



**ADMINISTRATIVE BARRIERS TO INVESTMENT WITHIN
SUBJECTS OF THE RUSSIAN FEDERATION**

PERM OBLAST

**Study of Administrative Barriers to Investment
in Land and Real Estate in the
Perm Region**

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June 30, 2003

A Report to the Foreign Investment Advisory Service (FIAS),
a joint facility of the International Finance Corporation
and the World Bank

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EXECUTIVE SUMMARY

Issues:

- There is concern about monopolization of the land and real estate market, hindering creation of new businesses and the exercise of property rights by existing businesses.
- According to businessmen, there is an "information gap" which affects mostly small businesses and private entrepreneurs, who cannot afford to hire experts to provide the necessary information and guide them through the permit and other regulatory procedures. While the information gap was raised primarily in relation to laws and regulatory procedures, which are said to change frequently and in a non-transparent way, the unavailability of information is also evident in real property relations.
- There is a lack of Transparency and Clarity in Land Ownership Procedures.
- Cumbersome Land Allocation Procedures.
- There is a prevailing view that the lease deals for city-owned premises are one-sided in favor of the city and place unacceptable risks on lessees, including arbitrary rent increases and the ever present threat of termination.

Based on the consultants' recent inquiries in Perm, and a review of the available evidence, there is good reason to believe that the perceptions of the business community as described above are correct in many respects, or at least that there is a significant core of truth which should be addressed.

Objectives:

- Develop a regional strategy on management of state and municipal real estate assets.
- Encourage further divestiture of state and municipal land and creation of a private land market in the region.
- Take steps to increase the supply of land and real estate facilities in the region available for formation of new businesses and expansion of existing businesses.

- Take steps to increase demand for land and real estate facilities by greater dissemination of information, more transparent allocation procedures, and reducing the risks and costs of investment.
- Implement a system of performance indicators and performance monitoring to periodically assess progress towards achieving the objectives and implementing the main tasks.

Constraints:

1. Delayed division of ownership of land plots among state, regional and municipal governments.
2. Inadequate cooperation by federal authorities in the land privatization process.
3. Complex and uncertain land privatization and allocation procedures.
4. Poor co-operation between the registration, land cadastre and technical inventory services.
5. Lack of accessible property inventory.
6. Lack of a single window investment promotion agency to assist potential investors with real estate location issues.
7. Long delays in obtaining land and construction rights.
8. Infrastructure deficiencies and difficulty obtaining technical conditions.
9. Competitive procedures (auctions or tenders) for allocation of land and property have not yet been implemented.
10. Outdated city planning.
11. Shortage of land suitable for construction; inappropriate center city land uses.
12. High and inelastic housing prices.

Opportunities:

- The new Land Code and other recent Federal legislation.
- Supportive National Government.

- Supportive regional and municipal administrations.
 - Relatively low land privatization prices.
 - Active regional assistance to the land privatization process under Article 36 of the RF Land Code.
 - Commencement of competitive auctions/tenders of land plots.
 - Ongoing work on new municipal planning and land use regulation in Perm city.
 - The Perm city "One Window" facility for land use and construction permits
 - Creation in 2002 of the special "targeted budgetary fund for housing development.
 - Intensive dialog between the regional and city authorities and business community on the issues of real estate market development.
 - Relatively high economic potential of the region.
 - The draft Administrative Barriers Action Plan.

Recommendations:

Asset Management

1. Develop a regional strategy on state ownership of real estate assets.
2. Prepare the strategic inventory and plan for regional real estate assets.
3. Create a regional working group or steering committee on state real estate.

Supply

1. Audit all outstanding regional or municipal acts for allocation of land rights and terminate those that have exceeded the time limits; prohibit multiple consecutive renewals of preliminary allocations of land sites.
2. Consider creation of an independent urban development agency empowered to designate, plan, prepare and sell land plots for new development.
3. Implement a pilot program for preparation of serviced land sites for industrial facilities.
4. Acceleration of applications for privatization of land parcels under article 36 of the RF Land Code.
5. Accelerate privatization, consolidation, and liquidation of inefficient regional and municipal enterprises.
6. Bring land and premises rents to market levels and eliminate land rent concessions for enterprises.

Demand

1. Complete and make widely available an inventory of state and municipal real property.
2. Create a "single window" investment promotion agency with responsibility for maintaining an inventory of state and municipal property available for development, or redevelopment, and providing advice and assistance regarding real estate matters to potential investors.
3. Improve terms of purchase for land privatization and sales of long term lease rights by offering an extended payment schedule and other options.
4. Implement competitive procedures for allocation of land rights.
5. Implement transparent procedures for non-competitive allocation of land rights.
6. Improve the terms of leases for municipal premises.

Time and Costs

1. Complete the zoning program in Perm city and accelerate implementation of land zoning in the remaining municipalities of the region.
2. Complete and refine the "one window" land allocation and permit facility in Perm City; "roll out" the model to smaller cities in the region through appropriate seminars and technical assistance sponsored by the regional administration.
3. In refining the concept of the single window through the current experiment in Perm city, the city should:
 - (a) install "permit tracking" software systems which highlight roadblocks and bottlenecks;
 - (b) implement performance standards for issuance of permits;
 - (c) hold officials accountable for performance standards.
4. Audit the land allocation and permit issuance procedures to identify bottlenecks and establish performance base lines.
5. Establish reduced construction permit requirements for small projects.
6. Deal with issuance of technical conditions and terms of connection to utility services under the region's authority to regulate the provision of public services.
 - (a) Require transparent publication of information concerning service lines and connection points and general technical conditions for municipal districts.
 - (b) Establish time limitations for issuance of technical conditions.
 - (c) Establish standards and formulas for connection fees and charges.

Performance Monitoring

It is highly recommended that the regional and municipal administrations identify quantitative indicators of the performance of both real property markets generally and government service providers, and implement a monitoring system to periodically assess progress. The key indicators would draw on information available from government agencies and registries to assess levels of supply and demand in the market as well as progress toward achieving the objectives identified in this report. Indicators can help to assess the management performance of certain government agencies responsible for carrying out policy reform in the real estate sector. Accordingly, attached as Appendix II to this

report is a set of tables which suggest the types of indicators that would be *minimally necessary* for assessing progress in real estate market development, elimination of administrative barriers to investment in real estate, and, generally, improving the investment climate in this sphere. Much of this information is presently available from various federal, regional and municipal agencies. Examples of relevant data already gathered within the state statistical survey include:

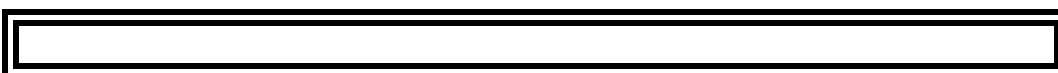
It needs to be stressed that the development of the land and real estate market and the associated investment activities in this sector are far ahead of the development of the informational support of these processes. Without quantitative records of changes, neither timely regulation by the regional and local authorities, nor adequate response of the private sector of the economy is possible. Therefore, any attempt to bridge this gap, including the proposed project of organizing regional/municipal monitoring of land and real estate, merits priority attention and the full support of those concerned with the economic development of the Perm Oblast.

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It is acknowledged now at all levels of the Russian political establishment that creation of an attractive investment climate is to a significant extent obstructed by an inadequate and unclear legislative and regulatory framework for allocation of land into private ownership; uncertain land rights; non-transparent procedures for issuance of land use and construction permits; and inadequate mechanisms for settling disputes and balancing public and private interests in the field of land use and town-planning. To assess the extent of these problems in the Perm Region the consultants conducted a mission to Perm for the Foreign Investment Advisory Service (FIAS) of the International Finance Corporation from May 19-23, 2003. During the mission the consultants met and held discussions with regional and municipal officials, as well as representatives of private sector businesses and organizations. The purpose of the mission was to identify policy initiatives that may be taken by the regional administration, with the cooperation of the Perm City administration, to improve the use of real property as a regional asset and a resource for attracting investment. This report is the product of that mission.

Issues:

The main investigations of the mission related to various issues raised in a series of discussions conducted by FIAS with regional and local officials and representatives of the Perm business community on two separate occasions (April 15-16, 2002; February 4, 2003). Issues raised in the course of those discussions included the following:

- There is concern about monopolization of the land and real estate market, hindering creation of new businesses and the exercise of property rights by

existing businesses. It is alleged, for example, that a small number of enterprise groups - the former "construction kombinats" of the Socialist era - control the land allocation process and access to desirable building sites, as well as access to vacant premises and the real assets of bankrupt unitary enterprises. These same interests allegedly have stalled implementation of competitive and transparent land allocation mechanisms such as auctions and tenders, preferring the less competitive and transparent procedures of the past. Leading the list of "administrative barriers" identified in the discussions with the business community were (1) the high rents and non-transparent procedures for allocation of business premises, and (2) non-transparent, slow and complex procedures for allocation and registration of land sites.

- According to businessmen, there is an "information gap" which affects mostly small businesses and private entrepreneurs, who cannot afford to hire experts to provide the necessary information and guide them through the permit and other regulatory procedures. While the information gap was raised primarily in relation to laws and regulatory procedures, which are said to change frequently and in a non-transparent way, the unavailability of information is also evident in real property relations. Noted in particular were lack of information provided by authorities on availability of land sites, buildings and premises, and the practice of allocating real property assets behind closed doors in closed transactions to which most businesses did not have access. Also noted was the absence of open and competitive offerings of real estate assets, which rely on open information. The failure to provide information on state and municipal real estate assets was viewed as supporting monopolies in land and real estate held by the government and a handful of favored enterprises.
- The participants indicated that the lack of transparency and clarity in land ownership procedures is of great importance due to a number of factors, including:
 - An inadequate legal and regulatory framework at the federal level.
 - Existence of the same problems at the regional level, which the participants tend to attribute to the local administration.
 - Lack of communication between government agencies and structural divisions in charge of coordination in real estate relationships.
- Business people allege that the land allocation procedures are cumbersome, expensive and uncertain, and that investment in construction carries a substantial risk of loss. The process has been characterized by complex and ambiguous rules which frequently change in the course of

project planning and development. The region is perceived to be unprepared for implementation of the new Land Code procedures regarding land privatization and allocation of land plots for new construction. Urban planning documentation is inadequately developed (including utilities development plans), and there are no transparent zoning schemes. Obtaining the right to connect to utility services is time consuming and frequently the costs amount to legal extortion. There is some perception that the situation is improving, but there nevertheless remains a perception of corruption and arbitrary bureaucratic decisions in the land allocation and project approval process.

- Lease of municipal property was found to be very important for many businesses. There is a prevailing view that the lease deals for city-owned premises are one-sided in favor of the city and place unacceptable risks on lessees, including arbitrary rent increases and the ever present threat of termination. Lease durations are considered to be too short and uncertain, considering the practically unconstrained right of the city to increase rents, for tenants to risk investment in the premises. There are suggestions that the state and municipalities, including their unitary enterprises, are managing their property badly, leading to artificial shortages of space in the market and artificially high rents and utility costs.

Based on the consultants' recent inquiries in Perm, and a review of the available evidence, there is good reason to believe that the perceptions of the business community as described above are correct in many respects, or at least that there is a significant core of truth which should be addressed.

Objectives:

To address these issues, the consultants recommend that the Regional Administration establish several policy objectives, as follows:

- *Develop a regional strategy on management of state and municipal real estate assets.*
- *Encourage further divestiture of state and municipal land and creation of a private land market in the region.* Currently the land plots owned by individuals constitute 1.7 percent, and owned by legal entities – only 0.2 percent of the total area of the Perm Oblast. Further land privatization offers secure land rights and encourages investment in improvements to the land. Secure land rights may also attract the type of investor that insists on land ownership, which may include many foreign investors. Over the longer term, private ownership of land and free transferability in

a private market encourages conversion from less valuable to more valuable land uses, and densification of development. More secure land rights and increase in land ownership may also encourage more mortgage lending for investment in improvements. Finally, dealing with privately owned land decreases the time and complexity of the land allocation and development procedure for investors.¹

- *Take steps to increase the supply of land and real estate facilities in the region available for formation of new businesses and expansion of existing businesses.* Increases in supply of land and real estate facilities will act as a control on increasing prices. Greater availability of a broad range of land and real estate options and lower costs can attract investment.
- *Take steps to increase demand for land and real estate facilities by greater dissemination of information, more transparent allocation procedures, and reducing the risks and costs of investment.* Steps to achieve these objectives include development of information resources, implementation of competitive procedures, simplification of procedures for issuing land use and construction permits, and improvement in the lease terms for municipal property.
- *Implement a system of performance indicators and performance monitoring to periodically assess progress towards achieving the objectives.*

Constraints:

Constraints on achieving the objectives fall into two categories: those which are affecting most or all regions in Russia today and which arise mainly from national policy, and those which may be attributed primarily to local action, or lack of action, as the case may be. In the first category are:

1. Delayed division of ownership of land plots among state, regional and municipal governments.

¹ For example, the international cereal joint venture "CPW" which recently located in the Perm region found it more efficient to acquire an entire existing Russian company, and its property rights, rather than to deal with the local administrations to locate land and facilities for new construction. Whether this investment would have been made in Perm if new construction were the only alternative is a reasonable question to ask. This may be a point in negotiations with Rezidor SAS concerning the Country Inn project which are under way now. It was also mentioned that several construction companies from Europe and Turkey expressed their interest in participating in real estate development projects in Perm, but mainly as contractors and not as strategic investors. This may be an indication of the lack of guarantees provided in the form of secure land rights.

