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PROPERTY RIGHTS
AND LAND POLICIES

Edited by Gregory K. Ingram and Yu-Hung Hong

Property Rights and Land Policies

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Gregory K. Ingram and Yu-Hung Hong

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Property Rights and Real Estate Privatization in Russia: A Work in Progress

Bertrand Renaud, Joseph K. Eckert, and
R. Jerome Anderson

Why Is Russia So Different? _____

The institutional response in Russia to the collapse of the Soviet order and the development of markets—in particular, of land and real estate markets—has been different from the historical experience of Western countries. It has also been different from the experience of the post-communist societies of Central and Eastern Europe and of the Baltic states over the past two decades. It took Estonia only four years to enact a better and more complete set of laws for land and real estate than exist in Russia today. Why may it take Russia three decades and possibly more to develop its institutions for land and urban real estate markets? How have property rights and real estate privatization developed since the new Russian Federation emerged from the collapse of the Soviet Union in December 1991?

The struggle for legal clarity and consistency, administrative effectiveness, and operational stability in the development of property rights and real estate privatization over the past two decades in Russia appears to result from three immediate factors: (1) an initial level of significant ideological objection to private ownership of land; (2) a weak governance environment, as compared with international standards; and (3) emergence of conflicting economic incentives and sharp day-to-day competition among federal, regional, and local governments over public revenues from land and real estate resulting from the weak governance environment. These conflicts are usually built upon the remaining

institutional legacies of the Soviet era. Upon further examination, it is also difficult to ignore the extent to which Russia's history explains the fitful pace of reforms so far.

The following analysis is organized in five parts. First, we examine the path dependence of Russian institutions and governance historically. Second, we contrast Russia with Estonia to highlight the critical impact of the quality of governance on the development of property rights and real estate markets and the importance of institutions to the transition. Third, we review the often conflicted legal development of property rights during the first two decades of the Russian transition. Fourth, we evaluate the current status of property institutions today, especially the land registration system and the urban land use rules that affect the development of real estate markets. We close with the argument that effective land use and real estate market institutions are a major channel of Russian long-term economic growth. Flexible and cost-effective real estate markets will be essential to the diversification of the Russian economy away from its rising dependence on the energy sector and extractive industries generally.

Path Dependence of Russian Institutions —————

By path dependence of Russian institutions over time, we mean that past and existing institutions shape the development of new institutions.¹ At the start of its transition in 1991, the Russian Federation did not have a tradition, long or short, of well-defined and secure property rights. Property relations have been characterized through virtually all of Russian history by the threat of confiscation by government power and by a lack of any concept of mutual obligations between state and citizen. Thus, the state, in both czarist and Soviet times, was not viewed as an impartial enforcer of private property rights.

Probably the single most important element of path dependence throughout Russian institutional development is the lack of reciprocity of obligation, which is a core element of all sound legal systems and of the modern rule of law.² Both Velychenko (1995) and Hedlund (2001) emphasize the lack of reciprocity of obligation in Russian feudalism: the lord commanded, the vassal obeyed, and the vassal did not expect the czar to provide for him in return for his obedience. This lack of reciprocity in obligation, which significantly differentiates Russian feudalism from Western European and East Asian feudalism, has had lasting consequences for property relations in particular. In Hedlund's analysis, it gave rise

1. See David (2000) on path dependence in historical economics. For a discussion of path dependence in the context of U.S. common law, see Hathaway (2000).

2. We appreciate Robert Ellickson's private remark at the Lincoln Institute of Land Policy's 2008 land policy conference about the critical role of reciprocity of obligation as a core element of any sound legal system.

to the creation of private networks designed for maximum self-benefit, with the state not viewed as legitimate because it was not a guarantor of private rights.

A brief review of Russian history shows a number of practices and laws that support the conclusion reached above. These historical practices are ingrained in Russian political economy and society, and today the World Bank's World Governance Indicators (WGI) show Russia ranked consistently low on governance criteria. Among those historical laws and practices affecting Russia are the following:

- Pipes notes that Russia was the only country to have established a Chancery of Confiscations. "From the end of the fifteenth century to the end of the eighteenth, Russian rulers appropriated the estates of their subjects at will, without observing any legal procedures because they considered all the land in the realm to be ultimately theirs" (1994, 530).
- The 25 chapters and 967 articles of the *Ulozhenie* (Muscovite Law Code) of 1649 is a landmark in the legal history of Russia. The code relied on fear, obligation, and rewards. Under it, nobles were subject to a variety of punishments, and historians report that punishment was prevalent. The code also formally established hereditary serfdom for peasants. While Weickhardt (1993) has argued that the law in Muscovite Russia gave the nobles rights in land equivalent to that of a fee simple, his is a minority view. Pipes (1994) argues that, by the end of the sixteenth century, the lands held by the nobility were conditioned on service in the feudal sense, and the nobles did not hold the equivalent of freehold estates as maintained by Weickhardt.
- The obligation of service to the state by the nobility did not end until 1762, and confiscation without due process of law was not abolished until the Charter of Nobility of 1785, during the reign of Catherine the Great (Pipes 1994). Thus, feudal land relationships lacking reciprocal obligation continued for a long time in Russia, at least up to the time of American independence.³
- The 1906 Stolypin rural land reforms in favor of peasants were based, in large part, on a "growing recognition that the land commune prevented economic growth, and that reform must be focused on the individualization of economic activity" (Skyner 2003, 889). It should be noted that land and property markets existed in the cities of industrializing Russia in

3. In his classic book *Empire of the Czar* originally published in 1839, Adolphe de Custine gives a firsthand account of life in Russia in the nineteenth century and illustrates how the lack of reciprocity between ruler and ruled had become deeply embedded in Russian behavior. Custine repeatedly describes how the czar meted out swift, frequent, and severe punishments on the aristocracy that trickled down throughout society. Because of its continued societal relevance, this account was republished in the United States in 1990 with a foreword by Daniel Boorstin and an introduction by George Kennan.

the early twentieth century prior to the revolution of 1917 (World Bank 1995).

- The Bolshevik Revolution of October 1917 imposed its own notions of rule by law, and “the real core of Lenin’s program was that of a resurrection of the patrimonial and essentially rights-free system of old Muscovy” (Hedlund 2001, 223).
- The 1922 Land Code of the Russian SFSR (*Zelmeniy kodeks*) was written under the direct supervision of Lenin. Codes for other Soviet republics modeled after it followed between 1922 and 1929. It took until the 2001 Land Code of the Russian Federation, together with modification of the Civil Code, to have an operational recognition of private ownership of land for the first time in Russian history. Legal application of the new code to rural land occurred only the following year.⁴

What is important for understanding the current dynamics of land and real estate privatization processes is that early Bolshevik leaders determined not to establish a rights-based government or society, so the lack of a reciprocal relationship between the ruler and the ruled that originated in czarist times continued through the Soviet period (Hedlund 2001). It even continued after the end of socialism as rights became privately enforced by oligarchs and others (Braguinsky 1999). As Polishchuk and Savvateev (2001) note, public protection of rights discourages plundering. When the gains from plundering exceed the gains from legitimate production, plundering will be encouraged and public protection of rights discouraged. According to Polishchuk and Savvateev’s analysis, this is exactly the situation that prevailed in Russia through 1998 as the oligarchs sought to maximize their returns through plunder. Through their influence on the government, they sought to prevent public enforcement of private rights. Braguinsky (1999), approaching the issue from a somewhat different perspective, reaches the same conclusion.

Four challenging initial conditions prevailed in Russia in the late 1980s. They shaped the first decade of transition and the overall emergence of a market economy as well as the emergence of land and real estate markets (Hedlund 2001). First, the transition to market carried the requirement of a total change in the mode of operation of government at all levels from the command economy to the use of incentives relying on tax, subsidies, and regulations. There was a strong official bias to the point of hostility against small and medium enterprises (SMEs). The high transaction costs of dealing with administrative systems remain a barrier to entry to this day. In 2007 Russia had one of the lowest SME output to gross domestic product (GDP) ratios (in the low 10 percent range) of the emerging market economies.

4. For a perceptive commentary on this historical moment, see chapter 6, “Land Privatization: The End of the Beginning,” in Aron (2007).

Second, there were no Soviet enterprises with legal autonomy and economic accountability to privatize. State-owned enterprises were specialized components of the bureaucracy that focused on physical output, not value creation for the client (Dyker 1976). In fact, the notion of customer did not exist. The level of technology was inferior by international standards, except in some military areas. “Red managers” responded to a totally different set of incentives than did profit-oriented, market-focused managers.

Third, the political agenda of transforming the Soviet-educated population into a nation of stakeholders and even stockholders was unrealistic, at least in the short and medium term. There was a profound and widespread historical distrust of the state and its bureaucracy. The notion of rights was, at best, seriously undeveloped. During 70 years of Soviet control, market behavior was punishable by law as “speculation” (Hedlund 2001). None of the laws and institutions of the market existed, even in rudimentary form.

Finally, for 70 years the implicit goal of using the law had been to build bureaucratic organizations that were the real power base in the Soviet system. Understanding of the dual technical and ethical dimensions of property rights as social norms was uncommon (Hedlund 2001). There was not even a basic market terminology. During the first contacts between Russian officials and international experts in the 1990s, there was a strong demand for developing glossaries of new market-oriented Russian terms such as *loan*.

