

PN-ABL-569
77818

**Housing
Privatization
in the
Russian
Federation**

March 1992

OFFICE OF
HOUSING AND URBAN
PROGRAMS

U.S. AGENCY FOR INTERNATIONAL DEVELOPMENT



W O R K I N G P A P E R

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Housing Privatization in the Russian Federation

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Office of Housing and Urban Programs
U.S. Agency for International Development

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Contract # DHR-1008-C-00-0108-00

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Abstract

In July 1991 the Russian Federation passed legislation permitting tenants of municipal and departmental (housing owned by enterprises or federal bodies) to purchase their units. Tenants were entitled to receive a generous amount of floor space free of charge. Local governments were given the power to provide additional space to the free-of-charge entitlement and to make several other important determinations.

This paper examines the antecedents of the Federation legislation and describes the provisions of the law in some detail. It then presents information on the early experience with the actual implementation of the program in three cities: Moscow, Ekaterinburg, and Novosibirsk. Because local governments had to pass their own legislation for implementation to proceed, the program has generally only been operational since early 1992. Hence, the period of analysis is from January to May 1992.

The final section of the paper offers a critical assessment of the privatization program as it is being implemented. Our overall conclusion is fairly pessimistic. The Russian housing privatization program is in genuine danger of not accomplishing its major objective of transferring a substantial share of the stock to the population and thereby "shocking" the housing sector into operating more on market principles. Moreover, it may result in a distribution of housing assets (including implicit property rights) which is more inequitable than that existing before privatization began. Such a conclusion is, of course, highly speculative, since a variety of factors could suddenly encourage a massive wave of privatization. Leaving aside such a *deus ex machina*, the Government of the Russian Federation would be well advised to consider major adjustments to its program.

Executive Summary

In the face of severe problems in the housing sector, the dominance of state housing in the existing stock, and the Federation's limited resources, the government of the Russian Federation grasped housing privatization early in the reform period as a cheap tool for improving the nation's urban housing stock.

The obvious line of argument is that making tenants into owners will increase their willingness to spend the money necessary to maintain and improve their buildings, and state subsidies for this purpose can be cut.

Another, and perhaps the most important, argument is that the transfer of a substantial share (perhaps 25 percent or more) of units into private ownership will serve as a catalyst for the private housing market: some of the new owners will sell their units, either to build a new home or to move a more desirable existing dwelling.

The main features of the sales procedure are:

- The law concerns only the state-owned and municipality-owned housing stock.
- Only tenants officially registered as the occupant of the flat can purchase the unit.
- The tenant is given, in effect, a voucher free of charge. The value of the voucher is the price of a square meter of an average quality housing in the city in which the tenant lives times the number of square meters to which he is entitled. The entitlement is computed as 18 square meters of area per person plus an extra 9 square meters for the family.
- The tenant pays the difference between the assessed value of the unit and the value of the voucher. Families living in a unit with a value less than the voucher receive no additional compensation.
- Those living in cooperative projects and in individual houses do not receive a voucher.

- The general method for determining the cost of privatized housing was to be determined by the Council of Ministers of the Russia Federation. (Guidelines to local governments were issued by the Republic in October.)
- During the transition period (length not specified), the old system for allocating units remains in effect.¹ Those allocated a unit have the right to purchase it under the same conditions as listed above.
- Each family can only purchase a single unit under the privatization procedures.

Within the framework of the national law, local governments developed their own models of privatization, but began to implement them only at the beginning of 1992. The main characteristic of the implementation is the diversity among cities. Diversity is evident in the amount of housing given free of charge, the estimation of the average value per square meter of housing, and differences in methods and outcomes for determining the variation in values of different qualities of housing. The paper illustrates this diversity with information for three major cities: Moscow, Ekaterinburg, and Novosibirsk.

The foregoing discussion makes clear that the Russian Federation and individual municipalities have acted boldly to effect rapid privatization, i.e., the transfer of state-owned housing to private ownership on a massive scale. We subject the program in existence at the end of May 1992 to evaluation from three different perspectives:

1. Is the privatization program a strong element of a broader strategy of sectoral housing reform?
2. Is the privatization program likely to succeed in jolting the private housing market into a vibrant existence?
3. Is the program resulting in reasonably equitable treatment of households?

¹ During the transition period the maintenance services for privatized units will be provided by the state maintenance companies. The charges for maintenance are being defined as being the same as the rents on municipally-owned and state-owned units.

