2001	Building	13.30 p a	13.30 p a	-
2002	278 sq.m	139	139	-
2002	Building	467.40	467.40	-
2002	Building	8.40 p a	14 p a	66.67%

<sup>5</sup> Out of the 25 cases concluded by the LAB between 1999 and 2002, 13 were excluded from Table 7 in the absence of comparable valuations.



**4.17** Table 6 indicates that, on average, owners seeking redress from the LAB were claiming roughly three times the values applied by the GPD to the lands that were being acquired.

**4.18** Cases concluded by the LAB between 1998 and 2002 were analysed in order to compare valuations by LAB architects with the GPD's valuations when determining prices for the purpose of issuing Notices to Treat. Table 7 refers. Most of the acquisitions in this table were valued by the GPD in the 1990s.

**4.19** Table 7 indicates that:

- In seven out of the 12 cases, the LAB applied higher valuations than the GPD, on a percentage basis ranging between 67 and 396 per cent.
- In the remaining five cases, the LAB's valuations were the same as the GPD's, except for one which was marginally lower.

### Potential Conflicts of Interest

**4.20** With reference to cases concluded by the LAB between 1999 and 2002, whilst the NAO confirmed, from available records,<sup>6</sup> that none of the architects involved in the GPD valuations also valued the same properties for the LAB, it was observed that two architects currently appointed on the LAB also appear on the list of architects contracted to carry out valuations of lands in the course of expropriation, on behalf of the GPD. This could lead to conflicts of interest. The GPD was to seek legal advice on this issue.

### Financial Implications of the Delay in Determining the Value of Land Acquisitions

**4.21** The lengthy delay to determine the price of acquisitions has a negative impact on the final payment of compensation to land

<sup>6</sup> In six cases, including three for which the relative Court files were not produced at the time of the audit, the names of the architects who carried out valuations for the LAB were not found. (The names of these architects were not recorded in the relative GPD files).

owners. Out of the 226 random-sampled acquisitions, the values of 83 had not yet been determined by the end of 2002; 33 of them had been outstanding for over 20 years.

**4.22** The value of land increased over time due to three factors: inflation, opportunity cost (interest rate forgone in equivalent investment in monetary terms) and the intrinsic value of land (the scarcer it becomes, the higher its value).

**4.23** The NAO sought to assess whether delay in determining the value of land in the process of acquisition led to a situation whereby Government incurred unnecessary higher costs.

**4.24** If the growth rate of the real value of land increases over time, any delay in freezing the price of acquired land would result in increased costs. The rate of appreciation of the value of land over time has a critical impact on the price that Government must eventually pay by way of compensation, in those cases where the value of expropriated lands has not yet been frozen.

### Land Value Growth Rates

**4.25** The rate of growth of the value of land is a highly elusive concept to render into a reliable, quantifiable factor. This is mainly due to lack of national data.

**4.26** The NAO, therefore, sought to determine, in simple terms, the average land value growth rate for acquisitions in the sample where both an initial valuation and a revaluation for the purpose of issuing the Notice to Treat were on record at the GPD. Appendix II explains the approach used in this exercise.

**4.27** Table 8 indicates the annual intrinsic land value growth rates, after adjusting for inflation and opportunity costs, of nine acquisitions in the sample, where the dates of initial valuations and the final determined prices ranged between 1973 and 2002.

**4.28** The NAO was not in a position to determine whether the growth rates shown in Table 8 (column 9) reflect the market or otherwise. At best, they could be compared with the value growth rates of 6.98 per cent

Table 8 – Additional Costs Incurred - The Intrinsic Growth in the Value of Land<sup>9</sup>