These four conditions rendered a shock-therapy approach to privatization and market creation unlikely to succeed. The first decade of Russian transition brought about a disastrous economic depression twice as severe as the Great Depression in the United States. Russian per capita income did not return to its 1990 Soviet level until the end of 2007 (International Monetary Fund 2008). This difficult social, political, and economic environment has contributed to the fitful and erratic development of property rights and real estate markets.

Privatization in Estonia and Russia: A Study in Contrast —————

Both Russian and international analysts have noted the difficulties experienced in the development of private property rights in land and real estate resources in the Russian Federation since the official collapse of the Soviet system in December 1991 (Braguinsky 1999; Heller 1998; Lazarevsky, Khakhalin, and Trutnev 2000; Skyner 2003). In countries of Central and Eastern Europe as well as in the Baltic states, privatization of real estate resources has proceeded quickly and relatively smoothly, comparatively speaking (Meyers and Kazlauskiene 1998). These different outcomes raise the question of why.

We begin by comparing the transition experiences of the Baltic Republic of Estonia with those of the Russian Federation to note similarities and differences in the processes by which the two countries approached the issue of privatization of land. While the two countries are obviously different in a number of respects,

the comparison may be instructive precisely because of the sharp contrast in the way they have approached land privatization.

LAND REFORM IN ESTONIA'S TRANSITION TO MARKETS

In the early 1990s, at the beginning of the transition from administrative-command systems to market economies, it was often said that some countries, such as Russia, did not have usable pasts upon which to create market economies. Other countries, however, did have usable pasts upon which to build. To understand the land reform process in Estonia following its secession from the Soviet Union, it is necessary to understand Estonia's usable past—the processes of land privatization in Estonia in the latter part of the nineteenth century and in the period between the two world wars.

According to Meyers and Kazlauskiene (1998), by the late nineteenth century many of the large estates that had characterized Estonia had been divided and peasant farming established. Peasants were granted the right to purchase the land they worked. Estonia was independent between the two world wars. It continued land reform by redistributing land to, among others, small landholders. By the time of World War II, there were more than 140,000 family farms in Estonia. The country thus established a tradition, albeit a short-lived one, of individual landholdings and private ownership of land.

Given Estonia's brief, but real, experience with private ownership of land, it is not surprising that land reform was one of the earliest measures taken as the Baltic republics moved toward independence. All three Baltic countries began the process of land reform in 1989, well before their independence from the Soviet Union. The 1989 laws granted the right to establish family farms based on long-term use rights. This set the precedent for non-state methods of farming and paved the way for the introduction of private ownership.⁵ Laws establishing private ownership of land in Estonia were adopted in June 1991, two months prior to the recognition of its independence.

After independence Estonia moved rapidly to establish the basis for private ownership of land and a free market in real estate. In October 1991 the Land Reform Act was passed. This comprehensive law, 50 pages long in English translation, sets forth the intention of the Estonian government to establish private property in land as the basis for all land relationships in both rural and urban areas. The law provides the mechanism by which citizens may apply for restitution of lands expropriated from them or their forebears during Soviet times. It also specifies the means whereby land may be privatized. Moving away from the operational problems caused by the vague concept of state ownership of land in

5. Lerman (1995) notes that these early laws in the Baltic countries distributed land to members of the collective farms and others who wished to engage in farming. When the restitution laws were passed, distributions of this type ceased.

socialist economies, provisions for state and municipal ownership of land are also included in the law. Estonian officials thus enunciated a clear policy toward land ownership and provided relatively straightforward procedures by which the policy could be implemented. Based on the legislative record, there was no ambiguity or confusion. The goal was private ownership of land, restitution where possible, compensation when restitution was not feasible, and an open market in real property.

In 1993 the Land Reform Act was followed by four new acts clarifying property rights and solidifying the market: the Land Tax Act in May, the Law of Property Act in June, the Land Register Act in September, and the Law of Property Act Implementation Act—clarifications of and amendments to various previously enacted laws—in October. In 1994 the Land Valuation Act was passed, changing the way land is valued for purposes of the land tax and for compensating individuals for illegally expropriated land. The Land Cadastre Act was also passed that year. In 1995 the Land Readjustment Act was passed, and in 1996 a law restricting alienation of land to foreigners, foreign corporations, and Estonian juridical entities was passed. This history is summarized in table 5.1.

Table 5.1
Estonian Laws Related to Real Property Privatization

Date	Law	Description
17 October 1991	Land Reform Act	The purpose of the Land Reform Act is to change the relationship of physical and legal persons to the land from state or socialist ownership to private ownership. The act states rules and procedures governing two major components of changing these land relations. One is restitution, in which land unlawfully expropriated in Soviet times is returned, to the extent possible, to the original owners or their descendants. The second means used to convert land to private ownership is privatization. Lands remaining in state ownership after restitution may be privatized according to the rules for privatization. The act also contains rules for lands in municipal and state ownership.
6 May 1993	Land Tax Act	This act imposes a tax on land. Usual exemptions for land owned/used by foreign embassies, governments, and cemeteries are granted. Land is to be valued in accordance with the Land Valuation Act. Data regarding the land are provided by local authorities; the tax is administered by the Tax and Customs Board and is paid to local government budgets.

Table 5.1
(continued)

Date	Law	Description
9 June 1993	Property Act	The Property Act sets forth a comprehensive framework of property rights and includes provisions for the creation, transfer, and extinguishment of those rights. Because the act covers both movable and immovable property, it is properly called a property act and not a land code. Among the rights covered by the act are the rights of ownership, servitudes, encumbrances (other than mortgages), superficies (important because buildings have been built on land owned by third persons), preemption, and security. The provisions on security cover both movable and immovable property and provide for security interests in intangibles.
15 September 1993	Land Register Act	This is a comprehensive act establishing and regulating the registry to be established in county and city courts. It prescribes the contents of the registry, describes how entries are to be made, details the registration process, provides for appeals, and, importantly, provides for open access to registry records. An electronic register is also authorized.
27 October 1993	Implementation Act for the Property Act	The Implementation Act for the Property Act deals with practical problems arising due to the complexity of the various rights sought to be established and implemented through the privatization and restitution processes. Rights of owners of structures vis-à-vis the owners of the underlying land are defined; rules governing illegal constructions are stated; the right of perpetual use of agricultural land is clarified; and the respective rights of owners of land and owners of utility structures erected on that land are enunciated. Rights of spouses in collective farmlands and farm households are also specified.
9 February 1994	Land Valuation Act	This act sets forth the rules for valuing land for purposes of the land tax and for compensating individuals for unlawfully expropriated land that cannot be returned by restitution. For purposes of the land tax, valuation is to follow international best practice, and is to follow the comparable sales, capitalization of income, or cost approaches to valuation.

(continued)

Table 5.1
(continued)

Date	Law	Description
12 October 1994	Land Cadastre Act	The Land Cadastre Act establishes the land cadastre, a national spatial database containing digital map data at scales of 1:10,000, 1:2,000 and 1:500 covering the entire country. The cadastre is maintained by the Ministry of the Environment, and stores data from the land registry to create a comprehensive description of land parcels and the rights and other attributes associated with them.
25 January 1995	Land Readjustment Act	The Land Readjustment Act complements land privatization and restitution. Its purpose is to allow landowners whose plots are not economically efficient to adjust their boundaries with their neighbors to make more usable land plots. Readjustment may be accomplished by "simple" procedures of agreement by adjoining landowners, or may be effected by more elaborate "reallotment plans." County governments supervise the process. Compensation and dispute resolution procedures are contained in the act.
29 May 1996	Restrictions on Transfer of Immovable Property Act	This act regulates the ownership of land plots (but not apartments) by non-Estonian natural and legal persons as well as Estonian legal entities. The act contains a list of areas in which land may not be owned by any of the three listed categories, unless the government of Estonia grants an exception. Outside of the listed areas, the local governor may permit foreign individuals or legal entities or Estonian legal entities to own land.

Source: Analysis of Estonian laws by the authors.

While other acts covering particular issues of land reform were passed, the acts enumerated above were the primary laws governing land reform in Estonia. Most were passed within three years of independence, and amendments were few and generally involved technical corrections, not substantive or policy changes. In this short time, Estonia developed a coherent and comprehensive legal framework for property rights and real estate market reforms comparable to most other transition economies.

This clear legal framework has resulted in the registration of a significant number of parcels in the land cadastre. According to statistics provided by the Estonian Land Board (2008), the number of registered properties in the Estonian Land Cadastre increased from 104,086 in 1997 (no month was given) to 544,841 in July 2007, an increase of 440,755, or 423 percent.

LEGAL FRAMEWORK FOR PRIVATE PROPERTY RIGHTS AND LAND REFORM IN RUSSIA

The process of land reform in Russia could not be more different. The first major difference between the two countries is the history of land relations. The second major difference is in the legislative process for creation of property rights reforms. In Russia the process has been marked by a lack of clarity, coherence, and consistency across laws (*zakoni*) passed by the Duma and executive decrees (*ukazi*) issued by presidents of the Russian Federation. There is also inconsistency among various legal documents over time. The first two decades of transition have been marked by frequent antagonistic relationships across levels of government and across the 89 regions and autonomous ethnic republics as well as between oblasts and municipalities.

