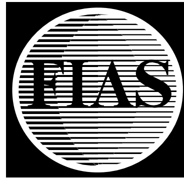


**Foreign Investment Advisory Service,**
**a joint service of the**
**International Finance Corporation**
**and the World Bank**

**Project is co-financed by the**
**European Union**
**in the framework of the**
**Policy Advice Programme**

# PROJECT
# LAND REFORM PRIVATIZATION PROCEDURES AND MONITORING SYSTEM

## FINAL REPORT ON BUSINESS ACCESS TO LAND

**PREPARED FOR**
**THE MINISTRY OF ECONOMIC DEVELOPMENT AND TRADE**
**OF THE RUSSIAN FEDERATION**

**OCTOBER 2005**

**The Report is prepared by FIAS consultants Stephen B. Butler and Andrei V. Khakhalin.**

**Disclaimer (EU)**

This publication has been produced with the financial assistance of the European Union. The contents of this publication are the sole responsibility of its authors and can in no way be taken to reflect the views of the European Union.

**Disclaimer (FIAS)**

The Organizations (i.e. IBRD and IFC), through FIAS, endeavor, have used their best efforts in the time available to provide high quality services hereunder and have relied on information provided to them by a wide range of other sources. However they do not make any representations or warranties regarding the completeness or accuracy of the information included this report, or the results which would be achieved by following its recommendations.

**Content**

EXECUTIVE SUMMARY ....................5

I. BACKGROUND ....................5

II. PRIVATIZATION OF LAND OCCUPIED BY ENTERPRISES AND BUILDING OWNERS (RIGHT OF RE-REGISTRATION) ....................5

Re-Registration ....................5
Cadastral Valuation, Generally ....................6
Speculation ....................6
Boundary and Title Disputes ....................7
*"Systematic" resolution of boundaries and titles under "land management" procedures* .................... 7
*The concept of "conditional title registration"* .................... 7
*Cadastral survey requirements and the concept of "general land boundaries"* .................... 8
*Development of Federal Rules on Settlement of Boundary Disputes for Re-registration Cases* .................... 9
*Encouragement of "Alternative Dispute Resolution"* .................... 9
Re-registration Procedures and the Roles of Local and Federal Governments ....................10
Land Leasing ....................10
Re-allocation of receipts from rents, sales and taxes ....................11
Reservation of land for future public needs ....................12
Monitoring Progress ....................13

III. AVAILABILITY OF UNIMPROVED LAND FOR NEW CONSTRUCTION ....................13

Experience with Land Auctions ....................14
Non-competitive land allocation procedures ....................14

FINAL REPORT ON BUSINESS ACCESS TO LAND ....................16

I. BACKGROUND ....................16

II. PRIVATIZATION OF LAND OCCUPIED BY ENTERPRISES AND BUILDING OWNERS (RIGHT OF RE-REGISTRATION) ....................18

A. Why Re-Registration? ....................18
B. Current Experience with Re-Registration ....................19
C. Main Issues Affecting Re-Registration ....................20
1. Valuation/Pricing ....................21
2. Cadastral Valuation, Generally ....................24
3. Speculation ....................27
4. Boundary and Title Disputes ....................29
*(a) "Systematic" resolution of boundaries and titles under "land management" procedures* .................... 29
*(b) The concept of "conditional title registration"* .................... 32
*(c) Acceleration of timing between registration of transactions and registration of rights.* .................... 35

*(d) Cadastral survey requirements and the concept of "general land boundaries"* ..... 36
*(e) Delineation of state land* ..... 39
*(f) Development of Federal Rules on Settlement of Boundary Disputes for Re-registration Cases* ..... 41
*(g) Encouragement of "Alternative Dispute Resolution"* ..... 42
5. Re-registration Procedures and the Roles of Local and Federal Governments ..... 45
6. Compulsory Conversion of Rights ..... 47
7. Re-allocation of receipts from rents, sales and taxes ..... 50
8. Reservation of land (removal of land from circulation) for future public needs ..... 51
9. Monitoring Progress ..... 54

III. AVAILABILITY OF UNIMPROVED LAND FOR NEW CONSTRUCTION ..... 56

A. Current Law ..... 56
1. The Land Code ..... 56
2. Recent changes to auction procedures for residential land ..... 57
3. Current auction regulations affecting commercial development - Government Resolution 808 ..... 59
B. Experience with Land Auctions ..... 60
C. Improving the efficiency and transparency of land auction procedures ..... 62
D. Non-competitive land allocation procedures ..... 64
E. Land Allocation and the RF Urban Planning Code ..... 66

ANNEX CONDITIONAL AND POSSESSORY TITLE UNDER UK LAW ..... 68

# EXECUTIVE SUMMARY

## I. Background

This report is the product of a program of cooperation between the Foreign Investment Advisory Service (FIAS), a joint service of the International Finance Corporation (IFC) and the World Bank, and the Russian Federation Ministry of Economic Development and Trade (MEDT) under a grant from the European Union Policy Advice Programme in Russia. The main subjects of cooperation were urban land reform, in particular improving access to land for small land medium enterprises; the role of the anti-competition laws in addressing business land issues; and development of a system for MEDT to monitor developments in land reform over time. This report summarizes only the conclusions and recommendations on the urban land issues and business access to land.

## II. Privatization of Land Occupied by Enterprises and Building Owners (Right of Re-Registration)

### Re-Registration

In its ongoing surveys of the attitudes and experiences of Russian businesses (reports forthcoming in early 2006), FIAS has determined that the progress with re-registration of enterprise land rights has been poor.

The main issues affecting re-registration of land rights identified in our discussions were pricing; speculation in land; cadastre and title registration issues; and procedures for re-registration and the respective roles of local and Federal governments. The conclusions and recommendations provided by FIAS with regard to the program of land re-registration included:

- The indirect and long term benefits of encouraging privatization of enterprise occupied land through low prices outweigh the direct, short term benefits budget revenues from land sales. Those benefits include increased investment in land improvements, increased employment, higher value uses of underutilized urban lands, increased tax revenues and a more vibrant private market.
- It should be acknowledged that there is a difference between the cadastre/taxation value of the land and the value as encumbered by the occupants' long term right of use, which must be taken into consideration in pricing. The land presently occupied by privatized enterprises and businesses has little value to the region or municipalities, as the rights of use are virtually perpetual and strongly protected by law.
- We continue to recommend that continued testing be done on a sample basis to determine the relationship of the new formula prices to prices that would be

determined by application of international appraisal standards, taking into account the crucial issue of the rights of use encumbering the land.

- While we believe that there is strong historical evidence that reduction in prices will increase demand for land by enterprises, prices are only one part of the issue. It is our belief that demand for land privatization may increase if more favorable terms are offered to potential purchasers, including: improving transparency in privatization procedures, extending the period for payment of the land price to reach 3-5 years; authorize subdivision of large land plots into smaller ones and allow them to be purchased separately; permit land users to take ownership of only a portion of their land without affecting the rights to the remaining land.

**Cadastral Valuation, Generally**

In general, the work being done on cadastral valuation appears to be a reasonable start, though there is considerable disagreement on this point among Russian land experts, in particular professional appraisers. Based on discussions with the Federal Agency for Real Estate Cadastre, the methodology for the cadastral valuation substantially follows international norms, with adjustments to address the limitations of the data available in the Russian context. The most significant problem is the lack of market data on land prices in many areas of Russia, which requires substitution of other indicators in the valuation models. It appears that the approaches taken to address these problems are generally well conceived and creative for the time being, but will be replaced by more conventional approaches as the market develops and sufficient market data becomes available.

We reviewed the MEDT draft Law on Formation, State Cadastre Registration, State Cadastre Appraisal of Real Estate and the draft Regulation on State Cadastre Appraisal of Land and presented our views on the cadastral valuation and appeals processes in a separate report.

**Speculation**

When the proposal for a speculation tax was first raised the FIAS team raised the concern that exacting an excessive premium on re-development of the land could result in an impasse between the current occupants and the government and undermine the objective of urban redevelopment.

Particularly troubling is that this speculation tax appears to be in addition to the present infrastructure charge demanded by most cities, which can be as much as 25% of the costs of a land development project. Moreover, the combination of increasing cadastral values over time and the suggestion that the basis for the tax would be the cadastral value of the land subject to the new use and not its restricted use suggests that at some point land holders will be paying more for the land than if they bought it today at its market price.

We continue to believe this tax may be a disincentive to urban redevelopment for the reasons provided in the report.

**Boundary and Title Disputes**

The MEDT Report strongly implies that major barriers to progress in enterprise land privatization arise in the delineation and registration of land rights. The report considers several tools or mechanisms on which we have been asked to comment, and several other possibilities have been raised in discussions with MEDT. These proposals include "systematic" cadastre and registration of titles under "land management" principles; introduction of legal concepts of "conditional title" and "general land boundaries" into Russian practice; development of Federal rules on adjudication of boundary issues in privatization cases; and the relevance of principles of "alternative dispute resolution" to boundary and title disputes.

*"Systematic" resolution of boundaries and titles under "land management" procedures*

- We do not think that the conditions exist in Russian today to implement systematic registration on a large scale.
- Flexibility should be the main objective. A comprehensive law on cadastre and title registration should contain the option for administration officials to implement systematic programs on a compulsory basis, regardless of whether the option is ever used.
- The option to implement systematic cadastre in an area should be given to the Federal Agency for Real Estate Cadastre where the necessary conditions exist, including high land values, unsettled borders, and large numbers of privatization applications and land disputes.
- There should be the possibility to implement systematic cadastre and registration in small areas, less than an entire cadastral section or district. This would be the case, for example, in high value areas in which there are a significant number of existing or potential applications for re-registration.