Area (sq.m)	Land type	Initial valuation date	Initial valuation Lm	NTT date	NTT valuation Lm	'Present value' of initial valuation at NTT date	Intrinsic value change of land Lm	Percentage annual average change in the intrinsic value of land
(1)	(2)	(3)	(4)	(5)	(6)	(7)	(8)	(9)
219	BS	27-Apr-73	29	30-Dec-98	8,812	201	8,611	15.85%
112	BS	27-Apr-73	15	30-Dec-98	4,500	103	4,397	15.85%
770	A+BS	19-Apr-85	502	29-Apr-94	1,105	990	115	1.23%
4917	A+BS	02-May-89	22,436	28-Mar-01	116,000	54,892	61,108	6.48%
334	BS	01-Jul-96	12,000	02-Sep-02	62,850	19,082	43,768	21.29%
2886	A+BS	06-Aug-96	55,709	23-Oct-01	125,000	82,429	42,571	8.31%
31	BS	05-Nov-97	375	14-Aug-01	840	498	342	14.86%
271	BS	05-Nov-97	3,279	18-Oct-00	6,780	4,093	2,687	18.63%
1462	A	19-Jan-98	880	20-Sep-02	3,000	1,250	1,750	20.62%

Notes: The original estimates (column 4) were adjusted for inflation and opportunity costs in order to reflect their equivalent present values as at the date of price determination (column 7). The differences between the determined prices (column 6) and the resultant present values of the original estimate (column 7) were considered to reflect the growth in the intrinsic value of land (column 8) due to a higher demand for an increasingly scarcer resource, which the GPD incurred as a result of delay in determining the values of the relative acquisitions.

per annum for apartments in various areas since 1982,<sup>7</sup> and 22.56, per cent per annum for plots during the period 1989 to 1999.<sup>8</sup>

**4.29** The nominal interest rate (inflation and real interest rate) was assumed at 7.8 per cent to reflect the highest rate for long term government stock issued to date. Long term bonds issued by Government during the periods under review did not differ significantly from this rate. Government would have

incurred these costs if the GPD decided to pay on the date of initial valuation.

**4.30** In the nine cases shown in Table 8, Government could have made a saving of circa Lm165,000 had price determination not been delayed.

#### Outstanding Acquisitions

**4.31** The proportion of unpaid land acquisitions occurring in the sample, where

<sup>7</sup> Sourced from an updated paper by D. H. Camilleri dated 9 July 2001 concerning 'Housing Affordability in Malta'.

<sup>8</sup> Adapted from a set of average prices listed in a paper by

G Bonnici presented at the conference 'Housing Affordability in Malta' on 4 November 1999.

<sup>9</sup> Calculated on the basis of GPD valuations.

the price of the land had not yet been frozen by the end of 2002, was high at 36.7 per cent - 83 such cases emerged in the NAO sample of 226 acquisitions.<sup>10</sup> This level of incidence is considered to be a cause for concern. In the light of the analysis above, such cases could have a serious impact on Government funding requirements in future.

**4.32** The recent amendments to the LAO, as stipulated in the Administration of Lands Act 2002 (vide paragraph 1.7), are expected to have a positive impact in limiting the escalating level of funds required to fund

the acquisition process in future, by freezing the price of the acquired land as at the date of the President's Declaration, rather than the date of issue of a Notice to Treat. This means that the values of acquisitions are determined at the earliest possible time. The Act came in force in March 2003.

**4.33** Availability of funds, valuation practices and value determination dates of acquisitions discussed in this section are critical issues that should be given the highest priority attention.

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<sup>10</sup> The NAO sample is indicative and not representative, in view that the GPD did not maintain sufficient management information to establish reliable population sizes, including the actual number and value of outstanding, unpaid, land acquisitions.





## Conclusions and Recommendations

## Part 5: Conclusions And Recommendations

### Conclusions

**5.1** Accumulated outstanding dues in respect of compensation payable to owners of land acquired by Government have been building up over time. These outstanding dues have been crudely estimated by the GPD to have a book value of about Lm26 million as at end 2002. However, the NAO considered this figure to be unreliable, and it lacked an audit trail. Various factors contributed to the current situation.