The division of land ownership among the various levels of government started only last year and no strict deadlines for this process are set by the federal Law.² The process is going very slowly and there are few incentives for the Federal government to accelerate the process. The City of Perm has resolved with the Federal and regional governments ownership of only 75 land plots, with the expectation that another 120 cases will be resolved in 2003. This is a remarkably small number, given the size of the city. In the estimation of City officials, as the result of division of ownership of land about 70 percent of the Perm city territory would be transferred into municipal property, but the process of defining of municipal land in Perm may take from 5 to 8 years longer. The main result of failure to complete the division is vague rules for current transactions with land which result in the federal and regional governments taking a large share of proceeds from municipal land sales, thereby lessening municipal support for land divestiture. Also, vague rules on the roles and authorities of various government agencies at the national and local level in the approval of land transactions also threaten bureaucratic delays and uncertainties regarding the validity of sales made under the prescribed processes.

2. Inadequate cooperation by federal authorities in the land privatization process.

Pending completion of the delineation of land ownership rights among levels of government, the Federal government has asserted the authority to approve all land privatization transactions under article 36 of the RF Land Code. In any event, the Federal authorities must approve privatization transactions involving former Federal enterprises, which comprise a large and important segment of the land privatization applications in the Perm region. Despite a strong policy in support of land privatization expressed in the RF Land Code, Federal authorities have thus far not demonstrated a willingness to accelerate the application approval process. Privatization applications which are processed and approved by Perm regional authorities in several weeks have languished for more than 6 months in the territorial center of the RF Ministry of State Property located in Nizhny Novgorod, and more recently at the central office of the RF Committee on Property Relations in Moscow. This experience has been the same for many regions of Russia.

3. Complex and uncertain land privatization and allocation procedures.

The list of documents which are required to be attached to the application for buy out of the land plot contains 10 points, including the cadastre plan. This list was valid before the Land Code was enacted, but should be reconsidered now, particularly taking into consideration the provision of Article 36 of the Land Code, which states that the absence of the cadastre plan is not a reason for refusal

² According to the Resolution of the RF Government #745 as of 10/25/2001 "On Adoption of the Federal Target Program "The Creation of the Automatic System of Conducting the State Land Cadastre and State Inventory of Real Estate Objects (2002-2007)"

to accept the application, and that the municipal bodies should provide this plan to the applicants within one month.

The Land Code differentiates the land plots allocated for development (art. 30) and for purposes not related to real estate development (art. 34). Article 30, concerning "the land plots allocated for development" touches upon the issue of land auctions, whereas Article 34, concerning "the land plots allocated for purposes not related to real estate development," does not refer to auction and the allocation procedure is not regulated at all in terms of in what cases land sites are allocated upon request and in what cases auctions are mandatory.

As far as the case of land allocation for real estate development purposes is concerned, the Land Code provides for mandatory auctions only when an "advanced approval of the objects' location" is not necessary and whenever the property rights (ownership) are sold. It is unclear why the land plots are not required to be allocated on competitive basis when an "advanced approval of objects' location" is necessary. Moreover, in this case the land plot may not be sold into ownership, but may be only transferred into lease or "permanent" use. This case seems to do little more than preserve intact the old mechanism of granting construction rights inherited from the Soviet administrative system of land use regulation. The Land Code thus leaves important gaps on the issue of direct and competitive allocation of land plots, and the issue that has long been awaiting a legislative solution.

4. Poor co-operation between the registration, land cadastre and technical inventory services.

The national system for registration of property objects is fragmented and a cause of inefficiency and unnecessary delays and expense in registration of property rights. As the Chief Registrar of the Perm Oblast pointed out, one of the serious constraints is that the data on land and improvements to land are maintained separately. Local agencies are making efforts to coordinate their efforts and electronic data bases, but there are limits on what can be done given the fragmented institutional structure and management.

In November 2002 The Perm Oblast Law "On the Oblast Target Program "The Creation of the Automatic System of Conducting the State Land Cadastre and State Inventory of Real Estate Objects (2002-2007)" was adopted. This law is directed, in particular, on the creation of the automatic system of real estate management, reforming and regulation of land and property relations, division of state property on land between the federation, region and municipalities.

In the category of constraints that are due primarily to local action or lack of initiative, and which may be addressed by policy initiatives, are:

1. Lack of accessible property inventory.

It appears that in the Perm region obtaining relevant information on the availability of land and other real estate facilities and their technical parameters is extremely difficult and solely the responsibility of the potential investor. Neither the region nor the city has a comprehensive inventory of real property which is made accessible to citizens and potential investors. This situation has led to allegations of lack of transparency in the allocation of public lands and real estate assets; too much discretionary authority in the hands of a small number of municipal officials; and a small and closed circle of land speculators and investors who have monopolized the best development sites in the region.

2. Lack of a single window investment promotion agency to assist potential investors with real estate location issues.

Neither the regional administration nor the Perm city administration has a “single window” to promote investment and assist prospective investors to find good business locations. Agencies that have access to information on land and real estate facilities lack the mandate and the skill to effectively promote investment, but are rather more reactive. Agencies which have the responsibility and skill to promote investment opportunities in the region and the city lack information about land and facilities. (A "single window" investment promotion agency should be distinguished from a single window permit issuing agency. The latter is being created at this time in Perm city, as discussed further below.)

3. Long delays in obtaining land and construction rights.

Times for acquisition of land rights in Perm City range from 1 to 1.5 years, and in some cases longer. This duration is relatively long in comparison with other cities studied in the FIAS administrative barriers study. Various factors are cited, but among the most important are inefficient management of the land allocation and permit processes, bureaucratic delays and lack of urgency on the part of public officials in dealing with land allocation and privatization applications. The City of Perm is now in the process of making wide ranging modifications to the processes, discussed further below, the results of which may not be seen for a period of time.

To be fair it must be noted that according to the officials of the regional Department on Architecture and Construction, with the exception of Perm city, the problem of long delays obtaining land and construction rights does not exist in the other cities of the region, which are much smaller and it is rather easy to find an appropriate vacant land site and the land allocation procedures may be quite quick and “informal”.

4. Infrastructure deficiencies and difficulty obtaining technical conditions.

As in many other regions of Russia, obtaining technical conditions and rights to connect to utility systems appears to entail long delays and high fees. There are complaints that there is lack of uniformity in the setting of infrastructure fees, which are often exorbitant and can be enough to make new construction economically infeasible. The deteriorated physical condition of local utility networks is responsible for only a part of this problem. Another part is the failure of regional authorities throughout Russia to develop new regulatory regimes for local monopolies that will assure acceptable standards of service at fair and reasonable costs.

5. Competitive procedures (auctions or tenders) for allocation of land and property have not yet been implemented.

Competitive procedures for sale of land have not yet been introduced in the Perm Region, though the first steps have recently been taken in Perm city, which has prepared a draft auction regulation and advertised the availability of 29 sites. Land allocation remains a closed process which is carried out by direct discussions between land developers and a small group of municipal officials, leading to allegations of favoritism.

6. Outdated city planning.

Municipal officials are hindered from quickly resolving applications for allocation of land rights because municipalities lack updated planning documentation, and therefore each case of land allocation must be considered as a unique case. Lack of updated planning and zoning regulations also prevent competitive land allocation procedures through auction and tender. Steps are under way in Perm city to implement a modernized planning and zoning regime, but resources are not available to carry this activity out quickly.

7. Shortage of land suitable for construction; inappropriate center city land uses.

There is a shortage of well located, serviced land sites. Practically all new development in Perm city is reuse of occupied land. A part of the problem appears to be the large amount of prime land occupied by dilapidated, low rise housing and underutilized industrial uses which would be better located further from the center. Finding suitable land sites is complicated by property rights and relocation issues. However, it appears that another main part of the problem is that most land sites suitable for development have already been allocated, allegedly to a small and closed group of development companies, which hold what is essentially an unlimited option on these sites despite the fact that they have failed to meet the contractual conditions of the initial allocation.

The consultants were advised that the Governor Tryutnev's vision of the city center is as the business and office center. He is very concerned with the fact that the existing land allocation procedures result in predominantly elite housing construction in the center of Perm, much of which remains unsold today because it is beyond the incomes of most Perm residents. Moreover, a short walk in the center of Perm shows that a number of industrial enterprises with smoking tubes are located next to the main streets and occupy significant parts of the most valuable territories of the city.

8. High and inelastic housing prices.

Housing prices are acknowledged to be among the highest prices relative to incomes in Russian cities. Most new construction by the private sector has been concentrated at the upper end of the quality and price range, and is not accessible to most citizens in need of new housing. For several years there has been a significant surplus of these high-end housing units on the market, but prices have not dropped, suggesting a lack of competition in the market. The lack of affordable new housing opportunities complicates the issue of freeing up well located land in the center for new investment in needed non-residential facilities.

Opportunities:

Despite this formidable list of constraints, there are significant factors supporting achievement of the objectives, which the consultants view as the core elements of a regional strategy. These include:

- *Land Code and other recent legislation.* There are several significant pieces of legislation which have been put into place in the past several years, including the *Russian Federation Land Code*, The Law "On Privatization of State and Municipal Property,"³ The Law "On Delineation of State Property on Land" and related normatives, Article 17 of the Civil Code dealing with civil transactions in land and real estate, the Law "On Turnover of Agricultural Lands," and The Resolution of the RF Government #808 "On Organization and Management of Public and Municipal Land Sales and Leases, adopted in November 2002. Much of this legislation is flawed in some respects and will probably have to be modified over time, but for the moment provides the most comprehensive basis to date for formulation of a regional policy on land and real estate market development.

³ Due to enactment of this Law in March 2003 a special Decree of the President of the Russian Federation as of 03.26.2003 N370 declared invalid nearly all the presidential Decrees that regulated the land buy out process at the previous stages of privatization development and contained a lot of ambiguities and inconsistencies between each other.

- *Supportive National Government.* The Government of the Russian Federation has issued several important policy statements and programs which clarify strategic intentions of the Government in implementing land and property reforms, support greater efforts to divest public real estate assets and to create private sector real estate markets, including the "Action Plan of the Government of the RF in the Sphere of Social Policy and Economic Modernization for 2000-2001," and *The Program of Social and Economic Development of the Russian Federation in Midterm Prospect for the Years 2002-2004*" which has specifically emphasized that the crucial element of formation of the real estate market should be finalizing of the privatization process of real estate objects by transferring⁴ land plots occupied by enterprises and commercial real property in private ownership of their owners, which means creating legally "unified" real estate objects. Moreover, *The Concept of Management of State and Municipal Property*, and well as other significant documents, are expected to be approved soon at the federal level.

- *Supportive regional and municipal administrations.* The regional and Perm municipal administrations have already begun several very promising initiatives to improve functioning of land and real estate markets. The most noteworthy of these include:
 - *Relatively low land privatization prices.* In November 2002 the Perm regional legislature lowered the prices for privatization of land under article 2 of the Federal Law "On Enactment of the Land Code of the Russian Federation". The purchase price for land plots now ranges from 8 times the local land tax per square meter in the largest city, Perm, to 4,8 times in the mid-sized cities⁵ of the region, to 3 times the land tax in the smallest localities.⁶ While not as low as in some jurisdictions (The Tomsk Region, for example, recently adopted a land buy out price of 5 times the local land tax, the lowest possible legal price), these prices are significantly below the maximums that could have been established, and relatively lower than prices in many other regions. This is a positive step.⁷ The effect of the lower prices were

⁴ Noteworthy, in all the subsequently adopted legislative acts the concept of an "ownership transfer" was replaced by that of a "buy out".