Our overall conclusion is fairly pessimistic. The Russian housing privatization program--as being implemented in the spring of 1992--is in genuine danger of not accomplishing its major objective of transferring a substantial share of the stock to the population and thereby "shocking" the housing sector into operating more on market principles. Moreover, it may result in a distribution of housing assets (including implicit property rights) which is more inequitable than that existing before privatization began. Such a conclusion is, of course, highly speculative, since a variety of factors could suddenly encourage a massive wave of privatization. Leaving aside such a *deus ex machina*, the Government of the Russian Federation would be well advised to consider major adjustments to its program. Perhaps most important would be to begin increasing rents--which would raise the value of the unit--and to announce a time limit for making the privatization decision (perhaps 12-15 months), which would focus tenants' attention on this decision.

Housing Privatization in the Russian Federation

The problems of the housing sector in Russia are legend. Typically one-quarter to one-third of the households in a major city are on the waiting list of those qualified for better housing, and the waiting time for a municipal housing unit usually exceeds ten years (Andrusz, 1990). Other estimates, taking into account inter-generational households whose individual families would like to live separately, put the housing shortage in urban areas as high as 45 percent (Kosareva, 1992). Moreover, problems of housing quality abound, including a national rate of 7 percent of households sharing kitchen and bathroom facilities; an additional 8 percent live in hostels or temporary housing (Alexeev et. al, 1991).

These conditions make improving the housing circumstances of the population a high priority for the Russian Federation, despite the limited means at its disposal. To the average household, after the failure of successive communist governments to produce results, progress in this area may be a central test for the new regime.¹ Because 80 percent of urban Russian households live in a state rental unit (either a municipal unit or a unit belonging to a state enterprise or government agency [Kosareva, 1992]), housing improvement must come through the state stock. In the face of sector's problems, the dominance of state housing in the existing stock, and the Federation's limited resources, housing privatization was grasped early in the reform period as cheap tool for improving the nation's urban housing stock.

¹ Results from a survey conducted by the All Union Institute of Social Opinion and published in 1990 in an article without an author listed.

One obvious line of argument for privatization is that making tenants into owners will increase their willingness to spend the money necessary to maintain and improve their buildings, and state subsidies for this purpose can be cut.²

Another, and perhaps the most important, argument is that the transfer of a substantial share (perhaps 25 percent or more) of units into private ownership will serve as a catalyst for the private housing market: some of the new owners will sell their units, either to build a new home or to move a more desirable existing dwelling. For example, while no clear causal connection has been established, it is true that in Sofia significant privatization in 1990-91 was accompanied by a five-fold increase in private sales of real property from 1989 to 1991.³ In any case the volume of transactions will accelerate, opening up possibilities for those with effective demand to improve their housing circumstances.

It is important in assessing the "catalyst" argument to distinguish the situation in Russia where 70 percent of the national housing stock is owned by the State (80 percent in cities) from that in Eastern Europe where the State share at the beginning of economic liberalization did not exceed 30 percent in any major country and reached 50 percent only in the largest cities (Kingsley and Struyk, 1992). Hence, Eastern European countries began housing reform with a substantial private sector, while Russia starts with a sharply different legacy.

² Housing services and utilities have been estimated to be the most inefficient sector in the Soviet economy as measured by the ratio of input costs to producers' prices, with a ratio of 6.02. Kahn and Peck (1991., Table 3.1).

³ For information on privatization in Bulgaria, see Kingsley and Struyk (1992); data on sales is from Hoffman (1992).

An early analysis of Russian housing privatization is of interest for at least two reasons beyond the mere descriptive. First, the method of privatization chosen and its early experience will give an indicator of the likelihood of the policy being successful--in stimulating the private housing market, and in achieving an equitable redistribution of wealth, carried out through the subsidies involved in the transfer of units at below market prices. Stimulation will depend on a significant share of units being transferred, and hence on the terms of sale. Equity issues concern both the treatment of households who do and do not elect to purchase their units, but also the treatment of those on the waiting lists compared with those presently occupying a unit. Second, the structure of the privatization program will suggest the extent to which the Russian Federation has learned from the experience of its Eastern European neighbors in shaping its policies.

This paper proceeds in four sections. The first outlines the options for privatization which were advanced prior to the final July 1992 decree. The second describes the key features of the privatization law, including those issues which were left to local control. The third section examines the programs adopted by three major cities to implement the law: Moscow, Ekaterinburg, and Novosibirsk. The final section provides a critique of the Russian policies measured against the goals stated above and the general principals for housing reform and privatization set out by Struyk and Telgarsky (1992) and Renaud (1991).