As in Estonia, land reform legislation was passed by the Russian Soviet Federal Socialist Republic (RSFSR) in 1990 under then RSFSR President Boris Yeltsin prior to the dissolution of the Soviet Union. Several laws were passed, including the Law on Land Reform and the Law on Property. The Law on Property provided that physical and legal entities could own land parcels (Eagle 2006; Overchuk 2001). However, as Overchuk explains, these laws restricted other rights, such as the right to mortgage and the right to lease. They were restricted because of philosophic differences among members of the Duma regarding property rights; there was no real agreement as to how, or even whether, land privatization should move forward. Decrees of the president of the Russian Federation attempted to remedy some of the more egregious deficiencies in these laws (Overchuk 2001), but the result was a patchwork of legal requirements, not a coherent, unified legal regime. Following the adoption of the Constitution of the Russian Federation in 1993, the Law on Land Reform was repealed because it was not in keeping with the provisions of the new constitution. Thus, these laws did not have a lasting impact on land reform in Russia.

Article 35 of the 1993 Constitution of the Russian Federation guarantees all citizens the right of private property. This right includes the right to possess, use, and dispose of property and to receive compensation in the event of a taking by governmental power. However, these provisions were not self-executing, and Polishchuk and Savvateev conclude that “property rights in Russia [had] no adequate protection from the state” by the end of the first decade of transition (2001, 3). The authors identified many powerful economic actors who could gain more from predation than from state protection of all property rights.

Supporting the conclusion of Polishchuk and Savvateev, only one law tangentially relating to land was passed between 1993 and 1997, that being a law on organizing and operating agricultural cooperatives (Wegren 1998). Several decrees were issued and government resolutions adopted addressing specific issues such as agricultural experimentation in Nizhny Novgorod Oblast and allowing owners of structures to purchase the land under their structures. However, no comprehensive land reform legislation was enacted. The Russian Civil Code was

adopted in 1994, but members of the Duma could not agree on the property provisions contained in its chapter 17, so it was adopted without that chapter. In short, as Polishchuk and Savvateev (2001) note, the first seven years of the transition saw no improvement in the security of property rights in the Russian Federation.

In 1998 the Law on State Registration of Real Estate Rights and Transactions was adopted. It was the first significant land-related legislation to pass the Russian Duma since the adoption of the Russian constitution in 1993. That law originally assigned land registration to the Ministry of Justice, with implementation in the ministry's offices in each administrative region of the Federation. In 2004 the Federal Registration Service was established within the Ministry of Justice, and the land registration function was assigned to that body in 2005 (Rumyantsev 2008). In contrast with Estonia's 1993 Property Act, which reestablished the critical concept of property that recognizes land and improvements as a single integrated legal and functional economic entity, the Russian real estate legal and registration systems still separate land rights from the improvements over that land.

In 2001, three years after the Registration Law passed, the Land Code was finally adopted by a new Duma. This historical milestone recognizes for the first time in Russian history the full private ownership of land in both rural and urban areas (Aron 2007). That same year, chapter 17 of the 1994 Civil Code, which defines the implementation rules for private ownership, was also passed. However, the version of chapter 17 that was passed did not apply to agricultural lands. For political reasons, it was not until 2002 that the third Duma passed legislation applying the provisions of chapter 17 to agricultural lands. The last piece of legislation dealing with land was the 2007 law about a cadastre of real estate objects, which took effect in March 2008.

Symptomatic of the fitful Russian process of land reform, the Federal Real Estate Cadastre Agency, under the Ministry of Economic Development and Trade, had been created four years before the 2007 cadastre legislation was passed (Rumyantsev 2008). Rumyantsev notes confusion and overlapping jurisdiction between the duties of the Federal Real Estate Cadastre Agency and the land registration functions of the Federal Registration Service. Thus, even with land legislation in place, the confusion and uncertainty of the earlier years remains present in Russian land relations. A timeline showing the dates of enactment of various land-related laws in Russia is shown in the Appendix on pages 127–131.⁶

As Russia approaches the end of its second decade of transition, official statistics show a low level of land privatization for residential and industrial land

6. A more detailed timeline covering the period from *perestroika* and *glasnost* onward appears in table 5.4. As shown in that table, the passage of land legislation correlates well with the associated political periods as defined by Åslund (2007) in his review of the first two decades of the transition in Russia.

Table 5.2
Russian Residential and Industrial Lands in Private Ownership

	Percentage of All Russian Federation Land	Percentage of This Land Category in Private Ownership
Human Settlement Land	1.08%	18.5%
Industrial Land and Others	1.02%	0.39%

Source: Overchuk (2001).

and stagnation in the privatization of agricultural land. Confusion, uncertainty, and high transaction costs are reflected in the statistics showing the amount of land ownership by physical and legal persons. The relatively small percentage of private ownership of residential and industrial land is shown in table 5.2. These figures reflect privatization activity through the late 1990s.

Overchuk (2001) reports that federal tax and leasing policies appear to be important contributors to the low levels of private land ownership. Under Russian tax and leasing laws, rates for leasing land have often been lower than tax rates applying to owned land. Therefore, citizens and legal entities often choose to rent state-owned properties rather than privatize them because doing so is more economical.

With respect to agricultural lands, significant privatization has occurred. Overchuk (2001) estimates that 97 percent of all privately owned land in Russia is agricultural land, with nearly 12 million owners holding 117.6 million hectares. By the year 2000, there were over 200,000 peasant farmer enterprises in Russia, and more than five million citizens had applied for plots for private housing construction in agricultural areas. However, as Overchuk (2001) notes, the number of applications for land plots decreased substantially from a high of 1,827,600 in 1995 to a low of 336,400 in 1999. He attributes this decrease to the fact that the most valuable agricultural land had been privatized, with little good agricultural land remaining. Furthermore, some privatized land has been returned to the state, presumably because individuals decided to leave farming or found the tax burden excessive.

ESTONIA AND RUSSIA COMPARED

Cultural, political, and economic factors have resulted in stark differences in land and real estate privatization between Russia and Estonia. Table 5.3 compares the dates of passage of core land legislation in the two countries. The Estonian Registration Law was passed five years before the Russian Registration Law, the Land Code eight years prior to the corresponding Russian law, and the cadastre law in Estonia a full 13 years before the Russian cadastre law. Without a clear legislative

Table 5.3
Dates of Passage of Major Land Laws: Estonia and Russia

Type of Act	Year of Enactment	
	Estonia	Russia
Land Reform Act	1991	No equivalent law*
Land Code (or Equivalent)	1993	2001
Registration Law	1993	1998
Cadastre Law	1994	2007

*The Russian Soviet Federal Socialist Republic enacted two laws in 1990: (1) the Law on Land Reform in November; and (2) the Law on Property in December (Overchuk 2001). The Law on Land Reform was repealed following the creation of the Russian Federation, as were other laws (Food and Agriculture Organization 2008). No Russian Federation law passed in the early days of the Federation established comprehensive private property rights similar to the Estonian Land Reform Act.

basis for land reform, it is not surprising that Russia's land privatization has been so hesitant, tentative, and at times bewildering.⁷

Estonia, with its brief but important history of land ownership and private farming, created a land privatization process based on a coherent body of laws. These laws were enacted quickly after independence and implemented consistently. Russia, on the other hand, did not have a tradition of well-defined property rights. Following the demise of socialism, private parties, seeking to benefit from the plunder of state and private assets, helped to delay introduction of any cohesive system of public protection of private property rights.

RULE OF LAW, RULE BY LAW, AND THE QUALITY OF GOVERNANCE DURING THE TRANSITION

The development of the rule of law is the central pillar of the transition to political democracy. Under the rule of law, not only individual citizens but also the government itself is subject to and limited by the law. Specific human rights are protected against infringement by other individuals, organized groups, and the government itself. The concept of rule of law assumes a politically and socially legitimate source of the law. The prevalent view today is that democratic institutions and processes should be the sources of the law for a rule-of-law environment to exist.

It is not because they did not uphold the "rule of law" of market democracies that socialist societies were lawless. Rather the law was used as a tool to communicate and enforce the will of a powerful subset of society over the rest of society, with major implications for the structure and organization of the economy (Kor-

7. The only real exception to this consistent Estonian process was that initial privatization of agricultural land across the three Baltic states was to collective farm workers (Lerman 1995). This process was stopped quickly in Estonia once the decision was made to make restitution, wherever possible, to landowners as of 1940 or to their known descendants.

nai 1990, 1993). Alexander Yakovlev, who was one of the key framers of the democratic 1993 Russian constitution passed during the Yeltsin era, characterized the Soviet “rule by law” as “the law as a tool of dominance” (Lloyd 1998, 95).

The view that has emerged from the experience of transition economies as well as from the 1997 Asian financial crisis is that institutions and the quality of governance are critical factors for economic growth and long-term development—much more so than packages of economic policies such as the Washington Consensus or some institution-free, abstract reform proposals advocated by some Western economists for transition economies in the early 1990s. The sharp contrast between the transition in Estonia and in Russia suggests the central role that the quality of governance plays in the diverging experiences of these two countries.