⁵ Including such cities as Bereznyaki, Chaykovski, Solikamsk the population of which ranges from 200 to 400 thousand.

⁶ Previously these coefficients were set correspondingly at the level of 17, 10 and 5 times the local land tax per square meter.

⁷ The pricing mechanism for land privatization is a matter of some controversy, being based on local land tax rates, which are notorious for favoring some types of enterprises over others, thereby

reflected in the submission of 150 new privatization applications in the value of 200 million rubles within a period of one month. Since the beginning of 2003 the regional administration has already approved over 60 applications for land privatization, comprising approximately 390 hectares.

- *Active regional assistance to the land privatization process under Article 36 of the RF Land Code.* The Regional Committee On Property Management has taken a strong role in supporting applications for enterprise land privatization from former regional and federal enterprises, providing technical assistance to enterprises in the preparation of applications and maintaining strong pressure on Federal officials in Nizhny Novgorod (the Federal territorial office) and Moscow to see that applications receive proper attention. The regional committee appears to be capable of processing applications quickly and effectively. (The consultant's received some indications that the Perm city administration was not dealing as expeditiously with privatization applications submitted by former municipal enterprises, but were not able to obtain relevant data to support this point.)
- *Competitive auctions/tenders of land plots.* While there have been no competitive auctions of land plots in the Perm region to date, Perm City has recently advertised the availability of 29 land plots for competitive tender, which is the first step required by the RF Land Code. Of the 29 advertised sites, only 6 received more than one expression of interest in response to the advertisement, and presumably these sites will be prepared for tender. While the City has significant work to do to establish the forms and procedures for the tender process, the important first steps have been taken. The Regional Committee On Property Management has also expressed the intention to prepare the necessary documentation and procedures to assist the smaller cities and towns of the region to conduct their own land tenders. Unlike most regions in which land auctions and tenders are prepared and held by local administrations, the Regional Committee On Property Management intends to create a specialized independent agency which will professionally conduct the marketing campaign and competitive sales.

creating price inequities among enterprises. Moreover, there are strong arguments made in some circles that any price for land privatization is too high, as the land was paid for when the enterprise was privatized at an earlier time. A complete discussion of whether land privatization prices are fair is beyond the scope of this report and it is not intended to endorse the prices in Perm as fair, but only to commend that fact that they are not as high as they could have been.

- *Municipal planning and land use regulations.* Pursuant to the provisions of the RF Urban Planning and Land Codes three main local laws have been elaborated in a package for the city of Perm for the first time in Russia, though not yet adopted. This package includes:
 - 1) The new Master Plan (produced by ENCO, research and design company from Saint-Petersburg in 2000-2001);
 - 2) Zoning Ordinance – the so called Rules of Land Use and Development (drafted by the Institute for Urban Economics in cooperation with ENCO);
 - 3) The Design Plan of the Historical Preservation Zones (ENCO).

The structure and the contents of the Master Plan differ from those usually produced in the Soviet system. It is less detailed and directive, and contains two main chapters: a) the strategy of the city development and b) ordered priorities for urban development activities. The Master Plan is still in the process of ecological and other "state review" and will be enacted no earlier than this autumn.

The Rules of Land Use and Development for the moment contain the basic principals of zoning, the procedures of land plots allocation and issuing permits, the list of zones and the lists of permitted uses and uses requiring special permits for each of the zone. The proposed ordinance does not contain the construction requirements and normatives, as well as standards concerned with environmental protection, water flood protection, historical preservation, etc. The draft zoning ordinance has passed through several public hearings and is still being improved.

The City Administration intended to adopt the Zoning Ordinance before the new Master Plan would be put into force, but then concluded that the Master Plan should be the first (until that, the corresponding chapters on historical preservation, water protection and other regulations are only addressed in the draft Zoning Ordinance). Although the Zoning Ordinance has not yet come into force, the City includes in the APZ⁸ a set of permitted uses, based on the Draft.

⁸ Specific document called "Architectural and Planning Task" which is still issued all over Russia for each land plot, assigned for development.

A main problem facing the city and the regional administration now is finding the resources to complete this work and extend its benefits to the other municipalities in the region.

- *The Municipal "One Window" facility for land use and construction permits.* In 2002 Perm City began implementation of a "one-window" facility for land site allocation and issuance of land use and construction approvals. A preliminary regulation has been in effect since that time which aims at (1) transparency, (2) streamlining the procedure, and (3) limiting the number of employees who must interact with the applicant. The regulation defines the required documentation and the application procedure, dividing the procedure into discrete stages and assigning time expectations for each stage.

City authorities acknowledge that this initiative was severely criticized at first. Entrenched interests preferred a less transparent approach to doing business, which is one of the problems, and others did not see much change, but rather the imposition of yet another bureaucratic structure on top of a system that needed more fundamental improvements. The initiative was perceived as superficial. Acknowledging the complaints, the responsible authorities say that they have listened and are making improvements as they go along. A new physical facility is being prepared in the City administration building, appropriate hardware and software are being investigated, and a next step is a comprehensive operating manual for staff. A rudimentary explanatory brochure is already available for the public on a web site. Perhaps most important, a new look at the underlying procedures is underway, and some beneficial changes have been made or are under development. The process for obtaining design approval on privately owned land has been simplified. Some steps in the land allocation process, for example the mayor's approval to commence design and survey work, a vestige of the Soviet era, has been eliminated. (See Figure 1) The City is still in the process of improvement of the "one window" procedure of land plots allocation and issuing of the construction permits. While much work remains to be done, these are important first steps and as one city official said, it was a decisive breakthrough just to write the procedures down in a transparent regulation.

- *In 2002 a special "targeted budgetary fund for housing construction development" was established* by the Decision of the Perm City Duma N 142. The Fund is formed from the following sources: the total amount of rent for the land plots allocated for the period of "research and design works;" total amount of receipts

from sale of municipal housing; total amount of gratis transfers of legal entities and physical persons on engineering and social infrastructure development according to the agreements of share financing; total amount of receipts from sale of real estate construction which was financed from the Fund; other sources. The resources of the Fund are aimed for financing the housing construction (particularly, for resettlement of citizens from municipal dilapidated housing); design, development and redevelopment of the engineering infrastructure providing the fulfillment of "technical conditions" concerned with design and construction of housing within the territory of the city of Perm.

We do not have the data on the amounts of these assets, or whether they are being used effectively but we can assume that being used effectively they may be substantial factor in reducing fees for "technical conditions" and reducing prices of dwellings.

- ***Intensive dialog between the regional and city authorities and business community on the issues of real estate market development.*** The Perm Oblast administration (Department for Property Management) registered a non-commercial partnership "Collaboration" aimed at work with the enterprises on assisting them in land privatization, asset management and explanation of the regional policy in the real estate sphere. In parallel, the largest Perm companies, together with real estate brokers and developers, formed a Council for Perm Real Estate Market Development which represents their collective interests in relations with the regional and municipal authorities. The leaders of the Council state that the initiatives and proposals of the business community are received with a positive attitude by public officials. For example, last year real estate brokers came across a problem of getting the permission to transfer the ground floors in multi-family housing into commercial used premises. The Council applied to the City authorities and this issue was quickly resolved .

The Perm real estate brokers are associated in a strong "Perm League of Realtors and Appraisers" which holds regular exchange of opinions with the regional and City leaders on the most acute problems of real estate market development in the Perm Oblast. Just a couple of days before the FIAS mission arrived in Perm such a meeting took place to discuss the terms and procedures of enterprise land sales.

Public hearings on the most important draft local laws have come into practice in Perm. Particularly, the draft Zoning Ordinance has

passed through public hearings for several times in the course of the last two years.

- ***Relatively high economic potential of the region.*** The Perm Oblast is strong in the oil and gas industry, machine-building, metallurgy, chemical and woodworking industries. Investments in housing construction in 2002 increased 47.6% in current prices over the level of 2001. The growth of deposits of citizens in the Savings Bank of Russia in the 1st quarter of 2003 was about 1 bln. rubles or twice as much as for the same period in 2002, and currently amounts more than 7 bln. rubles, or about one quarter bln. \$US. In the structure of expenditures of the citizens the share of purchase of consumer goods lowered and the expenditures on accumulation of savings and purchase of foreign currency considerably increased. This may be an indication of the growth of demand for housing in the midterm perspective.
- ***Draft administrative barriers action plan.*** The regional administration has demonstrated that it is aware of and concerned by the issues raised and has prepared drafted an action plan to address some administrative barriers. In the sphere of land and real estate markets the draft action plan focuses primarily on simplifying the procedures for leasing of state and municipal property; balancing the rights and obligations of landlords and tenants under leases of municipal property; improving the efficiency and transparency of land allocation procedures, including land privatization; and improving procedures for issuance of land use and construction permits by implementation of a land zoning system.

Recommendations:

To achieve the objectives will require a comprehensive program of legislative and administrative steps, both short and long term. Some significant constraints on development of land markets may arise under Federal legislation, which the region perhaps may affect by documentation of the defects in the legislation, maintaining a dialog with Federal officials and legislators, and providing leadership towards implementing the necessary modifications. The recommendations made in this report focus primarily on those steps which the regional and municipal administrations may take without Federal involvement.

For convenience proposals are organized under five headings - asset management, supply, demand, time and costs, and performance monitoring. Asset management provides recommendations for improving the approach to management of publicly owned real estate assets. Recommendations grouped under the heading of

"supply" are aimed at increasing the amount of land and other real property that can be made available for investment. Recommendations grouped under the heading of "demand" are aimed at increasing the attractiveness of property ownership to investors and entrepreneurs and facilitating access to real property. Recommendations grouped under the heading of "time and costs" are a special subset of actions aimed at increasing demand. Performance monitoring provides suggestions for assuring that policy initiatives are meeting their objectives over the long term.

Asset Management

By "asset management" is meant the management of state and municipal real property assets in such a way as to maximize their value. "Value" in this case does not mean merely the balance sheet value or revenue potential to the state or municipality, but the broader concept of value to society considering all of the direct and indirect costs and benefits of retaining the real estate assets in public ownership.

The value of real estate assets presently in state or municipal ownership may be increased by divestiture to the private sector, rather than carrying the asset on the public balance. Good asset management includes divestiture of assets, as well as maintenance and improvement. Continuing state ownership of a real estate asset may result in lower returns to the asset if the state lacks the resources to develop the asset to its highest and best use and market it appropriately. The present value of divesting the asset, including sales proceeds, increased investment, construction and commercial activity, and increased tax revenues may far exceed any return the state can hope to see by holding for an indefinite period an asset which is not performing up to its potential. Moreover, as suggested frequently by business people throughout the FIAS experience in the Perm region over the past several years, the continued state and municipal domination of real estate ownership can lead to a perception of favoritism and an uneven playing field for businesses, which perception can itself can have serious adverse consequences for development of the local economy.

Most regions and municipalities in Russia do not have clear strategies on management of state and municipal real estate assets, but rather deal with such assets on an *ad hoc* basis. We are advised that there have been recent efforts in the Perm region, some still ongoing, to develop a real estate strategy. The "*Program Of Social and Economic Development of the Perm Region*" is in hearings in the regional legislature, and it has a section on land and real estate. Similarly, the regional "*Strategy on Industrial Policy*," elaborated with the participation of regional industrialists, includes a chapter on real estate. "*The Concept of the Housing Policy in the Perm Oblast for the Years 2003–2010*" adopted in April 2003, may be also mentioned in this respect. These documents were not obtained during the mission, but may be obtained at a later date.

Perm City appears to have the rudiments of an asset management strategy, which takes the approach that if a property's current revenues are greater than its costs it will remain in municipal ownership, and if not it will be divested. In addition, the city is willing to grant rent concessions to tenants in return for improvements to city owned buildings and premises. It appears that the city envisions a long term role as a property owner and manager, and city-owned property as a long term source of municipal revenues. We suspect that the city's approach to the analysis of whether it is in the public interest to own and manage property is probably simplistic, and does not consider all of the costs of ownership or the benefits of divestiture. It is noteworthy that based on sophisticated analysis of long term costs and benefits of public ownership of real estate assets, most governments in developed economies have concluded that owning and managing real estate is not a good public investment. Not the least of the arguments underlying this conclusion is that governments are typically inefficient property managers. Complaints of the private sector in the Perm Region suggest that this may also be the case there.

