

**REVIEW OF THE REAL ESTATE
LEGISLATION OF NOVGOROD
REGION
AND CITY**

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REVIEW OF THE REAL ESTATE LEGISLATION OF NOVGOROD REGION AND CITY

INTRODUCTION

This report is prepared as an initial element of the work under USAID's Partnership for Freedom (PFF) program, and provides a preliminary survey and analysis of the laws governing development of land and real estate markets in the Novgorod region. The primary purpose of this paper is to identify early in the project "impediments" to development of private real estate markets, and those areas of legal and regulatory reform on which the longer term work of the PFF project may focus.

While the report does not emphasize national law, it is practically impossible to discuss local legislative initiatives outside of that context. A premise of this report is therefore that work in the Novgorod region must be undertaken in the context of the national legal framework affecting real estate markets. This framework includes primarily the Civil Code as well as a series of laws enacted recently or nearing enactment to supplement or implement the provisions of the Civil Code. The Mortgage and Registration Laws are examples, as well as other public laws which may affect real estate markets, for example, the Laws of Privatization, Town Planning or Historic Preservation and the Land Code. These national laws may constrain the ability of the oblast to act on its own initiative, or, as suggested below, may provide perhaps the best impetus and opportunity to further develop the local laws.

This paper first identifies on an abstract basis the essential legal and regulatory framework for development of real estate markets in Russia, as formulated in the USAID program over the past 5 years. For each of those elements the report goes on to discuss the national legal context; the initiatives already taken by Novgorod oblast and city; and the opportunities which remain on which the PFF project may focus attention.

The following points should be noted:

- This report is a preliminary survey of the legal and regulatory framework for real estate markets in Novgorod, intended to provide a road map for a longer term work plan, and that the information and analysis provided in this paper will be developed in greater detail as a component of the PFF project.
- Novgorod region and city are separate legal entities. The regional administration is the subject of the Federation and holds the primary powers to enact legislation. The city presently operates under broad powers of home rule as expressed in a city charter, locally considered to be the most important city law. It is clear that most progress in reform is taking place within the city, apparently with the support of the regional administration. However, there are also some indications of policy differences and a sense that there is concern at the level of the regional administration that the city not get too far out ahead. A significant part of the regulatory reform agenda may be to extend some of the reform experiments of the city to the remainder of the region, an explicit objective of the PFF project.

- This report does not address the issue of agricultural land, which is addressed elsewhere, but the importance of these issues in Novgorod is apparent. Novgorod is primarily a rural and agricultural region, and the approach taken to agricultural land reform will likely have significant impact on its overall economic development, which is after all the primary focus of the PFF project. For example, agricultural land will sometimes be the focus of issues of highest and best use, particularly surrounding the larger cities. Perhaps more importantly, though, issues of privatization and ownership of agricultural land may have a direct impact on agricultural productivity, which in turn could lead to development of new products and expansion of agriculture-related industry. Appropriate focus should therefore be placed on agricultural land as an important part of the overall land market in the Novgorod oblast, and issues of privatization explored in detail.
- This report does not address issues of the existing residential stock as a component of the real estate market. These are largely issues of privatization, housing management, condominium formation and registration, and housing allowance, all of which the city and oblast appear to be dealing with adequately. Approximately 26 percent of the city's housing stock has been privatized; since the start of 1997, 2,000 residential units have been privatized. Recent city and oblast legislative initiatives include regulations governing: competitive bidding for housing stock repair and maintenance; formation and registration of condominiums; city relationships with condominium associations in partially privatized buildings; subsidies and privileges of condominium associations.
- USAID presently has several significant projects ongoing in Novgorod, including the ad valorem (mass appraisal) tax project, the zoning and land use project, and the land information system project. It is assumed that each of these projects will develop recommendations and working models of legislation and regulations needed for their implementation. Accordingly, this paper focuses primarily on initiatives which may be taken outside of these projects.

CONCLUSIONS

It is difficult to identify any particular local law or regulation as an "impediment" to real estate markets and investment in the Novgorod region. While the local laws are not perfect, the more serious shortcomings are in national law and policy, and it may be argued with substantial foundation that the City of Novgorod has made a genuine effort to enact local legislation to promote real estate markets within the constraints of federal law. Apparently the city is supported by the oblast to a significant extent, though the initiatives taken by the city have not necessarily found their way into the other towns and districts in the region. In effect, the city is operating under significant powers of home rule.

In several instances there has been so much recent legislative activity in the region that it is premature to say that "impediments" still exist; some experience with the new initiatives will be necessary first. A good example of this is the great deal of recent work on zoning rules and creation of a land use commission carried out under the USAID zoning project. Similarly, at this stage of the project there is insufficient empirical data on some aspects of the market to say whether existing legislation is working. For



example, before it is possible to say that the privatization laws are not working well it is necessary to have more information on market demand and the pace of real estate privatization. In the absence of such understanding any suggestions for reform would be purely formulistic.

Legal reform is only one component of market development. In the absence of effective economic demand for real estate products, the impact of legal reform may be marginal at best, particularly at this late date well into Russia's transition. Most commentary on the lack of private property rights in Russia today is highly exaggerated and not based on a detailed review of the entire corpus of civil legislation and actual practice. Moreover, what appears on a superficial level to be an "impediment" to the western observer may not be seen as such by the Russian investor.