**5.2** The land acquisition process was characterised by delay in its various stages. A significant component in the overall delay was the practice adopted by the GPD, determined by prevailing circumstances, not to issue Notices to Treat, thereby freezing the values of lands in the process of acquisition, before confirming the identity of the relative owners. During periods of high land value growth, this practice resulted in additional costs for Government.

**5.3** Insufficient funds were budgeted for the acquisition of land by Government. Consequently, the GPD could not pay timely compensation to all owners.

**5.4** The acquisition process was not supported by adequate management information systems. The number of outstanding acquisition cases awaiting settlement and the full amount due to owners were not known. In the absence of such critical management information, the GPD's planning and controlling capabilities with respect to processing acquisitions were significantly diminished.

**5.5** It also proved to be problematic for the GPD to ensure the fair and equitable distribution of the limited funds available by way of compensation to owners of expropriated lands. The GPD's operations, in this regard, were further handicapped by the general absence of operational policies and formalised procedures.

**5.6** Similarly, the absence of relevant policies and procedures led to a situation whereby user departments rarely consulted with the GPD – the Government's estate manager – when selecting sites which could be utilised for their projects. Moreover, on various occasions user departments exposed Government to avoidable risks by taking possession of private property identified for acquisition before the legal process commenced through the GPD.

**5.7** If and when current initiatives to computerise the Division's records are in place, the GPD should be in a position to manage the land acquisition process much more efficiently. Recent amendments to the Lands Acquisition Ordinance, which stipulate that prices are determined at the outset of the process, should act to diminish the rate of escalation of funds owed to land owners. On the other hand, the level of debts in respect of past acquisitions for which prices have not yet been determined will continue to increase, to the detriment of Government, for as long as the intrinsic value of land maintains a rising trend.



### Recommendations

**5.8** The National Audit Office proposes that the relevant government units concerned consider implementing the following recommendations:

#### The Role of User Departments

**5.9** The recommendations in this section concern government departments that request the GPD to acquire private property on their behalf.

- i. Guidelines should be issued so that user departments liaise with the GPD in order to identify opportunities to minimise land acquisition costs.
- ii. Possession of private property should not be taken prior to the legal commencement of the acquisition process.
- iii. Where, in exceptional cases, the price of land acquired or to be acquired is negotiated directly between the user department and the owner, the agreed price should be subject to confirmation by the GPD in its role as the Government's estate manager.
- iv. A procedure should be introduced whereby, on completion of projects, user departments are to inform the GPD of any acquired land remaining surplus to their requirements.

#### The Land Acquisition Process at the Government Property Division

**5.10** The recommendations in this section are directed at the Government Property Division.

- v. Appropriate time frames for all stages of the land acquisition process, as redefined by the amended LAO, should be established in order to ensure that the interests of Government and land owners are adequately safeguarded.

- vi. The implementation of appropriate management information systems should be addressed as a matter of priority. The GPD is also to maintain appropriate accounting records relating to outstanding acquisitions; this would require a policy decision to factor in, periodically, estimated changes in land values. The GPD would then be in a position to establish the current status of each outstanding acquisition, and to estimate amounts owed to individual owners. In turn, this would permit the exercise of appropriate management control over the entire process.
- vii. Land acquisition records should be adequately safeguarded against material risk (fire, deterioration and theft).

#### Compensation Issues

**5.11** The recommendations in this section are mainly directed at the Government Property Division and the Ministry responsible for finance.

- viii. The GPD, together with the Budget Office of the Ministry of Finance and Economic Affairs, are to establish a strategy to settle outstanding debts related to acquired land. Such a strategy is to address issues relating to budget allocations and the prioritisation of settling outstanding cases.
- ix. The current practice whereby Architects appointed by the GPD to determine valuations of expropriated land also serve on the Lands Arbitration Board, albeit with regards to separate cases, should be curtailed. This would ensure that situations leading to potential conflict of interests are avoided.
- x. The GPD is to document criteria related to the valuations of



expropriated land. Valuations of expropriated land determined by architects appointed by the GPD are to be backed by valuation reports indicating the relative factors which were taken into consideration. Moreover, the GPD

should establish a procedure to ensure that such valuation reports are, as a matter of course, reviewed for their reasonableness. Such an approach should ensure a more transparent process of valuations of expropriated lands.



