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**FINAL REPORT**

**SMALL BUSINESS DEVELOPMENT**

**PHASE II**

**PILOT PROGRAM TO INCREASE ACCESS TO REAL  
ESTATE IN YAROSLAVL, RUSSIA**

**CONDOMINIUM IMPLEMENTATION**

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## **I. Background and Overview**

### **A. General Situation**

The Russian program for the privatization of small scale enterprises was developed by the State Property Committee (GKI) and has been underway since June of 1992. Small scale enterprises in Russia are defined as retail trade, catering, and service outlets. As such, small scale enterprises include such diverse businesses as food stores, clothing retail stores, restaurants, cafes, tailoring services, and repair outlets. During the course of this program, over 50% of the previously municipally owned small scale enterprises have been privatized by city authorities and some cities have nearly completed their programs. The Russian government plans on completing small scale privatization by early 1994.

While the pace of small scale privatization has been impressive, there has been limited improvement in privatized enterprises. Customers often cannot discern any differences between a store when it was previously municipally owned and the same store once it is privatized. The public perceives that promised improvements in the quantity and quality of items and services offered have often not materialized. Russian small scale stores as a result continue to provide a level of quality much below their Central European counterparts. *(please refer to slide a in Appendix one)*

### **B. Project Background**

It is critical to the success of market reforms in general and privatization in particular to have strong, popular support. As small scale outlets represent the bulk of the enterprises with which a typical Russian citizen has day to day contact, they are one of the most obvious symbols of the success of privatization. Given that the poor performance of privatized stores has done little to create the public support needed, the GKI has undertaken a program to improve conditions so that small businesses can improve their performance.

As part of this program, the GKI, with funding from the United States Agency for International Development (USAID) hired Bain & Company to accomplish two objectives: in Phase I, to identify the key obstacles to improving the quality of small scale businesses, and in Phase II, to launch a pilot program on a local basis in order to eliminate these obstacles and develop a model for national legislation *(please refer to slide b in Appendix one).*

### **C. Phase I**

#### **I. Activities**

Bain's work began on 1 April, 1993 with a comparison of small business development in Russia and Central Europe. This work included a series of interviews of both city officials and local small scale entrepreneurs in various cities in the Central European countries of the Czech Republic, Poland and Hungary and four Russian cities - Nizhny Novgorod, Vladimir, Rostov On Don and Chelyabinsk.

The main conclusion of this comparison was that the key driver of the quality of small businesses was the level of competition as indicated by the density of outlets *(please refer to slide c in Appendix one)*. In Russia, density of small scale business outlets is hampered by five major obstacles *(please refer to slide d*

Beijing • Boston • Brussels • Chicago • Dallas • Geneva • Hong Kong • London • Madrid • Milan • Moscow • Munich  
Paris • Rome • San Francisco • San Jose, Costa Rica • Singapore • Stockholm • Sydney • Tokyo • Toronto • Warsaw

*in Appendix one*). Access to real estate, as a necessary prerequisite to the opening of a small scale outlet, was chosen by the GKI and Bain as the first obstacle to address.

From the middle to the end of May 1993 the Bain team worked with the GKI to identify a pilot city in which to review specific issues related to increasing the access to real estate. Yaroslavl was chosen based on 1) the expressed interest of city officials and 2) the fact that Yaroslavl is a relatively typical Russian city thus making it likely that changes introduced there would be applicable elsewhere in Russia.

## **2. Findings**

During the months of June and July, the Bain team, after getting information from city agencies and entrepreneurs, analyzed the real estate situation in Yaroslavl in order to identify the obstacles hampering access to real estate for small scale businesses. The findings are summarized below:

- 1) Better utilization of empty and current retail space can significantly increase the number of outlets in Yaroslavl. Specifically, based on a physical inventory of one city district, only 30% of non institutional ground floor space in Yaroslavl is either commercial space or empty, and of this space about 75% is underutilized. If these spaces were fully utilized, Yaroslavl could double the number of commercial outlets within the central district. Actions taken to improve utilization could also set the groundwork for the converting of non retail space to retail use.
- 2) To utilize this space fully, however, Yaroslavl must overcome the following obstacles:
  - The conversion of previously unoccupied space to retail use is hampered by the uncoordinated management of the three critical rental property functions - the right to set rents, the right to lease space and collect rents and the responsibility to maintain space - and the imposition of undue restrictions on the use of space. More importantly, there are insufficient financial incentives in place for the key players - the city property committee (KI) and the housing authority (ZhKU) - to aggressively seek out lessees for empty space.
  - Inefficient utilization of space is caused both by regulations imposing profile restrictions and confusion regarding lessee and sublessee rights and the perceived and real lack of financial benefits to be derived from better utilizing space.

## **3. Phase II Objectives**

Given the Phase I findings, the Phase II implementation program was developed with the intention of developing and implementing a local pilot program that will begin to create a free commercial real estate market in Yaroslavl. This was to be accomplished through the development of relevant legislation and the selection and creation of sites to pilot implementation of that legislation. The implementation program had the following objectives:

- Breaking the municipal monopoly on space and the reduction of the involvement of the municipality in allocating space
- Creating true private ownership and competitive supply
- Ensuring the freedom of private owners to make decisions on use and disposition
- Providing for proportionate and fair allocation of costs to private owners
- Providing a replicable model that can be used throughout Russia

## **II. Summary of Work**

From November of 1993 to July 31, 1994 the Bain team worked in the city of Yaroslavl on Phase II of a small business development program with an emphasis on implementing real estate reform. The following summarizes the work done and the results achieved from that work.

### **A. Activities**

Under the Phase II task order 5 major tasks were accomplished by the Bain team. They were:

- a. Creating a transparent, freely accessible commercial property registry
- b. Assisting in the creation of a system that allows commercial ownership of built-in spaces
- c. Beginning to create an efficient leasing and subleasing environment by making fundamental improvements
- d. Proposing reductions in legislative burdens on entrepreneurs
- e. Publicizing new legislation and programs

### **I. Explanation**

The justification for each of these tasks is as follows.

#### **a) Create a freely accessible commercial property registry**

In order for real estate transactions and, thus, a real estate market to function, there must be a physical definition of the property being sold and a legal definition of the rights of the person(s) selling that property. This information has to be centrally recorded and easily accessible. Typically, this is done through a property registry. Establishment of a property registry in Russian cities is important in two respects. First, it allows tracking of currently municipally owned real estate thus identifying property that is suitable for commercial lease or sale in the short term. Secondly, by recording available properties, the registry lessens the chances of property being 'hidden' or otherwise manipulated by municipal authorities. Thirdly, it provides a record of private ownership of commercial spaces that will be needed for the establishment of property rights in the long term.

#### **b) Assist in the creation of a system that allows commercial ownership of built in spaces**

##### ***(1) Assist in the creation of a methodology for the sale of built in space.***

In order to circumvent the obstacles hampering potential entrepreneurs' ability to lease and purchase real estate, the most radical solution is to eliminate the municipal control of this real estate by selling municipally owned commercial spaces to entrepreneurs. This transfer of property from public to private hands, by ensuring an end to the municipal monopoly on real estate, is critical in creating a true free real estate market.

##### ***(2) Implement local condominium legislation***

Because many commercial spaces are located within multiple-tenant buildings, the complication in the privatization of commercial spaces is that in order for it to work effectively, it has to address the issue of common area maintenance and shared utilities. The housing privatization legislation created a property right for apartment dwellers in multi-use buildings. Thus there are or will be commercial and residential spaces that have already been sold through the privatization process that exist only to have municipal ownership of common spaces. With municipal control of common spaces, no building is truly private or beyond the reach of the state. The way to address this complication is to develop condominium legislation allowing both private ownership and private control of common space. Once these rights are established, commercial - and residential - property should become more easily used and transferred thus increasing access to real estate and consequently encouraging small business development.

c) **Begin to create an efficient leasing and subleasing environment by making fundamental changes**

While the selling of commercial real estate into private hands is the most straightforward way of creating a free real estate market, it is not the only way. Realistically, it is not likely that the municipality will sell all of its commercial spaces. Firstly, unless forced, the municipality is likely to be reluctant in selling all of its commercial spaces because of its not wanting to lose all of its rental income. Secondly, even if the municipality wanted to sell all of its spaces, there are likely to be many spaces that are occupied by privatized enterprises who have rights to buy their space but are not willing to do so. Even if all spaces are eventually privatized, it will likely take more than a year before all spaces are sold. Because of the reality that the municipality will remain a major landlord of commercial spaces, improvements to the current methods used for the leasing and subleasing of space are needed.

**Increase Demand for Space**

Increasing the supply of real estate in and of itself will not necessarily mean achievement of the overall objective of increasing the number of small scale businesses. Because of this, the Bain team also focused its efforts on two additional activities aimed at increasing the demand for commercial real estate; proposing reductions of disincentives to starting small scale businesses and publicizing new real estate legislation.

d) **Propose reductions in legislative burdens on entrepreneurs**

There are many legal burdens placed on small scale businesses that hamper their ability to operate and thus discourage new businesses from opening. Two of the critical burdens are taxes and profile restrictions.

e) **Publicize new legislation and programs**

Successful implementation of new real estate legislation will depend on widespread awareness of the legislation by both citizens and city officials. The rights and obligations of both sides need to be made explicit so that each side can check the other if there is a violation of the new laws.

**2. Activities performed**

During the course of Phase II, the Bain team was successful in fulfilling all of the deliverables included in the original contract with USAID and was able to accomplish several additional deliverables that will help to continue the reforms. The tasks accomplished are detailed below.

a) **Created a transparent, freely accessible commercial property registry.**

The Bain team was successful in completing the following deliverables related to property registration in Yaroslavl.

- (1) *Prepared a physical inventory.* A physical inventory of all buildings on commercial streets was organized and checked by the Bain team to insure that the registry contained accurate, up to date information
- (2) *Established programs to track and make public ownership and use of commercial real estate.*
  - (a) *Developed a computer database that will act as a central registry.* Bain organized the structure and, with USAID funds, paid for the development of a real estate database in Yaroslavl.
  - (b) *Assisted city agencies.* The Bain team was able to get city agencies to agree on a common structure of the database and to agree on sharing the information that each of them had internally with other city agencies and the public.
  - (c) *Negotiated guarantees of access to the database.* Bain helped develop and lobbied for the passage of a mayoral edict that guaranteed public access to real estate information. The

Bain team also wrote an article explaining the edict and had the article and edict published in the local official newspaper.

- (d) *Developed low cost software suitable for use throughout Russia.* A database was developed for less than \$3500 and Bain, acting under this task order, has received full rights to distribute the software throughout Russia.
- (3) *Undertook pilot implementation.*
  - (a) *Used the registry to further the other real estate reform work.* The registry was used to gather legal information on potential pilot condominium sites. It was also used to identify unoccupied commercial spaces as potential pilot sites for implementation of new leasing legislation that Bain had created.
  - (b) *Tested the release of information.* The release of real estate information to the public was also tested through the use of a 'reality test' where local residents were used to request information from relevant city agencies.
  - (c) *Disseminated information to other cities and other advisors.* Bain was also successful in disseminating information on the real estate database to other cities by making agreements to distribute the software and an instructional manual to over 20 cities and by organizing 1 seminar and participating in over 4 additional seminars attended by representatives of Russian cities. Lastly, Bain established contacts with the weekly newspaper, *Economica i Zhizn*, and negotiated with them to advertise and distribute the property registration software and manual nation-wide.

**b) Assisted in the creation of a system that allows commercial ownership of built in spaces**

**(1) Assisted in the creation of a methodology for the sale of built in space.**

The activities completed under this part of the task included the following:

- (a) *Gathered legal information.* The Bain team gathered information on methodologies for sales of built in space currently in use in Russia
- (b) *Developed methodology.* Based on other Russian city's models and Bain's experience, Bain developed a recommended methodology for the GKI
- (c) *Identified potential pilot sites*
- (d) *Implementation support.* Bain assisted a local Yaroslavl entrepreneur to prepare an application for the purchase of his space
- (e) *Legal clarification.* Bain attempted to clarify the March 11 law on built in space sales with both Yaroslavl property committee officials and GKI lawyers
- (f) *Recommended changes to the March 11 law.* Bain made further recommendations to the GKI for revisions to the built in space sales legislation once Bain made it clear to the legislation's authors within the GKI that the law would not fulfill its original intentions.
- (2) **Helped to develop federal condominium legislation and implemented it at a local level**  
During the course of Phase II, The Bain team successfully completed the following deliverables related to condominium legislation in Yaroslavl.
  - (a) *Assisted in the development and passage of federal condominium legislation*
  - (b) *Clarified the federal law with the State Committee on Architecture and Construction (Gosstroj) and the Ministry of Justice.*
  - (c) *Developed and gained approval from the GKI of a standard condominium charter that was implemented on a pilot basis.*
  - (d) *Gained the approval of a local condominium law and charter by the Yaroslavl authorities.*
  - (e) *Developed legislation that will establish a system for the distribution of maintenance subsidies directly to condominiums.*
  - (f) *Chose pilot sites.* Over 15 buildings were identified as potential pilot sites. For each, legal information was gathered and city approval was attained to use them as pilot sites. Five of the 15 buildings were eventually used as pilot condominium sites.
  - (g) *Consulted occupants of the pilot sites.* General meetings were organized for and information brochures were given to residents of over ten potential pilot sites. At the

meetings the Bain team informed residents of the details of the condominium legislation and addressed resident concerns and questions.

- (h) *Worked with city officials to ensure their understanding of the condominium legislation.* The Bain team worked closely with all relevant city officials to inform them of the condominium legislation and to work out all of the practical details of administering the new condominiums.
- (i) *Trained potential maintenance contractors.* The Bain team met with five potential maintenance contractors informing them of the new condominium legislation and giving them informational materials on both condominiums and the maintenance of common spaces.
- (j) *Created and launched press releases making the public aware of the new legislation.* Bain was able to gain press coverage through the use of seminars held with city officials and the distribution of the Bain developed condominium charter and information brochure.
- (k) *Registered five pilot condominium sites.* Bain was able to have a majority of owners in five pilot sites agree to register their buildings as condominiums. Bain assisted the condominium associations in these pilot sites to receive building and land inventories, register with all relevant local agencies, open bank accounts and create management organizations.
- (l) *Trained condo associations in how to self govern and budget.* Bain developed a manual on condominium government and management and actually implemented its use in five pilot sites assisting local residents in establishing their associations and subsequently making decisions
- (m) *Monitored pilot sites for a period of three months.* Pilot sites were monitored by Bain from early May to the end of July of 1994 with education and support of their initial decision making process and their subsequent progression to self government.

**c) Began to create an efficient leasing and subleasing environment by making fundamental improvements**

The Bain team was successful in completing the following deliverables in this area in Yaroslavl.

- (1) *Designed and lobbied for legal changes in the process of leasing.* Two new regulations were developed that set out both an open bidding and a sealed bid procedure to leasing out space. The regulations were structured so that they:
  - (a) *Reduced the power of municipal institutions and streamlined the approval process.* Maximum times for approval and well defined, limited reasons for disapproval were set.
  - (b) *Created a proper incentive structure.* The new regulations allowed the KI to hold on to most of the lease proceeds and thus created an incentive for them to lease out space.
  - (c) *Reduced restrictions.* The regulations eliminated sublease taxes and disallowed other restrictions on the use of the property.
- (2) *Gained approval of the sealed bid regulation and a commitment to integrate reforms from the new to the old open bid regulation*
- (3) *Identified pilot sites suitable for implementation of the sealed bid leasing regulation*
- (4) *Lobbied for implementation of the new sealed bid leasing regulation*

**Increased Demand for Space**

**d) Proposed reductions in legislative burdens on entrepreneurs**

The Bain team was successful in completing the following deliverables in Yaroslavl.

- (1) *Developed legislative changes in critical burdens.* The Bain team developed proposals for legislative changes in restrictions on profile and subleasing.
- (2) *Lobbied for adoption of these regulations.* The Bain team, as part of its work with city officials, lobbied for legislative changes and succeeded in doing so with the passage of the regulation on sealed bid leasing.

**e) Publicized new legislation and programs**

The Bain team was successful in completing the following deliverables in Yaroslavl.

- (a) *Designed a public education program.* The Bain team developed a series of informational and training materials. These included a condominium information brochure and three detailed manuals outlining the creation of a city real estate database, the management of a condominium and the maintenance of buildings. Additionally, an article was written by Bain explaining the procedure for public access to real estate information.
- (b) *Use materials for training and information campaigns.* The Bain developed standard condominium charter and condominium information brochure were used to educate both city officials and residents of potential pilot sites. The article on public access to real estate information was published in the weekly city newspaper. Copies of both the sealed bid leasing regulation and the mayor's edict on the release of real estate information were also published in local newspapers.
- (c) *Revised materials to reflect any important issues.* Given over three months of working with the pilots, several revisions reflecting real world obstacles were made.
- (d) *Distributed the materials city and nation wide.* The Bain developed standard condominium charter and manuals on condominium management and real estate database creation were distributed throughout Yaroslavl, to other Russian cities and to other advisors
  - (i) The condominium manual was distributed to Russian cities directly and through conferences and to the Urban Institute and PADCO who were acting as advisors on other USAID funded, real estate related projects
  - (ii) The manual on creating a city real estate database was distributed to over seven other Russian cities

**B. Results achieved and Systems Developed**

The results of the Phase II work are the following:

- a) **Pilot Condominium Buildings**  
Five pilot condominium buildings with functioning condominium associations that contain both private and municipal owners and commercial and residential space.
- b) **City Government Real Estate Manual**  
A manual that should help other cities implement real estate reforms containing 'how to's' and standard documents that will give city officials the knowledge necessary to replicate the changes accomplished in Yaroslavl. The manual includes the following:
  - how to do an inventory of non residential space
  - computer programs and manuals to be used to track space and create a property registry
  - model lease, sublease and sales contracts to be used by city governments
  - model legislation and procedures regarding the leasing of built in space, the sale of built in space and the creation of condominiums
  - model condominium charter
- c) **Real Estate Incentives Program**  
A list of proposed regulations that would reduce legislative burdens on small scale businesses.
- d) **Model Public Relations Program**
  - an information brochure outlining new condominium legislation
    - . practical details

- . rights and obligations of government bodies
  - . rights and obligations of private citizens
  - manuals for
    - . the training of condominium association members
    - . the setting of maintenance standards
    - . the training of city agencies
- e) **Model leasing and subleasing procedures**  
Municipal procedures regarding the leasing and subleasing of commercial space.

**Note:** *The following sections (III and IV) are based on the latest information available as of September 1, 1994 and are as accurate as possible. Given the constantly changing nature of Russian politics and legislation, some of the recommendations below may not be applicable at a later date.*

### **III. Future of Developed Systems**

The Bain team worked with the city of Yaroslavl over a year long period to establish real estate reforms there. The long amount of time and the amount of outside support required can be explained by the fact that, as a pilot program, the work performed in Yaroslavl was the first of its kind in Russia and broke new ground in dealing with a variety of legal issues. As a pilot program, the Bain work was a critical first step in the reform process. While Bain's involvement in this first step was necessary in order to begin the reform process, the continuation of such reform is impractical with the same intense level of outside support.

Real estate is inherently local and handled by local governments. In order for reforms to continue, therefore, federal legislation that deals with real estate needs to set out guidelines and create incentives for local governments to proceed with reforms. Based on Bain's experience in Yaroslavl, the real estate reforms developed there can not continue in the rest of Russia without either significant outside or local support or clarification and augmentation of federal law. The following 3 sections detail what the federal Russian government needs to do in order to make reforms continue in the areas of a) real estate registration, b) condominiums, and c) sales of built in space.

#### **A. Real Estate Registry**

Future development of real estate registries within Russian depends on the development of legal procedures that detail how property registration must be performed. Currently, legislation related to property registration is very fragmented and covers several legal areas: land, buildings / premises, and property rights. No legislation currently exists that clearly states how and by whom property registration should be performed. In the area of real estate registration, most local governments see value in tracking property in their cities but they differ in what information should be collected in the registry and who can have access to that information. The following steps should, therefore, be taken at the federal level in order to insure that property registration continues and that the rights of property owners are protected by the registries.

- 1. Federal law should clearly state which parties are responsible for creating legislation related to property registration. Because property registration involves both land and buildings, and both private and governmental ownership rights, during the course of the Yaroslavl project, the Bain team had contact with not only the GKI, but with numerous other advisors and federal agencies also working on registration. The other agencies included the federal land committee and the State Committee for Architecture and Construction (Gosstroj). Confusion exists as to which of the three federal agencies is responsible for the development of a comprehensive registration process and the agencies themselves are fighting with each other for power over this process. A decision, therefore, has to be made at the prime ministerial or presidential level as to which of these agencies has the responsibility over property registration.*
- 2. Federal law should establish a standard procedure of property registration and develop standard property and land certificates.*

As previously discussed, Russian municipalities have developed their own system of property registration because there are no federal guidelines. This has led to a situation that property rights in some cities are registered and therefore protected in different ways. In order to reduce confusion and possible curtailment of rights it is necessary for the federal government -once it is clear which

federal body is responsible for property registration - to develop a federal registration process. This process should detail what rights are registered and by whom along with detailing which parties have rights to viewing the registry. As part of this process, the appropriate federal bodies should develop property rights certificates which would afford the holder certain guaranteed rights.

3. *The land reform process should be extended to provide support for the surveying of land.*  
It is most efficient to create a property registry so that is built based on land information. Currently, the process of surveying land and establishing a *cadastre* system whereby general zoning regulations rather than specific property by property restrictions are applied to land has barely begun in Russia. Without precise logistical and legal information about the land on which a building sits, a property registry has limited importance. The main issues are that there are limited funds and there is limited knowledge available for surveying and establishing a *cadastre*. One solution to the issue of funding is to use the proceeds of the newly begun non agricultural land privatization to pay for land surveying.
4. *In the short term, experience sharing among cities should be encouraged by the appropriate federal agencies.*  
Because cities already have incentives to develop registries and federal solutions to property registrations will take time to happen, federal agencies like the GKI, the Gosstroj and the land committee should sponsor property registration seminars for cities in order for these cities to share experiences and jointly develop a more standardized property registration system. Bain has tried to do this by sponsoring a registration seminar and attending real estate seminars sponsored by the World Bank and the Union of Russian Cities.

## B. Condominiums

In order to have a truly implementable condominium program, certain issues need to be resolved with federal legislation. These can be categorized in to two basic areas, registration and operation. The issues are as follows:

1. *Registration*
  1. *The standard charter has to be developed and approved at the federal level.*  
Although the *Temporary Condominium Regulations* approved by the President's Decree #2275 of December 23, 1993 became effective when published, the absence of an approved charter at the federal level means that the decree practically can not be implemented unless there is strong political will at the local level. The standard charter should have been developed by the State Committee for Architecture and Construction (Gosstroj), the State Committee for the Management of State Property (GKI) and the Ministry of Justice within three months from the enactment of the Presidential decree or April 6, 1994 but it still remains in the development phase.

In Yaroslavl, the Chamber of Licensing and Registration refused to register condominium associations in the absence of a standard charter and thus the Bain team was obligated to develop a charter that was approved by the GKI for use on a pilot basis. The tax and statistical authorities defined the status of such associations under the *Law on Enterprises and Entrepreneurial Activities* and were unable to comprehend the condominium's exact type of legal entity.

2. *Federal legislation must be clarified in order to make it clear that the registration of both condominium associations and condominiums as types of property is mandatory and has to be done within a limited time frame.*

Federal legislation must envisage that condominium associations are subject to mandatory registration as soon as a condominium type of ownership occurs, i.e. when two owners appear within a single parcel of real estate.