Unlike the Tomsk Region, the Perm Regional Administration did not ask directly for advice on real estate asset management. We consider the issue of a comprehensive real estate strategy to be so important that we are nevertheless offering the following recommendations:

1. Develop a regional strategy on state ownership of real estate assets.

Whether asset management is efficient or not must be measured against a set of principles and objectives. A regional strategy would include fundamental conclusions on the role of land and real estate assets in government activities as well as guidelines on how those conclusions are to be implemented. As an example, included in the body of this report as Appendix 1 are the so-called "Property Principles" of the Commonwealth of Australia, which are illustrative. A defining characteristic of these principles is that there is a presumption that public ownership of real estate assets should be limited, and that the financial analytical methods of private business must be applied to justify public ownership, improvement or sale of real estate assets. Real estate should be viewed as one resource among several, including human resources and capital, which contribute to the output of government goods and services, and should be retained only so long as the value of the output attributed to the real estate asset exceeds the direct and indirect costs of owning it. It is essential in any exercise of this sort that the true and complete costs of ownership and benefits of divestiture be identified.

It is not possible to anticipate here the precise content of these principles for the Perm region, but the following are offered as broad examples for discussion:

1. The real estate assets of the Perm region include all land and facilities in the ownership or use of the Perm region, or any of its agencies or enterprises.
2. The regional government of Perm, including its agencies and enterprises, will own land and real estate assets only as necessary to support their essential function and delivery of the goods and services of government, or if ownership is otherwise in the public interest. The public interest in real estate ownership includes: [To be defined]
3. It is the responsibility of each government agency and enterprise to periodically review its real estate holdings in terms of whether they contribute to carrying out the essential functions of the agency or enterprise. There is a presumption that all real estate assets held by government agencies and enterprises are disposable unless retention or improvement can be justified in terms of the essential functions of the agency or enterprise.
4. It is the responsibility of each government agency and enterprise to maintain complete and current inventories of real estate assets in its use, including the current use and condition of the asset.
5. It is the responsibility of each government agency and enterprise to maximize the value of real estate assets in its use, and to justify continued ownership of real estate assets in terms of the essential function of the agency or enterprise.
6. In deciding whether to own, acquire, improve, or dispose of real estate assets, commercial financial principles must be applied. In the absence of compelling reasons of public interest as defined in these principles, continued public ownership or improvement of real estate facilities cannot be justified if the present value of ownership is lower than the present value of disposition. In considering the present values of ownership or disposition all costs and benefits must be considered, including for example depreciation, the future costs of improvement and maintenance, availability of equivalent facilities in the private market at reasonable price, and the sum of indirect benefits from disposition.
7. There is a presumption that public ownership or improvement of real estate assets is not desirable if equivalent facilities can be obtained in the private market at lower cost.
8. There is a presumption that the area of office facilities in the use of any government agency or enterprise should not exceed [XXX] square meters per employee, and that after establishment of reasonable reserves for

growth excess office space should be divested or leased on the private market.

9. Accounting for real estate assets is a necessary component of the budgetary process for state agencies and enterprises. In budgetary reporting state agencies and enterprises are required to provide a strategic analysis of real estate assets including justification of continued ownership of under-utilized assets, proposed improvements and dispositions. Accounting statements of Perm government agencies and enterprises must include the full costs of continued ownership and operation of real estate assets. Accounting rules for real estate assets of regional agencies and enterprises shall be determined by the Regional Finance Committee.

These points are only examples, but they give some sense of the type of policy statement that might be formulated to guide future treatment of public real estate assets.

2. Prepare the strategic inventory and plan for regional real estate assets.

The Regional administration should commence preparation of a strategic inventory and plan for real estate assets. In this activity government agencies and unitary enterprises would be required to provide a current and complete inventory of real estate assets, their current use and condition, and provide an assessment of how the asset is contributing to performing the essential function of the agency or enterprise. Agencies and unitary enterprises would be required to project over a longer term the improvements and upgrades that would be necessary to maintain the functionality of the asset, and whether the costs of such improvements and upgrades would be justified by the expected contribution to the output of public goods and services. Agencies and enterprises would be required to identify surplus real estate assets that should be considered for disposition.

A positive step in this direction was undertaken recently by the City Department for Property Management within which a Division for Financial Analysis and Planning. The Division was created half a year ago with the main task to elaborate the long-term strategy of municipal property management. Currently the Department is working on identification of the most liquid municipal assets, particularly, the commercial and office premises of good quality meeting the market demand and putting them in rent, optimization of the Department's register of municipal property. This activity is going in hand with the adjustments of the structure of the Perm City Property Treasury.

3. Create a regional working group or steering committee on state real estate.

Development of a policy statement on real estate assets should be the work of a task force which includes representatives of the relevant government agencies, including municipal and Federal agencies, and the private sector. This group would consist of senior executives from the relevant government agencies and would oversee the development of asset management policy.

Supply

1. Audit all outstanding regional or municipal acts for allocation of land rights and terminate those that have exceeded the time limits; prohibit multiple consecutive renewals of preliminary allocations of land sites.

There is some indication that many usable land sites in Perm City have already been allocated on a preliminary basis under acts of the city architectural authorities which authorize preparation of design works. It also appears that this allocation has resulted in long term removal of valuable land sites from the market as holders of the rights routinely fail to meet the time conditions on their permits and obtain multiple consecutive extensions. We are advised that there are presently **365 land plots** which have been allocated to developers on terms of conducting the "research and design works," and on which little or no progress is apparent. This is in effect allowing some development entities to speculate in public assets for virtually no cost. We are advised that the city administration is now focused on this problem, and intends to take appropriate steps to review and, if necessary, terminate these land allocation acts. Currently, the City administration is sending letters to such developers inquiring whether they are willing to terminate their land use rights, and in case they agree the resolution of the Mayor on withdrawal of the land plot is issued. In our view the position of the administration on this issue should be more aggressive. Strictly enforcing the time constraints on design permits and prohibiting multiple consecutive extensions without extremely compelling justification, such as force majeure, would be a good step toward putting this land back into the market.⁹ These issues may perhaps be addressed in a regional law on allocation of land rights.

In addition, it would be useful to prepare and make generally available to the public a comprehensive report on the present status of these allocated land sites, at the least to counter the widespread perception that they are controlled by a relatively small group of favored enterprises.

⁹ The consultants understand that a more complex situation with these land sites arises in cases where they are already encumbered with uncompleted construction. In such cases the land plot may be withdrawn only on the basis of court decision, subject to evaluation and an offering at a competitive sale, with reimbursement to the holder of the right.

2. Consider creation of an independent urban development agency empowered to designate, plan, prepare and sell land plots for new development.

A key constraint on the real estate market in Perm City appears to be the lack of vacant, serviced land sites in good locations suitable for new development. We are advised that practically all new development projects in recent years have been located on land plots which were cleared of older existing buildings which had outlived their useful lives. While this is not unusual in many large cities, the shortage of immediately available land sites in Perm city is considered by many to be severe.

There are some indications that a good part of the land problem in Perm city is attributable to the accumulation of inappropriate uses in valuable center city locations. Primary among these inappropriate uses are dilapidated "barracks" type housing which is mostly of little historical value and beyond feasible reuse, as well as many small industrial uses which are either not operating or operating at reduced levels. The long term health of the city real estate market will require increased densification of the center city areas that are most interesting to potential investors for both housing and commercial projects, and replacement of these low-value uses with more high-value uses.

This is a normal process in most cities, but made more complex in Russia today because of the unsettled nature of real estate markets. Most land remains in state ownership. Land use planning is outdated and private redevelopment efforts are expensive and unpredictable. There are few alternatives for those wishing to relocate either their homes or other facilities. The case of housing relocation is instructive. Most new housing produced in Perm today is costly and out of the range of those who are most in need of housing improvement. Prices are high and inelastic even in the face of decreasing demand. In the absence of reasonably priced housing alternatives the likelihood of removing the large amount of dilapidated but cheap housing remaining in the center and relocating the current occupants is diminished.

Cities in developed economies that have faced similar challenges of urban deterioration and constraints on new investment have responded with a redevelopment partnership between the public and private sectors under the strong leadership of quasi-governmental agencies or public corporations ("redevelopment agencies") which act entrepreneurially and are given the authority to coordinate redevelopment efforts and clear away the "red tape" and bureaucracy which usually hinders purely private efforts.

Government sponsored redevelopment agencies can be regional or local. They typically take the form of independent public corporations or commissions, having legal existence and their own boards of directors. While they are often

created with public budget funds, they are expected to achieve a high level of financial self-sufficiency from fees and revenues from land sales.

Typical powers of the urban redevelopment agency may include:

- *Designation of redevelopment areas.* A redevelopment agency may be charged with the responsibility to analyze and recommend areas or locations for urban redevelopment activities, subject to approval of the local council.
- *Acquisition of land for redevelopment.* Land can be acquired in market transactions, but the crucial aspect of effective redevelopment agencies is the ability to take land for a public purpose. Under the laws of most countries in which the redevelopment agency is used the improvement of the urban economy and making land available for needed investment is considered to be a public purpose for which land may be taken by government or its agencies. Redevelopment agencies are typically vested with the public power to acquire land in involuntary transactions, subject the payment of fair compensation in accordance with law.
- *Land clearing and redevelopment.* Redevelopment agencies are authorized to engage in land clearing and installation or upgrading of utility services.
- *Land sales.* Sale of cleared and redeveloped land to private investors is the major source of revenues for redevelopment authorities. Land sales are also the main source of revenues to repay any debts of the authority incurred in its work. Sales are typically required to be through competitive bidding.
- *Investment in real estate facilities.* Some redevelopment agencies are permitted to invest in development of facilities, but this is not favored because of economic risk and the desire to make use of private sector resources. More typical is the power to retain a joint economic interest in a privately developed project as a source of revenues for the urban redevelopment program.
- *Raise funds/borrow money.* Redevelopment agencies are typically empowered to borrow money in the private market, and particularly to issue bonds or other debt instruments to support redevelopment projects. Borrowing authority is sometimes, but not always, supported by a guarantee or other credit enhancement from the unit of government which created the agency.
- *Planning powers.* Many urban redevelopment agencies are given independent powers to establish land use plans for the designated redevelopment areas, sometimes subject to approval of the city council. Redevelopment areas designated as such are typically exempt from the usual land use planning procedures of the municipality. These planning powers are often exercised in

the same way as planning powers generally, subject to the obligation to publicize proposed plans and provide a forum for public comment.

- *Financially self sustaining; cost recovery.* The premise of many redevelopment agencies is that they will recapture their costs of operation from land sales and the value which they add by coordinating land acquisition, clearance and upgrading, relocation, and planning will be reflected in land prices. A premise of redevelopment agencies is that a significant portion of revenues from land sales will be reinvested in redevelopment activities, thereby reducing the costs of borrowing.

Benefits of the Redevelopment Agency

The benefits of a specialized urban redevelopment agency can include:

- *Focused attention on redevelopment.* The specialized redevelopment agency has a clear and focused mandate to increase the value of city land and attract investment by making serviced land sites in good locations available to investors at competitive prices.
- *Market orientation.* As an independent agency expected to be financially self-sufficient, the redevelopment agency has the incentive to act in a market oriented and entrepreneurial manner, carefully selecting opportunities for their market potential and the expectation of recovering investment. Many agencies operate free from restrictions on public salaries, and are able to attract the best available talent.
- *Avoidance of bureaucratic conflict and red tape.* A primary purpose of specialized urban redevelopment agencies is to overcome bureaucratic conflict and “red tape.” Most often such agencies are authorized to carry out the functions of planning agencies and permit issuing agencies within the boundaries of designated redevelopment areas. As important, the agency is in stronger position with respect to local monopolies and the installation of utility services.
- *Off-budget financing.* If given the authority to borrow, the activities of the redevelopment agency can be partially or totally off-budget.
- *Ability to take land and buildings for a public purpose.* The ability to acquire land for a public purpose gives the redevelopment agency an advantage over private development entities, and allows it to move more quickly and with greater certainty than the private investor. Private investors are in particular subject to the time and cost uncertainties of acquiring numerous property rights to create a feasible development site

Drawbacks of Redevelopment Agencies

Some risks of public redevelopment agencies include:

- *Financial/ investment risk.* The feasibility of redevelopment agency activities depends on sound market analysis and business judgment to assure recovery of investment. Depending upon whether the indebtedness of the agency is guaranteed by the locality, poor judgment or market reversals could result in risk to the local budget.
- *Lack of market sensitivity.* The redevelopment agency must follow market forces objectively in the selection and planning of redevelopment sites and avoid capture by a limited set of political or commercial interests. The temptation must be avoided to impose planning requirements on redevelopment sites which limit marketability.
- *Tendency to grand projects.* There is sometimes a tendency of public redevelopment agencies to initiate very large and risky projects. This would be inappropriate for the current needs of Perm region.
- *Controversy related to taking of land and relocation of inhabitants.* Redevelopment agencies sometimes become involved in disputes regarding involuntary taking of land sites and relocation of occupants. Care must be taken to assure that fair compensation is paid and that with the assistance of local authorities occupants are provided with good relocation alternatives.