These points are particularly true in Novgorod, where a genuine effort at reform is already in progress and many useful principles have been enacted into law. At best, further legal reform may further reduce transaction costs and legal risks, thereby increasing the range of feasible real estate transactions. This is not to say that legal reform should not be pursued wherever helpful, but it is not a substitute for other market-creating factors such as good market analysis; good marketing of economic development opportunities in the city and oblast; and entrepreneurial leadership.

Adjusting the fine points of the many local laws and regulations can perhaps have beneficial results, but the better opportunities may lie in taking advantage of the recently enacted or pending federal laws affecting real estate markets to further develop and refine the local legislation and practice. This is particularly true with respect to land privatization (RF Land Code, now pending), land registration (RF Law On Registration of Real Estate Rights and Transactions), and land use (RF Town Planning Codex). Focusing on these three areas, for example, will make best use of prior USAID program aid and assure that the Novgorod region adapts quickly and with minimum disruption to the new legal rules and relationships which will be mandated by these new federal laws.

ESSENTIAL ELEMENTS OF THE LEGAL FRAMEWORK

Over the past 5 years the USAID program in Russia has developed a simple legal framework for creation of real estate markets. The core elements of the framework are:

- Rights of Tenure
- Privatization
- Contracts
- Conveyance
- Mortgage
- Lease
- Brokerage
- Identification and Protection of Legal Rights to Real Estate (Registration)
- Land Use
- Permitted Uses
- Construction
- Subdivision
- Preservation
- Environmental Protection
- Costs of Owning, Developing and Using Land
- Taxation
- Fees and permits
- Infrastructure and exactions

There are of course other laws which contribute to the development of real estate markets. For example, laws of mortgage presume laws on banking and lending contracts. The existence of these fundamental laws is taken as a given.

In most cases it is not necessary that the law be highly refined. It may be expected that the laws will be defined further over time as markets develop and experience is gained. However, to induce development of markets in each case it is necessary that the laws or regulations provide a minimum level of transparency and predictability.

TENURE

Tenure refers to the terms and conditions of possession, use and disposal of real property, and defines the content of rights of ownership, lease, easement or servitude and the surviving Socialist civil law conventions of permanent use and lifetime inheritable possession. For each of these forms of possession it is necessary to define how they are created, the “bundle” of rights associated with them, and how they are transferred or terminated.

Rights of tenure were defined and largely settled in the Civil Code of 1994, with the exception of land rights established in Chapter 17 of that law and which are held hostage to enactment of a Russian Federation



Land Code. The new Land Code, awaiting the President's signature when this report was prepared, defines the permitted rights to land and the contents of those rights, and does not differ in material respects from the Civil Code. If the Land Code is adopted, under Russian law at this time the standard forms of tenure to both land and real property—including ownership, lease and servitude—will be available and will not differ significantly from their counterparts in other civil law jurisdictions. In any event, the differences will be too minor to require belaboring here. The main distinction will be with respect to agricultural land, which under the pending Land Code would be subjected to a restricted legal regime. For example, it could not be mortgaged.

If the pending Land Code is enacted, it is possible that if Novgorod wished to simply rely on the Civil Code and Land Code there is little it would need to do (indeed, could do) to further define tenurial rights to land and real property; this is a matter of Russian Federation law and it has been adequately done. However, the pending Land Code contains the unusual provision that each subject of the Federation is entitled to decide on which forms of land tenure sanctioned in the land and Civil Codes it will permit. Aside from displaying a naive understanding of the strength of markets (imagine two adjoining oblasts, one of which allows land ownership and one which does not), if finally adopted this law may require the region to take some affirmative step to adopt the rights provided in the Civil and Land Codes, or some restricted set of those rights. Accordingly, it may become necessary to develop local land code or equivalent law to implement the provisions of the Land Code.

If the pending Land Code is enacted, it may also be necessary to closely review its provisions and determine its effects on Novgorod's present practices and procedures. Adjustments may need to be made to regional laws and regulations to conform to the provisions of the federal law. A main objective of the PFF project in this sphere would be to provide assistance to draft a local law which confirms the broadest range of rights to real estate available under the Civil and Land Codes.

If the pending Land Code is not finally adopted, Novgorod is in the same position as the rest of the Federation in that the land tenure provisions of the Civil Code, Chapter 17, remain ineffective until enactment of a Land Code. What this means in practice is that the determination of land rights will depend upon the now largely ineffective 1991 Land Code and the Presidential Decrees issued since that time, the most recent being Decree No. 485 (May 16, 1997), which apparently expands present rights somewhat by mandating that local administrations transfer ownership of an appropriate amount of land any time they sell a building or structure.