The Ministry of Justice and the Committee for Architecture and Construction have indicated in writing that the *Temporary Condominium Regulations* overtly support the requirement for condominium associations to be registered on a mandatory basis. While the Ministry of Justice has given its opinion, this needs to be made more explicit. The Yaroslavl experience indicates that local legislatures are unlikely to force the law upon their citizens for fear of political reprisal. However, if condominium associations are created on a voluntary footing, it will take too long for municipal property to be transferred to the ownership of residential and non-residential unit owners. This would be a brake on the housing reforms as envisaged in the *State Housing Program*. The federal law, therefore, has to be explicitly stated as mandatory.

A time frame needs to be fixed for the condominium program. Otherwise, it would be very difficult to create a mechanism to make municipal authorities expedite efforts in this area. We feel that the privatization of housing units has been delayed exactly because no time frame was fixed. An appropriate enforcement mechanism for the condominium program could be one similar to the one that was used in small-scale privatization providing for the personal liability of local property committee chairmen, including dismissal from office, for failure to privatize a fixed percentage of assets. One caveat to the mandatory enforcement of condominium registration is that along with this 'stick' there needs to be a clear set of incentives that encourages registration. How these incentives can be established at the federal level is outlined in the sections below.

3. *Federal law should define who needs to be involved and what documents are needed to initiate the condominium registration process.*

Although the present condominium legislation does not require more than two votes or signatures for a condominium association to be created, local registration bodies, in a bid to hamper the registration process, may require the minutes of an association's first general meeting with an accounting of votes for and against registration.

The condominium project in Yaroslavl has shown that the first organizational meeting should be mandatory, encouraged by the local government but run by a core group of owners with the sole purpose of providing necessary information to other owners. There must be no voting on the creation of a condominium association at the first meeting since such a vote would undermine the system of mandatory registration.

4. *The federal law should define and distinguish between a 'condominium' and a 'condominium association'*

This needs to be done in order to avoid legal difficulties in the registration of condominiums. Parcels of real estate structured on 'condominium' principles must be registered by bodies responsible for recording real estate deals, whereas a 'condominium association' as a legal entity must accordingly be registered by the local government.

The federal law should oblige authorities responsible for recording real estate deals to register condominiums on a mandatory basis as soon as more than two units in a building are privatized. This can be done using data supplied by bodies - such as the municipal agency for the privatization of housing or the local property management committee - that register the privatizations of residential and non-residential units.

Paragraph 1 of the *Temporary Condominium Regulations* does not clearly define the term 'condominium' - whether it is a legal entity speaking for real estate owners, or an object of law, or a form of ownership. In our opinion, a 'condominium' is a discrete form of ownership, whereas a condominium association is a consumer group. The consumer community law should be amended accordingly since the law as it stands now does not provide for the membership of bodies of government in consumer societies.

5. *The cost of condominium registration should be reduced.*

In order to be fully operational, a condominium association has to be registered with local government agencies, and the association has to open a bank account. As the cost of this start up process is expensive and discourages condominium creation, these costs should be reduced.

The first cost component is the cost of registering the condominium association with the registration chamber. The *Temporary Condominium Regulations* provide that the charter of a condominium association may be registered if at least two signatures affixed to it have been confirmed by the public notary. This confirmation requirement is superfluous and should be dropped. When the charter is validated, the notary only confirms the authenticity of the signatures therein since he has no right to check its legality, and, under Russian law, the cost of confirming one signature costs two minimum wages, - 58,480 rubles or \$28 as of August, 1994. Such registration costs appear unjustified since the legality of the charter and its correspondence to the standard charter is checked by the body that registers the condominium association. When the standard charter is approved at the federal level, the above procedure would become even less necessary.

The second cost component is the cost of registering with other government agencies. Following registration at the local government, a condominium association, in order to be able to open a bank account, must be registered at the Pension Fund, the Medical Insurance Fund, the statistical authority and the tax service. Registering with these bodies alone costs the association from 12 to 16 times the minimum wage. This equates to a per unit cost of 12 to 16% of the minimum monthly wage for a building of 100 units or 120 to 160% for a building of 10 units. Because of these high costs, unit owners and local authorities will delay the creation of condominium associations unless registration costs are eliminated.

The third cost component is the direct cost of opening a bank account which requires further expensive notarization of signatures. To reduce this cost, there are 2 possible solutions.

1. Drop the notarization or bank account requirements
  - by changing the requirements of becoming a legal entity or
  - by changing the requirements of opening a bank account (these last 2 measures would benefit the startup of new businesses but would require a broader scope of legal change beyond just condominiums) or
  - change the requirements for condominiums by changing their legal definition
2. Reduce the cost of notarization by reducing the requirements to become a notary.

6. *The cost of property surveying at registration must be reduced and the procedure simplified.*

The *Temporary Condominium Regulations* do not require a description of the condominium to be included in the registration documents submitted to local authorities. However, the Yaroslavl project has proved such description necessary in order to 1) identify common property

and individual units owned by individuals and legal persons within the condominium and to 2) divide owners' responsibilities both within and outside the property.

Local Yaroslavl registration officials have interpreted this description as being a complete physical inventory of the building performed by the local bureau of technical inventories (BTI) that includes the building's technical passport, physical layout and an evaluation of its condition. Based on our Yaroslavl experience, the cost of a complete inventory can run over 1 million rubles if one was not done recently. This cost is based on a set of federal norms of standard hours needed to do such work.

To address this issue, federal requirements on property description should, firstly, require that a description of a parcel of real estate should focus on civil-law aspects, not on technical repair, and include a description of common property and units owned by individuals and legal entities with a clear delineation of responsibilities among the owners.

Secondly, the federal law should state who can prepare property descriptions. Currently, most of the real estate deals are registered at the BTI which holds a virtual monopoly on real estate related services. This monopoly is due to the fact that the BTI keeps all state archives on real estate in all of the Russian Federation and that the BTI, in conformity with many regulations, issues opinions on real estate, including opinions on ownership and tax liability, which are recognized by all relevant legal authorities including courts of law, public notaries, property management committees, land resource committees and land reform committees. Because the BTI currently has the sole power to issue property surveys, survey costs can only be reduced if prices are regulated or the BTI's power is curtailed. This would require either regulating the time required and the amount charged by the BTI for issuing property descriptions, which may be hard to practically enforce and will encourage bribing, or allowing other private bodies to act as surveyors, perhaps after being licensed.

Privatization of housing can serve as a model on how to simplify the process. When a housing unit is privatized, the BTI provides the housing privatization agency with documents based on information contained in the BTI's database. This procedure is fairly simple and does not involve serious costs.

7. *The procedure and cost of registering the condominium association's common ownership of land should be clearly defined.*

The *Temporary Condominium Regulations* provide that the condominium association has the right to receive confirmation of its common ownership of the land its building sits upon. In order to receive such confirmation, the land must be included in the municipal cadastre through an inventory of the city's regions. Land inventories are the responsibility of the land resources and land reform committee and are financed from the municipal budget. In Yaroslavl, however, no funds have been provided for land inventories for two years because of the municipal budget deficit. In the Yaroslavl pilot program the condominium associations, therefore, had to pay for such inventories. The rates as fixed in the *Collection of Standard Rates for Social Works and the Prices of Design and Research Products Pertaining to Land Development and the Land Cadastre* of February 1, 1994, are quite high amounting to amount to one million rubles (\$475) per hectare of land. In addition, such inventories take approximately one month to complete.

This problem can be resolved in a fashion similar to that of property description. Regulations should be approved at the federal level providing for common ownership of land being granted against information provided by the BTI and the City Architect's Office.

8. *The procedure of transferring a building from the balance sheet of factories and municipal maintenance agencies to that of a condominium association should be clarified.*

When a building is registered as a condominium and the residents of the building register as a condominium association, the building is supposed to be transferred to the balance sheet of the condominium association. As a balance sheet holder, the condominium association is responsible for the maintenance of the building, but, legally, until 1998, the previous balance sheet holder - typically, either a municipality or a factory - is responsible for payment of capital repairs and subsidizing a portion of the maintenance costs. This situation raises issues for two reasons:

- a. It is unclear how the municipality and factories can subsidize the maintenance costs of condominium associations, as envisaged in the Decision of the Council of Ministers / Government of the Russian Federation, if they transfer a building to an association's balance sheet; since if a building is not on their balance sheet, they are not technically liable for payment for its maintenance and repairs and under Russian accounting laws can not expense any such payments
- b. When an entire building is placed on a condominium association's balance, dual taxation occurs (this is explained later).

There are two ways to address this issue. One way is to abandon the notion of a 'balance holder' which creates additional problems for delineating rights and obligations in the domain of real estate. This will be difficult since the notion of a balance sheet holder is central to the former Soviet and current Russian real estate ownership system. A second possible solution is to keep condominiums on the balance of the previous owner until the subsidies remain in effect, i.e. until 1998. After 1998, it should be easy for the building to be transferred to the condominium association's balance sheet since the association will have been registered. Because of the difficulty in resolving this issue, this was the approach taken in Yaroslavl.

2. *Operations*

9. *Regulations should be approved at the federal level to clarify the procedure of transferring maintenance subsidies from municipal authorities to condominium associations.*

The true value of the condominium program lies in the ability of the condo association to make decisions about the maintenance of its common space. This decision making power has no value unless the condo has access to the maintenance subsidies they are due from the municipality until 1998 as envisaged in the Decision #935 of the Council of Ministers/Government of the Russian Federation.

Currently there are two issues with the allocation of these subsidies. Firstly, no system of allocation exists. While Bain has developed a methodology that has been approved by the city of Yaroslavl, unless there is strong local support for condominium, it would be extremely difficult to negotiate similar agreements in each municipality where implementation takes place. Secondly, municipalities do not have the cash to support full subsidies. Currently, municipalities can provide financing to pay for maintenance because they pay their municipally owned REU's on credit. Thus, the financial transaction between the city and the maintenance organizations is on paper only. The moment that condominiums are entitled to subsidies they will demand cash in order to pay private maintenance contractors. While requiring cities to pay maintenance subsidies in cash rather than in credit will spur sounder fiscal planning and may stimulate more market driven leasing practices, there is no city that is likely to accept this proposal voluntarily.

A federal regulation on the distribution of maintenance subsidies should be passed and that law should detail how the subsidy will be calculated and how it will be given to condo associations. The regulation should also allow the city to charge only non-owners for a rent and maintenance charge rather than charging owners of privatized apartments living in a condominium.

10. *Rents and maintenance charges have to be separated and increased to reflect their true market cost.* Currently, rent and maintenance charges are lumped together as one minimal charge to all residents of municipally owned buildings, even those who have privatized. Until now almost all of the maintenance and utility costs were 'paid for' by the municipalities. However, starting in 1994 the municipalities will pay 80% to 85% and the residents the remainder. This will be reflected in a greater 'rent' charge to residents. In order to make these new charges understood and used as an impetus to privatize apartments and create condominiums, two steps have to be taken
1. Maintenance charges and rent have to reflect the true market cost of services.
  2. There must be a division of rent and maintenance charges so that owners do not end up paying rent.

In this way, as rents increase, the incentive to own apartments that do not have to pay rent will also increase as long as property taxes are not greater than rent. As maintenance charges levied by the city increase, the owners will see the value of becoming a condominium association and actively determining the cost of their maintenance.

11. *Maintenance agencies should be privatized.* There are several reasons for doing this. Firstly, many unit owners think that their maintenance costs will increase rather than decrease if they become members of condominium associations. Their reasoning is that no private maintenance contractor will be less expensive than the municipally subsidized maintenance agencies, (REU's). These beliefs continue despite the fact that they have been proven false in Urban Institute's Moscow private maintenance program. The only way to end the perception that REU's are cheaper than private contractors is to privatize the REU's and have them operate under the same principles as their new private counterparts. A second issue is that outside of Moscow, unless there are as large a number of units available as customers, private maintenance companies are likely to be created only slowly. Thirdly, since they are owned by cash-strapped municipalities, maintenance agencies often are not paid for the work they do. This has a negative effect on employee attitudes towards their duties that is reflected in poor quality maintenance work.

While the *1994 State Program for Privatizing State and Municipal Enterprises* envisages the mandatory privatization of existing maintenance agencies, ideally, these agencies should be privatized before condominium associations are registered in order to end the perception that REU's are less expensive and provide a higher quality, ready source of maintenance.

12. *The tax status of the condominium association has to be clarified.* The condominium association is, like other legal entities, subject to tax. But unlike other legal entities, it may not own real estate, and it is a non-profit organization that invests all of its profits into its own development. The association is made of legal and physical persons who are also subject to tax. Thus the tax status of the condominium association is ambiguous and may be subject to unduly restrictive property, revenue and profit tax that will discourage condominium formation.

According to federal condominium law, buildings registered as condominiums are transferred from the balance sheet of the municipal maintenance agency to that of the condominium. Under Russian

accounting practice, a building is thus considered as an asset of the condominium association which, in turn is obligated to pay property tax under the *Law on the Taxation of Property of Enterprises*. This leads to a situation of double taxation where condo association members, who own a portion of the common property as part of their ownership on their individual property unit, pay property taxes on common space both as owners of apartments and as condominium association members. A second tax issue is that condominium associations, as legal entities, have to pay revenue, profit and wage taxes. While the condominium association will have no revenues or profits in practical terms, the association fees it receives from its members may be subject to revenue, profit and wage tax by the tax authorities.

One solution to the problem of dual taxation is to keep the building off of the condominium association's balance sheet at least until 1998 as mentioned under point 8 earlier. However, this would only be a short term solution as the building would have to go on the association's balance sheet after 1998. In order to truly reduce the potential tax burden on condominiums, the legal status of condominiums should be clarified. Condominium associations should be treated as non commercial enterprises that are not subject to property and profit taxes. Property taxes should thus be paid by the individual unit owners only.

*13. The accounting system for condominium associations should be simplified*

Condominium associations are non-profit organizations. Their range of activities will be limited by the pending federal sample charter and condominium law. In the meantime, condominium associations have to use standard accounting procedures developed for all commercial organizations. Given that most condominium accounts will be prepared by laymen with little accounting experience, it is advisable to develop simplified accounting procedures for condominium associations. This should be the responsibility of the Russian Ministry of Finance.

*14. A procedure of calculating utility payments in a condominium association should be developed so that charges are made individually based on usage and are calculated in a way that does not contradict other laws.*

Currently, calculations of utility costs - hot and cold water, gas, etc. - are assessed based on the number of people living in an apartment while according to paragraph 4 of the *Temporary Condominium Regulations*, these costs are based on an apartment's area in square meters. For this reason, either the federal condominium law or the current procedure has to be changed so that the two are compatible.

*15. The procedure used to calculate votes must be clarified.*

Provisions for the calculation of voting rights and share of common space in the current federal law are open to interpretation. Firstly, there is no specification in the current legislation as to how, practically, the votes of the municipality are limited to 30%. Secondly, the federal law should spell out how a member's ownership interest in the association's common property is determined so that each member contributes in proportion to his interest in the common property. Ideally, a member's ownership interest in the common property should be defined as a ratio of the size of his residential and/or non-residential unit to the total size of the condominium property.

*16. The types of charges that commercial versus residential owners pay must be clarified.*

Because condominiums contain both commercial and residential occupants, both are liable for payment of common charges. However, there are many common costs - like elevator repair and courtyard improvement - that do not effect the space of commercial owners who subsequently, feel that they should not be liable for these costs. This situation is further complicated by the fact that the condominium legislation is purposefully vague as to for which types of common costs the

commercial owners are or are not liable. This situation can not continue, however, if there is to be a smooth national roll out of the condominium program.

*17. A system to enforce payment of condominium fees needs to be developed.*

At the moment there is no effective tool to make members pay their fees as required. Nor is there a procedure to evict owners and renters for failure to pay. If condominium associations are able to function effectively, a penalty system for failure to pay - through eviction or another form of legal recourse - should be developed.

This is a minimal, not an exhaustive, list of prerequisites for the roll out of a nation-wide condominium program. Without strong local support or these preconditions at the federal level, any type of roll out program will involve constant battles with municipalities and residents of individual buildings. The Yaroslavl experience has proved these issues to be manageable for a pilot program but impractical for a national program. The experience of the Voucher Auction Support Group suggests that even when there is a federal program that is mandatory and fairly well defined, there are still a myriad of issues to deal with. Without a federal program it can only be worse.

### **C. Built In Space Sales**

Delays in the passage of legislation related to sales of built in space kept Bain from implementing built in sales in Yaroslavl. However, given Bain & Company's work on condominium issues in Yaroslavl, we have been able to monitor the legislation process and provide advice to the GKI on the practical implications of its legislation.

Legislation related to the sales of built in space was first passed in March of 1994. However, because of deficiencies that Bain & Company highlighted for the GKI, the original law has been replaced by new legislation. Currently, sales of built in space should be performed in Russia according to three pieces of legislation:

1. The 1994 State Privatization Program (December 24, 1993);
2. The Fundamental Provisions of the State Privatization Program after July 1, 1994 ('Post-voucher Privatization Program');
3. Methodology recommendations on Applying the Fundamental Provisions of the State Privatization Program after July 1, 1994. (This document being basically a GKI explanation of how to apply the above mentioned documents).

Because the methodology of built in space sales is explained in these documents, they supersede all previous GKI regulations.

The main points of the legislation are the following:

1. The right of space, including built in space purchase can be exercised by the following groups:
  - Persons and legal entities who are property owners, and who became owners of this property according to agreements to lease with the right to buy. In essence, this means that if you own a small scale businesses' store counters, shelves and other equipment, you have a right to buy the premises it occupies as well;
  - Stock Companies which have sold 75% or more of their shares;
  - Persons and organizations who acquired the right to lease a premises at an auction or tender.
2. The application for the purchase of space can be submitted to municipal property committees at any time during the lease.

3. The methodology of determining the price at which to sell commercial space should be developed by local authorities within two weeks after the legislation was published, or August 5, 1994. However, the final price should not exceed the amount of annual rent multiplied by 2 for built in space and multiplied by 3 for separate, stand-alone buildings. If a local methodology was not developed, then spaces should be sold at the maximum price, i.e. the annual rent multiplied by 2 for built in space. This provision theoretically should lead to increases in rents charged by local authorities and this alone should have a positive effect on space utilization if tenants do not have restrictions on the use of their space.
4. The application to purchase premises can be rejected only if the space is located in a historic building which is a historic monument of national importance and if privatization of this building is prohibited. A list of historic monuments of federal importance is scheduled to be compiled by the Russian Federal Government. Other premises located in historic buildings can be sold if a 'preservation treaty' is signed by the purchaser with the municipality.

While the current legislation is an improvement over the previous version, there are still issues that need to be addressed by the federal Russian government in order to insure that implementation of this law proceeds with its intended effect, that is, rapid privatization of commercial spaces leading to a more efficient commercial real estate market and eventually more small scale businesses.

The federal Russian government should take the following steps:

1. *The federal legislation should be clarified so as to allow those who purchased their enterprises at auction or tender to purchase their space.*  
The new fundamental provisions of the state privatization program contain a passage that may contradict the right, established in the 1992 privatization program, of the purchaser of a small scale enterprise to purchase the premises of his shop. Thus, some local governments may try to keep large numbers of enterprise owners from purchasing their premises even though they received the right to lease their space as part of the enterprise purchase process.
2. *A limited list of historic monuments of national importance should be developed at the federal level.*  
In Yaroslavl, as in many cities within Russia's 'Golden Ring,' there are a large number of buildings deemed to be of historic importance. The municipal and oblast authorities have traditionally used this distinction to limit leasing of such sites, or when sites are leased, to force tenants to perform expensive restoration work before they can move in. The buildings deemed historic vary greatly in importance even by the oblast's own calculation. Many are just old, most are crumbling. As most of these sites would have no historical importance in any Western sense, a building's distinction as a historic monument only limits the ability of small businessmen to find space.

In order to a) limit the number of buildings on the national historic register, and b) speed up the process of creating such a register, certain steps should be taken. The federal government's agency, the Committee on Historic Monuments Preservation, should create a list of historic sites by giving each oblast a strict set of criteria for buildings that receive such a distinction and then asking each oblast to submit details of buildings that they wish to include on the historic register within a very strictly limited time frame, e.g. a month. The committee would then only accept buildings that met all of the strict criteria and had all papers submitted within the appropriate time frame.

3. *Criteria should be developed at the federal level for determining historical monuments at the oblast and municipal level.*

For the same reasons mentioned above, the number of buildings distinguished as historic but without national importance should be severely limited. The creation of a list of historic buildings without national importance should follow a path similar to those of national importance. By that it is meant that the Committee on Historic Monuments Preservation should develop a slightly less strict set of criteria for historic buildings without national importance that would give local authorities less discretion. The oblasts should then submit information on buildings they wish to have this distinction within a very limited time frame. This process could be done at the same time as the application for historic buildings of national importance.

4. *A standard 'preservation treaty' to be used for spaces within historic buildings should be developed at the federal level.*

Beyond the development of a list of historic buildings, a standard preservation treaty should be developed quickly in order to not delay space sales. Municipalities and oblasts have no incentive to develop preservation treaties as this process will take some time and will only help built in space sales that they will not necessarily endorse. Also, if local governments do develop preservation treaties they are likely to structure them so as to maximize the amount of money that a purchaser spends on restoration.

In order to insure minimal local interference and delays, a standard treaty applicable to all historic buildings should be developed at the federal level by the Committee on Historic Monuments Preservation. The current legislation sets no time limit, and mentions no responsible body for developing a preservation treaty. This has to be corrected and the committee should be given a deadline in which to develop such a treaty making it as simple and non restrictive as possible.

5. *Legislation guaranteeing the legal rights of space owners should be developed.*

Since private owners of built in space have only just recently started to exist and since many current 'owners' of built in space got their properties prior to the new legislation and thus from municipalities operating outside of their jurisdiction, the legal rights of space owners are vulnerable to attack. The federal government should, therefore, a) guarantee the rights of owners who received their property prior to the current legislation being passed, b) clearly state owners' rights and c) establish a system guaranteeing the defense of those rights in a court of law.

#### **IV. Lessons Learned / Operating Principles**

Through the implementation of pilot real estate reform programs in Yaroslavl, several lessons were learned. Reviewing these lessons has allowed us to create a set of operating principles that should help guide future reform work. These principles are directed towards three primary groups: 1) federal Russian agencies like the State Property Committee (GKI) and their direct advisory groups like the Russian Privatization Center (RPC), 2) donor agencies like USAID and 3) technical advisors like Bain. Before detailing these principles, it is necessary to clarify within which context of reform they are applicable.

##### **A. Types of Reform**

To be effective, Western aid to reforming economies like that of Russia has to respond to a very difficult environment; one that has too many problems with too few resources available to solve them. The goal of aid in this type of environment has to be to respond to crises and create the right basis for further changes rather than optimize the whole economic and political system. To address these crises Western aid should achieve one of the following four objectives:

1. National Program Design
2. Low Cost Reform Institutions
3. Demonstration Projects
4. Pilot Programs

##### **1. National Program Design**

The first possible objective that aid can achieve is assisting in the design of national reform programs. Typically, these would be programs with great potential impact that would benefit from a Western perspective. Advisors involved in these programs can provide information on programs that take place outside of the host country and assist in the design and drafting of legislation. An example of this is the USAID support given to develop Russian capital markets which included creating shares through the design of the voucher auction program and currently includes the development of clearing and settlement systems and a proper regulatory framework. In this area, knowledge of other countries' capital markets was necessary to build such a market in a country where it had never previously existed.

##### **2. Low Cost Reform Institutions**

Achieving the second objective, low cost reform institutions, means finding a low cost way to implement and continue the reform process once hired advisors have left. The idea is to build a low cost institution that involves local people in the reform process and establishes clear guidelines that will help these people adapt to the environment as it changes. In achieving this objective, aid moneys can be used to pay for the institution that should be able to proceed with little or no outside help. An example of this is the Voucher Auction Support Group that consisted of over 20 Russian professionals whose salaries and operating costs are financed by USAID. The group was hired and is currently supervised by a group of 5 Bain advisors. Until voucher auctions end in July of 1994, the group takes on the responsibilities of monitoring voucher auctions and supporting auctions in regions that need assistance in achieving federal objectives.