Prerequisites

Some prerequisites for creation of an effective redevelopment agency are:

- *Market failure.* The public redevelopment agency model is most frequently used where the private market cannot be expected to achieve the desired objective without public assistance. If private market entities can perform the same function there is no reason for the locality to assume the risks of direct involvement in preparation and sale of development sites.
- *Enabling legislation.* If a public redevelopment agency option is considered to be desirable, it should be created by legislation which defines its powers and obligations. Two of the crucial powers of redevelopment include the power to assemble land sites by involuntary acquisition and the power to avoid the usual municipal procedures for land use planning and construction permits.

- *"Seed" Capital.* A redevelopment agency would need some seed capital from the budget to support initial operations. Over a longer term funds for operations could be obtained from land sales.
- *Guarantee.* The possibility of off-budget funding for a redevelopment agency would probably require some form of guarantee or other credit enhancement from government.

It should be noted that the Perm City administration acknowledges the necessity of implementing effective approaches to the redevelopment process, and expresses the intention to elaborate a plan of "quarter by quarter" redevelopment in the center of Perm. Until now, all the reconstruction projects were implemented on the initiative of investors and developers, and not the city. One of the main concerns of the City's participation in the redevelopment process is that it is considered "impossible to withdraw the land plots for public uses." This may in fact be a practical problem with which the city is more familiar than the consultants. Nevertheless, the law does allow withdrawal for public purpose and provides the necessary guidelines. The city may have to establish this point in appropriate cases in the courts.

3. Implement a pilot program for preparation of serviced land sites for industrial facilities.

The Regional Administration, in cooperation with Perm City or one of the surrounding districts, could consider investment in a regional industrial park. The purpose of the park would be to provide serviced land sites for sale or long term lease to investors for development of new facilities. See, for example, the recent experience of the City of St. Petersburg with the Pulkhova Airport Industrial Park. The land would be serviced at the expense of the regional and local administrations. The prerequisites for consideration of this possibility would include a professional and comprehensive market study demonstrating the economic feasibility of the proposed project, which would consider, for example, actual demand, the availability of competing land sites in the market, and the need to recapture the public investment. Locating the site would be crucial, and this sort of project would be inadvisable unless complete cost recapture were determined to be likely.

The possibility of providing alternative locations for industrial and related commercial facilities is particularly important for Perm City, where relocation of inappropriate uses from valuable sites in the center should be a long term strategy.

Development of an industrial park can be undertaken by an appropriate redevelopment agency, as discussed above.

4. Acceleration of applications for privatization of land parcels under article 36 of the RF Land Code.

It is important to note as a preliminary matter that the processes of division of state land and the buy-out of land plots by enterprises or other owners of real estate objects are two independent processes and the first process is not a prerequisite of the second. The enterprises or other owners of real estate objects have the undisputable right to buy-out the land plots notwithstanding whether or not the division of state land (on which the enterprise is located) is fulfilled.

The main source of land and facilities for new investment is likely to come from privatization by enterprises and entrepreneurs under article 36 of the Land Code. Following introduction of the Land Code, there was a significant increase in applications for privatization of land parcels. This number may increase significantly in response to the recent decrease in privatization prices. The mandate of the Land Code to assure that land is leased or sold by the close of 2004 is an important opportunity to develop the private land market, which should receive adequate resources from the regional and municipal governments, including by providing sufficient staff to process applications in a timely manner.

5 Accelerate privatization, consolidation, and liquidation of inefficient regional and municipal enterprises.

As we were informed, there are about 400 federal unitary enterprises, about 100 regional unitary enterprises, and 82 municipal unitary enterprises in the Perm Oblast, and there are indications that a significant amount of land and facilities appropriate for development or redevelopment by investors may presently be held by state and municipal enterprises. It appears that there is a continuing effort to divest unitary enterprises in the region, and that in Perm city, for example, the number of municipal unitary enterprises is declining.¹⁰

It is likely that acceleration of the pace of divestiture will result in more land entering the private market. Including enterprise held land in the recommended inventory of publicly owned real estate assets would probably confirm this hypothesis. Once inventoried, it is important to take an "asset management" approach to these real estate assets, including assessment of whether they are underutilized and redundant and may be put to higher use. Pressures should be

¹⁰ According to the information of the City Department for Property Management a Privatization Plan for municipal enterprises is elaborated each year and approved by the Perm City Duma. Twenty-seven municipal buildings and three large municipal enterprises are included in the 2003 Privatization Plan, among which are the "Vodokanal" (the water and sewer monopoly) and "Permgrazhdanproect" (the city Planning and Design Agency). These municipal enterprises will be sold through tender procedures. In case the tender fails, the real property is usually re-evaluated and separately put up for auction a second time. This was a case with the cinema hall "Iskra" which was initially evaluated as 1 mln. \$ US but failed to sell at that price. Some large properties, such as the "Vodokanal" will be sold by issuing shares in the enterprise, in which the municipality will retain a position.

brought to bear on state enterprises to prepare real property asset management plans which free up valuable real estate assets by consolidation of existing facilities and placing underutilized property back into the market. In addition, reentry of these assets into the market can be facilitated by accelerating privatization or liquidation of remaining municipal and regional state enterprises.

6. Bring land and premises rents to market levels and eliminate land rent concessions for enterprises.

One cause of shortage and high prices can be rents for state and municipal land and premises that are set below market rates. As the Head of the City Department for Property Management noted, a new methodology of calculation of municipal land rent was adopted in July 2002, and now the rent is on average three times higher than previously, when it was the lowest in the Volga Basin Federal District. Still, as for rent for municipal premises, the consultants were advised by Perm real estate brokers that rents for municipal facilities remain approximately 20-30% below market rate, as evidenced by the widespread practice of profitable subletting of municipal space by tenants. There are also in place automatic land rent reductions for certain types of enterprises, in particular large land users. As with all subsidies, below market rents encourage occupancy of more land or space than is actually needed for operation of the occupant's business. In effect, the occupant is speculating on real estate at the expense of the budget. Raising rents to market levels could force users to reconsider the amount of space occupied and free up excess space for reentry into the market for other uses.

It is noteworthy that in one of the FIAS roundtable discussions with representatives of the business sector one enterprise representative complained of increases in land taxes, saying that some enterprises would be forced to "relinquish possession of some land." This is precisely the point! If the land is not necessary for operations, there is no reason to hold it, and it should be made available for alternative uses.

Land rent concessions for enterprises encourages enterprises to rent rather than privatize land, keeping potentially valuable land out of the market. Below market rents therefore lessen demand for land privatization. As with all subsidies, it also encourages enterprises to occupy more land than they need. The enterprises are in effect using the public budget to speculate in the long term value of real estate. Elimination of land rent concessions should increase demand for land ownership, which in turn will create pressures for privatization, sale, reuse and intensification of development.

There are conflicting indications whether the amount of premises available for commercial office and trade use is sufficient to meet market demand. Real estate market professional interviewed by the consultant's suggested that there was a significant shortage of high-quality office and trade premises in the center. This question cannot be answered without a thorough market study, which the mission

was not able to accomplish. An inadequate amount of space would result in discouraging new business because of lack of facilities or high rents and prices. If possible, it is recommended that a market study be performed to determine whether there is sufficient premises available to meet demand.

Even if the amount of space presently in the market is found to be adequate, below market rents are a hidden budget expenditure. They encourage occupants to engage in subletting, which apparently is widespread in the Perm Region, and in effect allocate public revenues to private individuals. These lost revenues could be better used to implement the market development strategies recommended in this report. One step that can be taken is to throw light on these hidden subsidies by requiring an audit of all present leases of state and municipal real estate to determine whether it is subleased and the differential between the official and sublease rent. This step, together with a professional market study to determine the relationship of official rents to market rents should provide information on the extent of budget losses from hidden subsidies. An analysis of these losses should be made available to local legislators in the course of the budgetary process.

Another step that should be considered is to base rents for significant buildings and premises on independent market appraisal, and not a normative calculation as at present. Recent experience suggests that normative formulas tend to overstate the values of lower quality properties, but understate the values of high quality properties. Neither outcome is desirable.

Demand

1. Complete and make widely available an inventory of state and municipal real property.

Increasing the transparency and availability of information regarding public real estate assets can increase competition, produce a better return on public assets, and decrease abuse of bureaucratic discretion. An important first step is to complete an inventory of state and municipal property available for development or redevelopment. The inventory should include vacant land, buildings and premises, as well as real property in the use of state and municipal enterprises, including federal enterprises, which has not yet been privatized. The inventory should be comprehensive for the entire region and should include all property of cities, towns and districts available for investment, and should be transparent and made widely available to the public and potential investors. A medium term goal would be to put on the internet that portion of the property inventory which is immediately available for development or redevelopment. In this regard, it is recommended that the Regional Administration refer to the St. Petersburg Unified Geo-Information System (EIST) and made available on the web at <http://us.statedevelopment.spb.ru/tias200e/indexe.phtml>.

The necessity of making a comprehensive inventory of property in Perm Oblast is already presumed by the process of division of state land in the region into federal, regional and municipal lands. Creating this comprehensive inventory is an expensive and time-consuming undertaking. Moreover, many municipalities in the region lack the resources to prepare such an inventory. In this respect, it may be expedient to first identify the land plots or the types of land plots which may be most attractive for investment and development, and these land plots should receive priority in the processes of inventory.

2. Create a "single window" investment promotion agency with responsibility for maintaining an inventory of state and municipal property available for development, or redevelopment, and providing advice and assistance regarding real estate matters to potential investors.

The regional administration should delegate to a single agency the responsibility to maintain a comprehensive inventory of investment property which can be marketed to potential investors. This agency could be a multi-purpose investment promotion agency. The Governor of the Perm Oblast has acknowledged the necessity of creation of a special Agency for promotion of foreign investments. Recently the Association of the Perm Region was established as a non-commercial organization with participation of the Department for Perm Oblast Property Management and the Department for Foreign Relations of the Perm Oblast Administration. This is an important step.

Services provided to potential investors could include identification of land and facilities and their technical parameters; advice on acquisition and development requirements and processes; unbiased references to local professional firms; introduction to, and interface with, local technical bureaucracies. The regional agency could carry out this function for the entire region, but to achieve economies of scale should definitely do so for the smaller towns and cities in the region. For example, in the Novgorod region the regional investment promotion agency gathers from the regional towns and districts comprehensive information on land sites and facilities which they have available for investment. To assure that the investment promotion effort is effective, it would be essential that Perm City contribute information to the agency. The "single window" agency will need to have the necessary amount of authority, including power to enforce cooperation.

3. Improve terms of purchase for land privatization and sales of long term lease rights by offering an extended payment schedule and other options.

Demand for land privatization may be increased if better terms are offered to potential purchasers. It is our belief that the land presently occupied by privatized enterprises and businesses has little residual value to the region or municipalities, as the rights of occupancy are virtually perpetual and strongly protected. It is

more in the interests of local economic development to simply divest the land into the private market. The recent decrease in the land privatization price was a very positive step, but prices may still be beyond the reach of many occupants. Accordingly, short of reducing the buy-out prices further, which should be considered, further demand may be induced if the time for payment of the land price were to be extended over a period of 3-5 years, with interest at the official rate. (To facilitate mortgage and improvement of the property privatized on such terms it would be advisable to actually transfer the title upon execution of the purchase and sale contract, subject to a mortgage in favor of the seller for the unpaid purchase price.)