The World Bank’s WGI quantify six dimensions of governance:

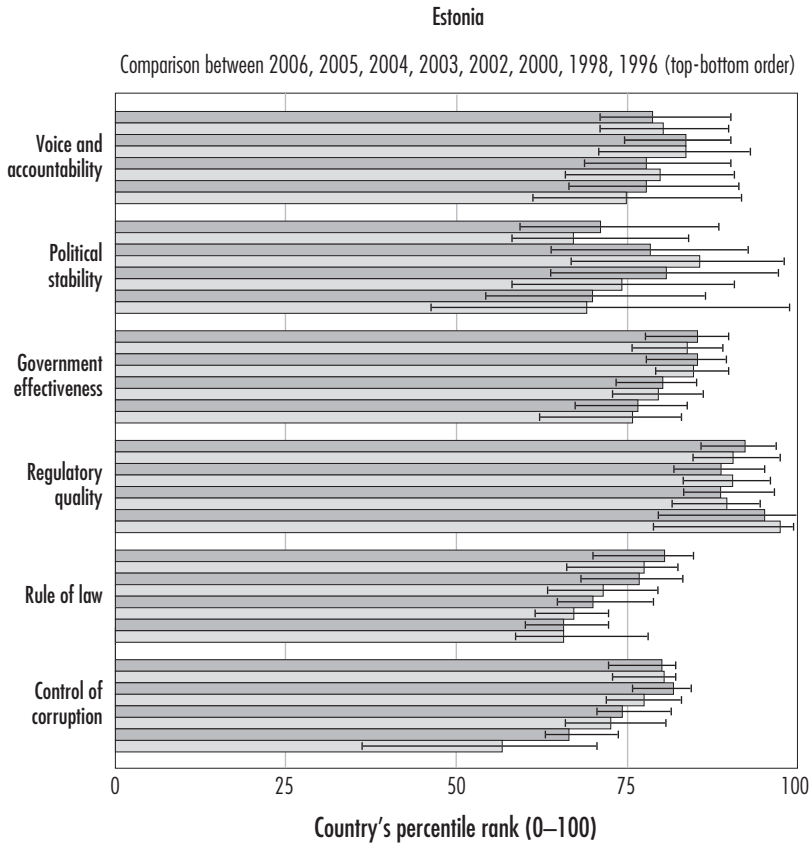
1. Voice and accountability
2. Political stability and absence of violence
3. Government effectiveness
4. Regulatory quality
5. The rule of law
6. The control of corruption⁸

These perception-based indicators of governance yield informative and sharply contrasting results for Estonia and Russia that correlate well with the development of property rights and real estate markets in each country. Estonia scores in the top 25 percent of countries for each of the six governance categories, and over the 10 years between 1996 and 2006, trends in the quality of governance have been rising (see figure 5.1). In contrast, WGI data place Russia in the bottom 25 percent of all countries, with unstable indicators of governance without clear trends over time. In particular, Russia scores comparatively poorly on rule of law and corruption indicators (see figure 5.2).

In an analysis of Russian land and real estate reforms at the beginning of the transition, Renard (1997) pointed out that both the starting and the end points of the transition to market economies and democracy differ across countries. In the case of Estonia, the end point of the transition was unusually clear and

8. The World Governance Indicators (WGI) research project that started at the World Bank in 1999 is the most systematic effort to develop credible indicators of the comparative quality of governance across countries. In 2007 the WGI project covered 212 countries and territories for 1996, 1998, 2000, and annually for the period 2002–2006. The indicators are based on “several hundred individual variables measuring perceptions of governance, drawn from 33 separate data sources constructed from 30 different organizations” (Kaufman, Kraay, and Mastruzzi 2007, 1). For disaggregated comparative indicators of individual countries and individual years between 1996 and 2006, refer to the Web site <http://www.govindicators.org>.

Figure 5.1
Rising Quality of Governance in Estonia

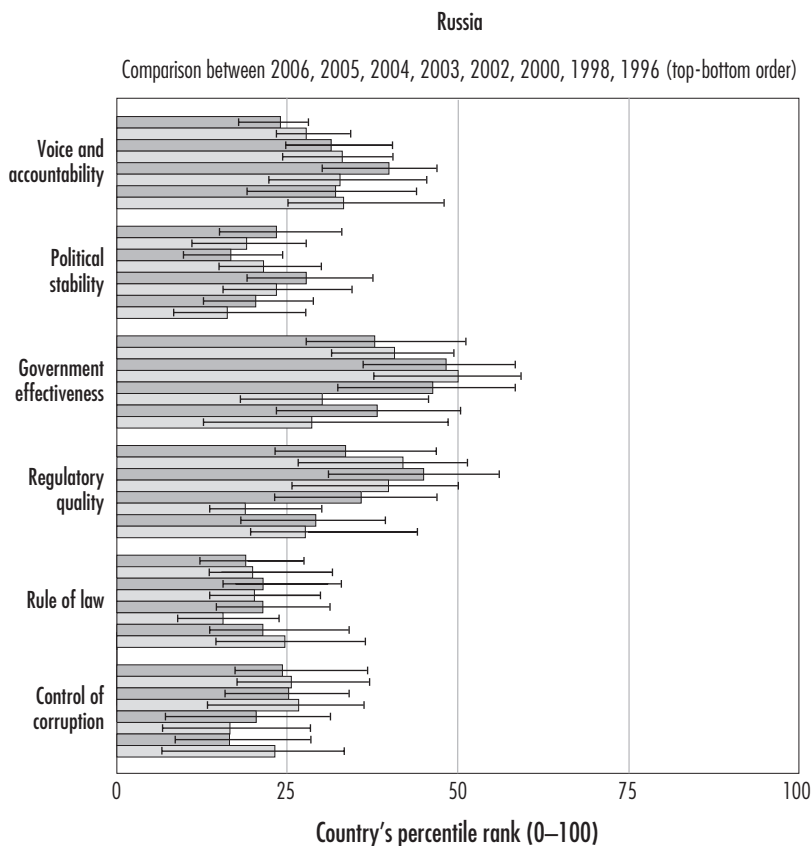


Source: From Kaufman, Kraay, and Mastruzzi (2007).

Note: The information is from the World Bank's WGI for 212 countries based on 33 data sources from 30 organizations.

agreed on by most Estonians even before the collapse of the Soviet Union in December 1991. The key strategic features were full independence from Russia by peaceful means, modernization and reenactment of the Estonian constitution in force prior to the Soviet invasion, move to a full and open market economy, and eventual entry into the European Union with its specific standards for the rule of law (*acquis communautaire*). It must also be noted that, from the beginning of its recovered independence, Estonia pegged its currency to European legal tender, first to the German mark and then to the euro. Privatization of land and real estate markets was an explicit part of the overall Estonian strategy.

Figure 5.2
Low Quality of Governance in Russia



Source: From Kaufman, Kraay, and Mastruzzi (2007).

Note: The information is from the World Bank's WGI for 212 countries based on 33 data sources from 30 different organizations.

Culturally, technically, and in terms of easy access to international information, Estonia has benefited from its close proximity to Finland, the country that holds the highest WGI scores for the quality of its governance. In the case of large, inward-looking Russia, the actual end point of the transition remains unknown. However, one may still ask why Russia scores so poorly on governance and what factors are shaping the institutional transition to private land ownership and open real estate markets across its system of cities.

Development of Property Rights in Russia: The First Two Decades

THE FIRST DECADE OF TRANSITION (1989–1999)

The first decade of transition began before the actual collapse of the Soviet Union. This decade was marked by a genuine push by Boris Yeltsin for what amounts to a democratic revolution in Russia, first in his capacity as president of the RSFSR within the Soviet empire and after December 1991 as president of the Russian Federation. The outcome of the reformers' efforts to move toward democratic institutions and a market-based economy were uneven. Notably, the period was marked by the massive and most problematic privatization of state-owned enterprises whose after-effects are felt to this day (Freeland 2000).

The legislative process to achieve the privatization of land and real estate assets generated a plethora of often inconsistent, contradictory, and/or incomplete laws and executive decrees. Often the reformist presidential administration felt the need to issue decrees to correct the negative effects of laws passed by the Duma. As explained earlier, this state of affairs arose because different parts of the government at the federal, regional, and local levels often aimed to achieve their immediate economic self-interest irrespective of the public's need for a coordinated institutional infrastructure for land and real estate markets.

Politics, economics, and severe infighting within the national government structure combined to create a dynamic that was once described as a "war of laws." Nonetheless, a lasting achievement of the period is Russia's 1993 democratic constitution. This document recognizes the principle of the private ownership of land and allows Russians to buy and sell land. Notwithstanding this pathbreaking constitution, the first two Dumas of the new Russian Federation did not enact laws that would put these rights into effect. Communists and Agrarians, who dominated the Duma in the Russian Federation's early years, strongly opposed land and real estate privatization and blocked all attempts to pass implementing legislation.

The failure to privatize land in Moscow illustrates the erratic nature of the reform process during the first decade of the transformation. Taking advantage of their political access and of the intense institutional debates, city authorities succeeded in having Moscow exempted from the privatization decrees and in giving the city itself ownership of all the land within its boundaries. Under current regulations of the Moscow city government, land in the city may be leased by private businesses for up to 49 years only, which is the length of lease taken from the old Stolypin land reforms of 1906. In practice, this means that land cannot be owned by private businesses in Moscow. In most other cities as well, myriads of conflicting regulations have stymied real estate privatization.