##### **3. Demonstration Projects**

Establishment of a demonstration project is the third objective that aid moneys can help achieve. The demonstration project is a first time implementation of new legislation. These projects are used to generate awareness and support of the new legislation, and tend to be ends in and of themselves rather than means to test the new legislation. As large, first time projects, they tend to require large amounts of time and outside help. One example is the privatization of the Bolshevik Biscuit Factory, one of the first major privatizations done in Russia. The purpose of this project was to show that privatization was possible and that the vouchers distributed to every Russian citizen had some value. This project included

the technical support of a team from the EBRD and CS First Boston over a 6 to 8 week period. In order to get the privatization to happen, special dispensations were given from the mayor of Moscow and documents were pushed through quickly. The project was successful in generating publicity but because of its special nature, could not be practically repeated and thus did not provide many lessons.

#### **4. Pilot Programs**

##### **a) Pilot Definition**

The fourth objective that aid moneys can help achieve is the establishment of a pilot program. Pilot programs are defined here as being like demonstration projects in that they implement reforms prior to the completion of all necessary legislation. However, they are different than demonstration projects in that their aim is to ultimately develop a roll out program with national implementation. Pilot programs take place prior to the development of a full set of incentives and penalties that drive towards one solution. Through initial implementation on a small scale, the pilot program identifies obstacles and issues that need to be addressed in order to create a legal and economic environment conducive to future implementation. Pilot programs also tend to be under the supervision of a host of federal and local government agencies whose rules and motivations may be contradictory.

##### **b) Pilot Phases**

There are four phases to a pilot implementation program. They are as follows:

1. Program Design
2. Pilot Execution
3. Federal Changes
4. National Roll Out

##### **(1) Program Design**

The first phase is program design which follows a series of steps. These steps include first defining what the basic symptoms of the problem are and, based on those symptoms, defining the goals of the program. Care needs to be taken to define the primary goal and the corresponding secondary goals that need to be achieved before achieving that goal. Once the goals are set, analysis is done to design solutions that will resolve the underlying cause of the problem, and, in turn, achieve the reform goals. This solution should include the development of appropriate incentive systems and legislation. Once this is done, a plan on how to execute the program should be developed.

For example, in the case of small business development, the basic symptom was that small businesses, once privatized, did not improve greatly. Given that symptom, the primary goal was to improve the development of small businesses and the solutions proposed included improving access to real estate. More specifically, the secondary goal included the establishment of a system that will allow owners of spaces within a single building to cooperate, i.e. condominiums. The way to achieve this goal includes the development of appropriate federal and local condominium legislation including a standard charter and regulations on the distribution of maintenance subsidies to condominium associations.

##### **(2) Pilot Execution**

The second phase of the pilot program is pilot execution where the reform program is implemented for the first time in a local government. On the local government side, this involves developing relationships with local officials, educating local officials about the benefits of the proposed reform program and lobbying for passage of necessary local legislation. On the public side, it involves publicizing the new legislation and training the local citizens. Finally, once completed, the funding agency, the federal Russian agency and the advisor need to measure the program against the original goals and identify issues that either limited the success of the program in the pilot or will limit the success of the program

once it is rolled out nationally. The real estate reforms implemented with Bain's assistance in Yaroslavl are all examples of pilot executions.

### **(3) Federal Changes**

The third phase is making changes - legislative and/or procedural - at the federal level. This is a critical step and can occur before the pilot execution as well as after. The amount of work in this phase depends on how many federal changes are deemed necessary to make the program successful on a national basis. If necessary changes are not implemented during this phase, the pilot execution is destined to be merely a demonstration project with little chance of being repeated. One exception, however, is when all necessary legislation is in place, in these cases, changes are not necessary and the appropriate next step is a roll out. Assuming that federal changes are necessary, this phase involves taking into account all the obstacles and issues identified during the pilot execution phase and developing solutions to them on both a legislative and non legislative basis. Once these solutions are developed, the appropriate federal agency responsible for the changes has to be identified and then lobbied to insure approval. This is the phase that the condominium program needs to go through in order to become truly implementable at the national level.

### **(4) National Roll Out**

The fourth and final phase of the pilot program is a national roll out of the reforms. At this point, the program as developed has to be publicized and manuals and guidelines to the program should be developed and distributed. One federal agency should be made responsible for answering questions and enforcing compliance. Deadlines and reporting guidelines should be set with the local governments and progress should be monitored. The central authority in charge should then follow up with localities that fail to show the proper progress. This is the approach used with the Russian small scale privatization and voucher auction programs. In both programs, publicity was used extensively, the GKI is the main authority and lackluster regions are given assistance to improve their performance.

The operating principles developed during the Bain work are applicable to all steps of the pilot reform program. The operating principles can be broken down at several levels. First are those principles that are applicable in general to any pilot reform programs involving federal coordination and local implementation. Secondly, there are principles applicable to the implementation of any small business development programs. Thirdly, there are principles applicable to any real estate reform program and lastly, there are those principles that are applicable specifically to the real estate reforms undertaken: real estate registry, leasing, and condominiums.

## **B. General Pilot Reform Program**

### **1. General Principles**

In general, any reform program, in order to be successful, needs to follow three general principles:

- a. Simplify the process and minimize the costs of reform to participants
- b. Empower the people involved
- c. Commercialize the process wherever possible

#### **a) Simplify the process and minimize the costs of reform to participants**

In a broad sense, the reform process in Eastern Europe can be categorized as an attempt to apply rational, market based processes where before there were irrational, bureaucratic processes or no processes at all. Where processes are already in place, as in municipal leasing of space, they typically are set up so as to make market led activity as difficult as possible. Where processes have not already been established, as in the privatization of enterprises, there is a strong likelihood that new processes developed could be

either misunderstood or made deliberately complex by government officials. In addition, complex processes are often costly to follow. Either way, the result of complex processes is that reform is slowed or even stopped.

The solution is simplification. In the case of leasing in Yaroslavl, a system existed that was complex, with no set time frame or criteria for approval or disapproval. Would-be entrepreneurs trying to obtain a lease either were successful because they had a connection with the city government or were unsuccessful, caught in an endless cycle of trying to obtain approval from a myriad of city agencies that eventually lead to frustration but no lease. The only way around this is to reorganize the process, limiting the steps involved and the approvals required while making approval automatic after a limited time period unless an application meets a limited, predetermined list of rejection criteria. The process should be created so that it is transparent to the public and government officials would have to expend an exorbitant amount of time and effort to keep the reform from happening. As mentioned earlier, the current condominium registration process is complex and costly. This made implementation of the pilot condominium program difficult, but, unless there is strong local support, it will make implementation of a national roll out all but impossible. The changes recommended above are aimed at both simplifying the process and making it less expensive.

**b) Empower the people involved**

Reforms and new processes do not occur by themselves, people have to make them happen. In a pilot program, it is often the advisor who is pushing for the reform to happen, but this is not enough. It is not enough to make the pilot program a success and it is certainly not enough to make a national roll out a success. What is required is the full involvement of a government official or group of officials that feel that successful completion of the reforms will benefit them personally. These officials also must be given the power to push the reforms through and insure that reform goals are being met. In the example of leasing reform, part of the simplification of the leasing process included eliminating most of the approvals of other city agencies and giving one agency, the local property committee, all of the power and the benefit of leasing approvals. The person in charge of the leasing process within the property committee, the deputy head of the property committee, was thus empowered to make leasing approvals both during the reform process and after.

**c) Commercialize the process wherever possible**

Reforms, by their nature, require a large amount of time and often a set of skills that local officials do not have. Beyond empowerment of government officials, the best way to insure that the reforms happen is to let someone, preferably a private citizen, make money on it. By this it is meant that a guiding principle of any reform process is to make part of the process dependent on market principles so that individuals that provide a service are rewarded for it. To some extent, this is merely applying the basic principle that already exists in local Russian governments; if you want something done, you have to pay for it, often in the form of a bribe to a government official. The concept here is to legitimize the paying for a service and to, wherever possible, allow more than just a single city agency to compete for the providing of that service. In Yaroslavl, the provision of information from the real estate registry, while not handed over to private individuals, became a service that the property committee, the BTI and other agencies could provide at a cost. Thus, the provision of real estate information became commercialized with several agencies competing to provide that service for a competitive price. The end result is that the public has a relatively cheap source of information from agencies who have the data and have an incentive to sell it whereas before the information was guarded as a secret.

Beyond the general principles, the operating principles for any pilot reform program can be divided into three categories. The first categories deal with project definition, the second with project preparation and

the third with project implementation. While these principles apply mostly to the second phase, pilot execution, they are also applicable to a large extent to all four phases of a pilot implementation program.

## **2. Project Definition**

Before planning the program, it is critical to define its goals, both primary and secondary and at each phase. This includes reaching an agreement between the federal agency, the donor agency and the advisor on well defined and tangible goals for the project. In developing the goals it is useful to look to regions within the host country or other countries for ideas on where goals should be set. In the goal development process, there should be a clear understanding of the trade-off between impact and relevance. This means understanding that major changes to one enterprise or piece of property, while being significant for that enterprise or property, are not necessarily relevant to the greater program of reform. It is often the case that the primary, long term goals of the project concentrate on relevance while the secondary, short term goals concentrate on establishing initial impact. Examples of primary, long term goals that guide all phases of a pilot program are the privatization of all companies or the improvement of small business development. Short term, secondary goals that apply to the pilot execution phase include the registration of 4 condominiums or the creation of a computerized property registry for a city district. Going through this process insures that the success of the project can be measured and that misunderstandings amongst the parties involved are minimized. This also insures that all parties involved in the project are always focused in their work and that lack of progress towards achieving stated goals can be used to chide reluctant players.

## **3. Project Preparation**

In order to prepare for implementation of a pilot program, the following steps need to be taken:

- a. Determine at what level, national, oblast, or city, it is appropriate to operate.
- b. For pilot execution work at a local level, pick a locality that is both representative and willing to participate in the reforms.
- c. Properly introduce yourself to the appropriate government officials.
- d. Assess the power structure existing within the government and identify the key players.
- e. Determine the objectives and motivations of the key players.
- f. Convince key players of the benefits to them of achieving the project goal.
- g. Have the appropriate government agency(ies) commit to proceeding with the reforms.
- h. Develop a work plan that details activities.
- i. Assign responsibilities for completing the activities to the appropriate people.

### **a) Determine the right level**

The first step in preparing for implementation is determining at which governmental level, city or oblast, does the responsibility for the reform program lie. This is an issue given that certain areas of the law fall within the realm of only the federal government, others within the oblast's realm while still others are better addressed at the city level. Unfortunately, given the vagaries of Russian law, determining which level is appropriate is not always easy. With regard to real estate reform, the city exercises control over municipal property and housing but legislation related to housing can be passed at no lower than the oblast level. To solve this issue in trying to register condominiums, a federal law was passed and the GKI gave permission to the city of Yaroslavl to develop its own condominium legislation, thus eliminating the need for oblast involvement.

### **b) Pick the right locality**

If it is determined that pilot execution work will be required in an oblast or city, the next step is to determine which city or oblast will be appropriate. Because the pilot execution is being done to test implementation ability and identify potential issues that would arise during a national roll out, the locality needs to be as representative as possible. At the same time, the locality had to be interested in

proceeding with the reforms and being part of a pilot project. These two criteria are sometimes contradictory because those localities that are seemingly most interested in making reforms (e.g. Nizhny Novgorod) are by that quality alone not representative. There needs to be, therefore, a balance between the two criteria so that both are found in the same locality.

**c) Properly introduce yourself**

Once the proper government agency is chosen, initial contacts should be made in order to let the advisor properly introduce himself while making officials aware of the potential pilot program. The chief contact should be able to help facilitate such contacts with an official letter of introduction explaining the scope and purpose of the advisors' work and requesting cooperation. A letter of introduction notwithstanding, because of a distrust of foreigners created during the Soviet era, it is critical to establish a proper understanding of the advisor and his role with government officials. The advisor should take time to explain not only his role as an agent of the federal government but also how he is being funded and how donor agencies, in general, provide funding to federal agencies and local governments. Given that most local governments have budget constraints and view Western advisors as sources of direct financial aid, the advisor should be clear as to whether or not it will be providing any such aid. The advisor should also give as complete a description of his company as possible elaborating on the types of projects it undertakes and the fact that the program being worked on is not the only one the company has. Doing this will help allay likely government officials' fears that the advisor is a spy, perhaps sent by a foreign government, that wants to steal government secrets and use them for commercial gain.

**d) Assess the power structure**

After making appropriate initial introductions, the next step is to assess the power structure of the identified local government or federal government agency. This means identifying the key persons whose support is needed to successfully implement reforms. In many cities these key people often include the mayor and one or more of his deputies. Other influential members of the city administration and дума may also be considered key people. Which position or person is critical to the success of the project depends on the type of project being undertaken (e.g. real estate reform vs. telecommunications improvement) and which locality it is undertaken in.

**e) Determine objectives and motivations**

The next step is to determine what the motivations and objectives of the key players are. The motivations of a city mayor are usually to retain popularity, increase investment in the city, reduce city costs and increase city revenues. They may also be to increase control over businesses or increase personal income. Whatever the motivations are, as a representative of the federal government and a large donor agency, an advisor quickly learns of at least the stated needs of government officials he interviews. It will take more time to understand the officials' true, hidden objectives.

**f) Convince key players of benefits**

Once the objectives of the key officials are made clear, the benefits of the project should be restated in a way that satisfies those needs. Both short and long term benefits should be defined. For example, the idea of implementing real estate reforms was presented to the city of Yaroslavl as a way for them to increase exposure to the foreign investment community and to international donors. The benefit of the real estate registry was that it allowed the city to track the space it owned and thus maximize potential real estate revenue. The benefit of condominiums was that they allowed the city to control its expenditures on maintenance. The communication of benefits should be made not only to the key players, but to all officials that will take a part in the program so that they are committed to the project.

**g) Get a commitment**

After the benefits of the project have been illustrated, an agreement should be developed and signed between the advisor and the government agency. The purpose of the agreement is not to create an iron clad contract but to force the governmental group to show its commitment in cooperating with the advisor. The agreement is also useful in showing lower level officials that the advisor has authority from the appropriate superiors to receive information.

The agreement should clearly outline goals of the project but still be flexible in describing activities. The obligations of both the advisor and the governmental group should be made clear. Because advisors are often paid for entirely by outside funding agencies, advisors should insure that governmental groups involved in the reform process make their commitment clear by agreeing to 'pay' for the reform process in one way or another. By this it is meant that these governmental groups should give something up so that psychologically they feel that they have something at stake if the reform fails. This 'payment' would include allowing access to all necessary data, providing office space and a telephone (for which the advisor should pay reasonable fees), and identifying a working group of city officials who will be responsible for the outcome of the project. The advisor should commit to paying for all expenses for extraordinary data and office expenses, developing necessary legislation and other documents, and acting as a liaison between the sponsoring federal agency and all other relevant governmental groups with regard to the legal area covered by the project.

**h) Develop a work plan**

Once an agreement has been signed, the next step is to develop a detailed work plan that outlines activities, not only for the advisor, but for all parties involved. The work plan requires a listing of activities, along with the party responsible and the timing allowed for completing those activities. The work plan should be developed in conjunction with and distributed to all relevant parties - the advisor, the federal agency(ies), the donor group and the local government.

The first step in developing the work plan is to outline, in as much detail as possible, all the activities needed to achieve that goal. In the case of the property registry, the activities included designing the property registry database structure, developing a database based on that structure, gathering all the necessary information, inputting the information into the database, testing the information and developing an agreed upon methodology to update and distribute the information in the database.

**i) Assign responsibilities**

Once activities are outlined, the advisor should specify which party is responsible for completing each activity. For example, in the case of creating a computerized property registry, the advisor, Bain & Company, was responsible for coordinating the efforts of city agencies, drafting agreements and supervising database creation. Several city agencies were each responsible for contributing their relevant information to the city property committee which was in turn responsible for inputting the data into the database.

In the same way that it is critical for each player to be aware of the goal, it is critical that each player knows what its individual contribution towards achieving the goal is by understanding what activities it is responsible for. The party responsible should be a specific person or group of people rather than an organization so that individuals feel personally responsible for completing assigned activities. Each person assigned to a task should review the work plan and sign off on it to show their commitment. To maximize commitment, the task should be linked to the personal success of the individual responsible for it. Again, the idea is to minimize misunderstanding and develop a very clear sense of purpose for all parties involved.

What is crucial is picking the right people to perform the assigned tasks. Often, it is the chief contact both within the local government and the federal agencies that is the most crucial to pilot success. For pilot execution, the chief contact chosen within the local government should be both someone with the appropriate level of power - as mentioned earlier - but also someone who can be relied upon to complete the task and convince others of the merits of the program. As an example, in Yaroslavl, the chief contact was the deputy mayor who had ultimate responsibility over any reforms undertaken in the city, including those related to housing and real estate. His success was thus clearly linked to the success of the condominiums. As a deputy mayor, he had influence both with the mayor and a variety of lower officials whose cooperation was needed to implement the project. Successful implementation of the project would not have been possible unless we had him as an ally and it was clear what we needed him to do.

Within the sponsoring federal agency, the chief contact should be the project's champion, someone who at every phase of the pilot program is effective in getting decisions made and powerful enough in facilitating official Russian contacts with both local governments and other federal agencies. The contact has to be someone who is committed to all phases of the program: design, execution, federal changes and national roll out. In the Yaroslavl project, the chief contact at the RPC was its head, Maxim Boycko, who had a limited ability to coordinate and gain the approval of all relevant federal agencies but still was able to get the GKI deputy minister Vassiliev to sign letters giving official requests or authorization for issues over which the GKI had jurisdiction.

Beyond picking the proper participants within the local government and the federal agencies, serious consideration should be given to using resources outside of government to perform sensitive analysis. This outside resource can be the advisor or a subcontractor. For example, in compiling the city real estate registry, students were hired at low cost to first gather data on sites and then, after the data was inputted by city employees, check the data accuracy to insure that city employees had not purposefully left out empty spaces that they could illegally but lucratively lease out without official knowledge.

#### **4. Project Implementation**

Several operating principles should guide the advisor during implementation in the last three phases of the pilot program. These are summarized below:

- a. Staff your local team with mostly Russian staff, preferably from different areas of the country, not just the capital, and preferably with someone from the area where the reforms are taking place.
- b. Keep an office in the area of the governmental group but distance it from government officials so that sensitive issues can be discussed freely.
- c. Be prepared to talk about reforms in general to local officials and citizens before talking about your specific project.
- d. Compare the city's reform program and current situation to that of other Russian and East European cities and encourage interaction between cities.
- e. Build and work with a client 'team' that is responsible for reforms
- f. Spend at least 3 days a week with the relevant government officials and contacts - the more contact the better.
- g. Build a program that will be sustainable after the advisor leaves by utilizing local resources whenever possible.
- h. Insure that information related to reforms is taken out of the hands of local agencies and put into the hands of the public
- i. Use direct funding of fundamental parts of the pilot program in order to limit negative financial consequences for pilot participants and provide quick, observable changes.
- j. Use travel and other perks not only as a reward for government officials who complete crucial tasks but also as a means to educate officials
- k. Find ways around obstacles rather than through them.

- l. Constantly update both the sponsoring federal agency and the funding agency of progress, issues and needed reform program changes
- m. Use public relations as much as possible to make the public aware of the reforms taking place

**a) Staff the team with Russian staff**

As alluded to earlier, all advisors need to be aware of the impression of government officials and citizens alike that reforms funded by international funding bodies are being imposed on them by foreigners. It is therefore critical that the bulk of the advisor's team be made of natives of the country in which the reforms are taking place. Some foreigners may still be beneficial, however, because some officials and citizens do not trust their own natives and appreciate a Western authority giving an objective view point based on experience outside of the country. Beyond having natives, having diversity amongst them is critical. Some citizens and officials distrust anything coming from the federal government and therefore distrust any native advisor who lives in the capital city. Some local citizens distrust local authorities and only trust directives from the center and they therefore may distrust advisors native to the locality where the reforms are taking place. In short, an advisor team should be staffed with a variety of people who will be appropriate in avoiding conflicts based on the prejudices of contacts.

For example, on the Bain small business development case, almost all contacts made with the city of Yaroslavl involved seven Russian staff who came from both Moscow and Volgograd. Two foreign staff on the team were more senior and met with city officials on official occasions such as the signing of the cooperation agreement between the city and Bain. Having only Russian staff from two cities deal with local residents helped allay the fear that a) condominiums were purely a foreign invention that was b) being imposed on them from Moscow. Both foreign staff and senior Russian staff provided information to the GKI and USAID on a regular basis. This reinforced the impression that there was an appropriate level of local knowledge coupled with a broader Western perspective.

**b) Set up a local office**

Once the staff is assembled, the advisor should establish a local base that will facilitate interactions with citizens and government officials while allowing some privacy. This means establishing an office separate from government officials. In Moscow and other capital cities where a commercial real estate market exists, this is relatively easy to do, but in smaller cities establishing an office may be difficult. As a result, obtaining office space in localities usually requires the influence of local officials and often this space is in government buildings. As mentioned previously, using officials' influence to find office space may not only be necessary but also desirable as it displays a commitment on their part towards the reforms team.

Given the likely close proximity of suspicious, local officials, it is important to have a separate space where contentious issues related to the program can be discussed openly by the advisor team. In Yaroslavl, the Bain team was given a separate office across from the deputy head of the property committee. Despite the fact that this office was close enough to those of key official contacts that face to face communication was relatively easy, having the office separated from the rest of the property committee meant that the team could use the office to discuss how to deal with sensitive issues, even those that related to the deputy head of the property committee.

**c) Be prepared to talk about reforms in general**

Advisors represent their federal sponsoring agencies and are the first face of reform for most local citizens and officials. As such, the advisor should expect to be questioned about almost all major reforms before he can begin to speak about the particular reform he is trying to implement. This is especially true when speaking to local citizens. To address this issue, the sponsoring federal agency should provide the advisor with background materials and any available press releases or information packets that would

help facilitate the education of local citizens with regard to reforms. The advisor should use these materials and any others to prepare for an explanation of general reform programs before beginning to explain the reform goals of his pilot project.

**d) Compare reforms in the target city to other Russian cities**

It is likely that the problems facing the target city have been faced by other Russian cities. Many cities, not only in former Warsaw Pact countries, but also in Russia, may have attempted reforms to address these problems. In establishing reforms in Yaroslavl it was important to emphasize these facts for two reasons. Firstly, city officials are comforted by the fact that reforms had already been done in other cities and are usually very interested in learning about the process from counterparts in other cities. Secondly, knowing that other cities have already established reforms can set off the competitive spirit of city officials especially when it is understood that these reforms are attracting outside investment.

**e) Build a client team**

As was mentioned earlier, it is critical to assign activities to individuals within the appropriate government agency(ies) whose personal success is linked to the success of the reforms. These individuals together should form a team that works together with advisors on implementing reforms. As members of the reform team, these government officials take part in the data gathering, data analysis and the decision making. Their close involvement with the advisors is needed in order for them to feel a personal stake in the reform process. Once they feel this way, they will be better able to withstand potential criticisms of the reforms from both within and outside of the government and they will be better able to continue the reforms once the advisors leave.