In the absence of the Land Code, a summary of present rights to urban land and real property are as follows:

- The bundle of rights associated with the different forms of land tenure are well defined in the Civil Code, but are ineffective until enactment of the Land Code. Forms of tenure of real estate objects, including buildings and parts of buildings, are well defined. Ownership of a real estate object is permitted, available to all natural and legal persons, and carries with it at least the right to use the underlying land, and now probably ownership.
- Ownership of land plots is presently limited by the type of owner and the use to which the land is put. If the owner or the use does not fall into the designated categories, the possessor is limited to lease or right of use. Ownership is permitted in the following cases:
 - Land obtained by natural persons for personal use, including home-building and gardening.
 - Land under privatized buildings or structures, generally.
 - Land privatized by privatizing enterprises or other entrepreneurial entities.
 - Land held in common ownership by members of condominium associations (though the pending Land Code would revoke this right and limit tenure of condominium members to lease or permanent use, for what reason we do not know).
 - Land acquired from someone who holds ownership, such as a privatized enterprise or an agricultural organization that has managed to have a portion of its land reclassified as non-agricultural.
- Rights of lease of real estate are well defined in the Civil Code and apply to land and structures.
- Rights of servitude in practice are used every day, but have their legal basis only in several vague presidential decrees on privatization; the Civil Code provisions on servitude, which are adequate, are contained in the Chapter 17 which is suspended pending enactment of the Land Code. (The provisions on servitudes and real covenants of the pending Land Code are far more extensive than the Civil code and an improvement.

Aside from the limitations on agricultural land, it seems then that the only land right effectively prohibited under Russian law at this time is the right to own raw land for commercial uses, and even that prohibition can be overcome by buying the land from an enterprise that privatized it. This is in keeping with the general fear of “speculative” activity with land, the last bastion of state monopoly.

Despite its limitations, the pending Land Code would help to clarify and settle urban land tenure rights. If the pending Land Code is not enacted, and the provisions of Chapter 17 of the Civil Code remain ineffective, land relationships will still be subject to a host of duplicative and often ambiguous decrees and laws. In fact, if the Land Code is rejected yet again, and this situation promises to continue indefinitely, it may

be useful for the project to pioneer a regional land code which brings some clarity and consistency to the land law within the constraints of Federal law—perhaps even to stretch the envelope by taking advantage of the absence of conflicting federal law at this time. Some other regions, most notably St. Petersburg, are contemplating such action.

PRIVATIZATION AND ALLOCATION OF STATE-OWNED REAL ESTATE

Privatization is the process of moving real estate from state to private hands. Laws of privatization are distinguished from laws of property rights in that they establish processes and not the content of property rights, though it sometimes occurs that the law of privatization will place restrictions on the property rights which may be granted.

There are two types of privatization in Russia. The first pertains to the process of granting ownership of real estate to those who presently occupy and use it under some other beneficial right from the state—use, inheritable possession or lease. Most current laws of “privatization” refer to this process. The second means of privatization is to simply make unoccupied land or real estate available to the public generally on the basis of some form of private tenure. For the sake of clarity, this latter process, carried out today through negotiation, auction and other competitive tenders, is usually referred to as “allocation” of state-owned real estate.

Though land issues are theoretically under the joint jurisdiction of the Federation and the oblasts, in reality privatization and allocation of state-owned land and real estate is subject to federal laws or decrees on housing privatization; privatization and allocation of land plots for individual use; and privatization of land and other real estate occupied by state owned enterprises and other privatized businesses. At the time this report was prepared, a new Land Code had been enacted by substantial margins in both the State Duma and Federation Council and sent to the President for signature. If signed, or enacted over a presidential veto, that law contains significant provisions on both the privatization and allocation of land plots. Though local administrations carry out privatization, and in that sense can either enhance or hinder its success, they are not free to contradict the fundamental rules and procedures established in federal law.

Today, under federal law, and assuming that the new Land Code will be enacted, most land, buildings and commercial spaces in buildings, including historic buildings can be legally transferred from state to private hands, if not in ownership, then by lease. Novgorod has been for several years in the forefront of legislative reform among Russian cities, partly as a result of its participation in the World Bank Housing Project, which required early development of procedures for disposing of unoccupied municipal land through auction and tender. Since that time the city (and where noted, the oblast) has enacted various laws dealing with the privatization or allocation of state-owned real estate, including the following:

- **Regulations “On Auction Sale of Municipally Owned Commercial Objects of Privatization” approved by the Chairman of Novgorod Property Management Committee as of 01/28/94.**