Stressed Russian Urban System During the First Decade of Transition The real estate privatization process was further hindered by the stresses placed on

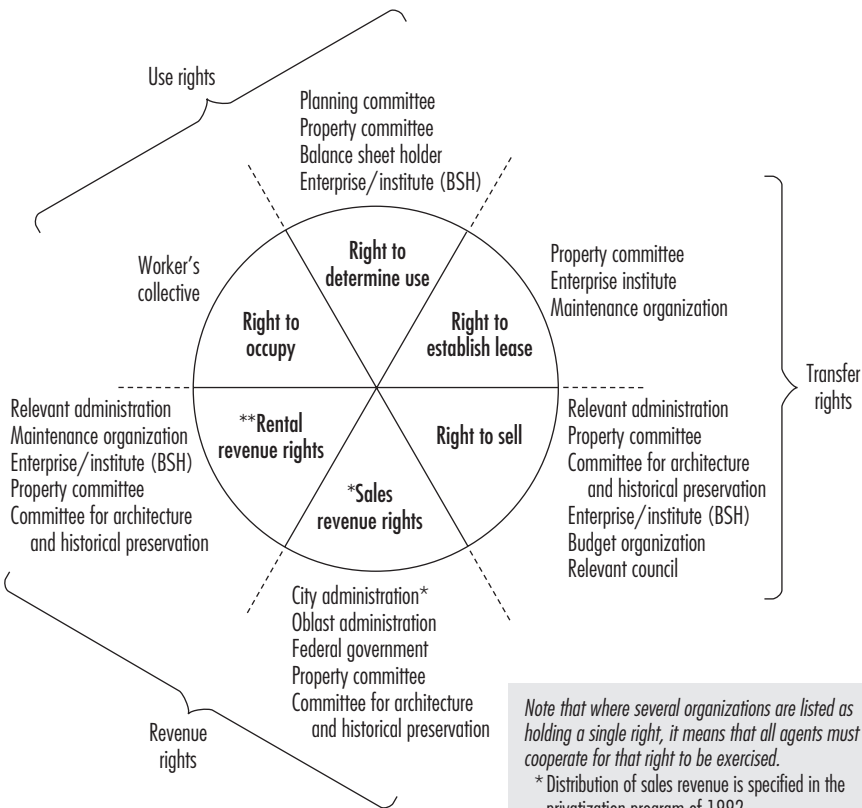
Russia's urban economy by the collapse of the inefficient and massive Soviet industrial structure. Urban economic restructuring when GDP growth was sharply negative meant no maintenance of urban real estate assets and infrastructure, as well as severe depreciation of the urban real estate stock. Domestic capital and the limited amount of foreign direct investment (FDI) that took place during the first decade went mostly to Moscow and St. Petersburg. These two cities received over 60 percent of total FDI, and much of the rest went to a few energy-based cities (World Bank 2002). On the urban consumer demand side, the economy was volatile and stressful for the great majority of the Russian population. Income inequalities rose very sharply, even compared with large emerging market economies like Brazil and India.

Two other factors added to the difficult Russian transition compared to the cities of Central and Eastern Europe: the severely distorted spatial structure of Russian cities, and the fragmentation of property rights among multiple owners of the same state property at the start of privatization. Both factors further depressed the potential demand for privatization of urban real estate by residents and businesses.

From the low level of urbanization of 16 percent at the start of the 1917 revolution, Russia reached its full urbanization level of 77.5 percent by the end of the Soviet era. The development of these socialist cities took place in the absence of land markets and without land recycling for over 70 years, resulting in the strikingly inefficient spatial structure of Soviet cities. Because the cities have low densities in the center and high densities at the periphery, they have very low energy and transportation efficiency as well as extremely poor environmental quality (Bertaud and Renaud 1994, 1997). The proportion of land in industrial use was a multiple of that observed in market cities. Moreover, the industrial land was in very central locations and was underutilized. During the transition to markets, the distorted spatial structure in Russian cities generated a majority of losers among urban residents living in the periphery and a minority of winners among those who acquired housing in the city center.

For commercial businesses and offices, privatization created new property rights that conflicted with the processes inherited from Soviet times when federal, oblast, and local governments allocated land and building rights. Use rights, revenue rights, and transfer rights were fragmented among different agencies that were initially unwilling or unable to cooperate, making it impossible to use desirable buildings (see figure 5.3 and Harding 1995). Anticommons property may appear whenever new property rights are defined. In Moscow, for example, multiple owners have been endowed initially with competing rights in each storefront, so no owner holds a bundle of usable rights and the storefront remains empty (Heller 1998). These "anticommons" property use problems were also present in the initial years of transition in other socialist economies, but they were resolved relatively rapidly by the new legal frameworks. This did not happen in Russia because a viable alternative legal framework had not yet developed.

Figure 5.3
Fragmentation of Rights Between Agencies



Note that where several organizations are listed as holding a single right, it means that all agents must cooperate for that right to be exercised.
 * Distribution of sales revenue is specified in the privatization program of 1992.
 ** Distribution of rental revenue is locally determined, and varies from city to city. These are the most common recipients of rental revenues.

Source: Harding (1995, 12). Reprinted by permission.

The End of the First Decade At the end of the first decade of transition, a review of the status of real estate market privatization by Lazarevsky, Khakhalin, and Trutnev (2000) found that the transition faced a series of major urban land and real estate market problems. Among their findings are the following:

- There is inadequate federal legislation.
- Sale prices of state land privatized by enterprises are excessive.

- Local administrations have generally unfavorable attitudes toward privatization and cause unreasonable bureaucratic delays.
- The procedures for the purchase and registration of land rights from the state are lengthy. For example, it could take two and a half to three years for a sale to be completed, and then another six months to one year for a title certificate to be issued.
- Interpretation of federal legislation by local administrations is arbitrary; prices are arbitrary; and treatment of companies that wish to sell their land is uncertain.
- Targeting of land use is rigid. Even as the owner of a land plot, a company cannot fully dispose of it. The use of a land parcel is strictly and very narrowly regulated, and the landowner cannot change it for a more beneficial use. Commonly, local administrations fail to provide clear procedures for changing land use.
- There is no secondary market for enterprise lands, land mortgages, and other market transactions.
- The procedures for registration of land rights when ownership rights are sold by state or municipal authorities are vague.

THE SECOND DECADE OF TRANSITION (2000–2008)

Significant economic and institutional developments took place from 2000 to 2008 during Vladimir Putin's presidency. The economy entered a period of sustained high economic growth driven by the continuous rise of export prices in the oil and gas sectors. There were major improvements in macroeconomic policy and taxation. This period has also seen a strong trend toward recentralization of government powers. The Kozak reform package submitted to the Duma in 2004 and in force starting in 2006 aims at greater uniformity and control over the "subject governments" of the Federation. The democratic revolution of the Yeltsin era was followed by the Putin restoration of centralized powers.

The central achievement of the decade with respect to land and property rights is the historic passage of the Federal Land Code on 29 October 2001. Almost 74 years to the day of the Bolshevik Revolution, the Federal Land Code overturns a core legacy of the Soviet Union: state ownership of land. The code finally permits private ownership of land with sales and purchase transactions. Together with chapter 17 of the Civil Code (also passed that year), the Land Code now governs transactions in land. Initially, agricultural land was excluded by the Putin administration to accommodate organized opposition in the Duma. The application of the Land Code to agricultural land was enacted in 2002. For the first time in its long history, Russia fully recognizes the private ownership of land. Technically, the 2001 Land Code defines seven "prescribed uses of land":

1. Agricultural land
2. Land for towns and settlements

3. Commercial land for use by industrial enterprises, power companies, communications companies, and other industrial activities
4. Protected areas (land situated beneath an object that is itself specially protected, such as a nature park)
5. Forestry land
6. Waterfront land
7. Reserve land (land that is owned by the state, is not used for commercial purposes, and can be transferred to any of the other six categories)

Looking back at the entire period of Russian transformation from 1985 to 2008, there has been a relationship between the dominant features of political periods and the development of the legal and regulatory framework to create the infrastructure of private real estate markets. Table 5.4 presents a timeline of key laws, decrees, and administrative decisions aimed at creating private land ownership and the institutional infrastructure for real estate markets, to which has been added a column showing Anders Åslund's (2007) characterization of the political periods during which new institutional developments took place.

The development of efficient and free real estate markets did not improve greatly in the second decade of transition. The problems in 2008 are similar to the inventory of real estate privatization problems made by Lazarevsky, Khakhalin, and Trutnev in 2000. At the start of the new Medvedev administration, unresolved problems remain in three critical areas: (1) the absence of an integrated real estate registration system; (2) the lack of market-oriented land use planning regulations; and (3) the very slow emergence of land and real estate markets in every Russian city.

Russia's Property Institutions Today —————

Russian land registration policy has developed in fits and starts. It has been heavily influenced by a strong vested interest in the inventory system for land and improvements that was in place at the time of the fall of communism. The immature development of a unified titling system is due as well to the lack of the development of a coordinated real estate finance system and unified property tax system. The situation is exacerbated by the lack of demand by developers for urban land that results from the continuation of the Soviet site-specific land use planning process. These factors, when taken together, significantly reduce the demand from both developers and real estate consumers who otherwise would want to develop or own urban land and would require a strong and rational registration system to protect their property rights.