**f) Spend at least three days a week with officials**

Implementing change in a reforming economy, either at a local or federal level, takes a large amount of time. This time is needed for two reasons. First, officials are busy with their own reform projects and in running day to day operations. For them, additional pilot reform programs are an additional, unwanted burden. Secondly, by definition, reforms are radical changes to the status quo and as such are hard to accept. For most reforms, it takes a significant amount of time educating, persuading and cajoling officials before they become true supporters of the reforms. As indicated earlier, this support is critical to the success of any pilot reform program. The time that pilot programs require demands that the advisor be in the locality, meeting with government officials at least three days a week. This has the effect of not only getting more time with officials but also the additional effects of showing the commitment of the advisor to the locality or agency and creating a better awareness of the broad issues facing that governmental body. Often, additional time is required to provide support on broader issues that are top priority for local officials - even if they are not directly related to the issues being covered by the reforms - so that the reforms can continue.

**g) Build a sustainable program**

The key challenge of a reform program is in making it sustainable without requiring help from outside advisors. This requires developing a set of incentives that will foster the development of local resources that will perform necessary activities. While some level of advisor support is expected in the pilot execution phase, the goal is to seriously reduce this involvement by the time of the national roll out. Doing so will depend on what federal changes are suggested and made at the end of the pilot execution phase. In order to develop the proper set of incentives for local involvement, the pilot execution phase should be used as a testing ground for local involvement. This can be done by always questioning when an activity could be done by a local group versus the advisor and what would motivate that local group to continue to do that activity after the advisor has stopped his supervision. In the case of Bain's real estate registry work in Yaroslavl, a local software developer rather than another outside advisor was hired to develop the registry's database. While USAID funds were used to pay for the development and

distribution rights of the software, the programmer has an incentive to distribute this software to other Russian cities because he can increase his revenue by modifying this software to suit individual city needs.

#### **h) Put information in the hands of the public**

Besides encouraging local involvement, another way to insure that market dynamics create an environment where reforms continue is to create systems where information related to the reforms is removed from the exclusive confines of city agencies and made available to the public. This involves two activities. The first and more difficult activity is creating systems whereby the city freely releases information to citizens that ask for it. This is critical because many government agencies make a business of trading in information but do so with a limited clientele. The ways to address this are first to break any monopolies that agencies have on information and allow agencies to publicly sell the information they have. The second activity is to publicize new legislation and reforms as soon and as broadly as possible explaining what the reforms mean to the average person and defining the rights and obligations of both the government and the citizens under the reform program. Manuals describing practical details and 'how to's' should also be developed and distributed to relevant citizens.

In developing the real estate registry in Yaroslavl, Bain realized that the real value of it was in giving citizens information on the availability of municipally owned commercial space. This information was originally held exclusively by the property committee, but, with Bain acting as an intermediary, was released to other agencies in return for other real estate information. Once all agencies had access to all of the city's real estate information, a mayoral decree allowed all of the agencies to sell the information at prices they could choose. In effect, this created a free market for real estate information. Once this system was established, the mayoral decree along with an article explaining how to receive real estate information was published in the local newspapers.

#### **i) Use direct funding of the pilot program to show observable changes**

Because pilot programs are developed ahead of the development of full laws and regulations, the costs of proceeding with reforms may be high for those citizens directly involved. Typically most outside funding of pilot programs go towards payment of fees of outside advisors, who, while critical to creating a pilot program and driving its implementation, are not intended to be the program's main beneficiaries. The advisor, however, as a recipient and distributor of outside funding has the leverage to use those funds to achieve program goals by directly applying funds towards reducing program costs that can not be reduced in the short time frame of a pilot program. The use of these funds will keep the program going and increase the rate at which visible changes - critical to the pilot's success - occur. Once the pilot is completed the advisor can work on suggesting practical and legal solutions to the process in order to reduce costs.

As has been previously mentioned, the condominium program as it currently stands is relatively expensive to implement. The various costs associated with registering a condominium association are quite high for the average Russian to pay. Because these costs could not be reduced without a long wait for corrective federal legislation, the pilot program would have stopped without outside funding. Therefore, part of the USAID funding was earmarked for the payment of these costs. In addition, because the system of providing maintenance subsidies from the city to the condominiums was not completely worked out, outside funds were also used to pay for initial, minor repairs of pilot condominium buildings. These funds, however, were not just given to the condominium associations. Each association had to hold meetings and democratically decide on the appropriate use of funds. Once this was done, the associations had to seek out contractors, negotiate a contract with one of them, supervise the work and approve it before the funds could be distributed to the maintenance organization contracted. The end result of this funding was that not only did pilot program participants have tangible

improvements in their buildings as a result of their involvement in the pilot program, but they also were able to make real democratic decisions and promote private maintenance contractors at the same time.

**j) Use perks as rewards and education**

Another way to channel funds in helping to achieve program goals is to use travel to other areas where reforms similar to those proposed have already taken place. Trips of this kind are typically viewed more as educational opportunities by advisors and funding agencies and more as pleasure trips with opportunities to buy hard-to-find consumer items by government officials. The reality should be that the trip is more of the former than the latter but still both in order to satisfy the officials. Advisors should use these trips to reward positive steps towards reform by officials. For example, in Yaroslavl, the mayor and deputy mayor were taken to the U.S. to tour condominiums and meet with USAID and World Bank officials but only after they had passed necessary local condominium legislation. The justification for this condition being that it did not make sense to study condos and meet with USAID unless their city already had committed to a condominium program. The 6 day trip had meetings scheduled day and night with only a half day of sightseeing and shopping. The officials viewed the trip as a great learning experience and were satisfied with the free time allotted.

**k) Find ways around obstacles**

The most important factor in every phase of a pilot reform program is dealing with problems effectively. Implementing radical reforms means covering new and uncharted legal ground and encountering numerous unanticipated obstacles. The main purpose of a pilot execution program is to identify those obstacles and propose ways of surmounting them with federal changes so that the same obstacles are not encountered during the national roll out. Often, during the pilot execution phase where it is important to achieve a secondary goal, the best way to deal with these obstacles is to go around them and then recommend ways to remove them entirely with federal changes. For example, in Yaroslavl, the cost of performing a legal property description required by the federal condominium law was determined to be an average of 1 million rubles. Most condominium associations could not afford to pay this much money. After investigating ways to reduce this cost, it became apparent that the only way to do so would be to change the definition of a legal description in the federal condo law. Given that our pilot execution deadline did not allow for the time required to make such a change, AID funds were used to pay the cost and further analysis of the cost structure was done in order to develop recommendations on how to reduce the cost of such a description for future condominiums.

**l) Update the sponsoring agencies**

The whole process of designing and implementing reforms is dynamic and at each step there is new information that may have an effect on the outcome of the program. This information needs to be communicated to the sponsoring federal agency, the funding agency and all other agencies involved with the reform process on a regular basis so that they are aware of any issues and changes that need to be made to the reform program. Because of the multiplicity of reform programs with similar and overlapping issues, the advisor has to act not only as expert on a particular reform process but also as a coordinator of all agencies involved in the process - even those that the advisor is not directly responsible to.

The advisor also needs to keep in mind that as his knowledge of the reform situation changes it is his responsibility to change the knowledge of the agencies he reports to so that they are prepared to make the changes to the program that the advisor recommends. In the case of the condominium work that Bain had done in Yaroslavl, suggested federal changes to the program were made first in April, 1994 almost a month before the first pilot was registered and five months before the proposed date for permanent federal condominium legislation.

#### m) Use public relations

Reforms are changes to the status quo and as such they are often new and confusing to the public. Public relations is thus critical to the reform process in both informing the public that changes are taking place and in educating them as to what the changes mean to them. Public relations is also critical in minimizing the negative backlash that reforms generate because of misinformation. It is important, however, to use public relations thoughtfully. Effective public relations requires a planned, phased approach rather than a press release here and there. In planning the approach it is necessary to determine which groups will be effected by the proposed reforms and what their concerns will be. Once this is done a variety of media should be used to address the concerns of the appropriate constituent groups. This often requires the development of not only press releases, but informational pamphlets, brochures and informational seminars. Once the target audiences and forms of media are determined, the content should be determined. Content at first is often general and educational explaining the broad concepts of the reform process and answering anticipated questions. At a later stage the content should focus more on practical 'how to's' that explain what peoples' rights are under the reforms and how they can participate in the reforms. While public relations is often the work of the advisor working on a particular reform process, there also needs to be a role for the sponsoring federal agency in this area.

Public relations was used successfully in implementing condominium legislation in Yaroslavl. The first step was identifying the groups that would be effected by the reforms: city officials, the public in general - since almost everyone lived in a government owned building that could become a condominium, - and residents of the pilot condominium buildings. The media used were one to one meetings and seminars for city officials and the residents of pilot buildings, and brochures and eventually press releases for the general public. At first, meetings and the brochure were used to focus on explaining the basic principles and benefits of condominiums, while later, seminars and manuals were used to explain what residents and city officials alike had to do to be registered as condominiums.

Public relations will also be used in promoting the real estate registry on a broader basis. The national newspaper, *Economica i Zhizn*, approached Bain to provide free advertising informing the public of the availability of the real estate database software developed in Yaroslavl. Thus public relations will be used to enable a greater sharing of experience with other cities and would further promote the reform process. In both the condominium and real estate registry areas, the GKI/RPC approved the public relations program but played no active role. This is in contrast to other reform programs - voucher privatization, agricultural land privatization, etc. - where they have separate advisors concentrating solely on public relations

### C. Small Business Development

Several lessons learned can be applied to pilot programs dealing specifically with small business development. These lessons are as follows:

- a. At both the federal and local government levels, there should be one committee that pulls from all of the relevant agencies and authoritatively deals with small business development issues
- b. Federal reform programs have to be created that encourage compliance by providing incentives and penalties for local governments
- c. There needs to be a reduction of controls and restrictions in order to reduce the influence of government corruption and the mafia
- d. The power structure of the relevant government agencies should be examined by understanding the flow of money
- e. Support for small businesses at the government level is minimal and has to be increased by
  - increasing public awareness of small business successes
  - demonstrating the ability of small businesses to absorb the unemployed

- demonstrating ways that small businesses can reduce budgetary pressures
- f. Small business reform programs should be sold as alternative work for city agencies that are losing importance

**a) Build a committee with all relevant agencies**

Small businesses are governed and in turn small business development is determined by a variety of federal and local government agencies. These agencies include the justice ministry that makes decisions on legal structure, the local and federal tax authorities that make decisions on taxation, the local departments of trade and economy that make decisions on a myriad of issues and, for privatized businesses, the federal and local property committees (GKI and KI) that make decisions on management, including profile, and access to real estate. These agencies often work independently and at times their goals conflict. This phenomenon, along with the fact that few of these agencies worry about small business development, has meant that there is no coherent policy towards small businesses. In Yaroslavl, this phenomenon was evident when Bain was told by the head of the property committee's privatization department that although he was willing to drop the profile restrictions placed on some small businesses he could not stop the trade department of the city and district administrations in inspecting these businesses and fining them for operating businesses outside of their original profile.

In order for any small business program to be successful there needs to be coordination and agreement between the agencies that govern small businesses. One way to do this is to establish, on both a federal and local level, a cross-agency working committee that focuses on small business issues and improving small business development. This committee would have to be made up of individuals that held appropriate levels of authority in their respective agencies so that once decisions on the type of legislative changes required were made, each member could go back to their agency and get those changes implemented.

**b) Encourage local compliance with incentives and enforce penalties**

While many federal laws govern small businesses, the real battles of small businesses are played on a local basis. The power of the municipality in controlling small businesses should not be minimized given the facts that privatized small scale businesses were once municipal property and most small businesses rent space from the municipality. It should also not be assumed that municipalities will follow a certain program because a federal law says to. Often, what may happen is that given a new law, the municipality may reject it entirely, accept part of it as a pilot program or interpret the law in a way that is favorable to them but not in accord with the original law. Therefore, in order to get local governments to implement federal laws in the way they were intended, federal programs should include a system of incentives and penalties that encourage compliance at the local level. Federal programs should also be as specific as possible so as to minimize the ability of local governments to violate the spirit of the reform while still following the letter.

Examples of how this principle was both well and badly applied exist in the Russian small scale privatization program. The program was successful in providing positive incentives to privatize by giving the cities a large portion of the privatization proceeds. As a result, a majority of small scale enterprises have been privatized. However, the program was not complete in either its specificity or in its enforcement. The lack of specific requirements for exclusion from the privatization process meant that many cities have kept up to 40% of their small scale enterprises from being privatized. The lack of a penalty or enforcement vehicle has allowed these cities to violate the privatization law - by removing businesses from privatization or imposing profile restrictions for a period longer than the federally set maximum - without any type of reprimand at all.

**c) Reduce controls and restrictions**

Russian small business, even those located in smaller cities, are increasingly plagued by the mafia who extort money for protection and control supply lines. At the same time, local and federal governments, in an effort to raise revenue and increase control, have increased the regulations effecting small businesses. These 2 phenomenon are not wholly unrelated. One of the reasons for the increase in mafia activity - otherwise known as the criminalization of the economy - is the fact that with increasing government regulation it becomes increasingly difficult to make a profit and keep a business running without somehow breaking the law. In initial interviews of small businesses located outside of Moscow, entrepreneurs freely admitted that they cheated on their taxes. While cheating on taxes is an almost international trait among small business people, the fact that the effective tax rate was 70% of profit meant that this trait was more prevalent among the entrepreneurs of Russia than those of the rest of the world. With the recent federal law reducing federal limits on municipal taxation, municipalities have imposed new turnover taxes and increased profit taxes thus increasing the need to cheat. With it being almost a necessity to break the law in order to be profitable, the ranks of small business people are both increasingly filled with and approached by 'mafia' types. In other words, if you are a small business person, you either have to be in the mafia or you have to pay money to the mafia because your technically illegal activities - along with the authorities' lack of power - keep you from calling the authorities to protect you.

Thus, one way to both decrease the influence of the mafia and increase small business development is to reduce regulations. This will allow more people to initially become entrepreneurs while allowing existing entrepreneurs to be honest and still make a profit. Less restrictions will mean that there is more opportunity for all entrepreneurs and that will reduce the need for the mafia to take from others in order to be successful.

**d) Understand the flow of money**

Small businesses are a source of revenue for both federal and local governments. The key to understanding the government power structure as it relates to small businesses, is to, therefore, track which parts of the government receive what small business generated revenue. Once this is done, potential arguments against and for proposed reforms can be anticipated. Understanding the money flow can also insure that reforms are structured in such a way that financial incentives are created that encourage government cooperation. In Poland, municipalities controlled all commercial space and used revenues from the rental of these spaces along with income taxes to support their budgets. In order to encourage small business development, the federal Polish government gave a one year tax holiday on both personal and corporate taxes to anyone who started a business. Because this law in effect made leasing the only source of revenue for municipalities it had the additional effect of encouraging leasing of commercial spaces or increasing supply while increasing demand for commercial space by encouraging the establishment of new entrepreneurs.

**e) Increase government support of small businesses**

Most municipalities have neutral or negative attitudes towards small businesses. The municipalities correctly realize that most of their revenue comes from taxes on large, formerly or currently state owned enterprises. The Soviet attitude was that the only businesses of value were production enterprises and that trading was merely usury and speculation where one bought at a low price and cheated others by selling at a higher price. This attitude still prevails to varying degrees throughout Russia. Any advisor or sponsoring agency needs to combat this view of small scale businesses before they can begin to gain support for any small business reform program.

There are 3 basic ways to increase government support of small businesses. The first way is to increase public awareness of small business success stories in order to encourage others to start businesses by

dispelling Soviet connotations of small business as black marketeering that provides no value to the general public. The second way is to make it clear to local officials by citing examples in both Central Europe and other Russian cities that the large enterprises they currently rely on for tax revenues are likely to reduce their production thus reducing their tax payments and, more importantly, their employment levels. The only way to quickly absorb the likely increase in the unemployed is through small businesses. The third way is to show how small businesses can reduce budgetary pressures. Because most local governments will be skeptical of how much additional revenue they will get from taxes on new small businesses, it is best to emphasize how small businesses can reduce city costs. For example, small businesses can reduce city spending on maintenance and renovation by paying for these costs as they relate to the commercial spaces they occupy.

**f) Sell reform programs as alternative work for shrinking agencies**

Small business reform programs are likely to involve work for the government agencies involved. This work is often initially unwanted because it appears to be an additional burden. However, a great benefit of this additional work is that it provides a justification to keep agencies that are losing importance. In local governments, these agencies often include former planning committees or the privatization departments of the property committees who may have privatized all the enterprises they can. In Yaroslavl, the privatization department of the city property committee realized that it had almost no enterprises left to privatize and that unless it took the lead on building the real estate registry it would have to shut down for lack of work. As a result, the privatization department became a strong supporter of our proposed reforms. *(please refer to slide e in Appendix one for summary of small business development lessons learned)*

**D. Real Estate Reform**

The lessons learned that can be applied specifically to real estate reforms are as follows:

- a. Before properties can be released to the public, there should be consolidation in one government agency of all controlling rights over a single piece of property.
- b. Property registries should be created to make critical information over ownership and status of sites available to the public and to keep properties from being 'hidden.'
- c. The development of third party brokers should be encouraged.
- d. Contacts and cooperation need to be established with all local agencies that control real estate: the PPI, KI, ZhKU, land committee and city architect's office
- e. Standard documents and procedures with maximum time allowances should be established and then publicized so as to minimize the extent of government 'judgment.'
- f. The reduction of government control over real estate should be encouraged by emphasizing the government agency's ability to profit from quick financial gain by selling space or giving out long term, secure leases.

**a) Consolidate controlling rights**

Most pieces of state or municipally owned real estate have three controlling interests. These are the owner who has the right to set rents, the lessor who has the right to lease space and the balance sheet holder who has the responsibility to maintain the space. Typically for municipal properties, these interests are held by different agencies with the city administration being the owner, the property committee (KI) being the lessor and the housing authority (ZhKU) being the balance sheet holder. As was found in phase I of the Bain small business development work, the uncoordinated management of these three critical rental property functions seriously hampers the leasing and eventually the selling of space. The best way to insure that these functions are coordinated and that properties are leased to the public is to have one agency control all three interests within a single piece of property. In Yaroslavl, we saw that when the KI took a property onto its balance sheet it also illegally acted as the owner and

retained the majority of the rent proceeds. The KI was more active a lessor of these spaces versus those that it did not have on its balance sheet.

**b) Create publicly available property registries**

Information on ownership and legal status of real estate is critical to would-be entrepreneurs but it is often hidden and traded for personal gain by the agencies that control it. Properties that may be available for commercial use can be 'hidden' by local officials that say they are being leased out when they are not. This is why establishing accurate, publicly available real estate registries is critical to the success of any real estate reforms.

**c) Encourage the development of third parties**

Government agencies are long accustomed to controlling the use of real estate. These agencies often have difficulty, however, in applying capitalist market principles to that real estate. Agencies should be told of the benefits of minimizing their personal involvement and maximizing potential rental revenue by using a third party. In the case of leasing, this third party would be a private individual who, by receiving a commission on rental revenue, would have an incentive to find tenants who most valued the available spaces and therefore, best utilized them.

**d) Work with the key players**

For almost all municipal real estate there are a few key players that any reforms would involve. They include the Bureau of Technical Inventories (BTI), an oblast agency that keeps general real estate data and information on buildings' physical characteristics and the oblast and city property committees (KI) that are in charge of leasing government owned property. Other players are the housing authority (ZhKU) that often has residential buildings on its balance sheet, the land committee and the city architect's office who has control over building plans. In addition to these government agencies, private and state owned factories often hold large amounts of real estate including both production related facilities like warehouses and research offices and residential housing. Since the cooperation of some or all of these groups will be necessary for almost any real estate reforms, time should be spent developing contacts with them.

**e) Develop standard documents and procedures**

Corruption in government comes when there is either too much control or too much leeway for personal judgment. In real estate, laws are often vague and do not prescribe set criteria required before an action can either take place or not. As such, these laws are subject to interpretation by local officials who often reward friends and contacts but not legitimate business people who happen to be strangers or not forthcoming with bribes. The way to attack this phenomenon requires two steps. The first step is to create standard contracts and documents and standard procedures that set automatic approvals unless a decision is made that a pre-defined set of limited criteria are violated within a set time allowance. Once these standards are created, they should be publicized so that both government officials and citizens know their rights and obligations. Following these two steps should have the effect of limiting the level of individual government 'judgment' that takes place in making decisions on real estate.

**f) Emphasize benefit of quick profits**

Russian oblasts and cities are caught in a struggle over maintaining control and staying financial solvent. With increasing political and economic freedoms and decreasing industrial output this struggle worsens. In order for real estate reforms to be successful, local governments need to be convinced that the loss of control over real estate that these reforms bring has minimal negative effect and that these negative effects are outweighed by the financial benefits of the reforms. There should be an emphasis on real estate reforms as, firstly, ways to reduce costs and, secondly, providers of revenue as city officials are often skeptical of the revenue potential of any reforms. In Yaroslavl, the city administration views

condominiums as a way to reduce costs and political backlash by reducing the involvement of the ZhKU in such buildings. *(please refer to slide f in Appendix one for summary of real estate reform lessons learned)*

### **E. Specific Real Estate Reforms**

In addition to the lessons learned that can apply specifically to all real estate reform projects, the Bain team has assembled those lessons or operating principles that can apply to specific real estate reform projects, namely, the establishment of a real estate registry and condominiums.

#### **1. Real Estate Registry**

The lessons learned in establishing a real estate registry in Yaroslavl are as follows:

- a. Persuade the city of the merits of creating a property registry by emphasizing the facts that it will...
  - provide work for the increasingly idle privatization department of the property committee
  - allow the city to maximize its real estate revenue
  - fulfill the legal requirement to collect information on municipal property
- b. Build on existing information and systems so as to simplify the process and get all parties involved.
- c. Persuade all parties to give up their real estate information to the registry by convincing them of the benefits of...
  - having access to all real estate information within the registry
  - distributing the information for a fee

For a national roll out,

- d. Publicize the program merits through the mass media and a brochure that summarizes all selling points
- e. Distribute 'how to' manuals and software

#### **a) Emphasize benefits to the city**

For the city, creation of a real estate registry had a few clear benefits. These were emphasized so that support was quickly won. The benefits included providing work for the property committee's increasingly idle privatization department which had completed privatizing all of the eligible small scale enterprises. A second benefit was that the registry, by tracking all property including that which was municipally owned, was an excellent management tool that could be used by the city's official lessor, the KI, to maximize rental revenue. Thirdly, the real estate registry fulfilled a federal legal requirement of municipalities to collect information on municipal property. These three benefits together provided the appropriate amount of incentive to keep the city interested in completing the registry even as the advisor assistance was decreasing. The benefits of the registry also created a positive attitude amongst city officials towards Bain and other reforms Bain was implementing.

#### **b) Build on existing information**

All municipalities are likely to already have some information on their real estate. They may even have some of it recorded in computer form. It is likely that this information resides with the BTI or the KI. In order to minimize the time required to complete the registry and maximize the acceptance of appropriate city agencies, the existing information and systems should be used as much as possible to build the new registry. In Yaroslavl, the Bain team led the restructuring of an existing database that was being constructed by a local computer programmer. The restructuring and updating of the existing database took much less time than the building of a new one and insured the use - for both creation and subsequent updating - of a local resource rather than a more expensive outside advisor. Using the revised version of the existing database meant that the data already in the database did not have to be re-entered and that agencies did not have to redo previous efforts.

**c) Persuade all parties to give up their information**

The most difficult part in building the real estate registry was to get each of the relevant agencies to give up their exclusive knowledge of real estate information to the registry. Each agency at first felt that the real estate information it had was confidential and that they would gain nothing and lose their influence if they gave it up. The way to fight against this attitude was to convince each agency involved that access to a registry with complete information on all pieces of real estate would have greater value to them than the limited real estate information they held on a limited set of properties. The registry, in effect, would be the only way for them to get real estate information on properties that other agencies held and in order to get access to this registry they had to contribute their own information. The value of having the registry's complete information was not only that each agency could get information it did not have before but that each agency could sell this information to the public for a fee. Thus, through cooperation, the agencies would thus have more information and revenue producing power than before. The benefit to the public was that there was no longer one agency with a monopoly on a certain piece of real estate information, several agencies now would compete to provide that information.