Privatization Alternatives

Discussion about privatization options began at least as early as 1987. In March 1988, a special resolution was passed by the Council of Ministers granting the right to private

ownership to members of housing cooperatives who had completely paid off any loans for their units.

More importantly, at the end of 1988 the Council of Ministers passed another resolution giving the right to tenants of state owned housing to purchase their units. The principal objective was to transfer lower quality units (i.e., those needing substantial repairs) into private ownership. Under this resolution purchasers were to pay the full assessed value of the unit. Local authorities had considerable freedom in establishing assessments on the basis of unit quality and location; and in Moscow, for example, premiums for better units turned out to be quite high. National policy makers believed that the lower prices for low quality units would lead to their purchase, but the low prices were not sufficient to make these units attractive. The scheme was abandoned when it became clear that it was not working as intended--by early 1991 only 53,500 units had been sold throughout Russia and these were predominantly of high quality.⁴ Even before then, however, individual cities, such as Moscow, had moved to control such sales.

A more wide-ranging debate about privatization options began in 1990-1991. The many alternatives proposed had in common the tenant's right to purchase his unit. Other variants--sale of the entire buildings, purchase of units by "outsiders"--did not enjoy widespread support. The various options proposed can be grouped into four categories.

Variant 1: "Transfer." All housing would be privatized to the extent possible through the free transfer to residents; only the floor space in excess of the fixed quotas for each family size would be sold at a positive--but depreciated (or otherwise sufficiently low)--price.

⁴ State Committee on Statistics of the U.S.S.R. (1990), p.85; State Committee on Statistics of the Russian Federation (1991), p.210.

This option assumed that privatizing housing at "any price" is the sine qua non for a large, quickly-expanding market. This was seen as the only mechanism which would trigger a boom in housing construction (by some of those receiving their units selling them and purchasing new units). In practice it implies a free transfer of housing within certain limits defined by floor space and tenants "buying out" of extra living space at a low price. Close to this variant is the first proposal by the Mayor's Office and the Government of Moscow.

Variant 2: "Buying Out." The estimated value of all apartments would be paid with only minimum discounts; in other words, residents would purchase their units from the state on commercial terms.

This variant has the objective of replenishing local budgets, with the revenues collected being earmarked for the housing sector. The city of St. Petersburg first proposed this option.

Under its proposal a city resident would have been entitled to free living space worth rub 1,000, i.e., 3 - 10 square meters at then current prices. Practically, it implies nearly full payment for the value assessed by a special method proposed by the city which in fact would have involved significant discounts from the true market value.

Variant 3: "Socially Just." A fixed amount of living space would be freely transferred to the purchaser and high, even prohibitive, prices would be charged for any space beyond this level.

This option rests on the need for strictly observing the principles of social justice. The Moscow Soviet, for example, proposed transferring a certain amount of floor space for free and then charging prices per square meter for the extra space which would rise progressively as the amount of extra space increased; for large space increments prices would have been at market or above.

Variant 4: "Compensatory Justice." Every family would receive a voucher for a set number of square meters of space. Only vouchers are used to purchase units and they are freely traded in the market.

This is the only option that compensates families occupying small units. Each person would receive a voucher for 18 square meters of space. Recipients can sell part or all of their vouchers to those needing them to purchase larger units. This scheme was proposed by a special committee on housing privatization of the Moscow Soviet, although the details were never fully worked out.

The Privatization Law of the RSFSR

The Russian Soviet Federation of Socialist Republics' law, passed in July 1991, builds squarely upon the ideas embodied in the options put forward by the major cities. Under the law tenants of municipal housing and departmental housing (housing belonging to enterprises and government departments) have the right to purchase their unit. The main features of the law are:

- Only tenants officially registered as the occupant of the flat can purchase the unit.
- The tenant is given, in effect, a voucher free of charge. The value of the voucher is the price of a square meter of an average quality housing in the city in which the tenant lives times the number of square meters to which he is entitled. The entitlement is computed as 18 square meters of useable living area per person plus an extra 9 square meters for the household.
- The tenant pays the difference between the assessed value of the unit and the value of the voucher. Families living in a unit with a value less than the voucher receive no additional compensation.
- Those living in cooperative projects and in individual houses do not receive a voucher.
- The general method for determining the cost of privatized housing was to be determined by the Council of Ministers of the RSFSR. (Guidelines to local governments were issued by the Republic in October.)

- During the transition period (length not specified), the old system for allocating units remains in effect.⁵ Those allocated a unit have the right to purchase it under the same conditions as listed above.
- Each family can only purchase a single unit under the privatization procedures.
- Some types of buildings cannot be privatized: those which are below the sanitary norms or are dangerous to inhabit, hostels, flats with shared kitchen and toilet facilities, and buildings of historical or cultural significance.