Other steps to stimulate the purchase of land plots by privatized enterprises and owners of real estate objects may include:

- establishing the land tax and rent rates for each urban “economic zone” in such a way as to stimulate the purchase, rather than rental, of land, by assuring that the land rental rate includes both the land tax to support municipal services as well as the reasonable rental value for use of the land;
- permission to subdivide a large land plot and buy-out by portions;
- fixing in the sale-purchase contract (until the zoning ordinance is adopted) a list of various permitted uses of the land plot instead of the existing fixed “targeted” use of the land plot.

4. Accelerate implementation of competitive proceedings for allocation of land rights.

To date, there have been no competitive procedures for sale of land in the Perm region. As noted earlier, Perm City recently advertised the availability of 29 land plots for tender, of which only 6 received expression of interest from more than one potential bidder, a condition of placing the land to a competitive auction.¹¹ The regional administration has not yet begun competitive land allocation procedures, but intends to develop the necessary documentation and procedures, and provide the necessary technical assistance, for the cities and towns of the regions to implement their own auction procedures.

Competitive procedures can increase demand by attracting a certain type of investor that is concerned with the certainty and transparency of the transaction. Competitive procedures

¹¹ The RF Land Code provides that land available for auction should be advertised prior to auction, and only if there is an expression of interest from more than one potential bidder is it necessary to allocate the land plot by competitive auction or tender. With respect to those land plots that are advertised but receive only one expression of interest, the seller is permitted to allocate those plots by long term lease, not sale of ownership, on a negotiated basis.

- provide equal opportunities and stimulate the appearance of new private developers of different scale and capacity;
- identify the Perm region as one that is supportive of transparent land allocation procedures;
- help to reduce the monopoly of the city planning and architectural bureaucratic structures in development of the private real property; promote the market-orientated planning solutions;
- helps to reduce the costs for assignment of land rights, the value of construction and planning, as well as expenses for obtaining the necessary permits;
- most important – they help to create market mechanism of land pricing and to fix basic market prices for city lands.

Apparently, there are various ambiguities regarding the Federal Resolution #808, *On Organization and Management of Public and Municipal Land Sales and Leases*, which governs procedures for auctions of land. In the expectation that these problems will be resolved it is recommended that the regional administration adopt the necessary local legislation to enable land an real estate auctions and tenders.

In our opinion, there are several problems with the approach to holding land tenders presently proposed by Perm City in its draft regulation:

- 1) The sale of land plot in ownership is not permitted; all the land plots from the above mentioned list are proposed for lease. Moreover, this is not a long-term lease granted at the time of tender, but the notorious lease “for the design and construction period” which is the subject of complaint from investors throughout Russia. The City officials explain this fact by the position of the regional administration, which allegedly does not approve of sale of land. However, this position was not confirmed by the Oblast administration officials.
- 2) According to item 4, point 3 of Article 30 of the Land Code, the transfer of land plots in lease without holding auctions/tender is permitted if only one expression of interest is received after preliminary notification in mass media about the availability of the land plot. The law does not require that the land plots be advertised for a second or third auction. Based on the recent experience in Perm City, where multiple expressions of interest were received for only 6 of 29 advertised land plots, it appears that most land plots will still be allocated through non-competitive and non-transparent procedures. A better approach may be to require that land plots which receive only one expression of interest will be offered again at a later time - perhaps 6 months - before it may be allocated without competitive

procedure. Markets change and other participants enter the market, and a second (or third) notice of tender might elicit a better response.

- 3) According to the City's draft regulations, the winner of the tenders has to “transfer the financial input aimed at the city infrastructure development” before he can get the construction permit. That means that he pays twice: for “the right to lease” (which is estimated by an appraiser and, so, reflects the market price of the land plot) and then for the very high infrastructure fee. The city should stipulate in the regulations that the costs of the infrastructure fee contribution, to the extent that it does not directly serve the project on the tendered land site, should be taken into consideration in setting the appraised market value or is an offset from the appraised market price of the land.
- 4) The list of documents which the applicant has to present to the tender commission includes 12 items or more. They include, in particular, the information on the experience, “technical capacity” to fulfill the project, accounting balance-sheets, information on all bank accounts, proved by the banks, explanatory notes on the sources of financing the project etc. Nothing is said that this information should be presented in a sealed envelope, and there is no distinction between the qualification and bidding stages. It is thus possible that high bidders could be eliminated on vague and subjective technical grounds pertaining to "qualifications," which increases the possibility of corruption and is contrary to best international practice. Qualification requirements should be set as minimum requirements and should be resolved prior to the tender proceeding, and separated from the competition.
- 5) The model land lease attached to this set of tender documents is a very flawed legal document, unbalanced in favor of the city and against the interests of the investor. It stipulates, in particular, the right of the lessor to set “limitations” on land use and encumbrances *post factum*; to terminate the lease at any time in case of vaguely defined infringements by the lessee, including “in case the lessee conducts the design works or construction so slowly, that it becomes evident that he will fail to finish these works by the end of the lease.” The rent rate within the terms of the lease may be changed unilaterally by the lessor. The draft Lease states that the lessee has the right to sublease the land plot or part of it “on the written approval” of lessor. Nothing is mentioned that this permission is not needed in case the Lease is signed for a period of more than five years (according to the provision of the Land Code). The document does not obligate the city to deliver a long term lease upon completion of the improvements.

- 6) The usual Lease term is only three years, which is unattractive to serious investors.

The following steps to stimulate the development of competitive procedures of land allocation may be recommended:

- Elaboration and adoption of the regional law, adapting to the local conditions the provisions of the federal rules on conducting land tenders enacted by the Federal Resolution #808 and eliminating the shortcomings and contradictions of the federal document;
- The criteria of land plots which can be allocated into property or lease exceptionally through the competitive procedures should be established; the lists of land plots which are going to be put on auctions or tenders within a year should be published in local press;
- The law should establish the presumption that the land plot will be sold unless leasing is justified; the criteria for offering a lease rather than the property right should be specified;
- Elaboration of the specific procedures of holding tenders in regard of the land plots with such encumbrances, as objects of unfinished construction, dilapidated housing, etc.;
- The land auction/tender documentation should contain the full and exact information on the on-site engineering facilities, on technical conditions and the fees for connection to utility services; these fees preferably are included into the starting price with giving the guarantees that no additional payments may be demanded by utility services;
- The starting price should reflect the relation between the supply and demand on the real estate market. The starting price may include the costs of preparation of design requirements (in case there are any imposed by the City and they are included in the invitation to bid) and the costs (part of the costs) of off-site engineering facilities, which the City provided for the land plot put on auction. The starting price may be reduced on the amount of costs, needed for demolition of constructions which do not comply with the permitted uses of the site, as well as the costs needed for cleaning the soil to the level of environmental standards set for the appropriate permitted uses.

5. Implement transparent procedures for non-competitive allocation of land rights.

Competitive procedures are not appropriate in all circumstances (and are not required by the Land Code for all cases, although there are still many unclear provisions in the Land Code in this respect, for example, in article 34 which is concerned with land allocation for non-construction uses and in which the issue of competitive procedures is omitted) and it is likely that targeted allocation of land

and property will continue at some level. There is no reason why negotiated transactions cannot be made more transparent as well, and in fact there is a strong argument that the Land Code requires transparency for all dispositions of publicly owned real estate. Consideration should be given to appropriate regional legislation governing all allocation of real property which would include:

- a prohibition on sale or lease of an asset the availability of which had not been advertised or otherwise included in a public inventory accessible to the public;
- a requirement for independent appraisal of sale prices and rents;
- a requirement for published notice of the terms of the sale prior to effectiveness of the transaction;
- a requirement that higher offers for the property be accepted.

6. Improve the transparency of lease transactions and the terms of leases for municipal premises.

A main complaint of local businesses was the uncertainty of lease terms. Duration of leases are believed to be too short - the majority being for less than one year to avoid registration requirements - and rent increases arbitrary and unpredictable. There is a perception that access to leases is not fair, and that city leases are concentrated in the hands of a limited number of firms and persons who then "arbitrage" the lower city rents by subleasing. Data to support or refute these perceptions is not generally available.

The consultants were advised by the Property Management Committee of Perm city that the average duration of leases is now increasing as an incentive for lessees to invest in improvement of the premises, and that any lessee willing to invest in improvements can obtain a lease of appropriate duration. Municipal property managers are also offering rent concessions to tenants who agree to make significant improvements to premises. We were further advised that recent modifications to the rental formulas makes the setting of rent levels more transparent and predictable, though the almost complete control of local authorities over the parameters that enter into the rental formula would appear to undermine this claim. Municipal officials also argue that any present lessee will have its lease automatically renewed upon expiration of the term, and that there is little threat of arbitrary eviction, though they acknowledge that city officials are not obligated to renew leases.

In addition to the recommendation that rents be increased to market levels made above, several steps could be taken to improve the operation and perception of municipal leasing programs.

- Increase the standard duration of lease terms. In developed real estate markets standard lease terms for office and trade premises are in the range of 5 years, and leases requiring significant investment from the lessee are

twice that duration. The standard term offered to lessees should be increased and modified downward only at the request of the lessee.

- Tie rent increases to objective and independently verifiable economic indicators such as a cost of living index.
- Include a legally binding option to renew the lease in the rental agreement.
- Offer leases in municipal premises on the basis of wide public advertisement in organs of mass media.
- Offer leases on municipal premises through competitive tender or other open process.
- Offer municipal premises for lease through private brokerage companies under commission agreements that create incentives for market pricing.
- Maintain and make available to the public a log of municipal leases identifying the key parameters of the premises, the holder of the lease and the rental rate.
- Make large amounts of municipal premises available for management by private sector firms under contracts of trust management which include financial incentives to improve the space and achieve market rate rentals. Incentive management contracts and the private sector's goal of profit maximization can limit the politicization of municipal property management and reduce the opportunities for corruption.

Time and Costs

The levels of demand for and investment in real property are affected by costs and prices, which are directly affected by the time spent in acquiring property and development permits. Reduction in the time and costs of acquiring real estate and development permits is therefore a main strategy in increasing demand and investment. Some important steps that can be taken to reduce time and costs of allocation of property rights and issuance of development permits include:

- 1. Complete the zoning program in Perm city and accelerate implementation of land zoning in the remaining municipalities of the region.*

The lack of comprehensive, transparent urban zoning regulations governing land use has been a major impediment to development of urban real estate markets throughout Russia. Without transparent zoning regulations each development proposal becomes a unique case, requiring greater time for processing. More

importantly, lack of transparent zoning regulations vests municipal planning authorities with too much discretion, which has often been abused. Without comprehensive zoning regulations, local authorities may also decline to offer land through competitive procedures. Implementation of comprehensive and transparent municipal zoning regulations is obligatory under the RF Land Code.

Perm city has taken positive steps to address this issue, and if its current work program in zoning is completed it will be in the forefront of municipalities in the Russian Federation. The consultants have reviewed the draft of the proposed zoning ordinance and are of the opinion that the draft is generally well prepared, reflects important "best practice" ideas taken from international experience, and will be a positive step once adopted. Regional legislation should establish firm deadlines for adoption of local zoning ordinances in the remainder of the municipalities in the region. In addition, the regional administration should exercise its authority under the Land Code to approve zoning regulations for the suburban districts of Perm City, which will likely be important areas of property development in the coming decades.

There is presently a decision in Perm city that elaboration of a zoning system is not possible until revision of the master plan for the municipality are complete. However, the inadequacies in the current Master Plan should not prevent elaboration and adoption of the zoning ordinance, even if actual implementation of the technical parameters of the zones must await completion of master plan revisions.

2. Complete and refine the "one window" land allocation and permit facility in Perm City; "roll out" the model to smaller cities in the region though appropriate seminars and technical assistance sponsored by the regional administration.

Like other Russian regions and municipalities, Perm has suffered from the same problems of divided responsibility among the various agencies that have a role in the allocation of real estate assets and issuance of land use and development permits. Divided responsibility together with inadequate monitoring of processes and outcomes has also led to a lack of accountability, as it has not been possible to cast light on agencies which are not performing up to the highest standards. (Unfortunately, a significant number of those agencies may be Federal organs over which the region has limited control, but this fact should not prevent an attempt to develop better coordination and accountability in these processes.)

The recent effort by Perm city to create a single window agency for issuance of land use and development permits is a very positive step. The agency should be operated under management principles which encourage professionalism, customer service and accountability. One approach would be to create in the single window facility the position of "case officer," who would be the citizen's

primary contact within the facility and responsible for processing the case, including assistance and advice as necessary. The case officer would be responsible for liaison with other agencies and departments, and for maintaining appropriate records on the processing of the application.