**d) Publicize program merits**

Given the lessons learned during the pilot execution phase of the real estate registry, the national roll out should have two major activities. The first activity is to publicize the merits of real estate registry creation through the mass media with the use of articles and brochures that summarize the aforementioned benefits to cities.

**e) Distribute manuals and software**

The second activity is to distribute practical 'how to' manuals that explain how to create the registry as well as software containing basic real estate database. This Bain team has already created both of these materials as part of the pilot program. Because of the relatively strong interest in Yaroslavl and other Russian cities in establishing registries it seems feasible that this program can continue without advisor support if there is an appropriate level of publicity and someone is present to drive the roll out process. The Bain team has made 2 arrangements to help make this happen. Firstly, with GKI and USAID approval, Bain signed a publicity agreement with the national newspaper, *Economica i Zhizn*, to publicize the existence of the software and the manual and to distribute it to interested municipalities for no additional cost to USAID. In order to insure that someone drives the roll out process, the *Economica i Zhizn* agreement allows the newspaper to make agreements with cities whereby the city provides non-confidential city real estate information in return for receiving the registry materials. The second driver of the process is the software developer, who, under the software development contract signed with Bain, has the right to offer his services of modification of the software to cities that receive it.

**2. Condominiums**

The lessons learned in converting buildings with residential and commercial units to condominiums are as follows:

- a. Assume that there will be skepticism and a negative attitude towards reform in general and that people will resist being part of an experiment.
- b. Use published materials and public seminars to proactively address concerns and educate both citizens and officials, stress:
  - that there is a choice between two types of change, not a choice between change and status quo
  - the ability of condominiums to provide private land ownership within city limits
  - the ability of condominiums to allow citizens to better control and utilize their space and city subsidies
  - the benefit to the city of setting known versus unknown subsidy budgets

- c. The single criteria for a good condominium candidate is a willingness to become a condo, therefore, use public relations and publicity to attract interested buildings rather than trying to pick pilots objectively
- d. Poll residents through the use of general meetings, one to one interviews and surveys in order to:
  - assess concerns
  - sell the benefits of condominiums
  - judge satisfaction with the building before and after condominium registration
  - increase tenant confidence in their ability to manage their building
- e. Train local authorities on the details of condominium registration
- f. Develop 'champions' in each pilot site and involve them closely in preparation activities so that they can carry on once advisors have gone
- g. Train condominium association members to do what is required, don't have advisors do it for them
  - use training materials that outline 'how to's'
  - provide detailed check lists

For national roll out, privatize the process since the level of effort required for pilot execution is not sustainable on a national basis. This can be done by taking the following steps:

- h. Use an implementation team to launch a publicity campaign using information brochures, press releases and positive opinions from existing condo association members
- i. Invite the public to general informational meetings run by the implementation team
- j. Distribute informational and training materials with check list of specific activities to self appointed building 'champions'
- k. Follow up with champions, assist in the registration process if necessary
- l. Train the initial group of champions and interested lawyers to perform registration

**a) Assume a negative attitude of participants towards change**

Reforms related to housing and directly affecting ordinary citizens are highly contentious. Russian citizens who have gone through a rough, three year, transition period from communism to capitalism are very wary of any new reforms and view them skeptically and negatively. In addition to a general dislike of reforms, ordinary citizens view any pilot project as an experiment where they are the guinea pigs and can only lose. It is because of these attitudes, that the first step for any condominium program is to educate people, proactively distributing informational brochures and press releases and meeting with people so that concerns are addressed and misconceptions are stopped.

**b) Proactively address concerns**

There are several points to stress in communications with the public and city officials alike. Firstly, the message that the alternative choice to condominiums is not the status quo should be stressed. Change is inevitable given that people own their apartments and technically a share of their building's common space and that the city can no longer afford to manage and maintain the buildings on its balance sheet. It should be stressed that condominiums did not cause these changes, they are merely the best solution to address these changes.

Secondly, publicity should stress the unique ability of condominiums to provide private land ownership within the city. At present, land privatization applies only to land located outside of cities and condominium associations are the only private entities allowed to own land within the city. For many would be condominium association members this is the only way to own land and more importantly control what gets built on it.

Thirdly, it should be clear that condominium association members are in a better position to control their common space and utilize city subsidies than their non condo counterparts. The only difference between

a condo and a municipal building is that in a condo, the condo association, not the city, decides on how subsidies will be spent and how much owners have to pay for maintenance. The level of subsidies is the same in both the condo and the municipal building, the only difference is who chooses how to spend the money.

Fourth, the city should be sold on the idea that condominiums allow them to better define budgets and get out of the politically sensitive job of maintenance. Some municipalities find that they have to exceed budgets for maintenance costs in order to provide an acceptable level of service to tenants. These cities are increasingly paying for the costs of theft and mismanagement rather than additional service. In distributing subsidies to condominiums the city can give a set amount of money based on the building's needs and leave the responsibility of spending that money fairly and efficiently to people who have an incentive to do so; the condominium association.

**c) Pick willing candidates as pilots**

Despite the fact that the current federal condominium law is mandatory, there is not real means of enforcing condo creation. Thus, condo creation is voluntary and requires the consent of pilot owners. Even after a thorough publicity campaign, not everyone wants to be part of a pilot condominium pilot. For advisors selecting condominium pilot sites, there is a limited market and that market is made of those willing to participate not the whole city inventory of buildings. Pilot selection thus depends on willingness to go through the process and public relations and publicity should be used to bring those willing parties forward to the advisor.

**d) Poll residents**

Once pilots are selected, the opinions of the residents should be monitored to insure their continued support. This requires a constant flow of information that can be garnered through the use of general meetings, one to one interviews and surveys. All of these forms of interaction should have several aims. The first is to assess residents' concerns and identify any issues that residents may have with the program. Secondly, once concerns are identified they should be addressed and other benefits of condominiums should be sold to the owners. Thirdly, the value to the owners of the condominium association should be gauged by comparing their satisfaction with their building and its management before they registered it as a condominium and after they have established a functioning association that has made and executed relevant decisions.

**e) Train local authorities on the details of condominium registration**

Given the sheer speed and volume of Russian legislative reforms and changes, most municipalities have a difficult time keeping abreast of what changes are happening let alone understanding how to administer each change. This is why it is critical for the advisor to not only inform the local government officials of new laws and convince them of the new laws' merits, but also to train them on what they need to do differently in order to administer the new laws. The training process is useful in two ways. It establishes the advisor as an expert and a helper rather than as a federally imposed burden and it insures that reforms continue once the advisors leave.

**f) Develop champions**

Advisors can not and should not lead all of the discussions on condominiums. Deciding owners can much better relate to a fellow owner than a foreign advisor. In any pilot where interest in condominium registration is raised, there is usually at least one strong supporter or 'champion' of the condominium concept. This supporter should be coached by the advisor and developed as an advocate for condominiums in his building. Once agreement on condominium registration is reached, the champion should lead the charge to have their first general meeting and begin true owner participation.

**g) Train condominium members**

With the development of a champion, the role of the advisor is to train and support that champion and his fellow condo association members. This can be done by providing owners with manuals that address the basic 'how to's' of condominium organization. The manuals should be supplemented by detailed and easy to follow check lists that detail the steps that condo association members have to take once the advisors are gone.

Because of the large level of effort required by the advisor, the previous lessons learned apply more specifically to pilot execution than national roll outs. Beyond the required federal changes, in order to have a national roll out of condominiums there must be a way to either reduce the amount of effort required or pass some of it off to private individuals or, in other the words, privatize the process.

**h) Launch publicity campaigns**

In privatizing the process, the assumption is made that a low cost implementation team run by the sponsoring federal agency would be involved in creating publicity and training private individuals to carry out details of the process. The first step in this process would be to launch a city specific publicity campaign focusing on educating the public and selling the benefits of the program. This campaign would include the distribution of information brochures and the circulation of press releases and positive opinions from current condominium association members in pilot cities.

**i) Invite the public to general informational meetings and identify champions**

As this initial campaign reaches its completion, the implementation team should invite the public to general informational meetings where interested parties can ask questions. The content of these meetings will be similar to the publicity campaigns in educating the public and selling the program. Additionally, the meetings can be used to assess and then directly address the concerns of citizens. The main goal of such meetings, however, would be to identify interested parties of self appointed champions who would be interested in converting their buildings to condominiums. Ideally, it would be best to identify a group of several champions who can work together and support each other through the registration and start up process.

**j) Distribute training materials**

Once champions are identified, the team should train them and support them with the aforementioned training materials and check lists taking them through every step of the registration process.

**k) Follow up with champions**

At this point, the implementation team can monitor the progress of the first 2 sites and support them when necessary. The team should insure that the first pilots are registered smoothly but should not spend more time on these sites than the buildings' champion.

**l) Train champions and lawyers**

Once the first pilots are registered, the implementation team should encourage building champions and interested lawyers to help other interested buildings through the conversion process. The team can train both on what specific activities they can perform for interested buildings and how they might be able to bill these buildings for these services. Given that the largest portion of the time required for registration is the time required for owners to decide on charter revisions, full time hired champions and lawyers can feasibly do several buildings at a time, thus leveraging their knowledge and reducing their cost to the condo association. If one assumes that condominium registration will truly be mandatory but still will benefit from outside support, being a hired condominium champion may be a desirable occupation.

## V. Summary

In April of 1993, concerns over the quality of service provided by privatized and new private small scale businesses were raised by the Russian State Property Committee (GKI). The United States Agency for International Development (USAID) provided funding to quantify this problem, identify its root causes and develop appropriate reform programs to address it. Bain & Company was hired for this task and discovered that a) the quality of small scale businesses in Russia was much lower than those of the reformed economies in Central Europe and that b) 5 major factors limited small business development. The major issue affecting the quality of small businesses was the level of competition measured by the density (number of outlets per inhabitant) of outlets. Limited access to real estate was, in turn, the major factor affecting the growth of new businesses and outlets.

Phase II was developed as a pilot reform program that would be replicable on a national basis with the objective of increasing access to real estate. The city of Yaroslavl was chosen for the site of this reform program which focused on 5 integrated, real estate related activities. These activities included:

- a. Creating a transparent, freely accessible commercial property registry
- b. Assisting in the creation of a system that allows commercial ownership of built-in spaces concentrating on
  - 1) assisting in the development of legislation for built in space sales and
  - 2) developing federal condominium legislation and implementing it on a local level.
- c. Beginning to create an efficient leasing and subleasing environment by making fundamental improvements
- d. Proposing reductions in legislative burdens on entrepreneurs
- e. Publicizing new legislation and programs

While Bain was successful in completing these activities, they, in and of themselves, will not realistically make a great impact on the development of small businesses in Yaroslavl or in Russia. While Bain addressed access to real estate in Yaroslavl, there are still other factors that effect small business development. Furthermore, the real estate reforms in Yaroslavl will not make an impact on the rest of Russia unless numerous legal changes are taken at the federal level to insure that the main reform programs undertaken - property registration, sales of built in space and condominium creation - can be rolled out smoothly on a national basis. In general, the changes required need to follow the general principles of any reform program. These are to:

- a. Simplify the process and minimize the costs of reform to participants
- b. Empower the people involved
- c. Commercialize the process wherever possible

Along with these principles, there were many lessons learned during the implementation of real estate reforms in Yaroslavl. These lessons learned are relevant to sponsoring federal agencies like the GKI, funding agencies like USAID and other advisors like Bain. The lessons can be applied at several levels. They are applicable to general reforms as well as reforms relating to small business development, real estate in general and real estate registries and condominiums in particular.

The Yaroslavl real estate reform program has made an impact, albeit small, on the general Russian reform program. Given the chaotic nature of reforming economies, we hope that our recommendations for future changes and lessons learned will be useful in continuing those reforms.

**VI. Appendix**

**A. Supporting slides**

- a) Russian quality of retail vs. Central Europe
- b) Project overview by phases
- c) Density as the driver of quality differences
- d) 5 major obstacles to small scale business
- e) Small business development reform lessons learned
- f) Real estate reform lessons learned

**B. Contract documents**

- a) Original Task Order
- b) No Cost Revision
- c) February 11, 1994 memo on work plan delays
- d) April 21, 1994 memo on completed deliverables as of March 31, 1994

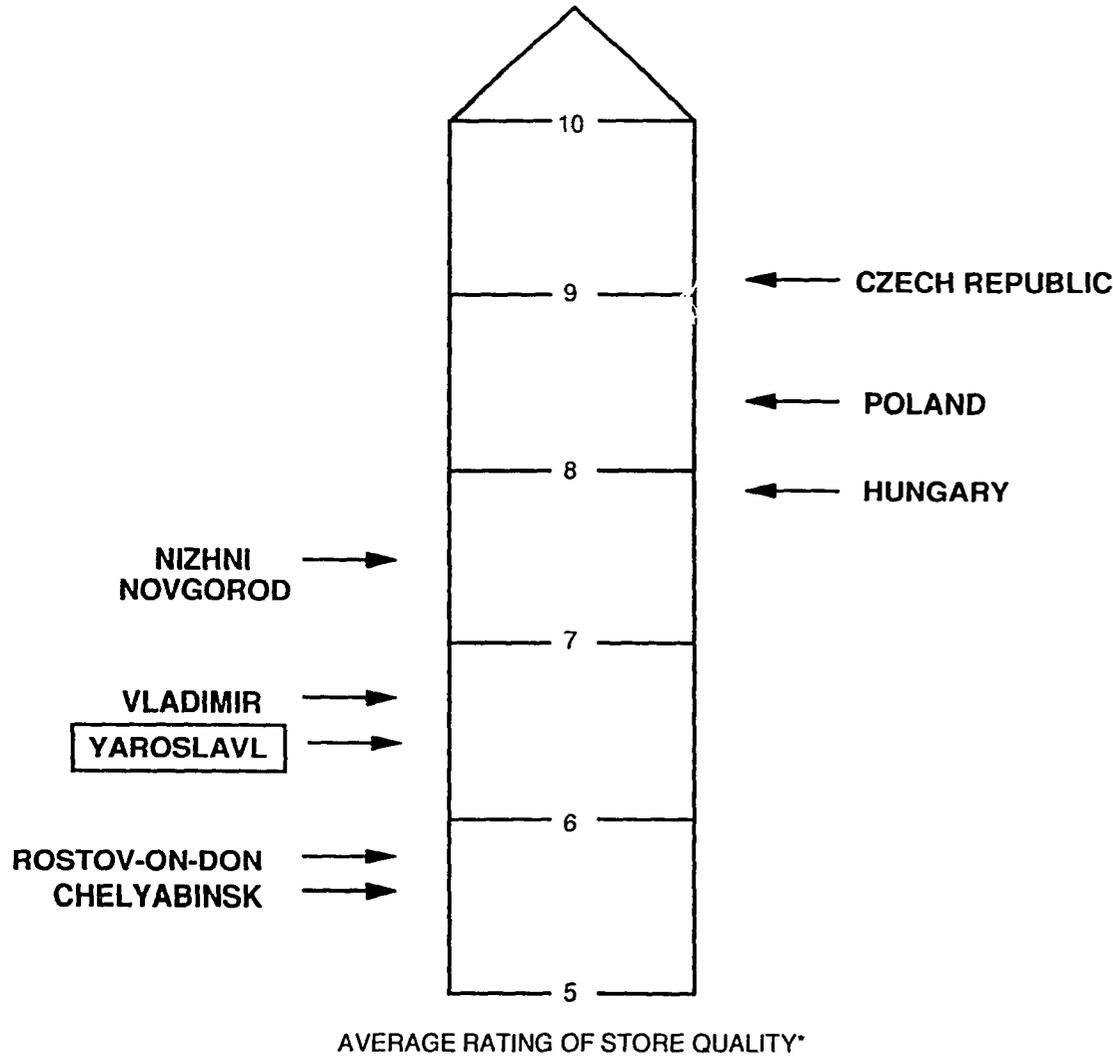
**C. Supporting Documents (to be sent under separate cover)**

- a) City Government Real Estate Manual
- b) Model Public Relations Program
- c) Performance Against Deliverables

**APPENDIX A**

**Supporting Slides**

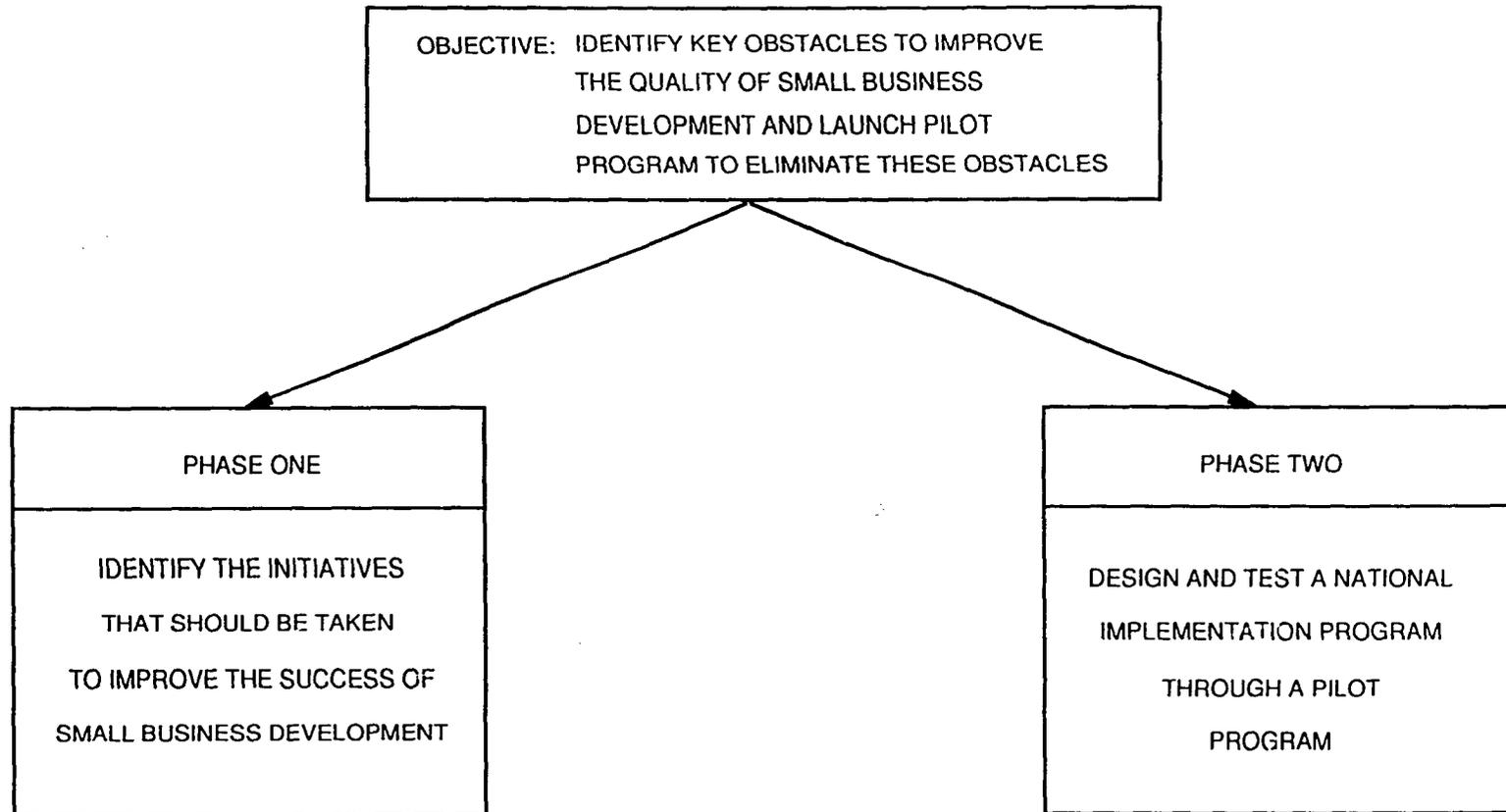
COMPARED PERCEIVED QUALITY OF STORES



- "SHOPS IN CENTRAL EUROPE, ESPECIALLY IN WARSAW, ARE NOW PRETTY CLOSE TO WESTERN STANDARDS"
- "RUSSIAN SHOPS, BOTH PRIVATE AND MUNICIPAL, ARE USUALLY POORLY DESIGNED"
- "THE RUSSIAN SYSTEM - CHOOSING AN ITEM, PAYING AT A DIFFERENT PLACE AND LINE AGAIN TO GET THE PRODUCT - ENCOURAGES LONG LINES AND IS A WASTE OF TIME FOR THE CUSTOMER"

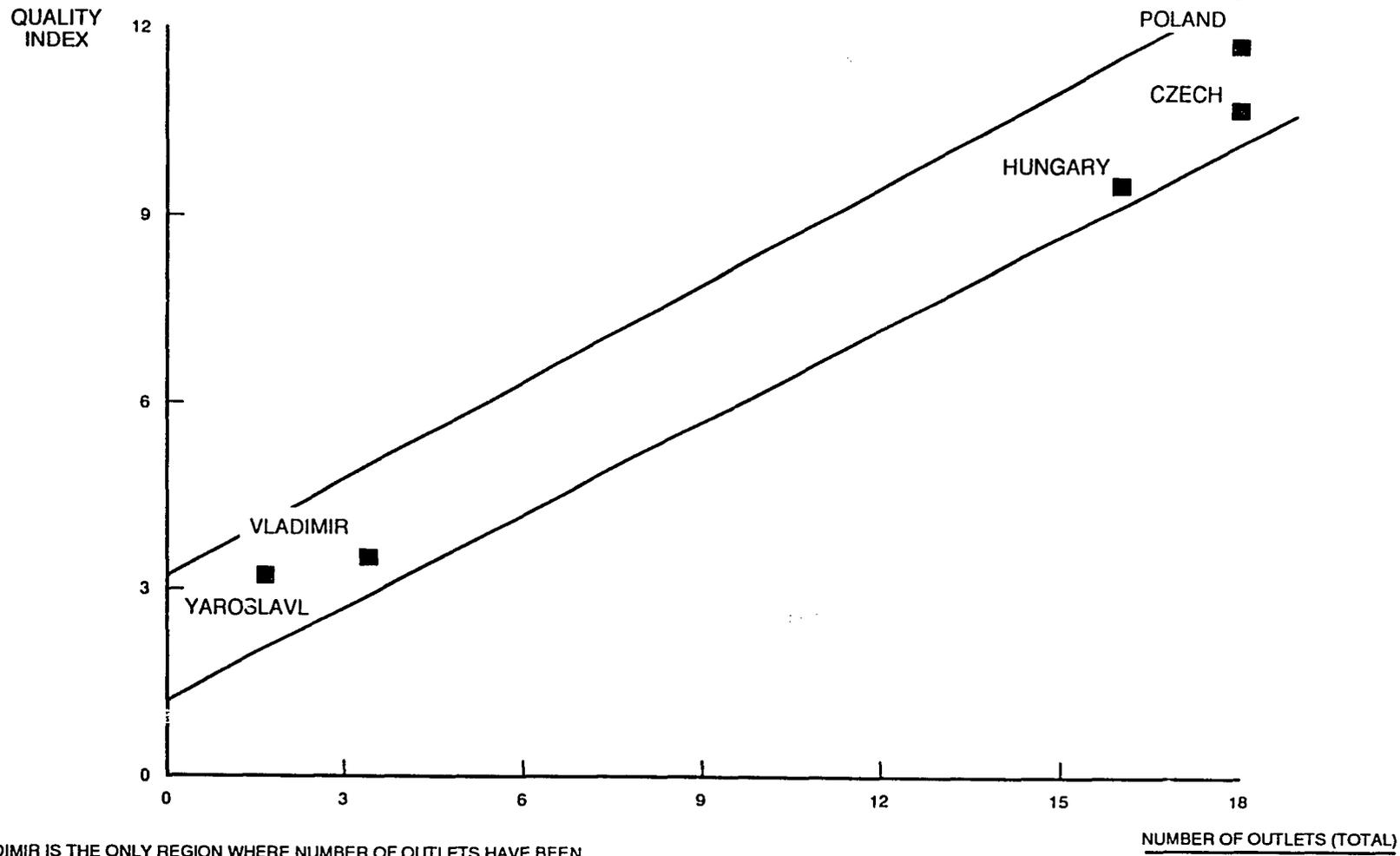
\* IN EACH CITY/REGION, 4 STORES (BOTH PRIVATE AND MUNICIPAL) WERE RATED FROM 1- LOW TO 10-BEST ON 10 CRITERIA