TRANSFORMATION, CONSOLIDATION, AND UTILIZATION OF THE REGISTRATION SYSTEM

A modern national registration system, if designed properly, will lay the foundation for a good real estate information system that is essential for the development

Table 5.4
Timeline of Russian Land Reforms, 1985–2008

Awakening	1985	<i>Perestroika</i> Announced
Collapse	1990	Law on Land Reform of the RSFSR Law on Peasant Farms Law on Property in the RSFSR Law on Enterprises and Entrepreneurship in the RSFSR
	1991	Land Code of the RSFSR Law of Privatization of the Housing Stock Presidential Decree "On Immediate Measures for Implementation of Land Reform"
Revolution	1992	Government Resolution "On the Course and Development of Agrarian Reform" Decree 301 "On the Sale of Land Plots to Citizens and Legal Entities Within Privatization of State and Municipal Enterprises" Law "On the Right of RF Citizens to Privatize and Sell Land Plots Designated for Subsidiary Farming, Gardening and Individual Residential Construction" Decree 631 "On Approval of the Procedure for Land Plot Sales Within Privatization of State and Municipal Enterprises, Extension and Development of the Premises of the Said Enterprises, as Well as Those Allocated to Citizens and Their Associations" Government Resolution "On Procedures for Privatization and Reorganization of Enterprises in the Agro-Industrial Complex"
	1993	Presidential Decree "On Regulation of Land Relations and Development of Agrarian Reforms in Russia" Decree 2130 of 1993 "On the Registration of Land Rights" Constitution of the Russian Federation
Rise/Fall of SOE Managers	1994	Government Resolution "On the Practice of Agrarian Transformation on Nizhniy Novgorod Province" Government Resolution "On Agricultural Enterprise Reform Allowing for the Experience in Nizhniy Novgorod" Decree 1535 "On Main Provisions of State Program of Privatization of State and Municipal Enterprises in the Russian Federation After 1 July 1994" Decree 478 "On Measures for Ensuring Stable Revenues to the Federal Budget from Privatization" Civil Code (Without Chapter 17)

(continued)

Table 5.4
(continued)

Rise/Fall of SOE Managers	1995	Government Resolution 96 "On Procedures for Realization of Rights of Owners of Land and Asset Shares" Law on Agricultural Cooperation
Oligarchy	1996	Presidential Decree "On Realization of the Constitutional Rights of Citizens Concerning Land" Decree 1368 "On the Purchase Price of Land"
	1997	Decree 485 "On Guaranteeing Real Property Owners the Acquisition of Ownership in Land Under Their Property" Decree 1263 "On the Sale or Lease of Land Parcels to Citizens or Legal Entities Located in Urban and Rural Settlements for Construction Purposes"
	1998	Law on State Registration of Real Estate Rights and Transactions Resolution No. 2 "On Approval of Procedures for Organizations of Sales (Auctions, Tenders) of Lands in Urban and Rural Settlements, or Lease of Them, to Natural and Legal Entities"
Stabilization	1999	Presidential Decree 632 "On the Right of Local Self-Government to Set Land Privatization Procedures and Terms" Government Resolution No. 1024 "The Concept of Public Property Management and Privatization in the Russian Federation"
	2001	Federal Law No. 45 Implements Chapter 17 of the Civil Code as to Nonagricultural Lands Law on the Delimitation of State-Owned Lands Land Code
	2002	Law on Circulation of Agricultural Lands (Implements Chapter 17 of the Civil Code for Agricultural Lands)
Authoritarian Recentralization	2004	Federal Registration Service Created
	2005	Registration Function Transferred to the Federal Registration Service
	2007	Law "About a Cadastre of Real Estate Objects"

Source: Authors' analysis of Soviet and Russian laws; Åslund (2007).

of the real estate sector and the overall economy. A sound and complete registration system should

- integrate land and improvements as property;
- organize the system around a parcel identifier within a national reference system;

- register the full bundle of property rights;
- limit restrictions to the bundle of rights based on public goods;
- list current and past right holders;
- provide dispute resolution; and
- provide state protection of real property rights.

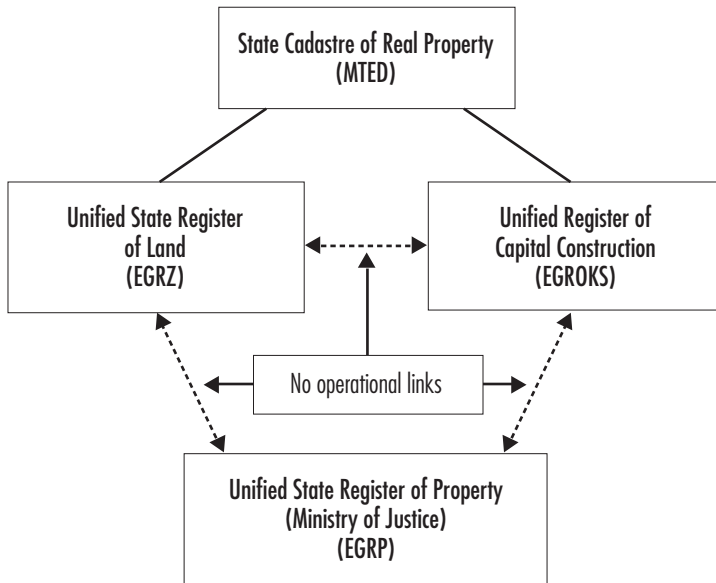
When matched against these design features, it is clear that the registration system of Russia remains a work in progress. Reforms are needed to bring the current system in line with international best practices.

Overview and Historical Legacies of the Russian System At the time of the fall of communism, information on land, buildings, and other improvements was managed by two different, independent agencies. The Land Committee (*Roszhcomzen*) managed national land information, while the Bureau of Technical Inventory (BTI), which was part of the Ministry of Construction, managed the information on improvements. Each institution used a different numbering system to identify land and improvement units. There was no system for consolidating information on the improvements located on a specific land parcel save for the address information in each inventory. The location of parcel boundaries under existing buildings was often not recorded.

The registration system inherited from the Soviet era remains virtually intact today, overlaid with new legislative requirements and organizations. The first change occurred in 1998, when the Registration of Rights in Real Estate law was passed. This law allowed the property rights provided by the Civil Code of 1991 (amended in 2001) regarding rural and urban land and improvements to be registered and protected in the Unified State Register of Property (EGRP) administered by the Ministry of Justice (see figure 5.4, bottom rectangle). In 1994 the land and improvement registration agencies were administratively consolidated to become the State Cadastre of Real Property under the Ministry of Trade and Economic Development (MTED). The land committee is now called the Unified State Register of Land (EGRZ), and the BTI is renamed the Unified State Register of Capital Construction (EGROKS), as shown in the upper three rectangles of figure 5.4. In 2007 the law about the Cadastre of Real Estate Objects was passed. It became effective in March 2008 and retroactively provided the legal basis for this reorganization.

Complicating matters further, the registration of rights is not mandatory under the 1998 registration law. Furthermore, there is no automatic data transfer of information from MTED to EGRP. Essentially, registration is conducted at two separate levels. At the first level, there are no operational links between the land registration registry (EGRZ) and the parcel improvements registry (EGROKS), or between either of them and the EGRP. Furthermore, because the two first-level registration agencies (EGRZ and EGROKS) do not share common ID numbers, buildings cannot be located on a specific land parcel.

Figure 5.4
Russian Registration System, 2008



Any registration of property rights in EGRP, and thus the transfer and consolidation of data from EGRZ and EGROKS into EGRP, must be driven by an owner who is intent on having the property registered. Without the active role of the owner, there would be no unified registration system in Russia today because such registration is not mandatory. The system is thus driven by its clients.

In practice, despite the 1998 law that established a unified cadastre, to the extent owners do register their properties, they tend to register buildings and land rights separately rather than in the new consolidated system. This is in part because of the bureaucratic battles to control the fees from registration that occur between the land registry (EGRZ), the improvement registry (EGROKS), and the integrated registry (EGRP). This situation is also a result of the multiple bureaucratic rules and changes in business processes that have been complicating the process since 1991. Both EGRZ and EGROKS have been privatized and operate as state monopolies at the *rayon* and municipal levels and are aggressive in protecting their respective registration businesses. Each registration unit has now developed its own database structure and software. Each also supports a parallel paper structure because the legal framework does not recognize rights registered in electronic form.

Additional factors that favor maintenance of the old system include the mandatory purchase of an expensive improvement passport from EGROKS in order

to activate the unified registration system. Also, people must waste considerable time waiting in lines to accomplish each step of the registration process.

Weak Demand for EGRP Registration from Residential Owners The bifurcated nature of property rights in Russia, stemming from the Marxist view that land has no value, is another reason that owners of residences typically do not register their properties in EGRP. An owner of an apartment (the main form of ownership of residential property in Russian cities) typically has no defined land rights and hence has no reason to register anything in EGRZ. For that reason, and also because existing properties already have a passport in EGROKS, it is much simpler and far less expensive to simply register the sale and purchase transaction in EGROKS. Hence, there is little demand for registration in EGRP by residential owners. The only exception is the ownership of dacha property, which does include land rights.

Weak Demand from Urban Landowners and Developers Urban landowners are a potential source of demand for the EGRP unified registry. This demand is muted, however, because most urban land available for business development remains in state or municipal ownership. While the public ownership of the land per se is not of particular concern, the problem is that most of this publicly held property has not been registered in any registry (Butler and Khakhalin 2005).

Furthermore, much urban land in Russia is difficult to privatize because there are too many right holders delineated by past laws (see figure 5.3 and the earlier discussion of the anticommons problem) and most city land has never been divided into parcels and linked to the improvements constructed thereon. It is thus common to find many buildings on the same land parcel or one improvement on a parcel that is not economically efficient, in other words, that is much too large. These factors cause uncertainty for urban developers.