*The concept of "conditional title registration"*

- Whether implementation of "conditional registration" in Russia would be useful depends on the facts. It is an open question whether the need for conditional titles exists, but there are indications that the usual conditions for implementation of conditional registration do not exist in Russia today.
- As usual in such circumstances, and in the absence of good statistical data relevant to the issue, we recommend flexibility. There is nothing to be lost by allowing a form of conditional title based on reasonable evidence. Such a registration would lack the state guarantee of accuracy. The most significant risks are corruption and abuse of the system by registrars or creation of public

confusion concerning the legal implications of registration, which can be addressed.

- Short of extending the concept of conditional title to all real estate, we believe that conditional registration could be useful in one important case, which is the registration of beneficial rights to re-registration of title to enterprise land or land occupied by building owners. Conditional registration of the title would be a means of protecting the land holders' rights until such time as issues are resolved and an unconditional title can be granted. Such conditional registration would be registered immediately upon submission of an application for privatization and remain in effect throughout the process, including court actions.

*Cadastral survey requirements and the concept of "general land boundaries"*

- The Russian system already incorporates an indirect concept of general boundaries by establishing different survey accuracy standards for different contexts, with much lower accuracies required for rural and agricultural areas. This relaxation of survey accuracy standards is also a means of increasing speed of survey and decreasing costs as it expands the range of technologies that may be used to delineate boundaries.
- There may be some cases in Russia in which a concept of general or approximate boundaries may be appropriate.
- The cadastre law should establish a broad definition of boundaries and leave details to appropriate regulations. For example, it should not be required that all boundaries be established on the basis of national coordinates system.
- Survey accuracy standards should not be set on the basis of whole territories or areas, but should be left flexible to be applied depending on the circumstances and the wishes of the land owners (defined circumstantially, not territorially).1 If adjoining land owners are willing to live with approximate boundary locations that should be a choice available to them, wherever they are located.
- In our opinion, the key to general boundaries is not necessarily the nature of the survey or the boundary markers, but the fact that the parties understand that the boundary is not legally fixed. This we believe is also the utility of the concept as a dispute avoidance tool. So, the benefits of general boundaries can be largely achieved by applying the relaxed survey accuracy standards of rural areas to the urban areas as well, if desired by the parties.

[1] For example, the draft Law On Cadastre provided to us states that "accuracy of location and borders may vary from territory to territory on which a real estate item is located," suggesting that standards must be set on a territorial rather than factual basis.

*Development of Federal Rules on Settlement of Boundary Disputes for Re-registration Cases*

- Since the entire re-registration program is a creature of Federal law, it may be useful to develop more detailed regulations and procedures for localities to follow in determining the size and contours of the land that is subject to re-registration. Such a detailed regulation would give flesh to the vague provisions of the Land Code, establish uniform practices and provide grounds to challenge arbitrary decisions of localities.

*Encouragement of "Alternative Dispute Resolution"*

- The proposal for systematic cadastre and registration is in effect a form of compulsory ADR. We believe this form of ADR may be most appropriate in high value areas populated by many large enterprise land owners whose claims should be resolved simultaneously but who otherwise have little incentive to participate in ADR procedures.
- If adopted, the cadastral surveying methodology proposed by the MEDT in its draft Law on Cadastre, on which we have commented, will implement a form of ADR with respect to boundary disputes.
- The objective of ADR is essentially to provide a means of dispute resolution that is quicker and cheaper than court action, which given court backlogs can take years to complete. There are many ways to do this, including administrative appeals procedures. In many cases laws require completion of an administrative appeal as a condition of filing a lawsuit in court. We recommend that a new system of administrative appeal for re-registration cases be established to resolve in particular disputes between applicants and municipalities.
- Some form of ADR could be useful in boundary disputes between private parties. It is in fact used in many places today, and has been used in Russia under several pilot programs sponsored by foreign donors.
- Private parties are not likely to seek ADR on their own initiative unless they are aware of its existence and benefits. Nor will they use it if it is costly and not likely to provide the same degree of resolution as a court decision. The most effective way to induce private participation is to make the mediation service available and to educate the public about its availability and benefits. Possible ways to establish the service is to use the personnel of the Federal Agency for Real Estate Cadastre as expert advisors and mediators, as a public service in support of completion of the re-registration program.
- Disputes to which municipalities are a party are not good subjects for ADR unless the municipalities agree or are compelled to participate. Whether either is likely is not for us to answer.
- Consideration should be given to establishing permanent local commissions that would hear land disputes. These "local land commissions" would be both a means of administrative appeal and a means of mediating disputes between

private parties. Composition of the commission would be independent experts in land matters.

- The present Law on Arbitration Tribunals in the RF (102FZ of July, 2002) establishes rules for creation and operation of permanent and ad hoc third party arbitration tribunals. This is a complex law which creates a formal system of arbitration. It provides for but does not require binding decisions, and allows for enforcement of decisions through normal executive procedures. Its utility in the types of disputes at issue in the present discussion could be limited.

**Re-registration Procedures and the Roles of Local and Federal Governments**

Among the complaints about the land acquisition procedures expressed by businesses in response to the ongoing FIAS surveys of business attitudes and experiences there are the necessity to obtain numerous official approvals; requirements to produce documents not specified in the law; arbitrary bureaucratic behavior; direct or oblique allusions to the necessity of unofficial payments; and arbitrary interpretation of the legislation. These are essentially issues of process management. The underlying problem may be that municipalities have inherent conflicts of interest in the re-registration process.

One approach to this problem would be to "Federalize" the re-registration process in an existing or newly created agency of the RF Government. Federalization of the process could also assure greater consistency in policy and implementation. A second and similar approach would be to require that the process be managed by local commissions that are independent of the municipal administration. One of the benefits of both the Federalization and the independent commission models is that they would implement a "one-window" facility for processing of applications. A less intensive alternative may be to create a Federal administrative appeals procedure for re-registration cases. This would leave local discretion and institutions in place, but subject to oversight by administrators with an interest in supporting the policy of re-registration.

**Land Leasing**

It is our view that the tendency of local administrations to offer land for lease but not as ownership conflicts with the national objective of creating private sector property markets. At this point in development of the Russian land economy, we view land leasing as a poor "second best" alternative which has many potential drawbacks for development of property markets, including continued legal separation of land and real estate rights; greater opportunity for government interference in private economic decisions; misallocation of land through under- or over-pricing and favoritism; administrative complexity; greater opportunity for official corruption; and inferior property rights. In general, we believe there are significant problems associated with government monopolization of any factor of production. We believe that our reservations are also reflected in the attitudes of most Russian business people, who prefer ownership to leasing. All of these can be debated, but our ultimate conclusion is that Russia needs a private land market to serve as a check on the current level of

government monopolization, and that market can be achieved only by mandating some level of land sales. This is not to say that there should be no public land ownership or that leasing may not be appropriate in certain circumstances even today, and the emphasis on sales may perhaps be reconsidered as the amount of privately owned land increases and true private markets develop.

Steps that can be taken to improve the quality of leases include:

- Consider clarifying the law to provide that a land plot must be sold as property ownership at an auction or tender unless leasing is justified, and identify specific and limited criteria for offering a lease rather than property ownership.

- Further with respect to change of use of leased land, the leases should provide that lessees are permitted any use which is permitted for the land plot by right under the town plans (not special permit uses), without the need for consent of the lessor. In their use of the land lessees should be subject only to the general rules of town planning and environmental protection.

- Regarding the term of 49 years, we have argued consistently that the emphasis on this term in Russian practice is misplaced, and that there is no reason not to extend the lease term to 75 or even 99 years, or alternatively to require extension of the term unless rejected by land holder. Longer terms are commonplace in other countries, and provide more security to the investor and to mortgage financiers.

- Leases issued under the re-registration program should follow a format established by rules. Those rules should prohibit termination of the lease for any reason other than willful environmental degradation and failure to pay rent for an extended period of time, perhaps 2-3 years. Beyond this, termination of the lease should be permitted only on the same grounds that confiscation of the land would be permitted.

- The leases should contain an option to purchase which may be exercised by the lessee at any time during the term at a price equivalent to the original buyout price adjusted for increases in cadastral value, with a credit against the buyout price for lease payments already made.

**Re-allocation of receipts from rents, sales and taxes**

An analysis of the history of land privatization in Russia leads to the conclusion that local obstruction of privatization of enterprise land is at least partly based on economic calculations. The situation is gradually changing. To encourage localities to support re-registration, consideration could be given to further amending the federal tax legislation to provide that until delineation of state-owned land property is completed, a greater share of revenues from sale of all categories of land go into local budgets. Still the better approach may be to introduce amendments to the federal law providing for: (1) the

revenue from sale into property and sale of leasing rights on unimproved land assigned for production and commercial uses, as well as in the case of unimproved land for housing development, shall go in full into local budgets until the delineation of state-owned land is completed; (2) 50% of the proceeds from the sale of all improved land (occupied by enterprises and building owners) located within the municipalities shall go to the local budgets, until the state-owned land plots are delineated by type of owner.