SOURCE: STORE CHECK RESULTS, BAIN ANALYSIS



# SMALL BUSINESS DEVELOPMENT

# DENSITY IMPACT ON QUALITY



NB: VLADIMIR IS THE ONLY REGION WHERE NUMBER OF OUTLETS HAVE BEEN PHYSICALLY INVENTORIED

SOURCE: GKI, IFC, GOSKOMSTAT, BAIN ANALYSIS

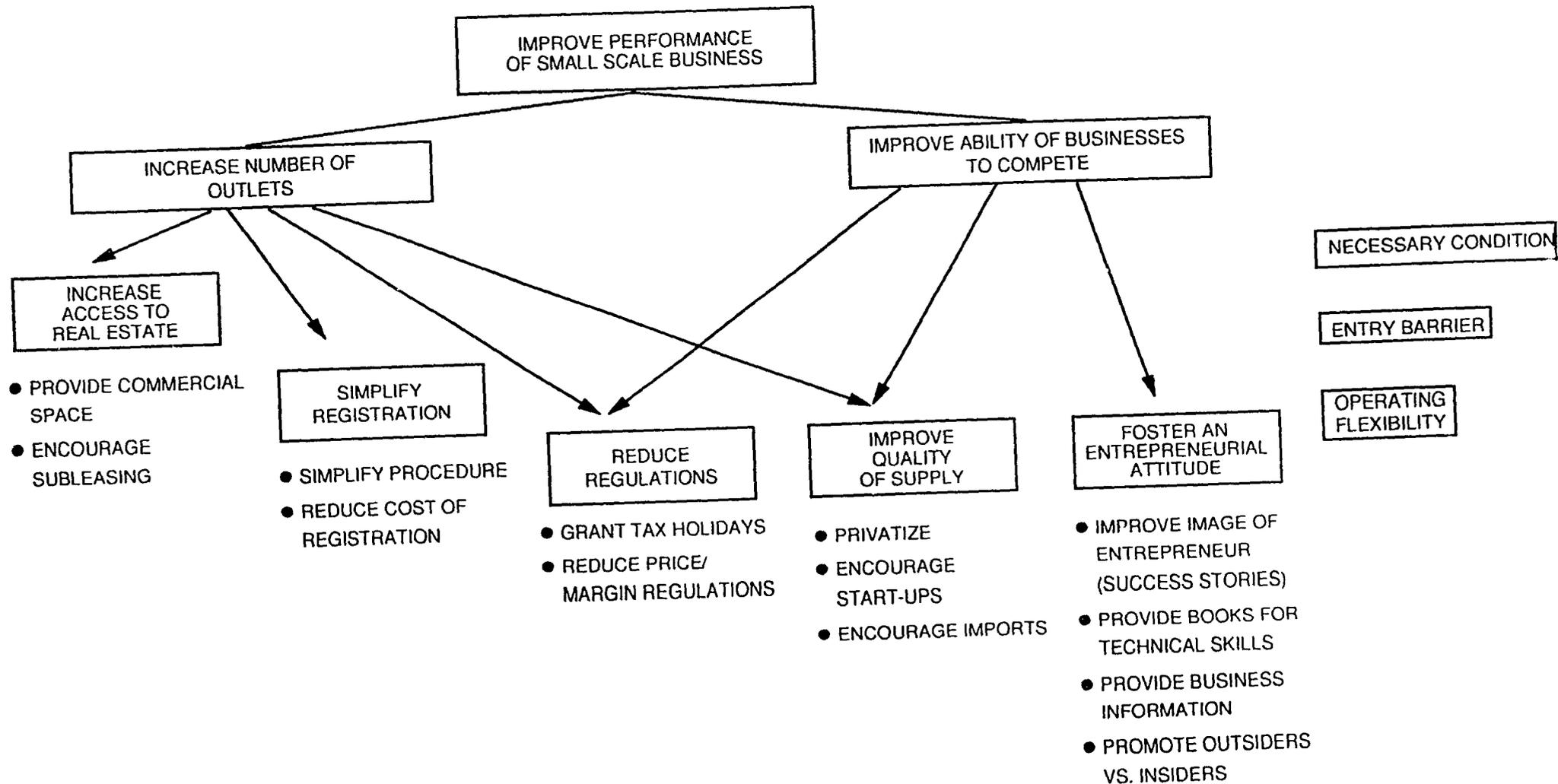
NUMBER OF OUTLETS (TOTAL)  
1000 PEOPLE

May 3, 1993; 0001MS288 USS

# SMALL BUSINESS DEVELOPMENT

## KEY INITIATIVES

### SUMMARY



- A. At both the federal and local government levels, there should be one committee that pulls from all of the relevant agencies and authoritatively deals with small business development issues
- B. Federal reform programs have to be created that encourage compliance by providing incentives and penalties for local governments
- C. There needs to be a reduction of controls and restrictions in order to reduce the influence of government corruption and the mafia
- D. The power structure of the relevant government agencies should be examined by understanding the flow of money
- E. Support for small businesses at the government level is minimal and has to be increased
- F. Small business reform programs should be sold as alternative work for city agencies that are losing importance

- A. Before properties can be released to the public, there should be consolidation in one government agency of all controlling rights over a single piece of property.
- B. Property registries should be created to make critical information over ownership and status of sites available to the public and to keep properties from being "hidden."
- C. The development of third party brokers should be encouraged.
- D. Contacts and co-operation need to be established with all local agencies that control real estate: the BTI, KI, ZhKU, land committee and city architect's office
- E. Standard documents and procedures with maximum time allowances should be established and then publicized so as to minimize the extent of government "judgment."
- F. The reduction of government control over real estate should be encouraged by emphasizing the government agency's ability to profit from quick financial gain by selling space or giving out long term, secure leases.

**APPENDIX B**

**Contract Documents**

ORIGINAL TASK ORDER

SUBCONTRACTOR BASIC ORDERING AGREEMENT NO. 3108-C

TASK ORDER NO. 002

Effective Date: November 1, 1993 Through January 31, 1994

Performance:

This Task Order is authorized under KPMG Peat Marwick's Prime Contract No. CCN-0005-C-00-3108-00. Performance shall be in accordance with the following:

The subcontractors will spend ninety working days in Moscow and other cities counting work for the privatization of small scale enterprises being developed by the GKI and which has been underway since June 1992. Small scale enterprises in Russia are defined as retail trade, catering and service outlets. Small scale enterprises include such diverse businesses as food stores, clothing retail stores, restaurants, cafes, tailoring services and repair outlets. To date, over 50 % of the previously municipally owned small scale enterprises have been privatized by city authorities and some cities have nearly completed their programs., The Russian government plans on completing small scale privatization in early 1994. See issues set forth in Attachment A. hereto and deliver a written report of findings.

Coordination:

Tasks and Reporting:

Mr. Roger Leeds  
(202) 467-3842

Contract Administration:

Mr. Jack Summers  
(202) 467-3433

Billing Shall Be Addressed To:

Ms. Pamela Fingers  
KPMG Peat Marwick  
2001 M. Street, N.W.  
Washington, D. C. 20036

Type of Task Order:

Cost Plus Fixed Fee (CPFF)

Ceiling Price:

\$620,389. Maximum for  
Labor, All Expenses, And  
International Business  
Class Airfare.

\*This corresponds to KPMG's Task Order #7-0025-KPMG.

Task Order No. 002  
Page 2

**Schedule:**

See Attachment B

Please note that fees for services should be itemized separately, KPMG Peat Marwick will reimburse Bain & Co., Inc., for the cost of Business class airfare on a U.S. flag carrier; therefore when reporting expenses, a copy of the travel itinerary identifying the cost of full coach airfare for each ticket should be included. Other expenses including food, lodging, local transportation and reasonable incidentals are also reimbursable up to an in country per diem. All lodging expenses being submitted for reimbursement should be itemized, and accompanied by ORIGINAL receipts. Meals and incidentals shall be paid at the flat rate of \$75 per day, no receipts are required for these expenses. (Rates may vary in other cities.)

Invoicing and payment shall be in accordance with Subcontractor Basic Ordering Agreement No. 3108-00-C ARTICLE VI-SPECIAL PROVISIONS - Paragraph B. entitled "Invoicing and Payment".

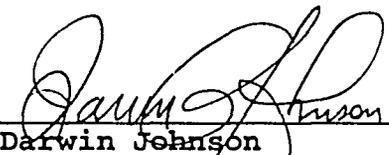
Limitation of Liability:

No liability on the part of KPMG Peat Marwick, legal or otherwise, shall arise for costs incurred by Bain & Company, Inc. in excess of \$620,389. for labor, all expenses and Business Class Airfare unless additional effort and/or airfare ceiling incorporated as a Modification to this Task Order.

**Acknowledgement and Acceptance:**

KPMG Peat Marwick  
2001 M. Street, N.W.  
Washington, D. C. 20036

Bain & Co., Inc.  
Two Copley Place  
Boston, MA 02217-0897

By:   
Darwin Johnson  
Principal

By:   
Mr. Colin Anderson  
Vice President &  
Treasurer

Date: 1/24/94

Date: 1-18-94

**ATTACHMENT A**

**STATEMENT OF WORK**

- To provide concrete examples of methods to improve the quality of small scale businesses in Russia: and  
  
To develop and implement a local pilot program that will begin to create a free commercial real estate market in Yaroslavl and that can be rolled out across Russia.

The two major components of these objectives are:

**Legislation.** Work with the relevant federal and local bodies to assist in developing and implementing pilot commercial sales, condominium and leasing legislation to:

- Break the municipal monopoly on space and reduce the involvement of the municipality in allocating space;
- Create true private ownership and competitive supply;
- Ensure the freedom of private owners to make decisions on use and disposition;
- Provide for proportionate and fair allocation of costs to private owners; and
- Provide a replicable model that can be used throughout Russia.

**Pilot Sites.** Test and showcase legislation through the creation of pilot condominium sites that will begin once local legislation is passed.

- Overall public relations work with the relevant city government (publicizing each region as a place where private business can function efficiently).

Small Business Development

Subcontractors (Bain & Co.)

I. Salaries	Expert	Daily Salary	Est Days	Allocation	# of days	Cost of Service
Overall Project Director	James Allen	331.92	68	25%	17	5,642.64
SB Dev Team Mgr (1)	Tsakalakis	331.92	28	50%	14	4,646.88
SB Dev Team Mgr (2)	Durham	331.92	68	80%	55	18,056.45
Lobbying/Govt Rel Mgr.	Savchenko	264.95	68	50%	34	9,008.30
Legislation Dev Mgr.	Vitrucek	113.77	68	50%	34	3,868.18
Real Est. Inventory Mgr.	Salpenikova	56.89	68	75%	51	2,901.39
Research Analyst	Karavaikin	20.51	68	100%	68	1,394.68
Research Analyst	Bobrovsky	46.84	56	100%	56	2,735.04
Assoc. Consultant Intern	TBD	20.51	68	100%	68	1,394.68
Assoc. Consultant Intern	TBD	20.51	68	100%	68	1,394.68
Case Team Assistant	Fedchenkova	9.58	68	100%	68	651.44
Office Administrator	Avdonina	23.00	68	20%	14	312.79
Contracts Supp. Mgr.	La Terz	185.91	68	25%	17	3,160.47
Contracts Supp. Asst.	Lareau	57.50	39	50%	19.5	1,121.25

Total Salaries 583.5 56,289

II. Fringe (17%) 9,569

III. Overhead (230%) 151,473

IV Allowances (25% differential or actual salary, whichever is less)

Overall Project Director	James Allen	25%	1,410.66
SB Dev. Team Mgr.	Tsakalakis	actual salary	384.30
SB Dev. Team Mgr.	Durham	25%	4,514.11

Total Allowances 6,309

V. Other Direct Costs (see attached for allocation)

Subtotal Subcontractors 352,750

Fixed Fee 576,389

Total Subcontractors 44,000

620,388.55

VI. Allowances 0

**OTHER DIRECT COSTS  
SMALL BUSINESS DEVELOPMENT**

<u>Category:</u>	<u>November</u>	<u>December</u>	<u>January</u>	<u>Total</u>
<b>SALARIES + BONUS</b>				
Lawyers (2)	\$2,200	\$2,200	\$2,200	\$6,600
Yaroslavl Secretary	50	50	50	150
Other (Interpretors, etc.)	1,360	1,360	1,360	4,080
Local Assistants	600	600	600	1,800
Public Relations Assistant	700	700	700	2,100
<b>TOTAL</b>	<b>4,910</b>	<b>4,910</b>	<b>4,910</b>	<b>14,730</b>
<b>TRAVEL &amp; INCIDENTAL</b>				
Russian Travel	11,040	11,040	11,040	33,120
Int'l Travel (see below)	15,200	15,200	15,200	45,600
Living Allowances	4,700	4,700	4,700	14,100
<b>TOTAL</b>	<b>30,940</b>	<b>30,940</b>	<b>30,940</b>	<b>92,820</b>
<b>EQUIPMENT</b>				
Capital	10,000	10,000	10,000	30,000
<b>TOTAL</b>	<b>10,000</b>	<b>10,000</b>	<b>10,000</b>	<b>30,000</b>
<b>FACILITIES</b>				
Rental	600	600	600	1,800
Operating Costs - Yaroslavl	800	800	800	2,400
Operating Costs - Other	6,000	6,000	6,000	18,000
<b>TOTAL</b>	<b>7,400</b>	<b>7,400</b>	<b>7,400</b>	<b>22,200</b>
<b>OUTSIDE EXPERTS</b>				
Working Commission	5,000	5,000	5,000	15,000
Lawyers	5,000	5,000	5,000	15,000
Other	11,000	11,000	11,000	33,000
<b>TOTAL</b>	<b>21,000</b>	<b>21,000</b>	<b>21,000</b>	<b>63,000</b>
<b>TRAINING</b>				
Manual	0	0	100,000	100,000
<b>TOTAL</b>	<b>0</b>	<b>0</b>	<b>100,000</b>	<b>100,000</b>
<b>TOTAL OPERATING COSTS</b>	<b>74,250</b>	<b>74,250</b>	<b>174,250</b>	<b>322,750</b>
<b>REGIONAL DISBURSEMENT</b>		<b>15,000</b>	<b>15,000</b>	<b>30,000</b>
<b>GRAND TOTAL</b>	<b>\$74,250</b>	<b>\$89,250</b>	<b>\$189,250</b>	<b>\$352,750</b>

<u>International Travel Breakdown</u>	<u># of Trips</u>	<u>Cost</u>	<u>Total</u>
	11	4,145	45,600

31

BUDGET NOTES

1. Adjustments may be made between line items up to 15% without Mission concurrence. Line item adjustments in excess of 15%, increases in the level of effort, increases in the grand total and/or changes in the work plan must be approved by all parties in an amendment to this Task Order.
2. The Consultant will seek a cost sharing arrangement with local counterparts when entering into subcontracts or rental of office space and/or communications equipment whenever possible.
3. Consultants must be approved by USAID based on experience and availability.
4. Russian labor who are not bonafide employees of the Contractor, will receive only the daily salary rate without fringe benefit, overhead or other indirect costs.
5. Procurement and placement of equipment in host country organizations will be in compliance with USAID procurement policies and procedures.
6. Any international roundtrips beyond one trip per consultant must receive prior approval (see special instructions in memorandum from J.J. Kryschtal dated November 22, 1993).
7. A six day work week is authorized for this Task Order and is reflected in the per diem budgeted.
8. All work days are assumed to be performed in Russia. Any exception from this rule must receive prior approval in writing from USAID and GKI.
9. In signing this Task Order, the subcontractor budget line item in the contract would have been exceeded beyond 15%. Therefore, a modification is pending for adjustment to the contract budget.
10. If a consultant, while in Russia, is working on another assignment, any associated costs of travel, per diem/housing, salary, etc. will not be reimbursed for those days.
11. In the event that it is determined that the contractor or any of its subcontractors billed costs (including salaries in excess of the FS-1 ceiling) at rates that are not approved by the Contracting Officer in writing, the Contractor will be required to reimburse the U.S. Government for any of the associated costs.

12. Regional disbursements will be used for three major categories of activity:
  - a. initial staffing of auction centers;
  - b. expansion of auction activities usually by subcontract with local banks or other financial institutions for the collection of vouchers; and
  - c. public information campaigns with regard to specific auctions or the auctions of specific enterprises.

Note: No capital equipment is purchased under these regional disbursements.

Regional disbursements will occur in compliance with the following process:

- A budget is developed with each region and closely reviewed by the Contractor;
  - Budget is given to GKI;
  - GKI approves budget and disburses funds to the region; and
- Upon completion of the work, GKI gets receipts from the regions and presents them to the Contractor for reimbursement under the Task Order.

*N/A - These disbursements relate to Real Estate not to Voucher Auctions*  
AR 1/18

NO COST REVISION

*failed 1/21*

**Bain & Company**

**Bain Link**

Scherbakovskaya Ulitsa 40-42  
105187 Moscow, Russia  
Telephone: (7) (095) 369-0386, -5948, -5950, -2643, -2333, -2351  
Facsimile: (7) (095) 369-5947, 166-6867

**MEMORANDUM**

**To:** Maxim Buyeko, GKI  
David Ross, GKI

**From:** James Allen  
Mikel Durham

**Date:** January 21, 1994

**Re:** Small Business Development Update

**Contract:** US AID Moscow CCN-0005-C-00-3062

Please find attached a document outline our request for a No Cost Revision, as discussed. We would like to review it with you prior to sending it on to USAID. As we understand that Walter Coles will be in town starting next Monday, we will, upon agreement with you, present it to him here in Moscow.

As we have been in close communication on a weekly basis, there will be no surprises regarding the background, and workplan, discussed in the document. Let me draw your attention to two items:

- 1- Replacement of Mikel Durham with the former manager of the case, Chris Tsakalakis.

We have worked diligently to bring Chris back to the case, in order to maintain as much continuity as possible. The change in manager has not and will not affect relations in the region which are managed by Sergei Savchenko, Arkady Viruk, and Julia Sapelnikova. Arkady has been on the case consistently since April of 1993, and Sergei and Julia have been involved since our work in Yaroslavl started.

- 2- Reduction in management allocation (on the case and in Russia) to 70%

The reduction in allocation is both a necessary requirement to accommodate on-going obligations which Chris Tsakalakis has to other projects, and a realistic assessment of the workload going forward. This level of effort is actually higher than the 50% Mikel discussed with David, and that reflects a thorough review of the management and implementation challenges facing the team, and the on-going reporting requirements. Both Chris and Mikel have agreed that a 50% allocation would not capture the level of effort required to achieve the results we hope for.

We believe that the rest of the attached document will be self explanatory. We are available to meet late this afternoon or tomorrow. We are equally comfortable with a telephone conversation, should this proposal be acceptable to you.

Please contact us the Kalpachny offices today. 227-2030  
297-0435

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SMALL BUSINESS DEVELOPMENT  
PHASE II: NO COST REVISION

A PROGRAM TO INCREASE ACCESS TO REAL ESTATE IN YAROSLAVL, RUSSIA  
CONTRACT: US AID MOSCOW CCN-0005-C-00-3062

**EXECUTIVE SUMMARY**

Bain proposes to extend the effort on Small Business Development in Yaroslavl until March 31, 1994, at no extra cost to USAID. This can be achieved by reallocating resources from the expenses budget to contracted staff and into professional fees. This extension is required due to delays in the release of Federal legislation critical to the aims of the project, including that of piloting condominium sites. The extension will require a replacement manager for the project-- this will have little impact on the work however, since Chris Tsakalakis, who managed the case prior to December, will be returning.

**I. Background**

Following a six month review of obstacles facing small businesses in Russia, Bain began to work in Yaroslavl in November of 1993. The objectives of Phase II of the Small Business Development work was to launch a pilot program for real estate reform on a local basis in order to develop a model for national legislation. More specifically, quoting from the task order:

- To provide concrete examples of methods to improve the quality of small scale businesses in Russia;
- To develop and implement a local pilot program that will begin to create a free commercial real estate market in Yaroslavl; which can be a model for Russia

Two components of this work are:

- To work with the relevant federal and local bodies to assist in developing and implementing pilot commercial sales, condominium and leasing legislation
- To test and showcase legislation through the creation of pilot condominium sites that will begin once local legislation has passed.

Tasks

The team was tasked with the following activities:

1. Create a transparent, freely accessible commercial property registry
2. Create a system that allows commercial ownership of built-in space
3. Create an efficient leasing and subleasing environment by making fundamental improvements
4. Propose reductions in legislative burdens on entrepreneurs
5. Publicize new legislation and programs

A critical component of these tasks was the creation of pilot sites in the area of condominiums, built-in space, and leasing/subleasing reform, and to develop manuals and other materials in support of these reforms throughout Russia.

## II. Progress to Date

The work in Yaroslavl has been proceeding despite the political disruptions and delays in Federal legislation on condominiums and sale of built-in space. Specifically, the team has accomplished the following objectives:

### 1. The first centralized, comprehensive city real estate database in Russia.

Data regarding buildings and premises was divided between 8+ agencies in Yaroslavl, which made it extremely difficult for any one agency, much less any entrepreneur, to identify the availability of space, and to ensure that proper records were kept regarding claims on property. The former, poor information on the availability of space, served as an obstacle for the immediate lease of space. The latter, poor record keeping regarding claims against property, is increasingly critical as the transformation to private ownership results in the rapid transfer of owners, and increasingly complex city management system of municipal property and utilities.

To date, agreements have been signed between all participating bodies to share information and to cooperate regarding the compilation and use of the information. A Mayor's edict regarding this procedure is awaiting signature. Software has been designed and written to combine the databases and the process of data comparison, field inventory, and data input has been underway for two months. With a primary focus on streets in commercial districts, the first phase of data entry and analysis will be complete by January 31st. The next phase, to be driven by the city, will incorporate all buildings in the city of Yaroslavl. The database has already been used to identify empty spaces to put up for lease, and to highlight conflicts in government agency claims to certain pieces of property.

### 2. A manual outlining the importance of real estate information and coordination to supplement specially developed software.

A manual introducing the concept of managing information on real estate at a central level and making it available to the public is in its final drafts, and will be completed by January 31st. This manual will be distributed to pilot cities, with the software and some technical assistance. It will also be discussed with other USAID contractors working in pilot cities and made available for their use.

### 3. Reforms in the leasing and subleasing procedures

A full analysis and set of recommendations has been presented to Yaroslavl, with the intent of reforming a currently complex leasing procedure, and reducing the constraints on entrepreneurs subleasing space. Negotiations are underway over specific components of the program, and five pilot sites have been identified to test the new procedures. These pilot sites were identified through the use of the new central real estate database.

### 4. Significant contribution made to the development of federal condominium legislation, signed by President Yeltsin on December 23, 1993.

In depth analysis and considerable time was invested in the development of concepts and documentation for condominiums in Russia, including the federal decree, as well as the model Charter and Foundation agreements. Contributions were seen as successful during November of 1993, after which the legislation went to the Ministries for negotiation and the President for Approval. This process took almost one month. The details regarding the treatment of condominiums under the government's repair, maintenance, and capital expenditure subsidy program, the registration procedures, and the required bylaws, although developed, were not included in the recent Federal decree.