Within these overall provisions, considerable freedom remains for local governments.

They can, for example, increase the amount of space to be given without charge (and thereby increase the value of the voucher). Also, they ultimately determine the procedure for valuing the average square meter of housing in their locality and differences in values with housing quality levels. Local governments can, in addition, override the RSFSR law to permit some types of units on the prohibited list to be privatized. Indeed, the republic-level law is written in such a way that local legislation is required for its implementation, and the time elapsed until such legislation passed--often six months or more--significantly delayed program implementation.

Implementation by Local Governments

Within the framework of the national law, local governments developed their own models of privatization, but began to implement them only at the beginning of 1992. The main characteristic of the implementation is the diversity among cities. Diversity is evident in the amount of housing given free of charge, the estimation of the average value per square

⁵ During the transition period maintenance services for privatized units will be provided by the state maintenance companies. The charges for maintenance are being defined as being the same as the rents on municipal-owned units.

meter of housing, and differences in methods and outcomes for determining the variation in values of different qualities of housing.

We illustrate this diversity with information for three major cities: Moscow, Ekaterinburg, and Novosibirsk (see Table 1). The information is through May 1992 and is based on field visits in March and subsequent telephone follow-up.

Units Ineligible for Privatization. In all three cities officials have declared that about 10 percent of the housing stock cannot be privatized because of units being in poor conditions or other factors.

Space Given Free of Charge. The greatest difference is between Moscow, on the one hand, where privatization is being conducted on a completely free-of-charge basis and all other cities, on the other hand, where some charge is made for house value above the norm. The city Soviet in Ekaterinburg decided to follow the RSFSR law exactly in this regard. In Novosibirsk the norm for space per household was expanded from 9 square meters as specified in the RSFSR law to 18 square meters. In fact, these distinctions appear to have made little difference, at least in the early stages of privatization: in all three cities at least 90 percent of the units are being transferred without payment by the tenant.

Average Price per Square Meter. Both Ekaterinburg and Novosibirsk follow the same general procedure in making these calculations. Both compute the basic value as the "residual replacement value" per square meter of floor space (RRV). This value is computed by first updating the original development cost to current costs using a construction cost index. Then this figure is decreased by the average amount of depreciation estimated to have occurred (based on the data available on the inventory of the housing stock).

Table 1

Key Features of Local Implementation of Russian Federation Privatization Laws

	<u>Moscow</u>	<u>Ekaterinburg</u>	<u>Novosibirsk</u>
1. Amount of space given freely (M ²)			
- per person	full	18	18
- additional per household	unit	9	18
2. Percent of units transferred free of charge	100	95	90
3. Average price per square metre of space above the norm (rub)	0	463	190
4. Range of adjusted prices for space (value) above the norm (rub/M ²)	NA	200-850	120-360
5. Processing fees paid by applicant (rub)	320	600	490
6. Date local law effective	2/92 (02.11.92) ^a	1/92 (01.09.92)	1/92 (01.20.92)
7. Number of units conveyed (municipal stock)			
a. period since adoption of law (months)	3.5 (data on 05.19.92)	4 (data on 05.09.92)	3.5 (data on 05.01.92)
b. number of units conveyed	98754	1288	1669
c. applications	112126	2259	6823
d. total number of municipally owned units (thousands)	2168	142	200
e. share of units forbidden to be privatized (%)	12	10	10

a. The privatization in Moscow according to the Russian Law had begun in September, but was halted and then restarted in February.

This calculation was done for the entire housing stock as a whole. In Ekaterinburg an average RRV of rub 463 per square meter was derived (\$4.60 at the May 1992 exchange rate); in Novosibirsk the comparable figure is rub 190 (\$1.90) per square meter.⁶ These are used to compute the value of housing to be transferred free of charge. That is, the RRV times the number of square meters in the norm is the value to be transferred without charge. It appears that the principal difference between the results for Ekaterinburg and Novosibirsk is that Novosibirsk elected not to take inflation since January 1991 into account in determining this value while Ekaterinburg did. Note, however, that these values can be adjusted annually so that the gap between the two cities may be closed.

Prices Charged for Space (Value) Above the Norm. As shown in Table 1, there is a considerable range in the price per square meter levied for "additional space." In fact, the actual computation is of the difference between the full value of the flat and the amount being given free of charge; i.e., the price per square meter for "extra" space is determined by dividing the difference between the full value and the value of space given without charge by the number of "extra" square meters. Hence, the problem facing each city is how to determine the value of the flat. The procedures adopted differ importantly in their details.