- **Resolution of the City Administration No. 118, On approval of the regulations on the Procedure of Conducting Open and Competitive Bidding for Obtaining the Rights to Develop Land Plots in Novgorod, 7/25/94.** This is the city's earliest general regulation on auctions and competitive tenders of city owned land. The regulation anticipates that land will be offered under a "right of development," not outright sale, through competitive bidding. In its details, the regulation is essentially the same model as used in many other Russian localities and which appears to be based loosely on a proposed land auction regulation prepared by Roskomzem (the federal land committee in charge of legislation) several years ago. However, unlike the regulations in the other cities, the Novgorod regulation appears to authorize only "open bidding" procedures, that is, bidding by voice in a room in which all bidders are present. Accordingly, there is no requirement or possibility that the identity of bidders can be held confidential prior to announcing the results of the competition.
- **Novgorod Oblast Law On Procedures of Allocating and Withdrawal of Land Plots in Novgorod Region, 06/28/95, as amended 07/01/96 and 07/29/96.** Since the beginning of 1997, rights have been issued for approximately 4,700 personal land plots. Since 1995 there have been approximately 45 land plots and/or buildings privatized by enterprises under Presidential Decree 1535 and the enterprise land sales initiative. This oblast regulation, amended through July, 1996 to reflect the changes in enterprise privatization rules, provides general rules for privatizing and allocating land for all permitted purposes. It incorporates and synthesizes the main provisions of the various Presidential Decrees affecting land allocation and privatization, as well as the remaining valid provisions of the 1991 Land Code. The regulation could be improved by a more comprehensive restatement and updating, but it is otherwise as adequate a land regulation as one might find in Russia today.
- **Resolution of Novgorod Oblast Property Fund No. 50, Procedures for Appraising and Selling Real Property, 5/24/97.** This regulation governs sale of oblast real estate through public sale, including the method for setting prices through appraisal. It follows the standard widespread format of the proposed but never enacted federal regulations, which have been adopted in all six cities participating in the World Bank's Housing Project, perhaps with some modifications. The regulation follows the auction and tender provisions of the RF Civil Code, to which it is arguably subject (though there is opinion otherwise). The regulations could be made more flexible—for example, by eliminating some of the very short time periods for action.
- **Regulation No. 27, On Procedure of Lease Out (Rent) of Novgorod Municipal Property, approved by Novgorod City Duma as of 12/19/96.** This is a concise description of the rules and procedures of leasing municipal real estate. It allows negotiated deals, open competitions and leases under a condition of carrying out capital repairs to the space. If the regulation has any serious flaw, it is in adhering to the restrictions on profiles, assignability, mortgageability and space improvement that were the hallmark of the early years of privatization. The regulation perhaps could be improved by (1) attempting to create a free secondary market in municipal leases, and (2) working with concepts of market rental rates, purchase options and other incentives for achieving highest and best use and inducing further privatization, as discussed further below.



- **Regulation No. 19, Standard Rental Rates for the Lease of Municipal Non-Residential Buildings, Structures, Premises and Public Property Declared in Established Order as Monuments of History and Architecture, approved by Novgorod City Duma as of 11/22/96.** This regulation establishes the basic normative rental rates for city-owned real estate, distinguishing among various types of nonprofit and profit making users.
- **Regulation No. 288, On Procedures of Sale to Owners of Privatized Enterprises, Buildings, Constructions, Structures and Other Objects of Non-Residential Stock of Land Plots under Them, approved by Novgorod City Administration Resolution as of 06/28/96.** Since 1995, 43 land plots and 10 other real estate objects have been privatized by enterprises, with most privatization occurring in 1995-96. This regulation implements Presidential Decree 1535 and does not depart from federal rules.
- **City Duma Regulation No. 103, On Procedures of Open Commercial Competitions for the Right to Lease Out Commercial Municipal Property, 4/17/97.** The city has approximately 700 leases of city-owned property, primarily retail spaces, outstanding. This regulation provides the procedures for holding auctions and tenders of lease rights, thereby supplementing Regulation No. 27, above. The regulation supplements Regulation 19, on normative rental rates, by establishing coefficients for rent increases for leased properties located in the historic center, or which are served by high quality engineering and transportation infrastructure (an interesting form of infrastructure exaction).

An important point to note is that the city does not presently allow privatization to ownership within the historic center, which comprises a relatively large and valuable area of the city. Accordingly, the rules on leasing, and creation of an active market in leases, become important.

The local laws and regulations on privatization of real estate, while typical of most Russian localities, are reflections of federal law and regulation. While they cannot be characterized as “impediments” to real estate markets, they are essentially dated, and do not necessarily reflect the best practices available to the city. For example, leases of city owned property are still subject to profile restrictions, prohibitions on mortgage, assignment and sublease (without the approval of the city), and close supervision of capital improvements.

The allocation procedures are still subject to the 1991 land code, but these procedures are so broad that it is difficult to say where they constitute an “impediment” to privatization. Much will depend upon interpretation and implementation. The auction and tender regulations related to allocation are typical of such regulations in the cities. They are not the most flexible procedures that one could design (for example, auctions at which only one bidder is present must be canceled, without discretion, even if there is an acceptable starting price). However, it must be noted that some of these provisions are subject to federal law and regulation, including the Civil Code, and cities may not have compete discretion to design their own procedures. Nevertheless, some improvements to procedures can probably be made.

Real estate privatization rules and procedures are largely governed by federal law and regulation. This is particularly true, for example, with respect to enterprise land privatization. Admittedly, these regulations are somewhat broad in certain issues, and it is perhaps possible for local governments to make improvements through administrative practice. Accordingly, it is not possible simply on the face of the law to determine whether the laws themselves constitute impediments to privatization until some further research is done into the city's implementation of the laws during the PFF project.