W

### 5. Preparation for Condominium Pilot Sites

Activities were undertaken to prepare for a pilot condominium program, including establishing an agreement with the Mayor of Yaroslavl and his staff to this end, reviewing early drafts of legislation with local lawyers and policy makers, surveying residents of potential pilot sites, and drafting condominium workplans and materials. Following Federal announcement of impending legislation, the Mayor of Yaroslavl requested further activities in this area be delayed to avoid publicity until the Federal legislation was public. With the federal decree in place, workplan activities have resumed, and pilot launch awaits resolution of a number of procedural and legal issues requiring Federal approval.

### 6. Public Information Materials

A pamphlet to support condominiums has been developed and edited to reflect the new legislation. This is the material which will first be made available to pilot residents, after which it can be re-edited to take advantage of lessons learned. Work has initiated to supplement and therefore speed up the release of an Urban Institute manual for condominium residents. A draft of a manual to city administrators regarding condominium implementation was initiated, and will be completed pending resolution of legal issues and the initial feedback from pilot activities. The real estate database manual will be completed by January 31st and will achieve limited distribution. Lastly, a memorandum on leasing/subleasing reforms is being compiled.

### III. Rationale Behind Extension Request

Although considerable progress was made in workplan areas which were not subject to political approval, that is the local establishment of central real estate database, the revision of leasing/subleasing procedures and documents, and the drafting of condominium materials, several key activities were delayed. In particular, the legislation regarding condominiums was delayed, pushing back by about 1 month our workplan. In addition, the federal regulation on the sale of built-in space has not emerged although our earlier impressions were that it was complete and awaiting signature. This has meant that we have delayed the piloting of commercial space sales.

Despite these delays, through joint agreement with the GKI, in December our level of effort was maintained. We focused efforts on providing assistance to the further development of condominium legislation and developing a program to reform the leasing/subleasing process in Yaroslavl.

With the signing of the federal legislation, we have edited our draft bylaws and have submitted these, along with a number of legal questions which require clarification, to the Federal agencies named as responsible for condominiums in the Federal decree. Following clarification of these points, and federal approval for use of the bylaws, we can commence our pilot activities in Yaroslavl. Even assuming rapid response by the federal government on these points, it is impossible to suppose that we would be able to launch and adequately support initial condominium sites in Yaroslavl by January 31, 1994. This drives one source of our request for an extension.

In addition, we have initiated discussions with the GKI regarding obtaining special permission for piloting the sale of built-in commercial space in Yaroslavl. We are uncertain at this time whether it will be granted, but we will continue to lobby with the initial goal of selling off the commercial space located in condominium pilot sites.

#### IV. Timing and Budgetary Issues Associated with Extension

Bain has calculated that it can continue operations in Yaroslavl through the 31st of March, 1994. In this time, we believe that we can implement and support 4-5 pilot condominium sites, 4-5 spaces leased under the reformed procedures, and create the documentation necessary to support broader dissemination of "lessons learned." Pending federal support for special status, we would begin development of procedures for the sale of built-in space, and possibly implement pilot sales.

The staffing and budget would be impacted in the following way:

- Management of the case would revert to Chris Tsakalakis, replacing the current manager, Mikel Durham
- The Manager allocation (both effort contributed to the case and time in the country) would reduce to 70%, reflecting the estimated true managerial effort required, as well as the preference for a replacement manager who is intimate with the details of the case
- No additional capital expenditures would be incurred
- Outside Expertise will be utilized at a lower rate than previously expected
- The costs for printing and distribution of large numbers of manuals will not be incurred. Budget remains for printing of a limited number of copies of manuals and other materials for use in Yaroslavl, to be distributed to experts and advisors as required, and to be offered on a limited basis to other regions. Considering the amount of resources sponsored or co-sponsored by USAID in the area of real estate reform and small business development, it is expected that the costs for Bain developed materials that are thought to be valuable to other regions can be born under other contracts

The following attachments summarize our budget estimates and reallocation of expenditures:

Attachment One: Budget Revisions Summary  
Attachment Two: Professional Fees Calculation

**Bain & Company, Inc.**  
**Small Business Development**  
**Budget Revisions Summary**

"SREXPNC"

**ATTACHMENT ONE**

	<u>ORIGINAL BUDGET</u>	<u>EST ACTUAL (11/01 - 01/31)</u>	<u>EST REQUIRED (02/01 - 03/31)</u>	<u>EST TOTAL (REVISED)</u>
<b><u>CONTRACTED SALARIES + BONUS</u></b>				
- Lawyers (2)	6,600	6,000	2,000	8,000
- Yaroslavl Secretary	150	102	102	204
- Other (Interpreters, etc.)	4,080	3,000	2,000	5,000
- Local Assistants	1,800	0	0	0
- Public Relations Firm	2,100	0	0	0
- Software Programmers	0	3,000	0	3,000
Total	<u>14,730</u>	<u>12,102</u>	<u>4,102</u>	<u>16,204</u>
<b><u>TRAVEL &amp; INCIDENTAL</u></b>				
- Russian	33,120	10,400	7,000	17,400
- International	45,600	7,000	38,000	45,000
- Living Allowances	14,100	9,375	7,882	17,257
Total	<u>92,820</u>	<u>26,775</u>	<u>52,882</u>	<u>79,657</u>
<b><u>EQUIPMENT</u></b>				
- Capital	30,000	6,500	0	6,500
Total	<u>30,000</u>	<u>6,500</u>	<u>0</u>	<u>6,500</u>
<b><u>FACILITIES</u></b>				
- Rental	1,800	0	0	0
- Operating Costs - Yaroslavl	2,400	900	600	1,500
- Operating Costs - Other	18,000	18,000	12,000	30,000
Total	<u>22,200</u>	<u>18,900</u>	<u>12,600</u>	<u>31,500</u>
<b><u>OUTSIDE EXPERTS</u></b>				
- Working Commission	15,000	0	15,000	15,000
- Lawyers	15,000	0	0	0
- Other	33,000	0	0	0
Total	<u>63,000</u>	<u>0</u>	<u>15,000</u>	<u>15,000</u>
<b><u>TRAINING</u></b>				
- Manual	100,000	0	50,000	50,000
Total	<u>100,000</u>	<u>0</u>	<u>50,000</u>	<u>50,000</u>
<hr/>				
<b><u>TOTAL OPERATING COSTS</u></b>	<u>322,750</u>	<u>64,277</u>	<u>134,584</u>	<u>198,861</u>
<hr/>				
<b><u>REGIONAL DISBURSEMENT</u></b>	<u>30,000</u>	<u>0</u>	<u>30,000</u>	<u>30,000</u>
<hr/>				
<b><u>EXPENSE TOTAL</u></b>	<u>\$352,750</u>	<u>\$64,277</u>	<u>\$164,584</u>	<u>\$228,861</u>
<hr/>				
<b><u>PROFESSIONAL FEES</u></b>	<u>\$267,638</u>	<u>\$267,638</u>	<u>\$123,890</u>	<u>\$391,628</u>
<hr/>				
<b><u>GRAND TOTAL</u></b>	<u>\$620,388</u>	<u>\$331,915</u>	<u>\$288,474</u>	<u>\$620,389</u>

20-Jan-94

WORK PLAN DELAYS MEMO

**Bain & Company****Bain Link**

Scherbakovskaya Ulitsa 40-42  
 105187 Moscow, Russia  
 Telephone: (7) (095) 369-0326, -5948, -5950, -2643, -2333, -2351  
 Facsimile: (7) (095) 369-5947, 166-6867

**MEMORANDUM**

**To:** Walter Coles, USAID  
 Deirdre Clifford, USAID

**CC:** Maxim Boycko, GKI  
 David Ross, GKI  
 Liz LaTerz, Bain & Company

**From:** James Allan

**Date:** February 11, 1994

**Re:** Small Business Development: Workplan Delays

**Contract:** USAID Moscow

The purpose of this letter is to summarize the discussion between Bain and USAID held on February 3, 1994, and on subsequent days, here in Moscow. In particular, we would like to document our concern regarding the deliverables of the case based on our reliance on delayed Federal approvals.

1. Bain has provided support to the GKI regarding condominium legislation, providing support for the Federal Ukaz of December 24, 1993, and submitting a recommended charter on January 28, 1994.
2. Bain put USAID on notice during the February 3, 1994 meeting that we had not received support according to our agreed timeframe from Sokin at the GKI, and that if we are unable to obtain pilot condominium charter approval from GKI (and support for subsequent approval from Gostroi and the Ministry of Justice) we will be unable to complete our contract deliverables with regards to condominiums.
3. Bain also discussed with USAID that the methodology for the sale of built-in space had not been forthcoming from GKI, and GKI had recently asked us to draft a methodology ourselves to submit to them. Bain and USAID agreed that we would continue to work on this part of the project, but that pilot sales of commercial space would not be included in our case deliverables.
4. Bain further contacted USAID by telephone on February 7, 1994, speaking to Deirdre Clifford, to underscore that again the expected support from GKI had not been forthcoming and to request support from USAID with Dmitri Vassiliev.
5. On February 8, Bain met with Albert Sokin at the GKI and discussed the following time frame and commitment: that Bain would submit a modified Charter by Friday, February 11, 1994, and following this, GKI would provide us with a letter of approval by Vassiliev to use this Charter. (Sokin said that pilot approval would not require co-approval by Gostroi and Ministry of Justice.)

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6. Following this discussion with GKI, Deidre Clifford of USAID was once again contacted and notified that a new timeframe was in place and that we felt that the "intent" of the GKI to support the pilot effort was in place.

Bain will submit a revised Charter to Albert Sokin on Friday, February 11. As you can see by the attached workplan, which we provided to you on February 3, these delays could result in delays in every subsequent step in the workplan. We require immediate pilot approval to guarantee deliverables. USAID support is required to ensure that approval, and Bain will remain in close contact.

In the meantime, we have been working closely with the city of Yaroslavl to reorder the workplan, to attempt to ensure that delays in the Charter approval will not wholly delay the case. To this end, we have been negotiating with them to sign their condominium polozheniye next week, regardless of the status of the charter. However, this is a high risk strategy, and we cannot be sure it can be successful.

It is our understanding that USAID is fully aware of our situation, and fully aware that the deliverables of the case are in question if Federal approval for the Charter is not obtained in the next week. It is further understood by Bain that USAID and GKI have to date been satisfied with Bain's level of effort on the case, and the progress made to date, as indicated by the recent approval of the No Cost Revision, submitted January 22, 1994 and signed by USAID on February 4, 1994.

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ACTIVITIES	FEBRUARY							MARCH								
	7	11	14	18	21	25	28	4	7	11	14	18	21	25	28	30
● OBTAIN FEDERAL (GKI) APPROVAL FOR THE PILOT BY-LAWS*	-----															
● MAKING CHANGES TO LOCAL POLOZHENIE AND BY-LAWS ACCORDING TO THE GOSSTROI AND MINISTRY OF JUSTICE LETTERS	-----															
● INTRODUCTION OF THE BY-LAWS AT THE LOCAL LEVEL - DESIGNING REGISTRATION PROCEDURE - RESOLVING FINANCIAL ISSUES AND ISSUES OF MAINTENANCE			-----													
● LOCAL APPROVAL OF THE POLOZHENIE AND BY-LAWS (PILOTS' APPROVALS)						⊗										
● SEMINAR AT YAROSLAVL, ORGANIZATION OF A SUPPORT UNIT				⊗												
● WORK WITH PILOTS - MAINTENANCE - FINANCES - REGISTRATION - ADMINISTRATIVE ISSUES													⊗			
● PILOT INCENTIVE PROGRAM - DEVELOPMENT - IMPLEMENTATION																
● WORK WITH LOCAL DUMA TO CONFIRM APPROVALS																
● TRIP TO THE US																
● MANUALS FOR - LOCAL AUTHORITIES - CONDO PARTICIPANTS																

NOTE: IF THE GKI APPROVAL FOR THE PILOT BY-LAWS IS NOT OBTAINED BY FEBRUARY 11, 1994 THE CONDO PILOT PROGRAM MIGHT BE SIGNIFICANTLY DELAYED (BEYOND THE TIMEFRAME OF THE USAID-EAIN LINK CONTRACT), DUE TO THE FEBRUARY 27 ELECTIONS TO THE LOCAL DUMA IN YAROSLAVL

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31 MARCH, 1994

CREATE A SYSTEM THAT ALLOWS  
COMMERCIAL OWNERSHIP OF BUILT IN  
SPACE

MAJOR  
ACTIVITIES:

CREATE A COMMERCIAL  
PROPERTY REGISTRY

IMPLEMENT  
CONDOMINIUM  
LEGISLATION

IMPLEMENT SALES OF  
BUILT IN SPACE

CREATE AN EFFICIENT  
LEASING / SUBLEASING  
ENVIRONMENT

PROPOSE REDUCTIONS  
IN LEGISLATIVE  
BURDENS

PUBLICIZE NEW  
LEGISLATION AND  
PROGRAMS

COMPLETED  
CONTRACT  
DELIVERABLES:

- PERFORMED PHYSICAL INVENTORY OF COMMERCIAL STREETS
- SUPERVISED AND DIRECTED DEVELOPMENT OF COMPUTER DATABASE AND SOFTWARE TO TRACK PROPERTY
- WROTE, LOBBIED FOR PASSAGE AND PUBLISHED EDICT ENSURING UP-TO-DATE AND ACCESSIBLE REAL ESTATE INFORMATION TO THE PUBLIC
- GATHERED LEGAL INFORMATION ON POTENTIAL PILOT SITES

- CHOSE, GAINED CITY APPROVAL AND GATHERED INFORMATION ON OVER 15 POTENTIAL PILOT SITES
- INFORMED THE RESIDENTS OF OVER 10 PILOT SITES OF CONDO LEGISLATION AND BEGAN REGISTRATION PROCESS FOR 6 SITES
- TRAINED RELEVANT CITY OFFICIALS
- INFORMED POTENTIAL MAINTENANCE CONTRACTORS OF CONDO LEGISLATION AND GAVE TRAINING MATERIALS

AGREED TO REMOVE THIS  
DELIVERABLE BECAUSE  
LAW WAS ONLY RECENTLY  
PASSED

- DESIGNED NEW LEGAL PROCEDURES AND LEGISLATION SETTING MAXIMUM TIMES AND ELIMINATING RESTRICTIONS

- PROPOSED REDUCTIONS IN LEGISLATIVE BURDENS TO CITY

- DEVELOPED MANUAL ON CREATING A PROPERTY REGISTRY
- DEVELOPED CONDO INFORMATION BROCHURE
- DEVELOPED DRAFT MANUAL ON CREATING AND RUNNING CONDOMINIUMS
- ESTABLISHED LOCAL CONDO "HOT LINE" ON A TEMPORARY BASIS
- DISTRIBUTED CHARTER AND BROCHURE
- PUBLISHED NEW REGULATIONS AND INFORMATION ON PROPERTY REGISTRY AND LEASING

ADDITIONAL  
ACTIVITIES:

- DISSEMINATING INFORMATION ON REGISTRY TO OTHER CITIES (SEMINARS ON 4 MARCH AND 28 MARCH)
- REALITY TESTING OF INFORMATION ACCESSIBILITY
- INVESTIGATING FREE NATIONAL ADVERTISING IN NEWSPAPER EKONOMICA / ZHIZN

- ASSISTED IN DEVELOPMENT AND PASSAGE OF FEDERAL CONDO LAW
- DEVELOPED AND GAINED SKI APPROVAL OF A STANDARD CONDO CHARTER FOR PILOT USE
- GAINED APPROVAL OF LOCAL CONDOMINIUM LAW AND CHARTER
- DEVELOPED SYSTEM TO DISBURSE SUBSIDIES TO CONDOMINIUMS

- GATHERED INFORMATION ON METHODOLOGIES CURRENTLY BEING USED
- RECOMMENDED A METHODOLOGY TO GKI
- IDENTIFIED POTENTIAL PILOT SITES
- BEGAN IMPLEMENTATION BY ASSISTING LOCAL LESSEE TO BUY HIS BUILT-IN SPACE
- CLARIFYING LAW WITH LOCAL KI AND GKI

- GAINED APPROVAL OF SEALED BID LEASING REGULATION
- IDENTIFIED PILOT SITES
- LOBBYING FOR IMPLEMENTATION OF NEW REGULATIONS

- DISTRIBUTING CONDO AND REGISTRY MATERIALS TO OTHER CITIES AND ADVISORS

CONTRACT  
DELIVERABLES  
NOT YET  
COMPLETED:

- ENSURE RECORDING OF CONDOS IN REGISTRY

- FINALIZE REGISTRATION OF 4 CONDO PILOT SITES

- FORMALIZE PROPOSALS

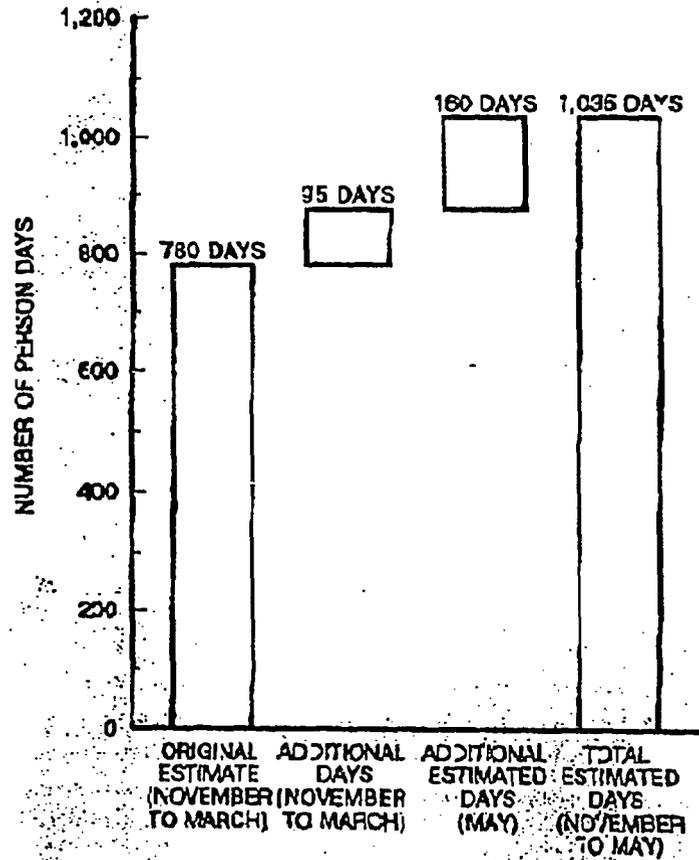
- DISTRIBUTE CONDO MANUALS

# SMALL BUSINESS IMPLEMENTATION

# PHASE II: IMPLEMENTATION

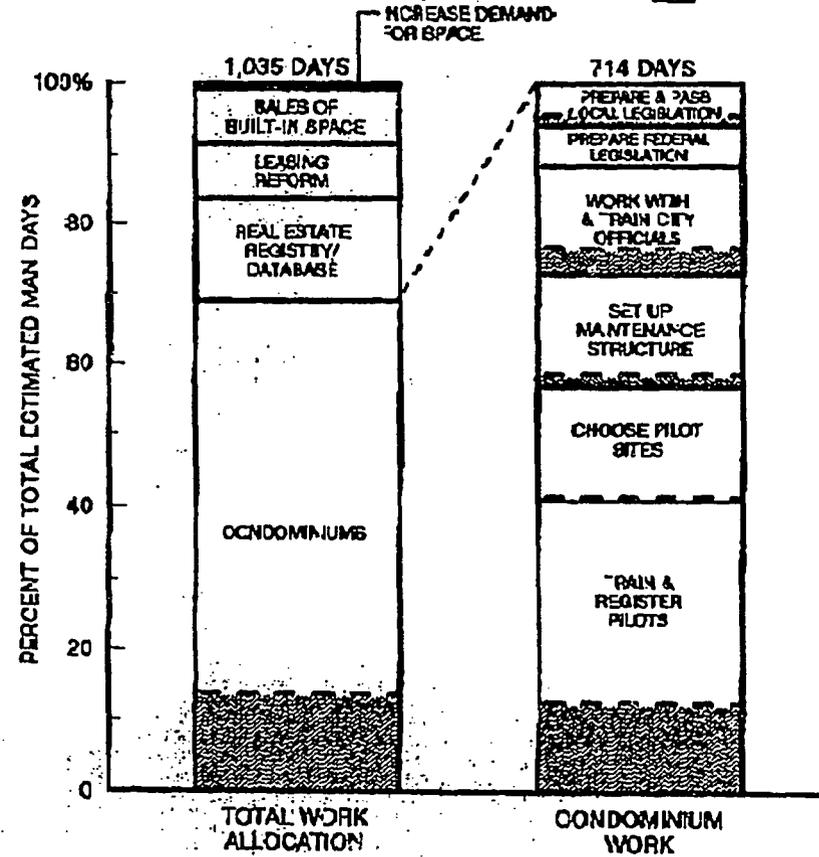
## WORK EFFORT

**TOTAL EFFORT**



**BREAKDOWN OF EFFORT**

INCOMPLETE AS OF MARCH 3, 1994



SOURCE: THE SHEETS. BAIN ANALYSIS

April 21, 1994. 0301JK142 S3E

COMPLETED DELIVERABLES, INCREASED FUNDING, REVISED TASK

**Bain & Company****Bain Link**

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**MEMORANDUM**

**To:** Maxim Boycko, RPC  
 David Ross, RPC  
 Walter Coles, USAID  
 Thomas Rishoi, USAID Moscow  
 Bill Richter, USAID Moscow

**CC:** John Smith, Bain Link  
 James Allen, Bain Link

**From:** Chris Tsakalakis *CT*

**Date:** April 21, 1994

**Re:** Small Business Development; Summary of Work as of March 31, 1994 and  
 Justification for Additional Funding

**Contract:** US AID CCN-0005-C-00 3108

**Task Order:** 7-0025-KPMG

**Objective**

In order to clarify the current status of the above task order, this memo will outline the following:

1. The progress of the Small Business Development Team in completing the deliverables delineated in the above task order by its end date, March 31, 1994
2. The reasons for not completing some of the contract deliverables by the deadline
3. A request for additional funding to complete contract deliverables and to provide follow on work

**Summary**

The Bain Small Business Development Team, as at the end of the task order performance period, made significant progress in completing most of its task order deliverables and in implementing true real estate reforms in the city of Yaroslavl. Due to developments beyond Bain's control, however, one major deliverable, the registration of 4 pilot condominium buildings, was not completed by the original deadline. Bain feels that the delay in completing this deliverable is justifiable and that with additional time the pilots can be registered as originally intended. Bain feels that we should receive additional funding to cover the additional time required to complete this deliverable and we hereby request that funding.

**Background**

Following a six month review of obstacles facing small businesses in Russia, Bain began, in November of 1993, to work on implementing specific real estate reforms under Phase II of the Small Business Development work in Yaroslavl. The objectives of Phase II were to launch a pilot program for real estate reform on a local basis in order to develop a model for national legislation. More specifically, quoting from the task order:

Boston • Brussels • Chicago • Dallas • Geneva • Hong Kong • London • Milan • Moscow • Munich  
 Paris • Rome • San Francisco • Sydney • Tokyo • Toronto • Warsaw

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- To provide concrete examples of methods to improve the quality of small scale businesses in Russia;
- To develop and implement a local pilot program that will begin to create a free commercial real estate market in Yaroslavl; which can be a model for Russia

Two components of this work are:

- To work with the relevant federal and local bodies to assist in developing and implementing pilot commercial sales, condominium and leasing legislation
- To test and showcase legislation through the creation of pilot condominium sites that will begin once local legislation has passed.