In Novosibirsk unit value (V) is determined as

$$V = \text{space} * \text{RRVav} * [1 + \text{sum (quality adj coefficients)}]$$

where RRVav is the average value of one square meter of housing space in the city that is to be transferred without charge, "space" is the number of square meters in the unit and the

⁶ Moscow, following the same procedure, arrived at a figure of rub 203 per square meter in the fall of 1991. It might be interesting to note that the City Soviet wanted to set the value at rub 850 based on a different calculation procedure.

"quality coefficients" adjust for thirteen types of differences among buildings and flats. The adjustment coefficients, which are based on local judgement, are both positive and negative from a normative standard. For example, the adjustments for location within the city relative to a location in the inner ring are as follows: central location, 0.07; suburbs -0.07. Another example is building materials relative to prefabricated panels: brick or concrete block, 0.04; wood or local materials, -0.04. The largest coefficients are for the size of the kitchen (+/- .07), location (+/- .07), and depreciation (+/- .09). Applying these coefficients has in practice resulted in a moderate range of prices for "additional space," i.e., rub 120-360 (\$1.20-1.30) per square meter.

In Ekaterinburg, in contrast, the calculations were done on a building-specific basis, also taking into account differences in building and flat quality. It is this RRVi (for the ith building) that is used in computing the value of the property to be transferred. The formula employed is

$$V = RRVi * space * (k1 * k2 * ... * k10)$$

where k_j is the coefficient for the j th quality factor; the k_s are both greater than and less than 1.0. Examples of k are: the largest adjustment is for the "prestige" of the building, with a coefficient of 1.2 for a high quality prestige building; a unit located on the first floor or the highest floor has an adjustment of .97; flats in the middle floors of mid-rise and high rise buildings have a coefficient value of 1.03; and, absence of central hot water has a coefficient of .98. These adjustments give rise to a much wider range of prices than in Novosibirsk, i.e., from rub 200 to 850 per square meter.

All three cities are charging small fees for processing the applications for privatization: the highest charge is equivalent to about 17 percent of the average family monthly income in

Table 2

**Summary of Russian Federation Action on
Policy Reforms Complementing Housing Privatization**

<u>Policy Action</u>	<u>Status as of May 1992</u>
increasing rents	Local government given permission to raise rents in mid-May; none acted immediately.
resolution of implicit property rights	No change in the rights of tenants. Owners rights to sell and rent their unit have been made clear. Owners have no rights to select management in partially privatized buildings, and absence of a condominium law restricts workability of rights in fully private buildings.
housing finance availability	The privatization law states that long-term, subsidized credits can be used for purchase. However, the State Savings Bank (Sberbank)--which has a virtual monopoly on long-term housing finance--is not offering loans for the purchase of units being privatized.
timely appraisal of properties	A method has been established for quickly determining the price for which a unit will be sold. The method produces a price which is not related to market value.
implementation of housing allowances	No action has been taken. This is logical since there has been no increase in rents.
improve housing management	The privatization law continues the monopoly of state maintenance companies. However, local governments are beginning to experiment with competitive private management for the municipally-owned housing stock.

the first quarter of 1992. Also, the privatization law in all three cities permits flats with shared facilities to be privatized, if all of the tenants in a flat want to do so.

By the beginning of December 1991, 139,000 flats had been privatized, less than 0.4 percent of state, municipal and public housing units (State Committee on Statistics, 1992b). However, as noted earlier, many cities only initiated units sales in 1992.

The variance in conveyances among the three cities being analyzed here is striking. In the 3.5 to 4 months that the transfer programs had been in effect, under 1,700 units had been transferred in Ekaterinburg and Novosibirsk, while Moscow had transferred nearly 100,000. Stated alternatively, in Moscow about 5 percent of the municipal housing stock has been transferred, compared with under 1 percent in the other two cities.⁷

While some of this difference can be attributed to Moscow's more lenient transfer terms, it seems more likely that it can be attributed to other factors. One is Moscow's being more aggressive in promoting the program. One sign of this is that the City geared up to process the large volume of applications received--in May processing time for an application was averaging about two weeks. Another factor has been the widespread press reporting in Moscow of the prices which units being auctioned are fetching. Additionally, the significant influx of foreigners looking for rentals is fueling a lively up-scale rental market; elderly persons living alone who privatize their units and have the possibility of living with their children are apparently those most likely to provide units for this market. While there has been some auctioning of units in the other cities, the volume is lower. Moreover, few foreigners have taken up residence and both cities are expecting very difficult