**Reservation of land for future public needs**

Major exceptions to the right of re-registration occur when the land is reserved for future public use or located in protected territory. These exceptions can undermine the policy of re-registration, and account for most denials of applications. One of the troubling aspects of this practice is that it effectively deprives land holders of a right without compensation. The RF Urban Planning Code addresses these issues in the most rudimentary way, and does not define precisely that the reservation itself has to be made a legal component of the territorial plans, adopted in the same way as any adoption or change to the plan. To avoid adverse results, further steps could be taken to limit this practice. Possible steps that should be considered include:

- Planning reservations should be permitted only through the usual processes for adopting or amending urban plans.
- Reservation of land in planning documents should be supported not just by planning standards, but by budgetary and financial standards. Economic feasibility and cost-benefit analysis should be required to justify inclusion of a reservation in a municipal plan.
- Limit reservations to public facilities. Exclude reservations which amount to nothing more than a proposed change from one use to another, such as "industrial" to "residential."
- The facility for which a reservation is made should be included in the capital budget of the municipality.
- Absence of urban planning documents for the developed area in which the land is located should not be recognized as legal grounds for denying applications for purchase.
- Non-conformity of the present use with urban plans should not be recognized as grounds for denial of application for purchase. The land holder should have the same rights as any owner of a building or facility that does not conform with land use restrictions adopted after construction of the facility.
- Establish time limits in which the municipality must actually take the land and/or pay compensation to the holder for termination of the right of use. Until there is an immediate cost associated with reservation of land for public use, and in the absence of other effective restrictions, municipal planners have the incentive to reserve too much land. Too much land will be reserved for unrealistic purposes.

- Provide that if the land is not taken within a reasonable period, perhaps 5 years, the reservation lapses, the holder's right to re-register the land as property is revived and it may be purchased at the initial re-registration price.
- Require periodic review and justification of the planning reservation.
- Require compensation for profits lost for denial of the right of re-registration on grounds of reservation for future public use, and develop regulations and formulas for calculating losses to the land holder.
- In connection with Federal oversight over the re-registration program, require municipalities to identify and justify all current reservations which can result in denial of a right of re-registration.

**Monitoring Progress**

In the course of this project the team attempted to obtain relevant statistics on land privatization in Russian cities, but without success. There is no requirement that localities report activities on land rights re-registration, and no Federal agency supervises this important national objective. At the same time, greater transparency may be one of the few tools the Federal government has to monitor the cooperation of local governments in implementing these policy objectives. We recommend that the Federal government establish a more detailed statistical reporting requirement for transactions in state and local land, covering not only the aggregate data, but the specific data on the terms and other conditions of these transactions as well, which are essential for policy making and land reform adjustments.

## III. Availability of Unimproved Land for New Construction

Re-registration of the land rights of enterprises and building owners is only one of the approaches to creating the private sector land market. Another important issue for improving business access to land is the legislation which defines the types of unimproved land plots which can be sold or leased for development purposes, which is mainly an issue of creating transparent competitive and non-competitive procedures for divesting state and municipal land into the private use and ownership.

The present law provides for mandatory auctions only (1) when land is sold into ownership and "prior conciliation of location" is not required, which is today a very small minority of cases, and (2) when land is made available for housing development pursuant to recent amendments to Article 38 of the Land Code.

The newly added clauses to Articles 30 and 38 of the Land Code are a step forward with regard to the allocation of land for housing, but raise a number of questions of their own, which are described in the report.

It would be more appropriate to develop details pertaining to land auctions and tenders for housing and commercial development in the "Rules of Organization and Management of Public and Municipal Land Sales and Leases" adopted by the Resolution of RF Government No. 808, as of 11.11.2002.

Except for housing, the procedures for competitive allocation of land plots used for commercial and other purposes are still governed by the Resolution of the RF Government No. 808. In our estimation, various contradictions, ambiguities and simple errors in Resolution 808, described in the report, may undermine the efficiency of the current auction procedures. Further amendment and elaboration of Regulation 808 should be considered, particularly in respect of industrial and commercial development.

### Experience with Land Auctions

Use of competitive procedures for selling unimproved land plots has not been widespread, and a number of issues remain. To facilitate development of competitive land sales and enhance their efficiency we recommend that the following ideas be considered:

- Conceptual flaws and ambiguities in the recent amendments to the Land Code regarding housing land should be resolved before applying these same provisions to allocation of land for other purposes.
- Consideration should be given to permitting a wider range of concepts and techniques in auction procedures, including an option to pay off the purchase price by installments and to compete on the schedule of payments; reasonable pre-qualification procedures; the concept of the reserve price.
- Elaborate and provide the regions and municipalities with comprehensive Methodological Guidelines on Preparing and Conducting Land Auctions and Tenders, containing detailed comments on the current law on competitive land sales, and recommendations on its application under different local conditions, with a full package of model land auction (tender) documents attached to it.

### Non-competitive land allocation procedures

Competitive procedures are not necessarily appropriate in all circumstances, and it is likely that targeted allocation of land and property for commercial use will continue at some level. However, direct transactions can be made more transparent, an implied requirement of Land Code for all dispositions of state and municipal real estate. With respect to all non-competitive land allocation generally, we recommend that several points should be considered.

- We believe that competitive procedures are not appropriate in all cases, and that the objective is to bring the same level of transparency and protection of the public interest to non-competitive procedures.
- All land sales and leases, without exception, should be based on independent appraisal of market value or market rental, and should not be leased or sold for less than appraised value.
- The provisions of art. 31 of the Land Code on informing the community about anticipated allocation of land plots could be further developed by regulation and made more precise.

- The same procedures should be applied to any transaction in which a grant of "conciliation of location" for preparation of a land site is proposed. The right to negotiate a "conciliation of location" should be treated as allocation of a land right in the nature of an option, subject to announcement and solicitation of expressions of interest.
- Prior to completion of any non-competitive transaction, the proposed terms of the transaction should be published again for objections.

# FINAL REPORT ON BUSINESS ACCESS TO LAND

## I. Background

This report is the product of a program of cooperation between the Foreign Investment Advisory Service (FIAS) of the International Finance Corporation (IFC) and the World Bank, and the Russian Federation Ministry of Economic Development and Trade (MEDT) under a grant from the European Union Policy Advice Programme in Russia. The main subjects of cooperation were urban land reform, in particular improving access to land for small land medium enterprises; the role of the anti-competition laws in addressing business issues; and development of a system for MEDT to monitor developments in land reform over time. This report summarizes only the conclusions and recommendations on the urban land issues and business access to land.

Issues addressed in this report were identified through discussions with representatives of the MEDT at commencement of the project and through two video conferences sponsored by FIAS under the World Bank's Global Development Learning Network program and held in Moscow on December 17, 2004 and April 21, 2005, in which representatives of the Federal and regional governments, civil society and donor organizations participated. Regional governments participating in the video conferences included St. Petersburg, Leningrad, Veliky Novgorod, Nizny Novgorod, Rostov, and Tomsk. The discussion of the December 17, 2004 video conferences centered mainly on recent policy initiatives regarding land issues prepared by the MEDT which were under active consideration by the Government, as reflected in the Report of the MEDT "On Measures for Land Reform Realization" prepared for the Session of the Government of the Russian Federation of February 10, 2005 (herein the "MEDT Report"). The project provided a detailed response to the MEDT Report at the time of its consideration by the Government, and elements of that response are reflected in the present report.

Topics discussed at the April 21, 2005 video conference focused on policy initiatives and materials prepared by MEDT relating to the proposed formula for calculating buy-out prices for state owned land plots by privatized enterprises; draft regulations on cadastral land evaluation for purposes of taxation; and the draft Federal Law "On Formation, State Cadastral Registration, State Cadastral Evaluation of Real Estate Objects" (the "Cadastre Law"). The project has already provided assessments of these issues to MEDT, which are reflected in the present report also.

From a series of discussions between the FIAS team and MEDT at commencement of this work it was determined that the primary objectives of the MEDT sponsored land reform activity were:

- to increase business investment in fixed assets, including facilities and equipment by assuring the availability of long term, reasonably priced and secure rights to the land on which they can be located;

- to increase business productivity by assuring access to land and business facilities on reasonable terms; and
- to increase tax revenues from land, new investment and increased economic activity, which is expected to flow from more rationale use of land assets.

It was generally agreed that various barriers stand in the way of achieving these objectives, including an inadequate supply of well-located and serviced urban land for investment; municipal obstruction to private land ownership, reflected in lack of transparency and excessive technical requirements in land re-registration and allocation procedures; unresolved ambiguities in the legal regime governing land re-registration and allocation; and lack of mechanisms for resolving land titles and disputes so that land rights can be transferred to enterprises.

Specific approaches considered by MEDT to eliminate these barriers and achieve its objectives included:

- Facilitating completion of the process of conversion of permanent (perpetual) right to use land plots into title or lease. Conversion of rights (re-registration of land rights) can increase the supply of land in the private market, achieve the Government objective of unifying land titles, and serve as a check on government monopolization of land. As importantly, conversion of land rights can create the incentives to move currently underutilized land to more productive uses.

- Increasing the supply of land by completing the process of delineation of state ownership of land and optimization of allocation between various levels of budgets of revenues received from land. Completion of delineation will clarify titles and interests in the land, and resolve financial conflicts that may in the past have led to impasse and reluctance to place land in the market.

- Encouraging rational utilization of land by creation of a new unified land and real estate tax, including formation of mass appraisal of real estate.

- Improvement of the cadastre and registration of property rights.