The original task order set 5 major tasks for the Bain team. They were to:

1. Create a transparent, freely accessible commercial property registry
2. Create a system that allows commercial ownership of built-in spaces
3. Create an efficient leasing and subleasing environment by making fundamental improvements
4. Propose reductions in legislative burdens on entrepreneurs
5. Publicize new legislation and programs

The intended results were to include

1. 5 to 15 privately owned commercial spaces
2. 4 to 6 pilot condominium buildings
3. A city government real estate manual
4. A real estate incentives program
5. A model public relations program

As the project progressed, several developments beyond Bain's control led to revisions in both the timing and scope of the task order. These developments included:

1. Delays in the passage of federal condominium legislation
2. Delays in the passage of a methodology regarding the sales of built in space

Given the delays, communication was made with both the GIKI and USAID regarding deviations from the contract and changes were made to the original task order with the following documents:

- The January 1994 No Cost Revision of the task order which:
  - extended the deadline of the work from January 31, 1994 to March 31, 1994 at no extra cost to USAID
  - changed the scope of the task order by:
    - eliminating the requirement of distributing manuals throughout Russia
    - making the implementation of sales of built in space contingent on the passage of appropriate laws or special GIKI permission
    - reducing the allocation of the case manager to 70% from 100% (see the Phase II: No Cost Revision in the appendix)
- A February 11, 1994 memo outlining work plan delays that again changed the scope of the task order by eliminating implementation of pilot sales of commercial spaces as a deliverable

**Progress Against Task Order Deliverables as of March 31, 1994**

The Bain team has been successful in completing a majority of the tasks and achieving most of the results agreed to by the deadline of March 31, 1994. For each major task, several activities beyond the ones called for in the original task order were also completed. The deliverables not completed by the project end date were connected with the registration of 4 pilot condominium buildings.

Deliverables completed, additional activities performed and deliverables not completed by March 31, 1994 are set out below in the same format as the original task order whose text is italicized. These are also summarized in a slide entitled "Phase II: Progress to Date" include in the appendix.

**1) Create a transparent, freely accessible commercial property registry.**

By March 31, the Bain team was successful in completing the following deliverables in Yaroslavl.

- a. *Take physical inventory.* A physical inventory of all buildings on commercial streets was organized and checked by the Bain team to insure that the registry contained accurate, up to date information
- b. *Establish programs to track and make public ownership and use of commercial real estate.*
  - (1) *Develop a computer database that will act as a central registry.* Bain organized the structure and, with USAID funds, paid for the development of a real estate database in Yaroslavl
  - (2) *Assist city agencies.* The Bain team was able to get city agencies to agree on a common structure of the database and to agree on sharing the information that each of them had internally with other city agencies and the public.
  - (3) *Negotiate guarantees of access to the database.* Bain helped develop and lobbied for the passage of a mayoral edict that guaranteed public access to real estate information. The Bain team also wrote an article explaining the edict and had the article and edict published in the local official newspaper.
  - (4) *Develop low cost software suitable for use throughout Russia.* A database was developed for less than \$3500 and Bain, acting under this task order, has received full rights to distribute the software throughout Russia.
- c. *Undertake pilot implementation.* Once the registry was created, it was used by the Bain team to gather legal information on potential pilot condominium sites.

Additional activities under this task included the following:

- Using the real estate registry to identify unoccupied commercial spaces as potential pilot sites for implementation of new leasing legislation that Bain had created
- Testing the release of real estate information to the public through the use of a "reality test" where local residents were used to request information from the relevant city agencies
- Disseminating information on the real estate database to other cities by making agreements to distribute the software and an instructional manual to over 20 cities and by organizing 1 seminar and attending 2 additional seminars attended by representatives of Russian cities
- Establishing contacts with the weekly newspaper, *Ekonomika i Zhizn*, and negotiating with them to advertise and distribute the real estate software and manual nationwide.

Contract deliverables not yet completed as of March 31, 1994 are:

- c. (2) *Record new information in the registry once transactions are completed.* This activity can not be done until such time as pilot condominiums are registered.

**2) Create a system that allows commercial ownership of built in spaces**

a. *Implement methodology for the sale of built in space currently being developed by the GKI.* While this deliverable was dropped as of February 11, the additional activities completed under this task included the following:

- Gathering of information on methodologies for sales of built in space currently in use in Russia
  - Developing a recommended methodology for the GKI
  - Identifying potential pilot sites
  - Assisting a local, Yaroslavl entrepreneur to prepare an application for the purchase of his space
  - Attempting to clarify the newly passed (March 11) law with both Yaroslavl property committee officials and GKI lawyers
- b. *Implement local condominium legislation*

By March 31, the Bain team was successful in completing the following deliverables in Yaroslavl.

- (1) *Choose pilot sites.* Over 15 buildings were identified as potential pilot sites. For each, legal information was gathered and city approval was attained to use them as pilot sites.
- (2) *Consult occupants of the pilot sites.* General meetings were organized for and information brochures were given to residents of over 10 potential pilot sites. At the

meetings the Bain team informed residents of the details of the condominium legislation and addressed resident concerns and questions.

- (3) *Work with city officials to ensure their understanding.* The Bain team worked closely with all relevant city officials to inform them of the condominium legislation and to work out all of the practical details of administering the new condominiums.
- (4) *Train potential maintenance contractor.* The Bain team met with 2 potential maintenance contractors informing them of the new condominium legislation and giving them informational materials on both condominiums and the maintenance of common spaces.
- (5) *Create and launch press releases making the public aware of the new legislation.* Bain was able to gain press coverage through the use of seminars held with city officials and the distribution of the Bain developed condominium charter and information brochure.

Additional activities under this task included the following:

- Assisting in the development and passage of federal condominium legislation
- Clarifying the federal law with the Construction Ministry (Gosstroj) and the Ministry of Justice
- Developing and gaining approval from the GKI of a standard condominium charter for use on a pilot basis
- Gaining the approval of a local condominium law and charter
- Developing legislation that will establish a system for the distribution of maintenance subsidies directly to condominiums

Contract deliverables not yet completed as of March 31, 1994 are:

- (1) (c) *Train condo associations in how to self govern and budget.* Due to delays in adopting a system to distribute subsidies to condominiums, the main training tool, the manual on condominium government and management, could not be completed by the end of March.
  - (6) *Monitor pilot sites for a period of one and a half months.* Given delays in getting approval of the standard charter and subsequent delays in passing local legislation, pilot sites have been monitored by Bain since early March, they were thus monitored for only 3 to 4 weeks by March end.
- Result 2) *4-6 Pilot Condominium Buildings.* Although the registration process had begun on over 5 potential sites prior to March 31, no pilots had been registered by the deadline.

- 3) *Create an efficient leasing and subleasing environment by making fundamental improvements*  
By March 31, the Bain team was successful in completing all of this task's deliverables in Yaroslavl.

- a. *Design and lobby for legal changes in the process of leasing.* Two new regulations were developed that set out both an open bidding and a sealed bid procedure to leasing out space. The regulations were structured so as to
  - (1) *Reduce the power of municipal institutions and streamline the approval process.* Maximum times for approval and well defined, limited reasons for disapproval were set.
  - (2) *Create a proper incentive structure.* The new regulations allowed the KI to hold on to most of the lease proceeds and thus created an incentive for them to lease out space.
  - (3) *Reduce restrictions.* The regulations eliminated sublease taxes and disallowed other restrictions on the use of the property.

Additional activities under this task included the following:

- Gaining approval of the sealed bid regulation and a commitment to integrate reforms from the new to the old open bid regulation
- Identifying pilot sites suitable for implementation of the sealed bid leasing regulation
- Lobbying for implementation of the new sealed bid leasing regulation

#### *Increase Demand for Space*

- 4) *Propose reductions in legislative burdens on entrepreneurs*  
By March 31, the Bain team was successful in completing the following deliverables in Yaroslavl.
  - a. *Develop legislative changes in critical burdens.* The Bain team developed proposals for legislative changes in restrictions on profile and subleasing.

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- b. *Lobby for adoption of these regulations.* The Bain team, as part of its work with city officials, lobbied for legislative changes and succeeded in doing so with the passage of the regulation on sealed bid leasing.

Contract deliverables not yet completed as of March 31, 1994 are:

- a. *Develop legislative changes in critical burdens.* The proposals made have not yet been formalized in written form.

5) *Publicize new legislation and programs*

By March 31, the Bain team was successful in completing the following deliverables in Yaroslavl.

- a. *Design a public education program.* The Bain team developed a condominium information brochure. Detailed manuals were developed outlining the creation of a city real estate database and the management of a condominium (draft). An article was written by Bain explaining the procedure for public access to real estate information.
- b. *Use materials for training and information campaigns.* The Bain developed standard condominium charter and condominium information brochure were used to educate both city officials and residents of potential pilot sites. The article on public access to real estate information was published in the weekly city newspaper. Copies of both the sealed bid leasing regulation and the mayor's edict on the release of real estate information were also published in local newspapers.
- d. *Distribute the materials city wide.* The Bain developed standard condominium charter has been distributed throughout Yaroslavl.

Additional activities under this task included the following:

- Distributing the draft condominium manual to the Urban Institute and PADCO who are acting as advisors on other USAID funded, real estate related projects
- Distributing the manual on creating a city real estate database to over 7 other Russian cities

Contract deliverables not yet completed as of March 31, 1994 are:

- u. *Design a public education program.* As was mentioned in the condominium implementation section, 2)b.(1)(c), the manual on condominium government and management, was not completed by the end of March.
- c. *Upon completion of pilots, revise materials to reflect any important issues.* Given that pilots were not yet registered by the end of March, final revisions were not made.

**Reasons for Non Completion of Contract Deliverables**

The major deliverable not completed by March 31 is the registration of 4 pilot condominium buildings. The delay in registering these buildings can be explained by 3 factors.

1. Delay of Mr. Vassiliev of the GKI in approving the standard condominium charter
2. Subsequent delay in the passage of local condominium legislation
3. Voluntary nature of the condominium legislation

In order to make the federal condominium decree implementable on a local basis, a standard charter had to be approved for pilot use in Yaroslavl. Bain first submitted a draft standard condominium charter to the GKI for their approval on January 28. Bain put USAID on notice on both February 3 and February 7 that approval from GKI had not been received and that if it were not received by February 11 we could not guarantee that deliverables would be completed by the scheduled project end date of March 31. On February 11, Bain communicated in a memo to Walter Coles and Deirdre Clifford of USAID (copy enclosed) that a modified charter had been submitted to the GKI but that approval had still not been received. On February 21, Bain finally received the approval for the charter.

While the Bain team made every effort to revise the charter as required by the GKI and to lobby city officials for approval of a local condominium law, the delayed approval of the charter had a significant effect in slowing the approval of the entire package of local condominium legislation. Firstly, as we had warned on February 3, the close proximity of the charter's approval to the election of a new city дума led to further delays in approving the local legislation. Given that the charter approval was given 5 days before the February 27 elections, the mayor of Yaroslavl felt it necessary that the new дума

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review and approve the condominium legislation before he signed it into law. The condominium legislation was thus presented to the дума at their first meeting on March 10. Secondly, the delay in approving the charter reinforced the perception that it, as one of the first of its kind in Russia, was experimental and this caused the mayor to take a further, precautionary step in distributing to citizens 5000 copies of the charter and waiting to see if any serious objections were raised. The end result of these delays was that the mayor finally signed the condominium legislation on March 21, almost a month later than our original estimate of February 25.

Given the perceived experimental nature of the legislation, passage was agreed to by the mayor after making 2 unanticipated restrictions. First, registration as a condominium was made voluntary despite the opinion of the Ministry of Justice that the federal law, once a standard charter is established, was mandatory. Secondly, the registration of condominiums was limited to 6 pilot sites. The first restriction meant that Bain would have to spend more time than anticipated to train and gain the agreement of residents. The second restriction reinforced the perception of the condominium legislation as experimental; thus making it more difficult to convince residents of registering their buildings as condominiums.

During the almost one month delay, the Bain team sought to minimize further delays by continuing to work on completing, and in some cases exceeding, all deliverables not directly dependent on the local legislation's passage. This included the completion and dissemination of the real estate property registry work and the increased effort in passing proposed leasing legislation. The work also included a significant effort in preparing for condominium registration. Efforts included educating and surveying both city officials and residents of potential pilot sites through the use of published materials and meetings on a multi-building, single building and individual person basis. Maintenance contractors were also trained and a manual on condominium management was developed to the extent possible.

The continuing delays in passing local legislation were communicated to both GKI and USAID on a weekly basis through update memos. The possible extent of delays in the project end were communicated as soon as March 7. The exact length of the delays continues to be hard to gauge, however, because of the highly charged, political nature of getting large, diverse groups of people to all agree on how they will manage their most precious asset, their homes.

#### Request for Additional Funding

Given the justifiable delays in the completion of contract deliverables, we would like to request additional funding to cover 3 areas:

1. Fees to cover the official performance period in which level of effort exceeded the budget
2. Fees and expenses to cover the additional time needed to register the 4 pilot buildings
3. Fees and expenses to cover a 2 month follow up period in which a reduced team would monitor the pilot condominiums and insure that progress continues

Because of the greater than anticipated work performed to gain the approval of the charter and to subsequently lobby for its passage in Yaroslavl, the level of effort for the months of February and March exceeded the budget by 95 days. Most of these days were for the team manager and the 2 people responsible for lobbying. To cover this additional effort, we would like to either request additional funding or permission to reallocate operating costs to cover the additional fees. (see slide on work effort in the appendix)

As has already been indicated, the additional time required to complete the registration of 4 pilot condominium buildings is difficult to determine exactly, but we feel that this work should be completed by May 13. The first of condominium should be registered this week and an additional building's application for registration as a condominium should be approved next week. We anticipate that the 2 additional pilots will take slightly longer.

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Given that all but the registration of 4 pilot condominiums remained as deliverables at the official contract end date, the manning of the case, since March 31, has been reduced. In general, the monthly effort has been reduced from 200 person days for March to 110 person days for April. Specifically, this meant the removal of 2 research analysts, the real estate inventory manager, and one of the persons responsible for lobbying. Reduction in allocations occurred for one senior analyst from 100% to 70% and for the overall project director from 25% to 5%.

Given the 6 additional weeks required, 160 additional person days would be required to finish the last contract deliverables. (see slide on work effort) Assuming that operating costs are used to cover the additional fees incurred in March, we would like to request additional funding to cover fees and expenses for the period from April 1 to May 13.

Beyond mid May, we feel that Bain support would be needed to insure that the pilot condominium buildings progress and provide positive examples both within Yaroslavl and throughout Russia. The Bain support would include work with pilot residents, city officials, outside contractors and outside advisors. Work in the pilots would include meeting with pilot residents, providing them with funding to do minor repairs, establishing maintenance contracts and clarifying issues with government officials. Work with city officials would include clarifying new laws related to condominiums, insuring proper treatment of pilot sites, and developing additional, necessary regulations. Bain would also work with outside maintenance contractors to set up contracts with pilots, and we would communicate and share experience with other advisors.

The pilot monitoring would require 50% allocations of 3 people or 33 person days per month. The work would continue from mid May to mid July until such time as an other advisor could monitor the sites. This other advisor could be the Urban Institute who have agreed to continue the oversight of the Yaroslavl condominiums under their current USAID contract beginning in June/July.

#### Next Steps

We would like your response to this memo as soon as possible. Assuming a positive response to the request for additional funding, Bain will, based on this memo, write a task order and submit it to the GKI and USAID for approval.

#### Appendix

- Phase II: No Cost Revision of Task Order
- February 11, 1994 memorandum regarding work plan delays sent to Walter Coles and Deirdre Clifford of USAID
- Case progress to date as of March 31, 1994
- Breakout of work effort
- Funding requirements

SUBCONTRACTOR BASIC ORDERING AGREEMENT NO. 3108-C

TASK ORDER NO. 002 (Amendment Three)

Effective Date: November 1, 1993 Through September 30, 1994

Performance:

This Task Order is authorized under KPMG Peat Marwick's Prime Contract No. CCN-0005-C-00-3108-00. Performance shall be in accordance with the following:

The subcontractors will spend eleven months working in Moscow and other cities continuing work assisting GKI with general management of the voucher auction effort. Support should be for the fees and expenses of a central management team with the following primary functions: provide project management resources to GKI for the coordination of regional efforts; assess regional resource needs; provide necessary financial and advisory support to the regions; recruit, train and supervise individuals to provide support to the regions; and monitor overall auction progress and resource allocation. See issues set forth in Attachment A. hereto and deliver a written report of the findings.

Coordination:

Tasks and Reporting:

Mr. Roger Leeds  
(202) 467-3842

Contract Administration:

Mr. Jack Summers  
(202) 467-3433

Billing Shall Be Addressed To:

Ms. Pamela Fingers  
KPMG Peat Marwick  
2001 M. Street, N.W.  
Washington, D. C. 20036

Type of Task Order:

Cost Plus Fixed Fee (CPFF)

Ceiling Price:

\$820,478 Maximum for  
Labor, All Expenses, And  
International Business  
Class Airfare.

\*This corresponds to KPMG's Task Order #7-0025-KPMG.

Task Order No. 002 (Amendment Three)  
Page 2

Schedule:

See Attachment B

Please note that fees for services should be itemized separately, KPMG Peat Marwick will reimburse Bain & Co, Inc., for the cost of Business class airfare on a U.S. flag carrier; therefore when reporting expenses, a copy of the travel itinerary identifying the cost of full coach airfare for each ticket should be included. Other expenses including food, lodging, local transportation and reasonable incidentals are also reimbursable up to an in country per diem. All lodging expenses being submitted for reimbursement should be itemized, and accompanied by ORIGINAL receipts. Meals and incidentals shall be paid at the flat rate of \$75 per day, no receipts are required for these expenses. (Rates may vary in other cities.)

Invoicing and payment shall be in accordance with Subcontractor Basic Ordering Agreement No. 3108-00-C ARTICLE VI-SPECIAL PROVISIONS - Paragraph B. entitled "Invoicing and Payment".

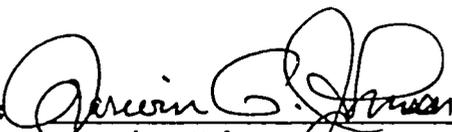
Limitation of Liability:

No liability on the part of KPMG Peat Marwick, legal or otherwise, shall arise for costs incurred by Bain & Company, Inc., in excess of \$820,478.18 for labor, all expenses and Business Class Airfare unless additional effort and/or airfare ceiling incorporated as a Modification to this Task Order.

Acknowledgement and Acceptance:

KPMG Peat Marwick  
2001 M. Street, N.W.  
Washington, D. C. 20036

Bain & Co., Inc.  
Two Copley Place  
Boston, MA 02217-0897

By:   
Darwin Johnson  
Principal

By:   
Mr. Colin Anderson  
Vice President &  
Finance Director

Date: 6-30-94

Date: 6-23-94

ATTACHMENT A

STATEMENT OF WORK

- To provide concrete examples of methods to improve the quality of small scale business in Russia: and  
  
To develop and implement a local pilot program that will begin to create a free commercial real estate market in Yaroslavl and that can be rolled out across Russia.

The two major components of these objectives are:

Legislation. Work with the relevant federal and local bodies to assist in developing and implementing pilot commercial sales, condominium and leasing legislation to:

- Break the municipal monopoly on space and reduce the involvement of the municipality in allocating space;
- Create true private ownership and competitive supply;
- Ensure the freedom of private owners to make decisions on use and disposition;
- Provide for proportionate and fair allocation of costs to private owners; and
- Provide a replicable model that can be used throughout Russia.

Pilot Sites Test and showcase legislation through the creation of pilot condominium sites that will begin once local legislation is passed.

Overall public relations work with the relevant city government (publicizing each region as a place where private business can function efficiently).

ATTACHMENT B

TASK ORDER 0002 - (Same As Task Order 7 - 0025-KPMG)  
SMALL BUSINESS DEVELOPMENT (AMENDMENT 3)

Subcontractors (Bain & Co.)

I. Salaries	Expert	Daily Salary	Est Days	Allocation	# of days	Cost of Service	
Overall Project Director	Allen	331.92	135.67	25%	25.7	8,530.34	
SB Dev Team Mgr. (1)	Tsakalakis	331.92	149.2	61%	87.2	28,943.42	
SB Dev Team Mgr. (2)	Durham	331.92	68	80%	62.1	20,612.23	
Lobbying/Govt. Rel Mgr.	Savchenko	264.95	110	50%	60.1	15,923.49	
Legislation Dev Mgr.	Vitruk	141.67	110	50%	104.8	14,847.02	
Real Est Inventory Mgr.	Sapelnikova	96.59	128	75%	83.4	8,055.61	
Research Analyst	Karavaikin	96.59	194	85%	136.8	13,213.51	
Research Analyst	Bobrovsky	52.89	213	80%	69.0	3,649.41	
Assoc Consultant Intern	TBD	22.85	110	100%	90.6	2,070.21	
Assoc Consultant Intern	TBD	22.23	84	100%	118.3	2,629.81	
Case Team Asst (Russian)	Fedchenkova	9.20	64	100%	103.0	947.60	
Office Admin (Russian)	Avdonina	23.00	110	10%	21.0	483.00	
Contracts Support Mgr	LaTerz	201.25	103	25%	29.2	5,876.50	
Contracts Support Asst	Lareau	57.41	66	50%	41.1	2,359.55	
Consultant	Arbuznikova	40.00	22	50%	22.0	880.00	
<b>Total Salaries</b>					<b>1,054.30</b>		<b><u>129,022</u></b>
<b>II. Fringe (17%)</b>							<b><u>21,934</u></b>
<b>III. Overhead (230%)</b>							<b><u>347,197</u></b>
<b>IV. Allowances (25% differential or actual salary, whichever is less)</b>							
Overall Project Director	Allen			25%		2,130.08	
SB Dev Team Mgr. (1)	Tsakalakis			actual salary		2,393.63	
SB Dev Team Mgr. (2)	Durham			25%		5,152.19	
<b>Total Allowances</b>							<b><u>9,676</u></b>
<b>V. Other Direct Cost</b>							<b><u>249,206</u></b>
<b>Subtotal Subcontractors</b>							<b><u>757,034</u></b>
<b>Fixed Fee</b>							<b><u>63,444</u></b>
<b>Total Subcontractors</b>							<b><u>820,478</u></b>



**BUDGET NOTES**

1. Adjustments may be made between line items up to 15% without Mission concurrence. Line item adjustments in excess of 15% , increases in the level of effort, increases in the grand total and/or changes in the technical direction must be approved by all parties in an amendment to this Task Order.
2. The Consultant will seek a cost sharing with local counterparts when entering into subcontracts or rental of office space and/or communications equipment whenever possible.
3. Consultants must be approved by the GKI and USAID based on experience and availability.
4. Russian labor and consultants will receive only the daily salary rate without fringe benefit, overhead or other indirect costs, unless as otherwise negotiated in the prime contract by the Contracting Officer.
5. Procurement and placement of equipment in host country organizations will be in compliance with USAID procurement policies and procedures.
6. Any international round trips beyond one trip per consultant must receive prior approval. (See Special Instructions).
7. A six day work week is authorized for this Task Order and is reflected in the per diem budgeted.
8. Except as specifically approved by the Contracting Officer, salaries reimbursed to the prime and any subcontractor are limited to a maximum of the FS 1 ceiling rate as noted in the contract. If a later audit review shows that the rate paid as salary to any individual and charged to the contract exceeded this limitation, the contractor will be required to reimburse the excess salary payments and associated indirect cost and fees.

(Extend the close out period of the task order to 9/30/94, recognizing that the work by the subcontractor will be completed by ~~June 30~~, 1994).

*JULY 31 → as per discussion w/ ART WARMAN*  
(No other direct cost breakdown provided).