OTHER IMPEDIMENTS TO LAND REFORM

The Land Code of 2001 and Local Land Use Regulation The revenue structure of local government is mainly supported by land rents. Without a clear idea of how this revenue can be replaced, local governments lack motivation to carry out land reforms and instead undertake activities that preserve the current system. For example, the Land Code of 2001 regulates land use at the local level and provides for ownership of land by legal entities and persons for housing, industry, trade, and services. This law authorizes zoning and appears to put in place a reformed system by which developers can move forward with projects based on rights to land provided for in the Civil Code, rather than relying on the previous city-initiated and potentially revocable rights to land. Unfortunately, the 2001 Land Code confuses the issue regarding construction upon and use of land without a rigid use (the zoning approach) and the site-specific approach

inherited from the past. Under a zoning approach, the legal status of the land is clear: a developer that buys zoned land can secure financing and begin construction of a permitted use without further government action.⁹ If a use subsequently becomes obsolete, it can be changed as long as the new use is permitted by the zoning regulations. Under the site-specific approach, the developer must pick a parcel and then complete construction of a predefined use before the municipality will transfer the ownership of the lease right to the developer. The developer does not choose the use. More importantly, if there is a future change in use, the land parcel must be legally redefined, and a new contract with the city must be made to permit the new use. This scenario carries the risks of financial loss, potential corruption, and lack of construction financing options. Unfortunately, the Land Code provides for both zoning and site-specific planning without resolving the conflict between the two approaches. This lack of clarity has led a few cities to embrace the zoning approach while most other cities, including Moscow, have continued with the site-specific approach.

Real Estate Finance Real estate finance in Russia is also problematic. In the formal banking sector, there is relatively little lending to developers who wish to develop residential properties. Commercial lending is complicated by low loan-to-value ratios and demands for equity participation by banks. Residential development outside the major cities is usually done via cooperatives organized by the developer. This process requires the ultimate owner of an apartment to contribute to the cost of construction by prepaying for the unit before construction begins, or by contributing periodic payment as construction progresses. The Russian banking sector does not act as an efficient conduit for collecting personal savings to be channeled into productive real estate investments. Furthermore, products such as equity loans that would allow capital to be taken out of real estate and be put to a better use do not yet exist in Russia. Thus, capital is trapped in real estate and unavailable to fund other uses that could accelerate economic development.

The Property Tax System The current property tax system is also problematic and has a dampening effect on the demand to develop urban land. There are three types of property taxes in Russia today: a tax on land, a tax on business assets, and a tax on personal property (apartments, garages, and cars). When a developer considers construction on a privatized parcel of land, there is uncertainty about the ultimate land tax burden as compared to the current land rent. This is because leases are based on current use and the land tax is based on the current market value of the land put to its highest and best use (cadastre value). If the development is residential, the personal property tax on the apartment house

9. Building or other permits may be required, but they do not relate to the use of the property.

would be based on inventory cost or original cost, which in this case is current construction cost. The tax would thus be much higher on a new apartment than on a similar apartment built 20 years ago, even though the market value of the apartments in the new and old complexes may be close to the same. The business asset tax, which is now based on the current value of the real estate of a new enterprise, could be considerably higher than that on a similar but older enterprise because of the new improvement housing the new plant. Disincentives to build new facilities are thus built into the tax structure.

RECOMMENDATIONS TO IMPROVE THE RUSSIAN REGISTRATION SYSTEM

Four reforms are needed to improve the current registration system: (1) land and buildings should be considered as a unit; (2) a single identifier should apply to the parcel and the buildings erected thereon; (3) electronic records should be as valid as paper records for title purposes; and (4) land use regulation should move to a zoning scheme.

The first two reforms are the most important. Currently, the land registry, EGRZ, and the improvement registry, EGROKS, use a classifier of administrative territorial division (KLADR) that identifies land and improvement information down to street level. When records from EGRZ and EGROKS are consolidated in EGRP, a record number is assigned that uses the date of registration and the book and page number of the current registration book. This system severely complicates the title search process that would be needed, for example, to verify title and encumbrances to support a viable mortgage system. A new Russian classifier of municipalities (OKTMO), which has been under development by the Unified State Cadastre Agency since 2004, provides identification to the parcel level. If it were adopted by the EGRZ, EGROKS, and EGRP to identify land and improvement on the land, quick title searches at EGRP by developers, banks, and buyers and sellers of real estate would be possible. Use of this single identifier would also allow for wide public access to the data.¹⁰ Further, integrated registration would facilitate the resolution of disputes and reduce government liability for inaccurate information on property rights in the EGRP registry.

Providing for property rights to be legally recorded electronically rather than just on paper documents would facilitate the automation of EGRP using uniform data formats and a common software platform operating throughout Russia. This could provide the technical basis for federal, regional, and local authorities

10. Laws would need to be changed to allow public access to real estate data; currently in Russia only parties interested in a particular land plot or improvement may have access to the data.

to move from a client-based system to a transaction-based system, improving the administration of local revenue generation and intergovernmental revenue sharing.

Finally, by eliminating the urban planning legacy of administrative and site-specific land use decisions that carry high transaction costs and instituting a rules-based zoning system, as well as replacing the existing property tax system with a transparent, predictable, and consolidated tax on real estate, cities would have the motivation to undertake land reforms. They would not be concerned with lost city income and/or the need to protect a large group of special interests who currently may prefer a titling system that lacks clarity.

VELIKY NOVGOROD AS A MODEL FOR REFORM

A model for these recommended reforms was implemented in Veliky Novgorod (Novgorod the Great) as a by-product of a tax experiment that began in 1996. This city now incorporates many of them in its legal and fiscal cadastre.

In July 1997 an enabling law was passed authorizing Tver and Novgorod to establish legal/fiscal cadastres and introduce a consolidated tax based on real estate—that is, on land and improvements together. The weight of the base was to be market value, and the taxpayers were to be physical persons and legal entities possessing the rights of use or ownership of real property. A computerized, parcel-based legal/fiscal cadastre that defined real estate as land and improvements together identified by a unified property record number was implemented to support tax administration. The historical site-specific land use allocation system was replaced by a rules-based market-oriented zoning system, and data on permissible uses were included in the cadastre. Currently, there are more than 260,000 real estate records in the electronic fiscal/legal cadastre. Registration and transfers of property are done at the Novgorod Unified State Register of Property (EGRP), and the records held at EGRZ and EGROKS are linked electronically to the corresponding EGRP records. In part because of the complete listing of properties made possible because of this reform and the use of transparent valuation methods, over 30 percent of Novgorod's municipal revenue now comes from the property tax, as compared to an average of 8 percent for all other municipal governments in Russia.

It is not clear how easily and how quickly this model could be extended to the other 170 cities in Russia. Veliky Novgorod has a long history of local democratic rules that were established well before the start of the communist regime. Elsewhere the current bureaucratic mindset is firmly locked into the site-based planning system of the Soviet era, and there appears to be little desire for change. This is evidenced by the attitude of many central government officials who continue to resist reforms that would encourage a stronger real estate market. Yet in spite of this inertia, and with Veliky Novgorod as a model, the federal government has embarked on a large new initiative that involves the Federal Tax Service, the State Cadastre of Real Property, the Federal Registration Service, municipal gov-

ernments, and the private sector. The object is to develop a cadastral mass valuation system for the Russian Federation and to test it first in four oblasts: Kaluga, Kemerovo, Samara, and Tver, after which the system will be implemented in 25 of the 77 territorial tax offices. This project is a promising indicator that the Russian government, at least in some branches at the federal level, is recommitted to moving to a market-based property tax system and to the complete registration of all real estate assets.

Conclusions: Known Unknowns for the Third Decade of Transition

Given the specific path dependence of Russian institutions, success in the transition toward a market-oriented real estate economy is dependent on four factors: technology, laws/legal framework, institutions, and the macro economy. Russia's current status, based on the authors' latest 2008 observations in the country, is that, in terms of technology and the macro economy, conditions in Russia have improved significantly and the country is poised to move forward. In working on property registration projects and real estate market development, Russian counterparts are every bit as savvy and up-to-date as experts in the West. Discussions with Russian colleagues indicate that modern real estate information systems could be quickly implemented, given the necessary political support at the federal level. It is clear that information technology is not an impediment to development of a market economy in real estate.

Likewise, until mid-2008 Russia's macro economy was doing well, thanks to high commodity and energy prices. Conditions have changed markedly due to the sudden drop in energy prices in the fourth quarter of 2008, likely resulting in a slowing of growth in 2009. Oil- and gas-producing nations, including Russia, will likely take steps to manage output to keep prices at a level that will provide the liquidity needed for economic growth and expansion. Problems will arise in the future if Russia's economy remains overly dependent on resource extraction, but for now budgets are flush, thus relieving some financial pressure and giving some room for flexibility and experimentation with market methods both at the federal and the local levels.