Based upon a review of the available documents governing the "single window" facility and the work procedures of the Urban Planning and Development Department of Perm City ¹² the consultants also offer the following recommendations for consideration:

- In all cases which do not involve allocation of state or municipal land for construction, eliminate the requirement for issuance of a letter authorizing design and survey activity. Owners of private land and buildings do not need such authorization.
- Projects which entail only renovation of existing structures without change to the type of use (commercial, trade, etc.) should move immediately to the construction permit phase, without need for any prior planning approval or issuance of an APZ.
- Make issuance of an APZ optional for all projects with private property. The APZ is an aid to the property owner. The owner should have the option of allowing private contractors of his choice to determine the regulatory constraints on the proposed project.
- In lieu of the APZ, permit the Architectural Department, on request of the property owner or his agents, to issue binding opinions or letters of guidance interpreting the regulatory requirements affecting the project.

As the single window concept is refined in Perm city, the regional administration should enlist the aid of the city to "roll out" this model to other cities of the regions through appropriate instructional seminars and materials.

In the course of its investigation the FIAS team was made aware of the role of the "PermArchBureau" in approving applications for land allocation and development permits. PermArchBureau is essentially a private company which has been given the authority to perform public functions of application and permit processing. On the one hand it is offering fee based consulting services to investors, while on the other it holds significant power to influence the decision on applications. We understand that it is intended to have PermArchBureau manage the new single window facility. We consider this to be a serious conflict of interest, and unfair advantage to PermArchBureau which may tend to drive other private sector consulting firms from the market. We strongly urge the

¹² The consultants reviewed in particular The Resolution of the Perm City Mayor 3 1730 of June 10, 2002 and the draft document entitled "Work Technology for Urban Planning/Development Department and Permarchbureau.

municipal administration to draw a clear line between performance of private consulting services and public functions, and to either remove from PermArchBureau the public functions it presently carries out - that is, to privatize the organization entirely - or prohibit it from undertaking consulting contracts in the private sector.

3. In refining the concept of the single window through the current experiment in Perm city, the city should:

(a) install "permit tracking" software systems which highlight roadblocks and bottlenecks;

(b) implement performance standards for issuance of permits;

(c) hold officials accountable for performance standards.

In the opinion of members of the Perm business community with whom the FIAS conducted interviews, many problems with allocation of land and real estate and issuance of construction permits can be attributed to poor management performance, which in turn may be attributable to lack of accountability. To address this, there are a number of reasonably priced, easily installed and user friendly software programs that can be used to track permit applications from date of application to issuance of permit. Such programs can be used as a management tool to identify persistent bottlenecks in the process and produce management reports.

Together with implementation of management tools, strict time standards should be established for each step of the permit process as benchmarks with which to evaluate management performance. These standards should be established on the basis of the audit of processes recommended above. Performance reviews of personnel should be related to the established standards.

4. Audit the land allocation and permit issuance procedures to identify bottlenecks and establish performance base lines.

Identification of processing bottlenecks and adjustment of performance standards should be a continuous management process. In connection with creation of its single window facility Perm city has begun a systematic assessment of the land allocation and permit issuance process which can help pinpoint where bottlenecks are consistently occurring, and has made some adjustments to the procedures (See Figure 1).

5. Establish reduced construction permit requirements for small projects.

Create a simplified, accelerated building permit process for rehabilitation projects having a small value, say 300,000-500,000 rubles. Eliminate most requirements for technical review, basing issuance of permit on certifications of licensed design and building professionals. Issuance of construction permits for such projects

should be a matter of days. Accelerated procedures may encourage owners to obtain permits rather than to construct illegally. Dealing with minor applications in a simple and accelerated way would also remove these applications from the desks and free up staff time for more complex applications, thereby improving the processing of those as well.

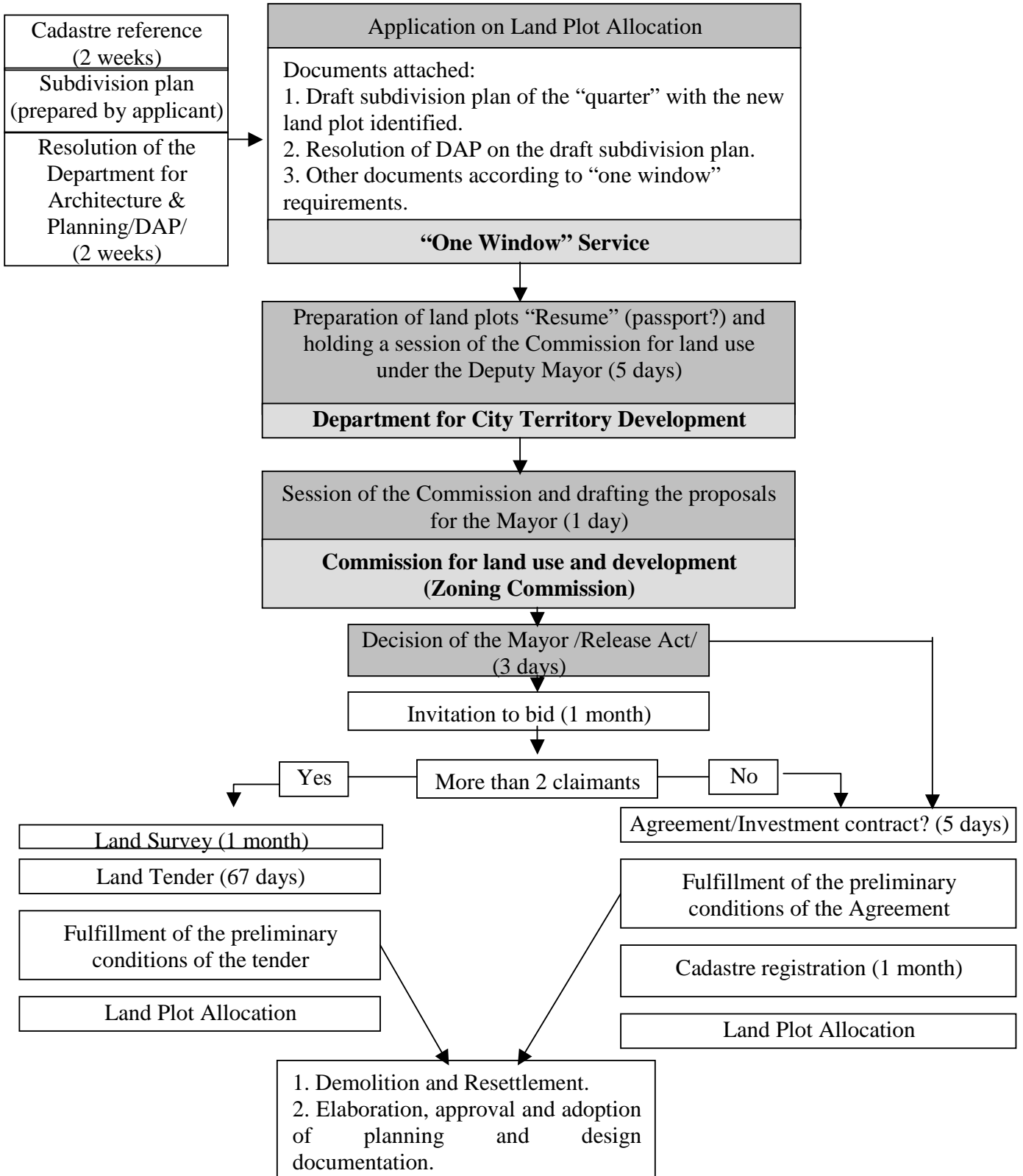
6. Deal with issuance of technical conditions and terms of connection to utility services under the region's authority to regulate the provision of public services.

(a) Require transparent publication of information concerning service lines and connection points and general technical conditions for municipal districts.

(b) Establish time limitations for issuance of technical conditions.

(c) Establish standards and formulas for connection fees and charges.

Figure 1: The New City Procedure of Land Plots Allocation for Development on Investor's Application



Addressing issues of technical conditions and the costs of connecting to utility services is a matter of properly regulating the utility monopolies, which to a significant extent is within the authority of regional governments. The behavior of “natural” monopolies, including local ones, may be influenced and regulated by administrative measures. Particularly, the tariffs, including fees for connection, may be regulated by joint decisions of the regional agencies of the Federal Energy Commissions and the regional Governments. This is essentially an issue of consumer protection. What is lacking are transparent "standards of service" and rate structures governing access to technical information, connection to existing networks and spreading of costs over all of the beneficiaries of utility upgrades.

Some local officials acknowledge that elaboration and improvement of the “one window” procedure for issuing permits would have limited success in the absence of proper regulation of the monopolies. A recent Mayor’s decision in Perm City intends that issuance of technical conditions will be placed under the authority of the City, and in particular the "single window" facility under development. This initiative is to be encouraged, though the practical realization of this approach will

need careful thought. Similar initiatives in other cities have met with mixed results.

In this respect, the recent Decree of the Governor of the Perm Oblast as of 05.08.2003 No. 88 “*On requirements to the process of issuing of optimum and substantiated terms of connection and technical conditions*” may play a positive role. The Decree requests from all regional services, enterprises and agencies, which participate in the process of issuance of the initial construction permits the following:

- a) do not charge fees for project design conformance, performed by municipal organs, state supervision and other budget organizations, for work (services) on issuing to clients and developers of initial data, technical conditions and requirements for connection to utilities if those fees are not included in tariffs approved by decisions of governmental authorities and municipal organs;
- b) do not require from clients any letters or conclusion of agreements for project documentation approvals which give the right to charge fees for rendered services;
- c) set up the maximum time period for issuance of technical conditions in regulations approved in concordance with the current legislation – not exceeding 30 days from the day of submission by clients of the full set of required documentation;
- d) a number of other measures which exclude groundless additional expenses during preparation of initial permissive documentation.

7. Eliminate architectural authorities from land privatization process under article 36.

The consultants have been advised that the Offices of the Chief Architects in Perm Oblast municipalities are a significant bottleneck for approval of land privatization applications. In Perm the permit of the municipal unitary enterprise “Permarchbureau” is necessary to get in the process of enterprise land buy out. Privatization of land plots by existing users holding rights of privatization should not require land use approval. Privatization is a simple matter of survey and coordination of boundaries. Involvement of architectural authorities should only be required if there is a simultaneous request for change of use. A clear distinction must be established between privatization of land, which is an economic decision, and use of land, and the two procedures should be kept separate as far as possible.

Performance Monitoring

It is highly recommended that the regional and municipal administrations identify quantitative indicators of the performance of both real property markets generally and government service providers, and implement a monitoring system to periodically assess progress. The key indicators would draw on information available from government agencies and registries to assess levels of supply and demand in the market as well as progress toward achieving the objectives identified in this report. Indicators can help to assess the management performance of certain government agencies responsible for carrying out policy reform in the real estate sector. Accordingly, attached as Appendix II to this report is a set of tables which suggest the types of indicators that would be *minimally necessary* for assessing progress in real estate market development, elimination of administrative barriers to investment in real estate, and, generally, improving the investment climate in this sphere.¹³ Much of this information is presently available from various federal, regional and municipal agencies. Examples of relevant data already gathered within the state statistical survey include:

- Form 22-1 *Data on Availability and Distribution of Lands by Ownership Categories and Forms* (approved by the RF Statistics Committee Decree #97 as of 16/10/2000);
- Form 22-5 *Data on Distribution of Urban Lands by Ownership Types* (approved by the RF Statistics Committee Decree #97 as of 10/16/2000);

¹³ The regional and municipal administrations could set a more ambitious task than proposed here to elaborate and implement a very comprehensive system of interrelated quantitative and qualitative indicators reflecting all main processes in the real estate sphere, including its’ role in the economic structure of the region or municipality, as well as all types of revenues to the regional and local budgets generated by the segments of private, federal, regional and municipal real estate located within the territory of Perm Oblast. Elaboration of such comprehensive managerial instrument for the real estate sector does not exist in Russia and goes beyond the objectives of the present report

- Form F3-zem *Data on Land Transactions*, Section 2 (approved by the RF Statistics Committee Decree #97 as of 10/16/2000);
- Form 1, *Housing Stock*, (approved by RF Statistics Committee Decree #71 as of 09/21/2001);
- Form F3-privatization *Data on Privatization of an Enterprise (Organization)*, Form F3-privatization *Data on the Results of Privatization* (approved by the RF Statistics Committee Decree #114 as of 12/31/99).