A suggested program in this sphere of regulatory reform might include the following:

- There are apparently over 800 city-owned commercial spaces subject to lease. Without more data, it is not possible to determine whether the city has aggressively pursued small-scale privatization of retail and other commercial spaces. An empirical analysis of this situation will perhaps reveal whether privatization of city space can be considered effective. We would need to look at the terms of leases, and the market for ownership rather than lease. If the market for ownership exists, it will be necessary to discuss with the city why ownership rather than municipal lease has not proceeded appropriately. With respect to city leases themselves, assuming they will exist for some time, an effort could be made to improve municipal leasing to approximate the benefits of ownership and a true market. This might require various legislative or regulatory initiatives, for example to remove profile and assignability restrictions.
- A review of the results of actual recent auction procedures might reveal practices which are causing problems, and which might be corrected by minor regulatory changes. A close review of the present procedures against the constraints of the applicable federal laws and regulations might reveal areas in which the city might develop better procedures for auctions and tenders.
- Conspicuously absent from the real estate markets has been allocation of land parcels on a non-targeted basis—that is, allocation of land subject only to general planning and zoning rules and absent restrictions on resale. It might be useful to ask the city to experiment with a speculative real estate market by making a certain amount of land available to the highest bidders with no restriction on time of development or resale. This experiment would track the use made of the land over time and perhaps provide better insight into local land dynamics. At best it might allay fears of “speculation” and lead to more unrestricted land auctions. The legal basis for unrestricted land sales might require some research and development.
- The city might be induced to experiment with other means of making property available to the private sector, including master leases or management incentive contracts for large blocks of retail or commercial space. The city might also be induced to turn over the marketing of space to private brokerage companies.
- A large part of the privatization effort is marketing. The city has demonstrated interest and skill in marketing development opportunities thus far. Further work might be attempted on the institutional front to develop a true municipal economic development or urban renewal agency with powers to package and market land development opportunities, together with all necessary land use approvals. The outline of such a municipal agency and the type of legislation needed

is provided in Section IX. B. of S. Butler, *Infrastructure Exactions on Development of Real Estate in the Russian Federation: Implication of International Experience for Russian markets*, June 1996, prepared for USAID.

CONTRACTS

As with rights of tenure, the Civil Code provides all of the necessary legal basis for transactions with real estate, including the legal basis for contracts of conveyance of rights; construction contracts; credit and mortgage contracts; contracts of lease; and agency relationships such as brokerage and power of attorney. There are numerous ambiguities in the laws, and they do not necessarily provide the flexibility and range of action found in more developed market economies (See, e.g., S. Butler, *Remaining Issues Affecting Mortgage Lending for Commercial Real Estate in the Russian Federation*, August 27, 1996). Nevertheless, it is safe to say that at an abstract level most basic real estate transactions can be accomplished under existing Russian law, subject to the risk that court intervention may place interpretations on the laws which cannot be anticipated now.

Basic law of contract is provided by federal law, and there is little in the way of law or regulation that can or needs to be done at the local level. However, at a practical level it may be useful to review with the region and the city the forms of contracts they are using in the privatization and allocation processes, most particularly leases, contracts of conveyance, and development agreements, and determine if improvements may be made. Typically, in most Russian cities today it is possible to improve the legal rights provided to investors under the contracts. This work was begun in Novgorod by USAID supported teams under the World Bank Housing Project, which developed basic land lease forms, but can perhaps be reviewed and updated in light of more recent developments in law and practice.

IDENTIFICATION AND PROTECTION OF LEGAL RIGHTS TO REAL ESTATE (REGISTRATION)

Up to the recent enactment of the federal law on registration of real estate rights and transactions the city of Novgorod was a leader in implementing an effective registration system. The system is in place today and appears to be working well, providing not only registration and privatization services but also much needed consultation service to the general public in their private real estate transactions. The present local laws governing registration of real estate rights are:

- **Regulation No. 2279 of the City Administration, On Assigning Cadastre Numbers to Land Plots and Inventory Numbers to Real Estate Objects on the Territory of Novgorod City, and On Keeping a Log-Book for Recording Land Plots' Cadastre Numbers and Inventory Numbers of Real Estate Objects, 12/16/94.** The Provision on Assignment of Cadastral Numbers is based upon Presidential Decree No. 2130 as well as the work and instructions of the Russian Federation Land Committee on creating a national cadastre. The regulation provides a format for assigning unique cadastre numbers to each land plot, structure or building ("real estate object") and portion of a structure or building which is held in separate ownership or use

(apartments, etc.). Land plots are assigned a cadastre number, while structures and their parts are assigned inventory numbers.

The scheme provides for a district (“cadastral body”), block (“cadastral block”) and lot (“sub-block”) system. The regulation provides rules for assigning new cadastre numbers when land plots are subdivided or merged. The official records of land cadastre numbers are to be kept in paper and electronic form by the city Land Committee in accordance with forms of data tables attached to the regulation. Official records of the inventory numbers of structures and parts of structures are to be kept separately, also in accordance with prescribed forms, by the “Municipal Enterprise: Housing Inventory Department.”

- **Resolution No. 20 of the City Administration, Provisional Procedures for Registration of Real Estate Rights of Citizens and Legal Entities on the Territory of Novgorod, 02/09/95, as amended by Resolution No. 98 of the City Administration, 05/05/96, and restated by Resolution No. 29 of the City Duma, 12/19/96.** This is the basic regulation for registration, based upon the Butler/Eckert draft prepared in connection with the World Bank Housing Project. The regulation purports to establish temporary rules, as under the Civil Code it was specified that the actual law on registration was to be a federal law. While serviceable, the regulation is now superseded by the national law on registration of rights and transactions.
- **Regulations On the Department for Work With Real Estate.** This regulation establishes the Department of Real Estate, a division of the Municipal Property Committee, as the coordinating body for real property privatization transactions and registration of real estate rights. As those who are familiar with the operations of the department know, it assembles in a single department representatives of various municipal departments which are authorized by law to deal with real estate and registration, and imposes a high degree of coordination on the them, effectively making them operate as a single unit.