⁷ We focus on the municipal stock even though both municipal and departmental stock (state-owned, i.e., that of enterprises and federally government agencies) are subject to the same privatization conditions because the enterprises are moving very slowly to respond to the law. In short, because housing is a benefit with which to attract workers, they want to retain most of it. The best units are being transferred to managers; and the enterprises are willing to let go of the worst units, but there are few takers for these.

economic times (including unemployment of over 10 percent) because of the cut backs in defense spending.⁸

Discussion

The foregoing discussion makes clear that the Russian Federation and individual municipalities have acted boldly to effect rapid privatization, i.e., the transfer of state-owned housing to private ownership on a massive scale. In this section we subject the program in existence at the end of March 1992 to evaluation from three different perspectives:

1. Is the privatization program a strong element of a broader strategy of sectoral housing reform?
2. Is the privatization program likely to succeed in jolting the private housing market into a vibrant existence?
3. Is the program resulting in reasonably equitable treatment of households?

Privatization and Housing Reform: of housing reform in Eastern Europe generally agree that privatization is only one element in overall sector reform. To be successful as an element in a comprehensive reform program, a program of ownership transfer must be accompanied by several complementary actions and have objectives broader than simply transferring title.⁹

In terms of objectives, in addition to the transfer of a substantial volume of state rental housing into private ownership, the broader reform program of which privatization is a part must seek to integrate the remaining state-owned rentals with the nascent but expanding private rental market by raising rents and improving services; it must also protect the poorest renters from bearing the full burden of the rent increases. To accomplish these objectives six complementary policy actions have been called for as part of a comprehensive privatization and reform strategy:

⁸ Information provided by officials in both cities during the authors' visit in March 1992.

⁹ Renaud, 1991; Struyk and Telgarsky, 1992; Kingsley and Struyk, 1992.

1. Undertake a program of gradually raising rents to market levels. Doing this increases the value of owning the unit (and thus spurs sales) and at the same time generates the rental revenues necessary to improve maintenance and operations for units remaining as rentals.
2. Resolve questions of implicit property rights. Tenants now have such strong rights of occupancy that they are already quasi-owners. Moreover, the new owners are living in buildings without homeowners associations and thus have little control over their housing. The rights of tenants need to be reduced (particularly through introducing the real possibility of eviction for due cause) and legislation is necessary for creating viable condominium associations.
3. Housing finance must be available (at market rates) to help households purchase their units. Without such finance, many households who live in units that are large relative to the standards for free allocations will have difficulty purchasing their units.
4. Timely and accurate appraisal of the value of units proposed for sale must be available. Without such services, the privatization process will be delayed.
5. Housing allowances must be implemented to protect poor renters from having to spend an excessive share of their income for rental payments as rents are increased. Housing allowances are rent supplements paid only to low income families under which the size of the payment varies inversely with the family's income.
6. The efficiency and quality of management services in rental housing must be improved both to save money and to induce renters to be willing to pay the higher rents.

In terms of the broader objectives and policy actions just enumerated, the Russian law on privatization is extremely limited. True, it may be asking too much for the law on privatization to be so comprehensive; and, indeed, legislation and regulations addressing many of these other points was hoped for during the spring or summer of 1992. Still, such legislation had not been passed in the eleven months following the July 1991 privatization law (i.e., at the time of this writing).

Most obviously, the privatization law addresses only the transfer of housing to sitting tenants. It is silent on the future of rental housing and on the benefits for those on waiting lists, except to say that those on such lists will retain their standing on these lists.

In Table 2 we summarize the situation with respect to the six complementary policy actions as of May 1992. The table indicates limited action on clarification of property rights, a process for quickly establishing purchase prices (although these bear little relation to market values), and the

Table 3

**Estimated Value of the State-Owned Housing
in Selected Russian Cities, 1992**

	<u>Floor Space (million sq.m)</u>	<u>Value of Stock, Valued at</u>	
		<u>Rub 3,000/ sq.m^a</u>	<u>Rub 5,000/ sq.m^a</u>
Moscow			
municipal housing	115.6	346.8	578.0
departmental ^b	29.2	<u>87.6</u>	<u>146.0</u>
		434.4	724.0
St. Petersburg			
municipal housing	61.6	184.8	308.0
departmental	13.1	<u>39.3</u>	<u>65.5</u>
		224.1	373.5
Ekaterinburg			
municipal housing	7.4	22.2	37.0
departmental	11.6	<u>34.8</u>	<u>58.0</u>
		57.0	95.0
Novosibirsk			
municipal housing	9.4	28.2	47.0
departmental	7.2	<u>21.6</u>	<u>36.0</u>
TOTAL		764.5	1,275.5

a. Billions of rubles.

b. Includes units of state-owned enterprises.