In case the collection of data would exceed the current requirements of the RF Statistics Committee the regional and municipal agencies should be instructed regarding the types of data that will be required for the monitoring effort, the methodological aspects of its' collection, and be required to adjust their data gathering activities accordingly. To be viable it is crucial that this new data collection procedure should acquire an official status, that is to say, it should be approved by resolution of head of regional administration that identifies responsible officials, reporting dates, and the exact division of the administration which coordinates all the activity and receives the final data.

Further suggestions with regard to monitoring of performance indicators include:

- Establish an interagency task force responsible for monitoring and evaluation of progress in real estate markets, including representatives of the land, property, architectural, and finance committees as well as the cadastre and registry.
- Establish relationships with key private sector development, brokerage and financial firms that would be willing to periodically contribute data; include private sector representatives on the monitoring task force.
- Consider establishing a formal annual report of the regional administration on development of the land and real estate market, which would present and analyze the performance indicators to all interested participants of the real estate market and the community.

In conclusion it needs to be stressed that the development of the land and real estate market and the associated investment activities in this sector are far ahead of the development of the informational support of these processes. Without quantitative records of changes, neither timely regulation by the regional and local authorities, nor adequate response of the private sector of the economy is possible. Therefore, any attempt to bridge this gap, including the proposed project of organizing regional/municipal monitoring of land and real estate, merits priority attention and the full support of those concerned with the economic development of the Perm Oblast.

APPENDIX I

"PROPERTY PRINCIPLES" OF THE COMMONWEALTH OF AUSTRALIA

TABLE 1: PROPERTY PRINCIPLES OF THE AUSTRALIAN GOVERNMENT

1. The Commonwealth should own property where the long-term yield rate exceeds the opportunity cost of capital, currently set at 11 per cent, or where it is otherwise in the public interest to do so.

2. Public interest considerations which may influence the decision as to whether the Commonwealth should own property include circumstances where the property has:

- national symbolic significance;
- national security requirements;
- strategic significance to future government use;
- highly specialized uses that would significantly inhibit commercial provision;
- significant heritage and environmental requirements;
- significant public usage;
- characteristics such that the nature of the use or development of the property by the Commonwealth would give a potential lessor excessive future negotiation power (e.g. where the Commonwealth needs to make a large investment in specialized fit out);
- special diplomatic requirements, where either no market exists or government-to-government reciprocity arrangements in the context of the Vienna conventions apply; or
- there exists clear evidence of market failure. This could include properties such as small regional offices in isolated locations where there would be no other tenants should the property become vacant or where private investors would demand excessive rates of return to recover their investment over the life of a lease; and those in markets where there is a predominance of Commonwealth ownership.

3. The onus should rest with the proposing agency to clearly demonstrate the characteristics of the property that warrants Commonwealth ownership.

4. Where market failure is claimed, the market circumstances for the property should be adequately tested, including consideration of offering lease terms or conditions that might allow private investors or developers to convert a `government guarantee of rental income into the capital necessary to provide the accommodation and earn a market return; and

5. Where market failure is established, the relevant Minister should take the proposal to Cabinet in the Budget context.

6. To encourage efficient, effective and transparent decision-making and accountability:

- the costs of property use (whether owned or leased, domestic or overseas) should be fully reported by the using agency or program;
- property costs should be measured (and wherever practical, charged) on the basis of competitive neutrality - i.e. costs to the Commonwealth should be measured on the same basis as the private sector; and
- property costs should recognize the costs of holding unused land in reserve for possible future use, except for certain land with national significance and where disposal is not an option.

7. When seeking the provision of accommodation to meet Commonwealth needs, a proactive approach should be taken to inform the market well in advance of the project so that the market has time to develop solutions to meet the Commonwealth's needs.

8. Where Commonwealth ownership is decided upon, the property should be managed so as to retain the maximum long-term economic advantage to the taxpayer. Financial and/or organizational arrangements should be made to ensure the effective maintenance and refurbishment of the facility are to agreed standards. Failure to do so risks Commonwealth exposure to high property vacancy rates, additional costs and failure to meet its legal obligations under Occupational Health and Safety legislation.

9. For Commonwealth agencies occupying property owned by another part of the Commonwealth, occupancy agreements should be formalized between the Commonwealth property owner and the occupying agency.

10. Conditions and rentals should be market based. All agreements between arms of the Commonwealth should be binding, and transferable on sale of properties. Where such properties are identified for sale, the occupancy agreements should be placed in a form that facilitates completion of the sale.

11. Property management services provided within Commonwealth bodies should be fully market tested, including the option of in-house bids consistent with the principles established in the Commonwealth's Competitive Neutrality Policy.

12. Where property is being provided on an internal market basis, there should be a clear separation of responsibility between the area responsible for maximizing the performance of Commonwealth owned property and any area responsible for tenant advocacy.

APPENDIX II

**MONITORING AND PERFORMANCE
INDICATORS**

**TABLE 1
REGISTRATION OF RIGHTS TO REAL PROPERTY IN THE PERM REGION**

Indicators	Units	1997-2001	2002	2003	2004	2005
Average duration of registration services:	Days					
Registration of ownership rights and other rights						
Registration of transactions of real property, encumbrances	“					
Abstracts	“					
Average costs of registration services:	Rub					
Registration of ownership rights and other rights						
Registration of transactions of real property, encumbrances, including	“					
Purchase and Sale	“					
Mortgage	“					
Etc.	“					
Abstracts	“					
Registration fees collected:	Rub					
Total	“					
From citizens	“					
From legal entities	“					

**TABLE 1
REGISTRATION OF RIGHTS TO REAL PROPERTY IN THE PERM REGION**

Indicators	Units	1997-2001	2002	2003	2004	2005
Number of Transactions Registered:	Number					
Total	“					
Sale of Residence, including	“					
Single-family	“					
Apartment	“					
Sale of Land Plot	“					
Sale of non-residential building/premises	“					
Lease of Land Plot	“					

TABLE 2								
LAND OWNERSHIP IN THE PERM REGION, SQUARE METERS BY TYPE OF OWNER								
Year	Total area	Owned by individuals	Owned by legal entities	Owned by state and municipal governments				
				Total	Including those transferred to			
					Individuals		Legal entities	
					For use	For rent	For use	For rent
1992-2001								
2002								
2003								
2004								
2005								

TABLE 3 OWNERSHIP OF NON-RESIDENTIAL BUILDINGS AND PREMISES IN THE PERM REGION, BY TYPE OF OWNER								
Year	Total area (sq. m.)	Owned by individuals	Owned by legal entities	Owned by state and municipal governments				
				Total	Including those transferred to			
					Individuals		Legal entities	
					For use	For rent	For use	For rent
1992-2001								
2002								
2003								
2004								
2005								

TABLE 4
SALE OF STATE AND MUNICIPAL LAND AND REAL ESTATE, BY PROCESS OF SALE

Type of Property	1992-2001	2002	2003	2004	2005	2006	2007	Total
Buildings, constructions, structures								
Direct Sale (not including privatization):								
Number								
Area (000 m ²)								
Revenues								
Auction/Tender:								
Number								
Area (000 m ²)								
Revenues								
Privatization:								
Number								
Area (000 m ²)								
Revenues								
Other:								
Number								
Area (000 m ²)								
Revenues								
Non-residential premises								
Direct Sale (not including privatization):								
Number								
Area (000 m ²)								
Revenues								
Auction/Tender:								
Number								
Area (000 m ²)								
Revenues								
Privatization:								
Number								

TABLE 4
SALE OF STATE AND MUNICIPAL LAND AND REAL ESTATE, BY PROCESS OF SALE

Type of Property	1992-2001	2002	2003	2004	2005	2006	2007	Total
Area (000 m ²)								
Revenues								
Other:								
Number								
Area (000 m ²)								
Revenues								
Land Plots								
Direct Sale (not including privatization):								
Number								
Area (000 m ²)								
Revenues								
Auction/Tender:								
Number								
Area (000 m ²)								
Revenues								
Privatization:								
Number								
Area (000 m ²)								
Revenues								
Other:								
Number								
Area (000 m ²)								
Revenues								

TABLE 5 CONSTRUCTION ACTIVITY IN THE PERM REGION							
Indicator	1996-2001	2002	2003	2004	2005	2006	Total
Building Permits, New Construction							
Number							
Square Meters							
Average Cost of Construction (rub/m ²)							
Building Permits, Renovation							
Number							
Square Meters							
Average Cost of Construction (rub/m ²)							
Permits Issued For:							
Multifamily residential							
Single family residential							
Office							
Trade and Service							
Industrial and Storage							
Hospitality							
Certificates of Completion Issued							
Number							
Square Meters							

TABLE 6						
LEASE OF STATE (MUNICIPAL) LAND AND REAL ESTATE IN THE PERM REGION						
Indicator	1992-2001	2002	2003	2004	2005	Total
Lease of Land Plots						
Number						
Square Meters						
Average Lease Term (Years)						
Median Lease Term (Years)						
Average Rent (rub/m ²)						
Assignments of Rights Under Land Plot Leases						
Number						
Square Meters						
Approved Subleases of Land Plots						
Number						
Square Meters						
Leases of Buildings and Premises						
Number						
Square Meters						
Average Lease Term (Years)						
Median Lease Term (Years)						
Average Rent (rub/m ²)						
Assignments of Rights Under Buildings/Premises Leases						
Number						
Square Meters						
Approved Subleases of Buildings/Premises						
Number						
Square Meters						

TABLE 7						
AVERAGE LAND AND REAL ESTATE PRICES IN THE PERM REGION, RUBLES PER METER SQUARED						
Type of Property	2002	2003	2004	2005	2006	2007
Land Plots						
City						
Residential						
Commercial						
Industrial and Warehouse						
Suburban (agricultural use?)						
Residential						
Commercial						
Industrial and Warehouse						
Buildings and Premises						
City						
Residential						
Commercial						
Industrial and Warehouse						
Suburban						
Residential						
Commercial						
Industrial and Warehouse						

TABLE 8 AVERAGE TIME AND COSTS RELATED TO ACQUISITION AND DEVELOPMENT OF REAL PROPERTY IN THE PERM REGION						
Indicator	Unit	2002	2003	2004	2005	2006
Land Boundary Survey						
Time to Approval	Days					
Cost	Rubles					
Technical Passport						
Time to Completion	Days					
Cost	Rubles					
Technical Conditions						
Time to Issuance	Days					
Electric	"					
Gas	"					
Water	"					
Heating	"					
Telephone	"					
Cost	Rubles					
Electric	"					
Gas	"					
Water	"					
Heating	"					
Telephone	"					

TABLE 8 AVERAGE TIME AND COSTS RELATED TO ACQUISITION AND DEVELOPMENT OF REAL PROPERTY IN THE PERM REGION						
Indicator	Unit	2002	2003	2004	2005	2006
Infrastructure Connection Fee	Rubles					
Electric	"					
Gas	"					
Water	"					
Heating	"					
Telephone	"					
Land Allocation - Application to Execution of Sale/lease Agreement						
Time from Application to Issuance (?)	Days					
Construction Permit						
Time from Application to Issuance	Days					
New Construction	Days					
Renovation	Days					

TABLE 9
RESIDENTIAL CONSTRUCTION IN THE PERM OBLAST

Year	Completed construction projects, total		Types of residential construction																		
			Multifamily buildings														Individual houses				
	State and Municipal								Private Sector								Private residences		Summer houses		
	1-room apartments		2-room apartments		3 room apartments		Other		1-room apartments		2-room apartments		3 room apartments		Other		K		Л		
	A		Б		В		Г		Д		E		Ж		З		И		K		Л
units	m ²	units	m ²	units	m ²	units	m ²	units	m ²	units	m ²	units	m ²	units	m ²	units	m ²	units	m ²	units	m ²
1992																					
2005																					

TABLE 10
GROWTH OF REAL ESTATE MORTGAGE LENDING IN THE PERM REGION

Indicator	2000	2002	2003	2004	2005	2006
No. of Mortgages:						
Acquisition of Existing Property:						
Land (only)						
Non-residential buildings and premises						
Residential						
Single-family						
Apartment						
New Construction:						
Non-residential buildings and premises						
Residential						
Single-family						
Apartment						
Amount of Mortgages:						
Acquisition of Existing Property:						
Land (only)						
Non-residential buildings and premises						
Residential						
Single-family						
Apartment						
New Construction:						
Non-residential buildings and premises						
Residential						
Single-family						
Apartment						