The real estate department is a centralized office which accepts and coordinates processing of all applications for privatization of real estate (including apartments), rental of city owned retail space, and land plots for development. The department is responsible for investigating the particulars of the application through inquiries to other departments; negotiating the transaction, if necessary; and providing the existing departments with the completed applications for formal approval. The existing departments are required to adopt the completed applications “without additional visas or registration,” meaning that they cannot impose application and registration requirements beyond those imposed by the real estate department. Upon completion of the transaction the department is responsible for registration of the rights conveyed.

Theoretically, the Land Committee and the Property Committee/BTI (Bureau of Technical Inventory) each continue to have independent responsibility for registration of rights to land and structures, respectively. And, only the representative of each agency sitting in the real estate department has the authority to enter changes to the registry which affect the type of real estate for which they are responsible. As a practical matter, the real estate department functions as a single office which uses a single computer network for registration of all types of real estate.

- **Resolution No. 52 of City Duma, Provisional Procedures for Condominium Registration, 01/23/97 (not reviewed).**

The major challenge for the PFF project may be to adapt the present registration system in Novgorod to the new federal law. This may require enactment of a new regional law on registration, as well as various ancillary regulations, to enable and implement the national system. This would have the benefit of bringing into the system the small towns and suburban areas throughout the oblast which have not benefited from the City of Novgorod's management initiatives in the area of registration. It is possible that there are conflicts between the federal law and the present practices of Novgorod which will have to be worked out in practice. Moreover, there are indications that the pending Land Code may undermine both the Civil Code and the new federal law on regulation by establishing a separate registry for land rights—that is, perpetuation of the dual system of real estate registration which the present Novgorod system of registration was designed to circumvent through management practices.

In short, enactment of the new registration requires a close review of local laws to determine compliance, but also provides the opportunity to update and improve the local legislation and expand its benefits to the remainder of the oblast through appropriate regional laws and regulations which are adapted to the new federal law.

A second issue which may be pursued in the Novgorod region is the issue of systematic adjudication and registration of land rights as called for under Regulation 105 of the Russian /Federation Government. Novgorod presently follows a sporadic approach to registration which relies on applications from owners as and when privatization is made or secondary transactions occur. A more systematic approach might be taken to identification and registration of land rights, as suggested under Regulation 105. This would entail a systematic demarcation of land boundaries in designated areas; identification and adjudication of land rights, such as rights of use, and third party rights, such as servitudes; and registration of such rights. This procedure would require that a local law and procedure for systematic adjudication of rights be adopted.

LAND USE

The right to use land for personal or entrepreneurial purposes is an essential attribute of possession, and the broader the possible uses of land and minimal interference by the state in determining those uses arguably results in improved private markets for real estate. A fundamental principle of USAID's approach to land reform in Russian has been to decrease the role of the state in determining permitted land uses, thereby spurring private market decisions and lower transaction costs.

The Russian Federation Town Planning Law was recently adopted by the Duma, and it will be necessary to assess the impact of that law on local land use control. Prior to enactment of the national law, the City of Novgorod has been in the forefront of experiments in reforming laws of land use, particularly in the case of its recent enactment of the city's regulations on land use and development, prepared under the auspices of the USAID zoning project. In addition, the city has taken steps to establish a city-wide "town-planning" cadastre, which can be described as a multi-level geographic information system and planning tool,

incorporating graphic and textual material on a wide variety of land use issues and intended to be made available for use by private landowners and users in planning their real estate acquisition and development strategies.

The most significant local laws dealing with rights of land use are:

- Regulation No. 61 of the City Administration, Provisional Regulations on the City Administration Committee for Architecture and Town Planning, 03/25/96.
- Regulation No. 156 of the City Administration, Law Enforcement Procedure for Public Control over Construction and Land Preservation, 06/20/96.
- Regulation No. 177 of the City Administration, Provisional Regulations of Town Planning Activities on the Territory of Novgorod, 07/26/96.
- Resolution No. 2627 of the City Administration, On Creation and Keeping of Town Planning Cadastre of the City of Novgorod, 08/13/96.
- Regulation No. 249 of the City Administration, Regulations on the Town Planning Cadastre Office of the City of Novgorod, 10/29/96.
- Resolution No. 36 of the Novgorod City Duma, Rules of Land Use and Development, 12/19/96.
- Resolution No. 228 of Novgorod City Administration, On Formation of Land Use and Development Commission of the City of Novgorod, 01/21/97.
- Resolution No. 29 of Novgorod City Administration, Regulations on Architecture and Town Planning Council of Novgorod Committee for Architecture and Town Planning, 03/19/97.



- Resolution No. 46 of Novgorod City Administration, Provisional Regulations On Novgorod Commission for Land Use and Development, 04/15/97.
- Resolution of Novgorod City Administration, On Provisional Rules of Activity of Novgorod Commission for Land Use and Development, 04/30/97.