- Increasing the supply of usable land by improving mechanisms for establishment of legal restrictions on land and real estate, including the procedure and terms of easements, reservation of lands for state and municipal needs, establishing transparent procedures for allocation of land, and ensuring adoption of legal zoning acts by the local governmental bodies.

The FIAS team was asked to provide views on these as well as other issues, which are the topic of this report. The main topic addressed is that of facilitation of the right of enterprises and building owners to re-register their land rights as ownership or lease. Under that topic this report discusses land pricing; procedures for re-registration and the role of local and Federal governments; boundary delineation and registration of titles, including systematic registration, the concepts of conditional titles and general

boundaries, and the relevance of mechanisms for alternative dispute resolution; the need for a performance monitoring system; land speculation; reservation of land for future public use; and land leasing policy. The second major topic discussed is allocation of undeveloped land plots for investment, which focuses primarily on the auction procedures of the Land Code, as recently amended and modified.

# II. Privatization of Land Occupied by Enterprises and Building Owners (Right of Re-Registration)

## A. Why Re-Registration?

Enterprise land privatization is a mechanism begun under the land legislation of the 1990s which entails sale of land ownership to privatized state and municipal enterprises and other owners of privatized buildings and facilities located on it. Sale of improved state-owned land to its users and occupants has been a mainstay of land privatization throughout transitional economies, perhaps for its simplicity, efficiency and sense of fairness. However, unlike the nations of Central and Eastern Europe, which typically required simultaneous privatization of enterprises and the land which they occupied, in Russia sale of land was not initially encouraged in the process of privatization of state-owned enterprises. The result is that most enterprises, buildings and other structures that became privately owned through enterprise privatization today remain situated on state-owned land.

The simple answer to the question "why re-registration?" is that it is the law. Today, owners of buildings and structures located on state-owned land, which includes most privatized enterprises but also a large number of new business that have managed to acquire ownership of buildings and facilities, have a broad legal right under the RF Land Code to acquire ownership of the land they occupy. Indeed, the present law actually requires enterprises and building owners to convert their permanent rights of use to rights of ownership or lease by January 1, 2006, a deadline which has been extended once and will probably be extended again for failure to make progress. Purchase and re-registration of the land is subject to application to the land owner, which may be the Federal, regional or municipal government, and payment of a purchase price. In cases where the boundaries of land to which the enterprise is entitled are not clear from previous land records, which apparently is true for many enterprises, acquisition may require prior resolution of boundary issues with neighbors and the local government.

The current law is based on a broad policy consensus in the RF Government. Important policy statements of the Russian Government establish that sale of enterprise occupied lands is an important component of Russian land policy today, believed by many policy makers to promise significant benefits for municipalities and regions as well as direct positive effects for the enterprises themselves.[2] Accordingly, since the year 2000 the RF

[2] These policy statements include in particular the Action Plan of the Government of the Russian Federation in the Sphere of Social Policy and Economics Modernization for the Years 2000 – 2001, adopted by the Resolution of the RF Government # 1072-p, and the Program of social and economic

Government has supported as official policy priority measures for effective use and development of real estate and involvement of land and real estate in market turnover, including creation of "unified" real estate objects by transferring land titles to owners of buildings and other constructed facilities, completion of privatization of enterprise land plots, and increasing legal protection for civil transactions in real estate.

Increased private ownership is viewed as a way to improve investor perception of the local investment climate and provide significant non-recurring revenues to government budgets. In addition, much land in and around Russian cities used for industrial purposes is believed to be underutilized, and private ownership is seen as a means to encourage investment, adaptive reuse and densification of land use. In particular, re-registration with rights of disposal can provide the incentive and resources for holders of underutilized urban land to relocate, clearing the way for more intensive use of the land.

The expected benefits of land privatization for the enterprises include guaranteed rights of use and disposal, protection from unpredictable rent increases on state and municipal land, the possibility of obtaining mortgage finance, and revenues from sale of excess and underutilized land. In addition, as suggested in the 2001 study of the Russian investment climate by FIAS, land ownership may influence investment decisions by some foreign and domestic investors for whom land rights are an important consideration.

## B. Current Experience with Re-Registration

The progress with re-registration of enterprise land rights has been poor. Though the situation differs among the regions, we know today from gross statistics provided by Gosstat that there are entire regions in which no land has yet been sold as property to privatized enterprises. In its ongoing surveys of the attitudes and experiences of Russian businesses, which are incomplete at this time, FIAS has made the following preliminary findings:

- Only about 6% of all enterprises actually own land.
- In a survey in one region, more than 70% of the respondents owned some of their buildings or facilities, but less than 30% of those owned the land beneath the building.
- One survey of four prominent regions found that one-tenth to one-third of new companies are trying to buy their land, but only 20% to 30% of those who applied succeeded.
- In one survey only 11% of respondents who tried to buy land actually completed the procedure; the other 89% were either in process or were unsuccessful. In that same survey 37.3% of respondents attempting to purchase their land reported they were forced to make illicit payments.

development of the Russian Federation in midterm prospect for the years 2002-2004, adopted by the Resolution of the RF Government # 910-p.

- In one survey only 6.7% of respondents actually attempted to buy land under their building. The main reason given was that over 50% of respondents did not own their premises, but 19% claimed that the land is too expensive, only 7.5% expressed a preference for leasing, and 9% believed that that the process of obtaining the land was too complicated (and presumably not worth the effort considering they held undisturbed use rights).

- Among the negative aspects of the procedures for acquiring land, respondents most often pointed out the necessity for numerous approvals. Almost 70% of respondents "fully disagreed" with this statement: “The rules of buying land are transparent and predictable”.

- The surveys find a range of experience among the regions studied. The most frequently encountered negatives expressed by respondents included the necessity of numerous approvals; demands to produce redundant documents which are not required by law; "bureaucratic despotism" of officials; the necessity of personal relations with government officials; direct or oblique allusions to the necessity of unofficial payments; and inconsistent interpretation of the legislation.

These findings are not surprising to representatives of Russian business. In the recent past business representatives and their associations have been sharply criticizing the provisions of the Land Code governing land privatization by enterprises and other building owners. In 2003 the discussion reached the level of the State Duma, were parliamentary hearings were held on the entire range of issues pertaining to land rights. The main objections raised by the enterprises during those hearings included unrealistically high prices, often based on arbitrary manipulation of land tax rates by local authorities; inability of businesses to deduct land prices from income for tax purposes; unrealistic time limitations on conversion of land use rights to other forms of tenure; and arbitrary and unlawful re-registration procedures.

Based on our own investigations, we are in general agreement with the issues raised by the business community, though not necessarily with all of the solutions recommended. For example, the FIAS team agrees with MEDT that a different approach to land rights re-registration is justified for natural resource companies and for holders of large amounts of land on which are located utility and communications infrastructure ("linear facilities"). Use of air space over land or space under land for normal utility facilities, including pipelines and overhead lines, does not require transfer of land ownership. Typically such uses would be subject to easement or concession rights over or under the land, which would allow efficient use of the land for multiple purposes.

## C. Main Issues Affecting Re-Registration

The main issues affecting re-registration of land rights identified in our discussions were pricing; speculation in land; cadastre and title registration issues; and procedures for re-

registration and the respective roles of local and Federal governments. In addition, the FIAS team has raised the issue of monitoring progress and compliance with the law.

### 1. Valuation/Pricing

The issue of pricing the land for re-registration of rights was discussed in great detail in the first technical response to the MEDT Report and during the video conferences organized by the present project, and the views of the team provided. It was agreed that pricing of occupied land is a key factor in the re-registration program. The FIAS team possesses good historical evidence that lowering prices leads to a significant increase in the number of re-registration applications. It was also agreed that the procedure for setting buyout prices in effect at the time of our discussions had been inefficient and did not reflect the true value of the land. As noted in the MEDT Report, pricing based on factors applied to the land tax is inappropriate because the tax is an historical artifact having little to do with the value of the land to either the state or the current occupant who holds the right of re-registration.

Our concern focused mainly on whether the MEDT proposal for basing re-registration pricing on "cadastre value" raised its own set of problems. As the MEDT Report acknowledged, "cadastre value" is not a well defined term, and it is treated differently in different localities. Adopting a uniform definition of cadastre value and improving cadastral valuation are long term objectives of the MEDT program. However, the point argued by the FIAS team was that it is almost certain that the ultimate definition of cadastre value will refer to the value of the property if it were unencumbered by the holder's right of use. The actual value of the property to the state or municipality and to the holder of the right of re-registration must take into consideration the encumbrance of the land holder's long term right of use. Simply put, the state can't sell the property to another user without first paying the current holder for its right of use, which by law must be calculated at market value. This required payment obviously reduces the value of the property to the state considerably, and this reduced value should be reflected in pricing.