Source: Goskonstat RSFSR, "Joint Report on the Dwelling Stock and Number of Occupants at the Eve of 190: Part 1. (Moscow: State Committee on Statistics, 1991).

granting of permission to local governments to increase rents.¹⁰ No action has been taken in other areas.

Privatization as a Stimulant to the Private Market. Clearly, the more rental units shifted to private ownership the greater the expected volume of subsequent unit sales, households relocating, units shifted to private rentals, etc. These types of transactions will stimulate further transactions and the overall movement of the sector toward a market basis. The question here is how large this shift is likely to be in the near-term.

The experience of some other countries gives room for optimism for quick privatization on a large scale. Both Slovenia and Lithuania privatized 80 percent of their state units in less than a year. On the other hand, Hungary has privatized about 20 percent of its stock over two years and Poland has accomplished much less over a similar time span. In all these cases, units were offered to tenants for purchase at very deep discounts. Other factors, including variations in expected increases in rents, the length of time the privatization process was to continue, appreciation in the housing stock, and alternative investment opportunities, may account for the differences observed among these countries.¹¹

On the side of stimulating sales, the Federation and local governments have certainly set prices so as to encourage sales. On the other hand, by leaving rents and tenant rights unchanged they did little to enhance the value of owning versus renting. Indeed, it would appear that it is only the sale of units at very high prices in the open market which has created an incentive to purchase.

Moreover, there are two important uncertainties which are discouraging tenants from buying. One is the future cost of housing maintenance. These services have been enormously subsidized in

¹⁰ This provision was (incongruously) contained in a budget law passed by the Supreme Soviet in mid-May.

¹¹ For a general discussion of the experience with privatization in Eastern Europe, see Kingsley and Struyk (1992). Information for Slovenia is in Mandic (1992); that for Lithuania is from an oral presentation by Bengt Turner at the Seminar on Eastern and Western Practices of Privatization Related to the Housing Sector, Budapest, March 1992.

the past, but analysts estimate that the total resources available were much below the amount required for quantity maintenance.¹² In the absence of comprehensive cost information, it is virtually impossible for would-be purchasers to know their expected future costs. It is essentially the case of a would-be purchaser of a condominium unit in the U.S. being asked to buy the unit with the monthly fees for operations only to be revealed to him in the future; few Americans would purchase under such conditions--and not surprisingly, Russians are similarly discomforted.

The other is the introduction of the tax on property. This tax is to be implemented in the fall of 1992 and the tax rate has been established at 0.1 percent of assessed value, according to the law "On Property Taxes for Legal Persons"; the method of assessment has been defined as the residual replacement value method, described above. While the population appears to be quite uncertain about the likely magnitude of the tax payments on their homes, simple calculations suggest that the tax bills will be quite small.

Equitable Treatment. Housing privatization potentially involves an enormous transfer of wealth from the state to individual households. Obviously a key question is how this wealth is being distributed among households.

Before addressing the equity question directly, it is worthwhile to have some understanding of the size of the potential wealth transfer involved. In Table 3 we have computed the value at the beginning of 1992 of the state housing stock in four of the largest Russian cities. Two assumptions about the value per square meter are employed: rub 3,000 and rub 5,000 (\$30 and \$50). In interviews in Moscow, Ekaterinburg, and Novosibirsk in March 1992, respondents reported that auction prices of rub 5,000 per square meter were standard in the latter two cities. In Moscow, auction prices were running at rub 20,000 to 80,000 per square meter; construction costs were in the

¹² International Monetary Fund (1991), p.324, states that available funding covers less than 40 percent of the estimated needed maintenance.

rub 10,000 to 15,000 range. Respondents in St. Petersburg reported values closer to those of Moscow. All of these prices are inflated, however, by the small volume of units on the market; and for this reason the rub 3,000 per square meter figure seems more realistic for Ekaterinburg and Novosibirsk and the higher figure for Moscow and St. Petersburg. In any event, these should be viewed as highly conservative estimates.

Using an overall figure of rub 5,000 per square meter, the housing stock in these four cities is valued at rub 1,276 billion (\$12.7 billion). By way of comparison, for the year 1991 Net Material Product in the Russian Federation was rub 810 billion (\$8.1 billion) (State Committee on Statistics, 1992). These figures can be interpreted alternatively: the average unit value (at rub 5,000 per square meter) is rub 270,000 or 6.4 annual incomes for a family with a monthly income of rub 3,500--the mean income level in first quarter of 1992 (State Committee on Statistics, 1992a, p.14). In short, the value of the assets being transferred is simply enormous.