# Appendices





## Appendix - I

### Report on Procedures

for

Valuation of Compulsorily Acquired Land

June 2003

## 1.0 Introduction

### 2.0 Definition of value in term of valuation with particular reference to valuations under compulsory acquisition

### 3.0 Procedures in establishing current market value for plots of land

### 4.0 Procedures in establishing historic market value for plots of land

## 5.0 Conclusion

## 1.0 Introduction

1.1 This report deals with issues concerning the valuation of Land acquired under the provisions of the Land Acquisition Ordinance (LAO) and refers to the transfer of plots of land under conditions of compulsory purchase.

1.2 The legislation places land under three categories, viz. buildings site, agricultural land and wasteland.

1.3 A building site is defined by the location of land, specifically in terms of its location on a road and its vicinity to a built-up area and more vaguely in terms of the probable expansion of the built-up area referred to in the foregoing.

1.4 It is pertinent to note that the legal definition of a building site is not linked in any manner to town planning schemes such as the Temporary Building Schemes or Local Plans. Nor does legislation recognise any zoning or particular urban designs on land, i.e. land to be utilised for community facilities, housing, road formation and so on.

1.5 No distinction is made between agricultural and wasteland within the LAO.

1.6 The LAO defines value as that amount which land, if it were to be sold in the open market by a willing seller, might be expected to realise.

## 2.0 Definition of value in terms of valuation with particular reference to valuations under compulsory acquisition.

2.1 In this report the following convention is adopted:

- *Price* is the actual observable exchange price in the open market.
- *Value* is an estimate of the price that would be achieved if the property were to be sold in the market.
- *Worth* is a specific investor's perception of the capital sum, which he would be prepared to pay for the stream of benefits, which he expects to be produced by the investment.

In the language of economics *worth* can be considered as *value in use*, whereas *price* or *value* can be considered as *value in exchange*.

2.2 In a perfect investment market where all investors have the same information, the same requirements and the same expectations, price and worth would produce the same figure for investors with identical circumstances.

However different investors may have different perceptions of the investment, and as such, there will be different perceptions of worth within the market.

2.3 In arriving at a valuation, it may be useful to consider the thought process underlying the pricing of the asset in the market. The traditional methods of valuation rely upon a benchmark on the analysis of comparable sales, rather than an explicit model of the thought process that seeks to reflect the evaluation of the return that some investors may undertake in reaching their investment decision.

2.4 The conditions of compulsory purchase preclude the establishment of price within a market exchange context, and valuations should be based on a clear model that reflects the real market value of land but within the parameters of the current legislation.

2.5 It would seem that a paramount concern is the need to ensure that valuations are presented to owners of compulsorily acquired land in a clear and unambiguous manner.

2.6 The manner in which legislation defines building sites is by and large clearly defined.

There is an argument that says that the establishment of a value for that land should take into consideration the parameters established by the legislation.

2.7 Under the LAO, developable land is categorised under one heading, namely, building site.

2.8 In the transfer of land market, land commands a price depending on several factors, which include not only whether the land is developable but also what intensity and type of development could be realised on the land. The latter issues are regulated to a certain degree by instruments of development planning legislation. However, the LAO takes no cognisance of these instruments.

2.9 In order to develop a workable model for establishing value as required by the LAO, one has to draw on two threads raised in the legislation text.

First, that land shall be considered as a building site if it satisfies the specific conditions defining such land in article 18 of the legislation.

Second, once land has been so defined, one has to establish what price a willing seller would expect to realise if the land were to be exchanged in the open market. Once land is defined as a building site, then the seller can be expected to transfer the land on conditions that respect the use of the land as a building site.