The initial conclusions and recommendations provided by FIAS included:

- **The indirect and long term benefits of encouraging privatization of enterprise occupied land through low prices outweigh the direct, short term benefits of budget revenues from land sales. Those benefits include increased investment in land improvements, increased employment, higher value uses of underutilized urban lands, increased tax revenues and a more vibrant private market.**

- **It should be acknowledged that there is a difference between the cadastre/taxation value of the land and the value as encumbered by the occupants long term right of use, which must be taken into consideration in pricing. The land presently occupied by privatized enterprises and businesses has little value to the region or municipalities, as the rights of use are virtually perpetual and strongly protected by law.**

- **Before deciding on a factor to be applied to the cadastre value to arrive at the re-registration price, analysis and economic modeling should show whether the result of that calculation has any actual relationship to the value of the land to either the state or the holder of the right of re-registration. If a factor is simply chosen on the basis of guesses or untested assumptions, there will be the same result as seen over the past 10 years, where enterprises are unwilling to purchase land or consider relocation because the prices are considered unrealistic. Ultimately the pricing formula may rely on application of a factor to the cadastre value, which has certain benefits of simplicity and efficiency, but the factor should be chosen with great care and on the basis of good financial modeling.**

- **For testing purposes, actual market values should be based on international appraisal standards.**

- **The cadastre value of land used in pricing exercises should be based on the current targeted use, and not a speculative use. It is essentially unfair to value the land based on speculation as to what it might be used for while decisions on use remain exclusively within the discretion of the local authorities.**

Since the initial discussions MEDT has made concrete proposals for pricing land for re-registration in a draft law intended to govern re-registration issues. The draft, entitled "Law On Amendments and Additions to the Legal Acts of the Russian Federation in Respect of Obtaining Rights to the Land Plots Which Are In the State or Municipal Property, on Which Buildings, Constructions and Facilities Are Located, And On Introduction of Exactions for Removal of Restrictions on Land Rights Prohibiting Reconstruction and Development" (hereafter the "MEDT Draft Law On Re-registration") provides that in settlements of more than three million population the price for re-registration of rights to land plots shall not exceed 20 percent of cadastral value, and in all other places not more than 5 percent of the cadastral value. Subject to these limitations, the actual price would be established by the RF Subject.

According to estimations of MEDT and the Federal Agency for Real Estate Cadastre the average prices for land privatization under this proposed formula will decline by 2 – 2.5 times, although increases may occur in some areas where prices are today particularly low. Some in the business community dispute this assertion and expect that land privatization prices will jump up in most cases from current levels (up to 20 times and more). Clearly, this is an empirical question that can be answered with some certainty.

MEDT has done extensive testing of the results of this new formula, comparing the new prices with existing prices. The tests do not compare new prices with actual market values, as recommended. Discussions of the FIAS team with the Federal Agency for Real Estate Cadastre revealed that recent ratio analyses of the current cadastre valuations show that cadastre values are at the level of 40-60% of actual market value, a wide range. Accordingly, a factor of 20% applied to a cadastral value which is only 40% of market

value would mean that the purchaser is paying only 8% of actual market value, which would increase to only 12% in the higher jurisdictions. Outside of the largest cities the price could be as low as 2% of actual market value. These do not strike us as a very high prices, but there is no way of assessing their relationship to actual value to the parties taking into account the highly encumbered state of the land. The wide difference in cadastre/market value ratios (40-60%) is troubling, suggesting that application of the new formula could lead to major inequities among enterprises, depending on where they are located.

If the cadastral valuation system is improved, as is the intention, these prices will undoubtedly increase as cadastral valuations approach market valuations. That process could take 5 or more years. The upshot is of course that enterprises would have the incentive to act now to acquire land rights, which is not a bad policy outcome. MEDT has in our view acted responsibly with the intention of keeping prices low and attractive, and has done significant financial testing and analysis. **We continue to recommend that continued testing be done on a sample basis to determine the relationship of the new formula prices to prices that would be determined by application of international appraisal standards, taking into account the crucial issue of the rights of use encumbering the land. In addition, it seems to us that some effort should be made to adjust for the wide range of cadastre/market value ratios among the regions, to assure equitable treatment of enterprises.**

While we believe that there is strong historical evidence that reduction in prices will increase demand for land by enterprises, prices are only one part of the issue. It is our belief that demand for land privatization may increase if more favorable terms are offered to potential purchasers. Other steps that could be taken include:

- **Extending the period for payment of the land price to reach 3-5 years, with interest accrued at the official rate. (To facilitate mortgage and investment in improvement of the property privatized on such terms, it would be advisable to transfer title promptly upon execution of the purchase and sale contract, subject to a pledge for the benefit of the seller as security for the unpaid purchase price.)**
- **Authorize subdivision of large land plots into smaller ones and allow them to be purchased separately.**
- **Land users should be permitted to take ownership of only a portion of their land without affecting the rights to the remaining land, which could be relinquished or held under lease. Land which continues to be held under lease could be purchased at some time in the future.**
- **If a land holder agrees to relinquish a portion of its land rights a credit be provided against the purchase price of the remainder of the land in an amount determined by the pricing formula.**

- **There should be included in the sale and purchase contract (until the territorial zoning regulations are adopted) a list of various permitted uses of the land plot instead of the existing designated use of the land plot.**
- **It is recommended that the concept of what amount of land is necessary for efficient operation of a facility be defined liberally and in an incontrovertible way to put an end to the illegal practice of granting the footprint under the building, without sufficient area for other necessary purposes.**
- **The buyout registration process should be as easy as possible, the documents review period should have strict limits, and the total procedure period should be clearly defined. A "single door" principle should be applied, when an applicant submits his application and receives a final decision from one and only agency that is authorized to independently collect and prepare all additional documents not listed among the minimally required ones.**

Ultimately, the price of the initial re-registration of the land may not be the main issue in light of the other provisions of the MEDT Draft Law On RE-registration which would impose a "speculation tax" on changing the use of the land which could reach as high as 80% of cadastral value. Those provisions are discussed further below.

### 2. Cadastral Valuation, Generally

The issue of whether cadastral valuation is the appropriate basis for pricing enterprise land is different from the issue of whether improvement to cadastral valuation is an important objective, which in our view it is. The RF has decided to implement a system of mass appraisal of real property as the basis for real property taxation and land privatization pricing. The current property tax system is based upon normatives that have little relationship to actual market value. The new cadastral valuation system in accordance with the current legislation must be in place by October 1, 2005, when it will serve as the basis for the national land tax, which ultimately may be converted into a local real property tax.

Based on discussions with the Federal Agency for Real Estate Cadastre, the methodology for the cadastral valuation substantially follows international norms, with adjustments to address the limitations of the data available in the Russian context. The most significant problem is the lack of market data on land prices in many areas of Russia, which requires substitution of other indicators in the valuation models. It appears that the approaches taken to address these problems are generally well conceived and creative for the time being, but will be replaced by more conventional approaches as the market develops and sufficient market data becomes available.

In general, the work being done on cadastral valuation appears to be a reasonable start, though there is considerable disagreement on this point among Russian land experts, in particular professional appraisers. Recent testing shows that the statistical valuations prepared by the cadastre agency have correlation coefficients with actual market values ranging from 40-60%. While such results would be unacceptable in developed market economies, they are probably acceptable for the time being given the data limitations in

Russia. As markets develop and more reliable data is gathered, allowing refinement of the statistical valuation models, the system can only improve. This will be a long term process. It is possible to say at this time that despite its flaws, which are known to everyone involved, the current approach provides a level of transparency and consistency that was heretofore lacking and is a reasonable basis for implementing the real property tax system.

Other issues under development regarding cadastral valuation are the process for approval of valuations, the respective roles of the federal, regional and local authorities in implementing and supervising the valuation process, and the procedure for citizens and businesses to appeal valuations which they consider to be unfair. In this regard we reviewed the MEDT draft Law on Formation, State Cadastre Registration, State Cadastre Appraisal of Real Estate and presented our views on the cadastral valuation and appeals processes in a separate report. At that time we did not have the draft Regulation on State Cadastre Appraisal of Land, which we have now reviewed and have the following additional comments and recommendations:

- **There are several apparent contradictions between the draft law and the draft regulations, which presumably will be corrected. For example, the law provides for appeals only on the grounds of procedural violations, while the regulation allows appeals for substantive discrepancies between cadastral and market values. We think the approach of the regulation is correct.**

- **Minimum standards should be established for appeals procedures to assure fairness and uniformity. Those standards should include, for example, the right to be represented; the right to present witnesses, documents and other evidence; the right to obtain documents from the government in support of the appeal; etc.**

- **The drafts do not make a clear statement that the main objective of mass appraisal is to approximate, within a permitted range, the fair market value of the property. Approximation of fair market value is essential for fair taxation. There should be a general principle established that it is the objective of mass appraisal to approximate the fair market value, and the law should prohibit appraisal of the property in excess of its market value.**

- **In addition, neither the law nor the regulation describes other legal objectives of the system, such as fairness and equalization of tax burdens among tax payers and types of property. In the absence of clear statements of legal objectives and principles, the "audit" function of the Federal Cadastre Agency is not anchored.**

- **The standard for regional cadastral value reports, which must allow an auditor to determine the cadastral value "without involvement of the**

**appraiser," could be further refined to require that the individual valuations be reproducible and mathematically predictable.**

- **Consideration should be given to putting in the law or regulations a standard definition of fair market value provided in international appraisal standards.**

- **The cadastre agency should be specifically required to develop and apply statistical methodologies to test the relationship between appraised values and market values, and to reject the appraised values if they fail the tests.**

- **Additional grounds for appeal should include: (1) that the appraised value departs significantly from the appraised value of equivalent properties in the market area; and (2) that in terms of the relationship to fair market values, the appraisal results for a type of land is discriminatory and significantly different from the results for other types of land.**

- **The procedure for commencing a dispute should be clarified. A hearing should be given if the land owner presents prima facie grounds for dispute, such as an independent appraisal that show a discrepancy of more than 30% between cadastral and market values. But that evidence is sufficient only to obtain a hearing, and it can be rejected by the hearing commission. In the hearing the land owner still has the burden of proving the validity of his evidence.**