Conditions are more problematic at the legal and institutional levels. As noted, registration of rights to real estate objects is not mandatory, a situation that should be remedied. In addition, the law should provide for electronic substitutes for paper records. This will facilitate transaction-based legal and fiscal cadastres. A further need in the legal framework is abolition of site-specific land use requirements and their replacement with zoning schemes along the lines developed in the West. This will give developers and owners greater flexibility in using their properties. Concomitantly, computer-assisted mass appraisal (CAMA) systems based on market valuation should be developed to support a modern property tax. These latter two changes will facilitate the highest and

best use of land resources in Russian cities, thus raising property tax revenues for local budgets and stimulating the development of efficient land and property markets across cities.

In terms of institutional development, a distinction should be made between the federal government and governments at the local level, which are tellingly called “subject governments.” The uncertain registration situation at the federal level described earlier should be resolved so that property owners know where and how they should register their properties. Infighting among registration offices should likewise be curtailed and a more customer-oriented approach developed. At the municipal level, there is evidence that local governments are beginning to see the benefits of following the Novgorod model in order to increase revenues. Diffusion of the Novgorod model to other municipalities should be encouraged. The current registration project sponsored by key federal ministries and agencies suggests that institutional barriers and perverse incentives are on the decline. As the results of the initial four-oblast registration project are evaluated and other cities are invited to replicate those efforts, the diffusion of international best practice in real estate taxation and management will spread across the Russian Federation. This will not be a rapid process at first, but diffusion can be steady and successful with the proper municipal involvement. If these legal and institutional changes are made, significant changes in the development of real estate markets can be expected.

Russia will soon enter its third decade of transition. Dmitry Medvedev, who was inaugurated as president of the Russian Federation in May 2008, is a lawyer by training and has declared that strengthening the rule of law is one of his top priorities. This could lead to a better environment for improving the institutions of real estate markets across the country. However, the outcome will result from the interplay among federal agencies, the demand for registration services, and better land use regulation at the local level. After the period of government recentralization during the two terms of Vladimir Putin, there appears to be strong interest among local governments to improve their fiscal autonomy, which could broaden nationwide support for market-oriented real estate reforms and a better registration system.

The Russian government’s current economic objectives are to consolidate the macroeconomic successes of recent years, to maintain stable growth, and to widen, diversify, and internationalize the economy. These goals imply structural changes that are urban based: diversification into new industrial and services activities, expansion of the small and medium enterprise sector, sustained productivity increases, and a broadly based opening to the international economy. This strategy requires a sound real estate sector operating in revitalized cities because real estate costs rank second only to labor costs for service firms and small and medium enterprises (SMEs). The opportunities for growth are there because the SMEs’ share of GDP is extremely low by international standards, less than 15 percent in 2007. A faster pace of development of the institutions of urban real estate markets will reduce a major constraint on the diversification of urban economic activities. This

urban outcome, however, is not a foregone conclusion, as Russia may continue to depend heavily on its energy and natural resources and fail to develop a more broadly based economy.

APPENDIX

Table 5.5

Timeline of Land- and Property-Related Laws (and Selected Events) in Russia, Eleventh Century to Present

Date/Year	Name of Legal Document	Description
Eleventh century	The Russian Law, short version	"First great codification in Rus" (Weickhardt 1993, 666)
Twelfth century	The Russian Law, expanded version; codification of Russian law	
1280 or earlier	Court Law for the People	Maybe a code of laws or maybe a "set of moral guidelines" (Weickhardt 1993, 667)
Fourteenth and fifteenth centuries	Pskov Judicial Charter	Code of Laws
Fifteenth century	Novgorod Judicial Charter	Code of Laws
1497	Muscovite Code	Code of Laws
1550	Muscovite Code	Code of Laws
1649	<i>Ulozhenie</i>	Code of Laws
1729	Chancery of Confiscations	Kept records of lands confiscated by the czar
1785	Nobility Charter of Catherine the Great	"marks the beginning in Russia of private property in the true sense of the word" (Pipes 1994, 530)
1835	Codification under Nicholas I	Code of Laws
3 March 1861	Emancipation Manifesto of Alexander II	Abolished serfdom in Russia
14 December 1893	Legislation	Confirmed that peasant allotments were part of the system of administration of peasant estates; prohibition on alienation of allotment land
1901	Special Conference on the Needs of Agriculture	Conclusion: "Commune was the principal obstacle to agricultural advancement" (Powelson 1989, 117)

(continued)

Table 5.5
(continued)

Date/Year	Name of Legal Document	Description
9 November 1906	Decree "On additional regulations for the implementation of the law on peasant land ownership and land use"	Households taking title to land could not leave their villages
1 January 1907	Law canceling redemption debt	Abolished the obligation of peasants to compensate nobles for the land they acquired upon abolition of serfdom
14 June 1910	Law "On Peasant Ownership"	Reaffirmed that transfer of land held by (peasant) individuals was controlled by 1861 legislation
1911	Land Organization Statute	Codified previous decrees; provided for division and enclosure of communal land among individuals
9 November 1917	Bolshevik government organized	
19 February 1918	Land nationalized	
Spring 1921	New Economic Policy	
30 December 1922	USSR came into being	
27 December 1927	End of New Economic Policy	
1 October 1928– 31 December 1932	First Five-Year Plan	Collectivization begins
1936	Stalin's constitution	
11 March 1985	Gorbachev becomes general secretary	
October 1985	Gorbachev announces <i>perestroika</i> reform plan	
23 November 1990	Law on Land Reform of the RSFSR	
November 1990	Law on Peasant Farms	
December 1990	Law on Property in the RSFSR	
December 1990	Law on Enterprises and Entrepreneurship in the RSFSR	
April 1991	Land Code of the RSFSR	
August 1991	Independence of Baltic states recognized by the Soviet Union	
July 1991	Law on the Privatization of Housing Stock	

Table 5.5
(continued)

Date/Year	Name of Legal Document	Description
25 December 1991	Gorbachev resigns; USSR dissolved	
27 December 1991	Presidential decree "On Immediate Measures for Implementation of Land Reform"	
March 1992	Government resolution "On the Course and Development of Agrarian Reform"	
25 March 1992	Decree 301 "On sale of land plots to citizens and legal entities within privatization of state and municipal enterprises"	Permits enterprises to purchase land under their facilities
14 June 1992	Decree 631 "On approval of the procedure for land plots sales within privatization of state and municipal enterprises, extension and development of the premises of the said enterprises, as well as those allocated to citizens and their associations for business activities"	Permits purchase of land under privatized enterprises
23 December 1992	Law "On the Right of RF Citizens to Privatize and Sell Land Plots Designated for Subsidiary Farming, Gardening and Individual Residential Construction"	
September 1992	Government resolution "On Procedures for Privatization and Reorganization of Enterprises in the Agro-Industrial Complex"	
27 October 1993	Presidential decree 1767 "On Regulation of Land Relations and Development of Agrarian Reforms in Russia"	
11 December 1993	Decree 2130 of 1993	Registration of documents affecting rights to land in the RF Committee for Land Resources and Land Management

(continued)

Table 5.5
(continued)

Date/Year	Name of Legal Document	Description
December 1993	Constitution of the Russian Federation	
April 1994	Government resolution "On the Practice of Agrarian Transformation on Nizhniy Novgorod Province"	
July 1994	Government resolution "On Agricultural Enterprise Reform Allowing for the Experience in Nizhniy Novgorod Province"	
22 July 1994	Decree 1535 "On Main Provisions of the State Program of Privatization of State and Municipal Enterprises in the Russian Federation after July 1, 1994"	Permits purchase of land under privatized enterprises; apparently permitted a price of from 20 to 200 times the land tax
1994	Decree 478 "On Measures for Ensuring Stable Revenues to the Federal Budget from Privatization"	Regulates the purchase price of land; uses land tax rate and permits a price of five times the rate, with no ceiling
October 1994	Civil Code	
1 February 1995	Government resolution no. 96 "On Procedures for Realization of Rights of Owners of Land and Asset Shares"	
December 1995	Law on Agricultural Cooperation	
March 1996	Presidential decree "On Realization of the Constitutional Rights of Citizens Concerning Land"	
1996	Decree 1368	Regulates the purchase price of land
16 May 1997	Decree 485 "On Guaranteeing Real Property Owners the Acquisition of Ownership in Land Under Their Property"	Regulates the purchase price of land
26 November 1997	Decree 1263 "On the Sale or Lease of Land Parcels to Citizens or Legal Entities Located in Urban and Rural Settlements for Construction Purposes"	

Table 5.5
(continued)

Date/Year	Name of Legal Document	Description
30 January 1998	Law on State Registration of Real Estate Rights and Transactions	
7 May 1998	Resolution no. 2 "On Approval of Procedures for Organization of Sales (Auctions, Tenders) of Lands in Urban and Rural Settlements, or Lease of Them, to Natural and Legal Entities"	Procedures for sales
1999	Presidential decree no. 632	Right of local self-government to set their own land privatization procedures and terms
1999	Government resolution no. 1024 "The Concept of Public Property Management and Privatization in the Russian Federation"	
16 April 2001	Federal Law no. 45 implements chapter 17 of the Civil Code	
July 2001	Law on Delimitation of State-Owned Land	Marked the start of the process of allocating ownership rights to state land among the federal, regional, and municipal governments
25 October 2001	Land Code signed into law	
25 July 2002	Law "On the Circulation of Agricultural Lands" signed into force	Implements chapter 17 of the Civil Code with respect to agricultural lands
2004	Federal Registration Service created	
2005	Registration function transferred to Federal Registration Service	

Sources: Analysis of Russian laws by the authors and sources cited in the Appendix.

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