2.10 As has been stated in the foregoing, a number of factors will affect the price (value in exchange) of a plot of land.

These factors may be tangible or intangible.

2.11 Tangible factors are those factors that affect the physical attributes of the land, such as topography, configuration, and 'shape' of the land.

By shape of the land, the meaning conveyed is in the sense that a thin corridor of land has severe restrictions on the quality of its development potential.

2.12 Intangible factors are meant to signify such factors as development permits, zoning of areas and other factors that are prescribed in planning regulations.



**2.13** In order to arrive at a reasonable model that may be employed to arrive at an equitable valuation of compulsorily acquired land, it seems safe to assume that the intangible factors should be taken to be exclusive of all other factors that are not contained in the LAO.

Hence, once a land is defined as a building site by virtue of the LAO, no other intangible factors such as zoning, or use of the land, ought to form part of the process of arriving at an equitable valuation.

**2.14** It seems safe to assume that once the intangible components of the valuation factors have been accounted for as described in the foregoing, then, tangible factors should be considered in arriving at a fair compensation for land acquired under the provisions of the LAO.

### 3.0 Procedures in establishing current market value for plots of land.

**3.1** The intangible factors or components of the evaluation process are tightly defined in legislation and lend themselves to unambiguous interpretation.

**3.2** Since the legislation refers solely to a building site, irrespective of its industrial, commercial or residential land use potential, it would seem reasonable to assume that, in order to formulate a basis upon which compulsorily acquired land may be valued, the most common form of development should be considered as a basis for establishment of the valuation.

**3.3** The tangible factors are not established under law, but are referred to indirectly in the legislation as contributing to the price a willing seller would expect to realise if the land were to be exchanged in an open market.

**3.4** The list of aspects that could be listed under tangible factors are numerous and varied. There is an argument that the inclusion of a large number of factors in a model to establish an equitable valuation for a plot of land could become unwieldy and impractical in use, thus defeating the purpose of its establishment.

**3.5** It can also be argued that a determining factor in establishing the worth of a plot of land, and consequently its value, is the manner in which it can be developed in terms of spatial layout.

Thus, it seems unreasonable to exclude the configuration of the land from any process in establishing land values.

This factor would, in a free market transfer context, apply to any form of development, whether it is industrial, commercial or residential in nature.

**3.6** Drawing together the two threads running through the LAO, a valuation scheme would include a basis price (value) for a given type of development potential for building land, which would then be moderated following due consideration of the configuration of the land. Such a scheme may be used as a basis for land valuation of plots of land compulsorily acquired under the LAO.

**3.7** In extraordinary circumstances, one or more tangible factors (apart from configuration or shape of the plot) could be expected to have an influential impact on the amount that a willing seller could reasonably expect a plot of land to realise in the open market. In these instances the valuation of the land, may, after being considered in terms of the factors mentioned in para 3.6 above, be moderated for any exceptional tangible factors.

Such exceptional tangible factor(s) would have to be identified and the manner in which it (they) impinge(s) on the valuation of the land justified by the person(s) drawing up the valuation.

3.8 In the valuations carried out under this exercise, the price bases adopted for the intangible factors are: (a) price for agricultural land and (b) a value for building land upon which terraced housing is to be developed.

A percentage reduction to account for the configuration of the land was adopted where deemed relevant.

3.9 Therefore, while in practice a large number of factors may be taken into consideration and somehow arbitrarily weighted to arrive at a value for land, it seems safer, for the purpose of compulsorily acquired land, to follow a procedure as outlined in the foregoing.

This should prove to provide an equitable value for such land.