- **The threshold of a 30% difference between cadastral and market value does not appear to take account of the fact that today the differences frequently exceed 30%. Cadastral officials advise us that the current ratios are roughly 40-60%, which means practically all cases will be subject to dispute.**

- **There is no indication in the law or regulations of what the consequences of an appeal are for the tax payment. The law and regulation imply that the appraisal will be re-considered, and if incorrect will not be entered into the cadastre, but does not carry the implications further. Standard procedure is typically to require payment of the tax by the property owner pending resolution of the appeal, subject to reimbursement if the appeal is successful. Otherwise, the government can be deprived of large amounts of revenue for considerable periods of time.**

- **In general, it is not advisable to have the land owner or his representatives sit on the dispute resolution commission. Better alternatives are to have individual hearing examiners, panels of independent experts, or panels of cadastre and tax officials sitting ex officio.**

- **It is questionable why cadastre value must be determined for each category of land, of which we understand there are now 17. A much simpler system can be devised. Moreover, appraisal parameters can include the category of land as an independent variable, making classification of land by category unnecessary.**

- **The proposal of the regulation to delay entry of the data for entire regions into the cadastre only after "disputes have been resolved out of court" is probably unrealistic, and could have serious consequences for tax collection. This intention should be further clarified.**

### 3. Speculation

The MEDT Draft Law on Re-Registration provides that in settlements with population of more than three million the local administration shall, simultaneously with execution of the land sale contract, prohibit change of use or redevelopment of the land plot. Reconstruction of facilities without change of use would be permitted. These restrictions would be removed at any time upon application of the land owner and payment of an additional charge to the locality. The rate of the charge could not exceed 80 percent of the cadastral value of the land plot. How the actual rate would be established is ambiguous in the current proposal.

The MEDT proposal reflects the position that profit from redeveloping land acquired through re-registration of rights is appropriate, but that the state expects to share in the gains made from the land. The MEDT Program would therefore demand an additional price, beyond the basic re-registration price, to redevelop a land site to a higher and better use than at present. The price would be calculated by applying a factor to cadastre value. It is not clear from the proposal whether the cadastral value is based on the restricted current use or the use for which the land owner is applying, which would make a significant difference. It is also unclear whether the tax is meant to apply only in the largest municipalities, with populations of 3 million or more, or in all municipalities. The proposed amendment to the tax code suggests the broader application.

Our sense is that MEDT has moved gradually from a position of supporting a low price for land re-registration to encourage privatization and redevelopment to a position of supporting market pricing. Such a policy moves away from the main principle we have proposed, that land should be priced based on its encumbered value, giving appropriate recognition to the value of the existing rights of use.

When this proposal for a speculation tax was first raised the FIAS team raised the concern that exacting an excessive premium on re-development of the land could result in an impasse between the current occupants and the government and undermine the objective of urban redevelopment. The enterprises will not take ownership and relocate if there is insufficient financial incentive, and the local authorities cannot take the land for redevelopment without paying the occupant the market value of its improvements and the replacement value of its land. This is a significant sum and many localities lack the

resources. (They may also lack the legal authority to take the land for private redevelopment, which is an open issue under Russian law.) Consequently, the status quo will prevail.

Particularly troubling is that this speculation tax appears to be in addition to the present infrastructure charge demanded by most cities, which can be as much as 25% of the costs of a land development project. Moreover, the combination of increasing cadastral values over time and the suggestion that the basis for the tax would be the cadastral value of the land subject to the new use and not its restricted use suggests that at some point land holders will be paying more for the land than if they bought it today at its market price. The allocation of risks and rewards in the transaction would become too heavily weighted in the favor of the state.

Our views on this tax have not changed and we believe it is a disincentive to urban redevelopment. We can only repeat here the points made at the start of the discussions:

- **There are many objectives to land rights re-registration program, including the tenure security and predictability of costs that will encourage more investment in fixed assets and allow better access to mortgage finance. However, today an equally important objective is to release a great deal of underutilized land into the market for redevelopment as higher value uses. Taxing redevelopment through higher land prices conflicts with the objective of encouraging redevelopment.**

- **Particularly important in this respect is the need to relocate some inappropriate urban uses to more appropriate locations. That is a very expensive process, including not only replacement of land and facilities, but also the costs of the move and perhaps upgrading of plant and equipment. The profits from sale of land may be necessary to encourage some users to attempt this process.**

- **There is a strong argument to be made that this charge on redevelopment is the exact opposite of the approach that should be taken at this time. Considering the shortage of serviced vacant land in cities, particularly for housing, it might be more appropriate to waive the redevelopment premium entirely for a period of 5 years for any enterprise that takes ownership of the land for the purpose of relocation and redevelopment. This waiver could be tied specifically to any program which envisions housing development, or development of housing designed to serve the moderate and lower income portions of the population. In this way a time-bound incentive for relocation and provision of land for housing would be established. Similarly, the tax could be waived for any redevelopment activity in an area designated be the locality as deteriorated and in need of economic redevelopment.**

- **The premium for the expanded land use should take into consideration the value of the current land use right of the occupant, an encumbrance on the property.**

- **There should be a time limit on the obligation to pay the premium. For example, the premium could be reduced by 20% for every year that the occupant owns the land prior to redevelopment.**

- **Consideration should be given to eliminating any municipal infrastructure charges in cases in which the speculation tax is paid.**

- **In no case should the tax exceed the difference between the amount paid for the land and the actual cadastral value of the land as of the time it was acquired.**

## 4. Boundary and Title Disputes

The MEDT Report strongly implies that major barriers to progress in enterprise land privatization arise in the delineation and registration of land rights. In particular, numerous boundary disputes among adjoining land holders, among whom are included the municipalities, as well as ambiguous and poorly documented boundaries and rights. The report considers several tools or mechanisms on which we have been asked to comment, and several other possibilities have been raised in discussions with MEDT. These proposals include "systematic" cadastre and registration of titles under "land management" principles; introduction of legal concepts of "conditional title" and "general land boundaries" into Russian practice; development of Federal rules on adjudication of boundary issues in privatization cases; and the relevance of principles of "alternative dispute resolution" to boundary and title disputes.

### *(a) "Systematic" resolution of boundaries and titles under "land management" procedures*

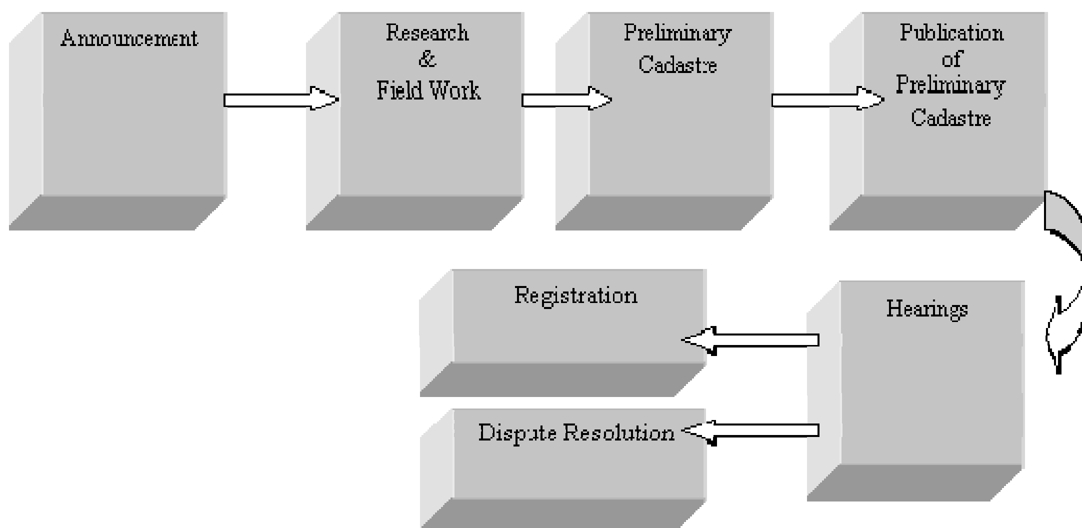
The MEDT Report proposed, as an approach to resolving boundary and title disputes more quickly, the use of "systematic registration under land management procedures" and we were asked to comment on that proposal. Many past and current World Bank cadastre and title registration programs include some systematic registration component, including currently Moldova, Slovenia, Croatia, Serbia and Macedonia.

Systematic registration is generally understood as an administrative process initiated typically by a national cadastre agency under which teams of highly trained professionals, primarily cadastral engineers and lawyers, engage in systematic identification of legal property objects and registration of the rights to those objects. The process is typically applied in a single cadastral district or even smaller area. It is begun by legal announcement of commencement of the process and issuance of an invitation to all property owners to provide evidence of the claims and titles to the investigating team. At the same time the team will research all available current and historical property

records and undertake extensive field investigations of the actual situation "on the ground," including discussions of property boundaries among neighbors. Upon completion of research and field investigation the cadastre will prepare and publish a preliminary cadastral map and schedule of property rights, and invite identified property owners to appear before a special panel of professionals to either confirm or dispute the preliminary findings. Upon expiration of a period set by law the preliminary findings will become final and entered into the cadastre and registry, unless disputed. Disputed findings may need to be resolved through other proceedings, including court action.

The benefits of systematic cadastre and registration of titles are well known. It is an active approach that does not rely on the initiative of the individual land owners to develop the cadastre and registry. The alternative, called "sporadic" registration, which relies on capturing transactions made at the initiative of individual land owners, can delay completion of the cadastre and registry for long periods, depending on the rate of property turnover. Moreover, in situations where boundaries are unclear, a systematic process can address all contiguous land parcels as a complex, which is more efficient than case-by-case resolution.