There are several dimensions to the seemingly simple question about wealth distribution. One concerns the degree to which households living in different cities are being treated comparably in the privatization process. Another concerns the treatment of those purchasing versus those renters who elect not to purchase and those on waiting lists. Finally, one can inquire about the distribution of wealth among those who do purchase.

With respect to equity across cities, it appears that rough justice is being done. In the cities studied the great majority of those purchasing their units pay nothing for the asset. There are real differences among the 10 percent who do make payments; however, none of the payments approach market prices and those purchasing the largest units are typically the only ones paying a positive price.

In contrast, there are severe inequities between purchasers and those who remain renters and those on the waiting list. Purchasers receive large wealth transfers; the renters receive nothing, and

those on the waiting list are at risk of receiving little or no gain. One can think of the wealth transfers as a payment to the new owners for the implicit property rights they enjoyed as renters. If the implicit property rights of those who remain renters are gradually reduced in the future without any compensating payment--and this is the pattern which is beginning to develop in Eastern Europe¹³--then there will be severe inequity between sitting renters and purchasers. The inequity between purchasers and those on the waiting list is still greater. Purchasers receive both a unit to occupy and a wealth transfer. Those on the waiting list, i.e. those living in a unit with less than 5 square meters per person, are in a quite different position. They can receive their current without charge, and then, they can subsequently also privatize a larger unit when they are allocated it. On the other hand, they may not be allocated a new unit and exercise their purchase right while privatization is still an option.¹⁴ Subsequent legislation may attempt to deal with these inequities; but because of the extreme generosity of the transfers to those purchasing their units, it will be very difficult (expensive) for the state to come close to achieving real equity.

Finally, with respect to equal treatment among purchasers, it should be clear that there is little hope of equitable treatment. First, the distribution of units in Russia at the beginning of the privatization process was one in which higher income households occupied the better and larger units (Kosareva, 1992: 39). This pattern will not be materially changed by the terms of privatization because there are only modest adjustments in the price of the unit for location, quality, and other factors and because in general the sales price for space above the value of the implicit voucher is so far below the market level. Hence, those occupying the better units at the beginning of the privatization process will receive larger wealth transfers.

¹³ The rights of renters have already been sharply restricted through legislation in Bulgaria and somewhat attenuated by amendments to the Civil Code in Czechoslovakia. Housing reform legislation introduced in the Hungarian Parliament in April 1992 moves cautiously in the same direction.

¹⁴ At this time there is no time limit on privatization, although some draft legislation has introduced the idea. Privatization is time limited in Slovenia, Croatia, and some of the Baltic countries.

There is no information available yet for Russia on the distribution of capital gains among purchasers, particularly with respect to income. Hungary is the one country in Eastern Europe for which systematic data on this point has been collected. These data, which are only for rentals privatized in Budapest, show that for the units privatized in 1990 and 1991, 40 percent of the total capital gains associated with all privatized units accrued to purchasers in the highest income quartile, while only 16 percent accrued to those in the lowest income quartile. Moreover, the average per unit capital gain for those in the highest income quartile is 46 percent greater than for those in the lowest quartile.¹⁵ Consistent with this finding, knowledgeable observers in Moscow, Ekaterinburg and Novosibirsk reported their impression that the better units were being purchased at a much higher rate than other units.¹⁶

Our overall conclusion is fairly pessimistic. The Russian housing privatization program--as being implemented in the spring of 1992--is in genuine danger of failing to accomplish its major objective of transferring a substantial share of the stock to the population and thereby "shocking" the housing sector into operating more on market principles. Moreover, it may result in a distribution of housing assets (including implicit property rights) which is more inequitable than that existing before privatization began. Such a conclusion is, of course, highly speculative, since a variety of factors could suddenly encourage a massive wave of privatization. Leaving aside such a *deus ex machina*, the Government of the Russian Federation would be well advised to consider major adjustments to its program. Perhaps most important would be to begin increasing rents--which would raise the value of the unit--and to announce a time limit for making the privatization decision (perhaps 12-15 months), which would focus tenants' attention on this decision. As sales volume increases, it will

¹⁵ Hegedus, Mark and Tosics (1992), Table 3. Findings based on a survey conducted in January 1992 of 1,000 randomly selected units which were state rental in January 1990.

¹⁶ Interviews conducted by the authors in March 1992.

become increasingly imperative to address the various issues between those purchasing their units and those who do not.

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