Most of the activity in this sphere has been very recent, particularly relating to the work of the USAID zoning project. The local regulation on land use development rules produced under the auspices of that project is a significant piece of work which departs significantly from past Russian land use practice. Until there is further elaboration and experience with that law, it is not possible to say whether any “impediments” to real estate markets exist in this sphere of activity.

Considering the relatively advanced stage of these laws in the city of Novgorod, and the good faith efforts being made by the city, the legislative program of the PFF in this sphere may be simply to follow through on the zoning project objectives. The regulation on rules of land use and development is clearly an incomplete document, needing further elaboration, for example, in the areas of historic preservation, environmental protection, land subdivision and the procedures of public hearings. Until that is done any comments on land use is premature. The local regulation now simply refers to the existing SNips (federal land use and construction regulations) in several of these areas, including subdivision and processing of building permits. If not already done in the context of the zoning project, further work may be to review in detail the content of the applicable SNips to see whether appropriate changes and adjustments might be made to further improve local land use regulations. This may particularly be true with respect to standard procedures for applying for, processing and issuing construction permits, which have been the subject of complaint throughout Russia as being overly complex and costly.

It is noteworthy that all of the recent laws and regulations listed above pertain to the city. The oblast has not yet applied these initiatives to the small towns and districts. It is perhaps possible that lack of such laws constitutes an impediment to regional development, but an answer to this question would depend upon a better understanding of the real estate market outside of the city; planning and zoning laws may be the least of the problems.

The work done under the auspices of the zoning project is not necessarily applicable outside of large urban settings. The PFF project acknowledges this when it seeks to adapt the work to fit the needs of those areas. Except in the largest towns, it is likely that the direction of such work will be toward concepts of regional planning and regional planning entities which may be more appropriate for non-urban areas. These types of laws take somewhat different approaches than reflected in the work of the zoning project. Exploring such laws with the oblast could be a useful exercise resulting in appropriate legislation for non-urban areas.

It is likely that during the term of the PFF project there will also be finally adopted the new national laws on preservation of historic and cultural monuments and on town planning. These acts are pending as of the time this report was prepared, and any further work on this type of legislation the Novgorod region will have to take the provisions of the new laws into account. Assistance may therefore be provided in review and coordination of local legislation with federal directives.

COSTS OF OWNING, USING AND DEVELOPING REAL ESTATE

The costs of owning and developing real estate can include taxes and rents, fees for permits, and fees for infrastructure connections and exactions. The costs of developing real estate can also include the time and transaction costs of obtaining development permits. The theory has been that interest in owning and developing real estate will decline if the costs can not be predicted with accuracy. (See, e.g., S. Butler et al., *Land for Housing: Urban Land Privatization Demonstration Project—Final Report*, Urban Institute, January 1996; S. Butler, *Infrastructure Exactions on Development of Real Estate in the Russian Federation: Implication of International Experience for Russian Markets*, Urban Institute, June 1996). The theory arguably has been borne out through extensive discussions with investors.

It should be noted that in Russia all basic tax policy is set by federal law, which gives to localities the discretion to enact certain local taxes. Moreover, as to the major taxes such as the profits tax, the tax proceeds are divided by formula among the federal and local governments. Accordingly, local governments are limited to manipulating only those local taxes over which it has complete discretion, or those portions of other taxes which accrue to the local budget. For example, the locality may offer privileges and exemptions only with regard to the portion of the profits or property taxes which belong to the local government.

The basic laws governing taxation in the Novgorod region and city are as follows:

- **Resolution No. 19 of Novgorod City Duma, Standard Rental Rates for 1997 for the Lease of Municipal Non-Residential Buildings, Structures, Premises and Public Property Declared in Established Order as Monuments of History and Architecture, 11/22/96.** This law provides the normative rental rates for 1997 for lease of city owned commercial property.
- **Novgorod City Duma Resolution No. 20, On Fixing Standard Amount of 1997 Land Rental in the City of Novgorod, 11/22/96.** The basic principles of setting land rents are determined under federal law. This local law is the implementing act which sets actual 1997 land rental rates in accordance with federal directives.
- **Novgorod City Duma Resolution No. 46, On Approval of Resolutions on Local Taxes and Fees Levied on the Territory of Novgorod, with Attachments, 01/05/97.** This is the local tax code, describing the rates and exemptions for taxes which are considered to be local under federal law, including the housing maintenance (“turnover”) tax; advertisement tax; motor vehicle sales tax; and business licensing tax.
- **Novgorod Region Law No. 78-03, On 1997 Tax Privileges to Organizations Located in Novgorod Region, 1/27/97.** This oblast law is a wide ranging list of exemptions and privileges for the regional portion of the profits and property taxes. It is the enabling law for the local “investment tax credit,” described further below, and establishes other privileges against local taxes to encourage restoration and maintenance of historical structures.