3.10 To recapitulate, the procedures adopted for arriving at a value for land that has been compulsorily acquired under the current provisions of the LAO are as follows:

- Land is designated within the categories as defined by the LAO, viz., building, or non-building site (agricultural or wasteland).
- Land that has been categorised as agricultural land is assigned a value that reflects the current market value of land where there is no potential for building development.
- In the case of land designated as a building site, in the deliberation of the value of the land, the intangible factors such as land use ( i.e. whether it is zoned as a commercial, industrial, residential zone or whether it will accommodate a building, a public open space, street, etc.) should not be taken into consideration to arrive at a value for the plot of land.
- With regard to tangible factors visible on site (lie of the land, topography, configuration of the plot), it is only the configuration factor that should normally be allowed to impinge on the final valuation of the plot of land.
- Where exceptional tangible factors are deemed to have a significant impact on the value of the land, such factors should be described and justified.
- The value of the most common form and arguably one of the least intensive land uses should form the basis of the final valuation of building land, namely land upon which terraced housing is developed.
- This 'basis' value is then moderated for the effect of land configuration where applicable and exceptional tangible factors, again where applicable.

#### 4.0 Procedures in establishing historic market value for plots of land.

4.1 The procedure for establishing the historic market value of land follows the same procedure as that described in the previous section, *mutatis mutandi*, for the historic rates of agricultural land and the value of land upon which terraced housing is developed prevailing at the time.

4.2 It has been established that a working average figure for the appreciation of land values over the past 30 years is nine per centum per annum (9%). This figure is quoted in the valuations accompanying this report, however the historic market values were taken into consideration.

4.3 The intangible factors quoted above remain immutable in the historic consideration of land values, as they depend solely on the categorisation of land according to the provisions of the LAO.

4.4 The tangible factor of configuration is evident from plans of plots and thus may be taken into consideration at arriving at a market value.

4.5 Other tangible factors prevailing at the time of the date of the historic valuation may be more difficult to ascertain. Hence, it seems that there would be some difficulty in ascertaining whether exceptional tangible factors should have some impact on the valuation. For example, the context of the plot of land may have differed significantly with the passage of years since the historic date of valuation, and thus a site inspection may reveal very little of the prevailing conditions at the said historic date.

### 5.0 Conclusion

5.1 The valuation of compulsorily acquired land presents a particular situation in that a market value has to be attached to land that is being transferred in a non-market context.

5.2 The LAO establishes a specific context and categorisation of land within which land valuations should be established.

5.3 The procedure described in this document is an attempt to arrive at a fair valuation through a process which, while working within the parameters of the LAO, attempts to constrain as much as possible the arbitrariness that could be associated with the establishment of equitable valuations of compulsorily acquired land.

18.06.2003



## Appendix – II

### Estimating Government's additional cost as a result of delaying determination of compensation

The NAO applied the following equation to estimate the additional cost to Government as a result of delay in determining the price of land acquired:

$$P_1 = P_0(1 + i)^n(1 + \pi)^n(1 + \gamma)^n$$

$$\Delta = P_1 - P_0(1 + i)^n(1 + \pi)^n$$

$$\Delta = P_0(1 + i)^n(1 + \pi)^n(1 + \gamma)^n - P_0(1 + i)^n(1 + \pi)^n$$

$$\gamma = \left( 1 + \frac{\Delta}{P_0(1 + i)^n(1 + \pi)^n} \right)^{\frac{1}{n}} - 1$$

The equation relies on the interaction of the following elements:

$\Delta$  = difference between final payment and initial value increased to reflect inflation and opportunity cost up to date of payment

$P_0$  = initial valuation of the property (Lm)

$i$  = real rate of interest

$\pi$  = inflation rate

$n$  = time between initial and final valuations

$P_1$  = final valuation of property (Lm)

$\gamma$  = real growth rate of land

Whilst the equation takes into consideration Government's financial opportunity costs as well as the time-value of money, or inflation, damages (or interest), payable from the date when the relative user department took possession of the land up to the date of settlement, are excluded.

Assumptions associated with the methodology adopted for the equation are:

- constant geometric rates over time [nominal rate of interest, including inflation, and the land value growth rate (premium/intrinsic)];
- the return from an alternative investment of funds allocated for land acquisition is not taken into consideration, as the profit motive is not an objective of governments.



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