**SYSTEMATIC REGISTRATION AND CADASTRE**




In most cases it can be shown that systematic processes are less expensive in the aggregate than were the same number of titles to be registered individually. This stands to reason as economies of scale are achieved in practically every area of work. However, a main difference between the sporadic and systematic approaches is that the costs of sporadic registration fall on the individual land owner while the costs of systematic registration are typically budgetary costs. The costs to the budget can be considerable. While the costs can differ substantially depending on circumstances, including particularly the standards of survey accuracy applied in the process, a range of $10 to $40 US per registered title is possible. However, in most cases, government policy makers have determined that indirect budgetary returns from quick and effective completion of

the cadastre and title registry in terms of investment, turnover and taxes would exceed the budgetary costs.

Systematic titling must be specifically authorized by law, as it results in creation of property rights. This is a hurdle that would have to be overcome before systematic cadastre and registration could proceed on any basis in Russia. The key element of systematic cadastre is compulsory registration of findings. It would be doubtful whether investment in the process could be justified if property owners were not bound by the findings, or if the process did not result in large scale registration of titles. The current Russian laws do not provide for systematic cadastre or registration of titles. In fact, systematic registration was specifically discussed and rejected at the time of adoption of the Law on Registration. A recent draft of a new cadastre law (Draft Federal Law on Formation, State Cadastre Registration, and State Cadastre Appraisal of Real Estate) also does not contain provisions on systematic cadastre and registration, but instead seeks to delegate similar powers to private sector cadastral engineers to be exercised on a case by case basis. (A separate commentary has been provided on that draft).

Whether systematic cadastre and registration procedures are implemented is a policy decision. Because of the high budgetary costs, some might argue that the target population for systematic titling should be low income. There is some opinion also that systematic procedures are most efficiently applied to agricultural land and registration of urban apartment rights. It should also be noted that the perceived need for systematic cadastre in this case is to settle disputes concerning high value land among experienced business people. In such cases, so long as the results of the process are not absolutely binding as a legal matter - that is, appeals to court are permitted - the likelihood of success are diminished.

Our recommendations on this issue are:

- **We do not think that the conditions exist in Russia today to implement systematic registration on a large scale. In most areas boundary disputes are not so numerous as to justify the expense and complexity of a large program. Moreover, in settled areas systematic registration can cause problems where they do not presently exist, if people are forced to actually commit to a boundary. As discussed further below, a more limited and targeted approach relying on ADR techniques may be more appropriate.**

- **Flexibility should be the main objective. A comprehensive law on cadastre and title registration should contain the option for administration officials to implement systematic programs on a compulsory basis, regardless of whether the option is ever used. There are many legal models of systematic cadastre and registration which can be provided, but they typically follow the rough outline provided above. The key concern is scrupulous protection of the rights of landholders through communication and rights to challenge and appeal findings.**

- **The option to implement systematic cadastre in an area should be given to the Federal Agency for Real Estate Cadastre where the necessary conditions exist, including high land values, unsettled borders, and large numbers of privatization applications and land disputes.**

- **There should be the possibility to implement systematic cadastre and registration in small areas, less than an entire cadastral section or district. This would be the case, for example, in high value areas in which there are a significant number of existing or potential applications for re-registration.**

- **Alternatively, implementation of systematic cadastre and registration could be made subject to a referendum in a particular location, or even initiated at the request of land owners. It is conceivable, for example, that a large number of land holders in a specific area would want a systematic program as a means of reducing surveying and transaction costs, including importantly the transaction costs of negotiating boundaries among many adjoining land holders. Large industrial areas are a case in point. It is also conceivable that the costs of such activity could in those circumstances be borne to a large extent by the private land holders who would benefit from the program. Where implementation of systematic cadastre is chosen voluntarily by land owners, there should be a binding legal obligation to accede to the results of the work, with limited and well specified exceptions.**

*(b) The concept of "conditional title registration"*

We have been asked by the MEDT specifically to comment on the feasibility of implementing a concept of "conditional titles" into the Russian law. "Conditional," "provisional" or "phased" titles are an established element of registration systems in some highly developed economies, such as the UK, and are often recommended by land administration professionals for title registration systems in developing and transitional countries.

The statutory provisions on conditional title form the UK's law are attached as an Annex to this report. These devices are primarily tools to capture more data in the registry in situations of uncertainty and provide a minimum degree of legal recognition to facts of property possession and occupancy.

The theory of conditional title is that registration systems should seek to capture as much data as possible regarding the ownership, use and possession of real property. However, in some countries that do not have highly developed and long standing systems of private property ownership and registration (E.g. Russia), or in which property registration systems have been severely disrupted by war and other civil disturbances (E.g. the former Yugoslavia), property rights are poorly documented and good legal proofs of rights of ownership or use are lacking.

At the same time, in many cases where title documentation is poor or non-existent it is nevertheless clear that some right probably exists just from the simple fact of long and

undisturbed possession. Failure to enter these facts into the system simply encourages informal transactions, as transfers of the properties will continue to occur regardless of whether they are registered. Continued accumulation of informal transactions aggravates the situation further, ultimately making titles even more difficult to establish. It is widely considered that a better approach is to register the fact of possession or occupancy as such, as a lesser form of right, and to also allow subsequent transactions to be registered at the risk of the parties. Ultimately, when the title is resolved (which it will have to be), the chain of title will have been already established in the registry and converting the title from a conditional to a legal one is much simpler and quicker matter.

The key elements of the conditional title include:

> *Legal authority to register mere facts of occupancy or possession under claim of ownership*. At this time, the Russian law allows registration only of an ownership title only on the basis of a fully documented chain of title originating with a state act and followed, in some cases, by valid civil documents of transfer and entries in the appropriate registries. In contrast, a conditional title may be registered on the basis of a wider range of proofs, including proofs of long occupancy such as utility bills, property tax payments and affidavits of neighbors.
>
> *Discretion of the Registrar*. Registration of a conditional title often requires exercise of discretion by the registrar. A registrar must carefully consider the facts of the case and determine whether it is more likely than not that the applicant will eventually be shown to be the rightful owner of the property. In addition, a registrar may have discretion to establish specific conditions for the title, such as delivery of additional legal documentation. We are aware that many procedures in Russia today are designed to avoid granting discretion to administrators that can be abused, and this may be a significant consideration in the present case. An alternative may be to describe a set of conditions for entry of a conditional title into the registry, with regard to which the registrar would have very limited discretion.
>
> *Differentiation between the legal benefits of unconditional registration and conditional registration*. The main distinction between unconditional and conditional registration is that the conditional registration entails no representation that the title is guaranteed by the registration system to be true and correct. Any further transaction with the conditionally registered title is at the risk of the transacting party. Put another way, the purchaser of a conditional title cannot become bona fide, as the conditionality is notice that the title may be flawed.
>
> *Publication*. Registration of a conditional title is a derogation from the usual rules of registration, and as such it is sometimes required that the intention to register be published prior to registration to provide notice to any possible adverse claimants. How far this requirement should be taken is open to question.

*Eventual conversion from conditional to unconditional title*. All titles should be resolved eventually. A good system of conditional title would provide for conversion from conditional to unconditional title either on the satisfaction of specific conditions or on the passage of time. Specific conditions may be established by the registrar (E.g. delivery of a missing document) depending on the case. Passage of time may be related to the current rules for prescriptive acquisition of real property, which are presently quite long, or a more realistic, shorter period of time appropriate for a person who is in undisputed possession of the property.

These principles are significantly different than the present approach in Russia, and would require changes to the law. Whether implementation of this registration concept in Russia would be useful depends on the facts. Because private property rights are a very recent phenomenon in Russia (1992), and all rights essentially began with a grant from the state, there has not been a great deal of time since the origination of the rights and chains of title are mostly clear and well documented. Moreover, with respect to apartments and some forms of personal land holdings there have been registries which have registered the original state act and kept track of subsequent transactions. It is therefore an open question whether the need for conditional titles exists. Further analysis of the records to determine how many registration applications are rejected for defective or missing documentation would be a useful indicator. While such statistics were not available to us, informed commentators suggest that the number is less than 1%.

**As usual in such circumstances, and in the absence of good statistical data relevant to the issue, we recommend flexibility. There is nothing to be lost by allowing a form of conditional title based on reasonable evidence.** Such a registration would lack the state guarantee of accuracy. The most significant risks are corruption and abuse of the system by registrars or creation of public confusion concerning the legal implications of registration. The problem of public confusion can be addressed by appropriate educational measures and materials, which has been the key to implementation of the entire registration system since its inception. **We would therefore recommend that if further amendment of the Law on Registration of Real Estate Rights and Transactions are contemplated the concept of conditional title should be included.** Though we believe that the better systems of conditional registration involve an active registrar exercising some discretion, we believe it is possible to limit discretion, and therefore the potential for corruption, through appropriate rules.

It should be noted that the term "conditional title" is only one term among many. The entry to the register does not have to be characterized as a "title" at all, but merely registration of a fact of possession and occupancy, or even an unresolved claim to a title.