- **Oblast Duma Resolution No. 500, Procedures for Computing Break-even Point of Investments, Estimated Period of Recoupment and Determining Other Specific Features for Granting Privileges to Organizations Involved in Implementation of Investment Projects in Novgorod Region, 01/29/97.** This Resolution establishes the formula for calculating the “investment tax credit” against the local portion of the profits tax. Essentially, investors who invest in production facilities are permitted to recapture their investment before local tax liability begins to accrue.
- **Novgorod City Duma Resolution No. 100, On Procedure of Granting Tax, Fee and Rent Privileges to Citizens, Enterprises and Organizations in the City of Novgorod for 1997, 04/17/97.** This city regulation provides the exemptions to local taxes for various institutions and investors, described further below.

With respect to development exactions and charges for utility connections, the city and region apparently have not developed a comprehensive policy at this time which is expressed in law or regulation, though further research on this issue will be necessary during the course of the PFF project. Exactions are charged in the form of utility connection fees, which are still largely under the control of the individual utility companies. In addition, premiums are added on to rental rates under municipal leases for commercial facilities which enjoy high levels of engineering and transportation infrastructure. While in the past, as in most Russian cities, the connection fees were largely determined after the project was approved and the developer was committed, in the World Bank Housing Project land auctions, the city made an effort to identify the full charges for the project prior to the land auctions.

A key issue here is that in Russia today the rents charged for use of land and other municipal property, such as rent of a commercial store space, are largely normative, and not based upon market evaluation. In fact, under Russian law land rents and land taxes are virtually interchangeable, and only one will be imposed, depending upon whether the land is owned or leased. Similarly, rents for commercial spaces and buildings are set normatively by the Mayor at low levels. In fact, the opportunity to lease is paid for at the start in a lump sum, and these rent are also viewed as taxes, not rents for use of the space.

A problem with rents is that they are variable, like taxes. The normative level of rents is set annually by resolution of the administration, and not by lease contract. Accordingly, there are no assurances of rent levels. Thus far, since rents are treated as taxes, the rents have been held within reasonable ranges, but there is no assurance that this will continue.

There have been two recent and impressive aspects of local tax policy: the experiment with an ad valorem real property tax system under the auspices of the USAID program, and the use of tax incentives to attract investment, including investment in land and real estate.

The ad valorem tax system, on an experimental basis, holds out the possibility of encouraging greater privatization, as it will allow taxes to be based on a relatively predictable and market-based formula system. Accordingly, lease “rents” will become less essential. In addition, development of the ad valorem mass

appraisal system could rationalize the tax system and may contribute to achieving highest and best use market decisions.

The initiatives of the city and oblast in establishing tax incentives for development include the following:

- An investment tax credit against the local portion of the enterprise profits tax for investors who invest in construction of new production facilities. The tax credit is based upon a “first-out” formula developed with the assistance of USAID and Arthur Anderson & Co., which permits the investor to recoup his investment before local profits tax liability arises.
- A profits tax deduction for businesses and individuals which engage in restoration of historic buildings, to the extent of the charitable contributions they raise for such purposes.
- A profits tax deduction for maintenance and restoration expenses of historical and architectural monuments.
- Profits tax deductions for development of hotels and other tourist facilities.
- A city property tax exemption for condominium associations, and tourist facilities.
- Exemption from the city “educational tax” (3 percent of annual total wages based on normative minimum wage) for housing construction cooperatives and condominiums.
- Land tax and rent exemptions for low income citizens who construct a home on their own plot.

The city appears to be making a genuine effort to manipulate the tax system, within the constraints of federal law, to induce certain types of real estate investment. Opinion varies widely on the use of tax incentives. In the absence of empirical analysis, it is difficult to say whether the various tax incentives with which the city is experimenting are or can be effective, and, therefore, whether any changes are required to law or regulation. Thus, in this case, suggestions for legislative or regulatory reform must be closely coordinated with a review of the economics of the laws that exist. A suggested program at this time might include the following:

- Proceed with the mass appraisal tax experiment. Presumably, as a result of that work an appropriate local law or regulation will be developed by the persons performing that work, perhaps in coordination with other legislative reform on the PFF project.
- As noted above, there should be a concerted effort to accelerate privatization of city owned retail and office properties, an effort that may be encouraged by implementation of the ad valorem tax system. Pending that, it would be useful to explore the possibility of setting rents on municipal property on a market, and not normative, basis. Efforts should be made to lock in rents on some business basis, so that they are predictable and not subject to annual adjustment. This might



- require a re-thinking of the concept of rents on municipal property, which would need to be reflected in appropriate revisions to current procedures.
- It is impossible to say on the face of laws whether the tax program of the city is effective or counterproductive. This is matter for economic analysis. Only after that is done will it be possible to say whether revisions to the local tax laws and procedures are required.
 - With respect to other development fees and charges (exactions), including utility connection charges, more research into local regulations and procedures is necessary during the course of the project. In many cases such charges constitute a main impediment to inducing real estate activity, though there is no evidence for that in Novgorod at this time. Nevertheless, it would be useful to review further the local laws and regulations and determine whether the policy recommendations for regulatory reform in this areas set out in Section IX. B. of *S. Butler, Infrastructure Exactions on Development of Real Estate in the Russian Federation: Implication of International Experience for Russian Markets*, Urban Institute, June 1996, prepared for USAID, would be helpful. Local regulatory actions suggested in that paper included, for example, regulations on setting infrastructure or development exactions; authorization of infrastructure taxing districts; and local regulation of utility connection charges.