**Short of extending the concept of conditional title to all real estate, we believe that conditional registration could be useful in one important case, which is the registration of beneficial rights to re-registration of title to enterprise land or land occupied by building owners.** One of the main barriers to privatization of land plots appears to be failure to agree on technical issues such as boundaries. At the same time,

there is little doubt the present occupant holds a beneficial right to acquire some part of the land on some terms. Conditional registration of the title would be a means of protecting the land holders rights until such time as issues are resolved and an unconditional title can be granted. Such conditional registration would be registered immediately upon submission of an application for privatization and remain in effect throughout the process, including court actions. This change to the law could perhaps be addressed in the MEDT's proposed Law On Re-registration.

*(c) Acceleration of timing between registration of transactions and registration of rights.*

Related to the concept of conditional registration, we have been advised that long delays between the co-called "registration of transaction" and "registration of rights" under the Russian law are leading to legal problems, particularly with respect to tax obligations. We have been asked to comment on possible solutions to this problem.

It should be noted that in our own experience the RF registration offices, as a rule do accept and process both applications simultaneously, thereby reducing the inconvenience. We are even advised that some do not collect two fees. Accordingly, we have no independent knowledge of the significance of this problem today.

Nevertheless, Russia is still unique in the world in distinguishing between registration of transactions and registration of a right, a point we have made frequently in the past. How this distinction arose is water past the bridge at this point. Typically, registration of a transaction is the vehicle for registration of a right. The transaction documentation is evidence of the right and accompanies the application for registration. No separate registration application is required, and the registered right is modified on the basis of the transaction documentation. Registration of the transaction and registration of the right are therefore simultaneous. **Other than the additional revenues for the registration agency, there is no justification for separating registration of transactions and registration of rights, and we strongly recommend that this concept be eliminated from the law at the first opportunity.**

**Some more steps that might be considered would include assuring universal legal status of the application "log book" as an official "registration of the transaction" record** − allowing submission of a single application and payment of a single registration fee. **Transfer of the log book data to the registration book would be characterized as "registration of the right."**

The provisions of the Law # 196 of 12.29.2004 amending Art. 16 of The Registration Law and requiring date and exact time entries to a log book and are mainly addressing the burning problem of fraud of the third parties, but they still do not stipulate that the entry into the log book should be legally characterized as registration of the “transaction”, thereby eliminating the above-mentioned confusing and unnecessary aspect of the Law. Thus, the proposed approach would require further amendment of the present law.

### *(d) Cadastral survey requirements and the concept of "general land boundaries"*

Formal cadastral systems for delineating land boundaries sometimes distinguish between "fixed" and "general" boundaries. We have been asked to specifically comment on the relevance of systems of "general" land boundaries to the Russian context on the premise that implementation of a system of general boundaries can lead to quicker and cheaper completion of the cadastre, but also defer resolution of boundary disputes that are merely technical and have no significant implications for land use at this time.

At the risk of generalization, Russia today has a system of fixed cadastral boundaries. A fixed boundary is an ideal straight line between two points that are physically identified with an artificial monument. The system of fixed boundaries, sometimes referred to as a "numerical" cadastre, is characterized by boundary "turning points" which are precisely located and represented by physical markers, usually in accordance with a national geodetic plan or network, and plans typically show precise geodetic bearings and distances between the points. The fixed boundary system may carry a strong state guarantee of accuracy, but that is not necessarily the case. Some systems of fixed boundaries specifically decline liability for errors in boundaries.

In a general boundary system, the boundary line is demarcated by an artificial or natural feature of the landscape, including perhaps a fence, wall, ditch, hedge, tree, outcropping, or by ideal lines between such features; even perhaps the usual "red-lines" used in urban planning. Legally, an exact boundary is undefined, but for practical purposes the general contours and size of the property can be determined with sufficient specificity to avoid disputes and permit undisturbed use by the occupants. Unlike the fixed boundary system, the general boundary system does not require precise geodetic locations of physical markers in accordance with a widespread geodetic framework. It therefore entails a simpler form of surveying, and therein lies the perception of its ease of use relatively low costs.

The dispute resolution aspect of general boundaries is simply that it avoids or defers disputes by focusing neighbors' attention on their practical use of the land rather than meters and centimeters which might be gained or lost by the land holder if a fixed, legal boundary were to be established.

A common misconception of the general boundary concept is that no boundary line exists, or the line itself is many meters wide with the boundary being an indeterminate point within. This is not the case. Clearly, in Russia, where many formulas based on square meters of land exist, land taxes being the most obvious, an official boundary must be recorded to permit calculation of the size of the land area.

Consideration of the concept of general boundaries for Russia should be made in light of the following:

- We have been advised of concerns that the concept of general boundaries does not fit the Russian situation, where private land use is a recent phenomenon and

existing natural or man-made indicators of boundaries do not exist or are unreliable. This of course is particularly true with respect to large agricultural areas. Whether this is a generally accurate observation is beyond our knowledge. (But, any casual inspection of small towns and settlements in Russia, with housing plots marked by fences and hedgerows, belies this conclusion.)

- It may be said that the traditional concept of general boundaries assumes a long understanding of adjoining land holders of their land rights based on markers to which they agree. If there is no such understanding and neighbors are simply too far apart in their expectations, as may be the case with respect to many enterprises in industrial areas, general boundaries alone will probably not be an effective dispute avoidance measure. Many boundary disputes today deal with far more substantial areas, and crucial issues such as access, than would be resolved by general boundaries.

- The utility of general boundaries may decrease with urban density, as high land prices and strict planning parameters make high accuracy desirable, particularly for new construction. Moreover, in high value urban areas occupied by commercial and industrial interests the costs of survey are not really an issue. As a tool for avoiding or deferring boundary disputes, the concept also may have significantly less utility in highly urbanized areas. And, even in built up areas simple natural or man-made markers can be found - for example, the wall of the adjoining building.

- The Russian system already incorporates an indirect concept of general boundaries by establishing different survey accuracy standards for different contexts, with much lower accuracies required for rural and agricultural areas. This relaxation of survey accuracy standards is also a means of increasing speed of survey and decreasing costs as it expands the range of technologies that may be used to delineate boundaries.

- The two approaches are not mutually exclusive. It is possible to permit both fixed and general boundaries depending upon the circumstances, and many modern laws do.

There may be some cases in Russia in which a concept of general or approximate boundaries may be appropriate. While the intention now appears to be to create a "numerical" cadastre characterized by accurately located physical markers on the ground, such is not necessarily incompatible with the idea of general boundaries in appropriate cases. This is particularly true in light of the millions of land parcels currently in private possession and use that are not yet entered into the cadastre or are entered on the basis of general schematics which do not meet current survey standards. A general boundary concept could facilitate re-survey of the many objects which are already in the cadastre based on schematics or other low standards. We also believe there are likely to be many cases in which neighboring land holders would prefer to avoid long, complex legal

disputes in order to resolve their land rights quickly, provided that the uncertain boundary did not interfere with their practical use of the land.

It is recommended again that the main objective of the law should be flexibility, leaving the door open to various approaches and experimentation over the coming years. Recommendations on these issues include:

- **The cadastre law should establish a broad definition of boundaries and leave details to appropriate regulations. For example, it should not be required that all boundaries be established on the basis of national coordinates system.**

- **Physical markers should be flexible and include natural and man-made objects.**

- **Survey accuracy standards should not be set on the basis of whole territories or areas, but should be left flexible to be applied depending on the circumstances and the wishes of the land owners (defined circumstantially, not territorially).[3] If adjoining land owners are willing to live with approximate boundary locations, that should be a choice available to them, wherever they are located.**

- **In our opinion, the key to general boundaries is not necessarily the nature of the survey or the boundary markers, but the fact that the parties understand that the boundary is not legally fixed. This we believe is also the utility of the concept as a dispute avoidance tool. So, the benefits of general boundaries can be largely achieved by applying the relaxed survey accuracy standards of rural areas to the urban areas as well, if desired by the parties. This would allow use of a wider variety of cheaper survey techniques and give the parties comfort that the boundary is not legally fixed and may be subject to change. If this approach is taken, it would not be necessary to introduce a legal concept of "general boundaries," but simply to address the issue through survey standards.**

- **Implementation of a general boundary concept may require some consideration of other laws. For example, the laws on prescriptive rights could not be set up a defense to eventual fixing of the general boundary. Similarly, fixing of a boundary which resulted in re-calculation of land plot areas should not have retroactive affect on calculation of planning parameters based on land area and distances from boundary lines, and claims for encroachments on adjoining property would be disallowed.**

[3] For example, the draft Law On Cadastre provided to us states that "accuracy of location and borders may vary from territory to territory on which a real estate item is located," suggesting that standards must be set on a territorial rather than factual basis.

### *(e) Delineation of state land*

In connection with the present project we had opportunity the review the draft law On Amending the RF Land Code, the Federal Law On Enacting the RF Land Code, the Federal Law on Privatization of State and Municipal Property and On Nullification Of the Federal Law On Delineation Of the State Property On Land presented by V.Pleskachevski and a group of other deputies of the State Duma, as well as amendments to these drafts proposed by MEDT. Both of these documents are dated as of autumn 2004. In our opinion, the draft law reasonably proposes that the procedure for land delineation be greatly simplified by requiring only that the lists of land plots to be attributed as federal, regional or municipal property be prepared and submitted for registration by the relevant authorities independently of each other, simultaneously, and without the process of "cross" approval which is generally believed to have delayed the process. Instead, the authorities would simply inform each other on the lists of land plots presented for registration, and the cross-approval procedure would continue to apply only in cases of errors or particular land plots subject to dispute. We are in complete agreement with this proposal and have recommended a similar approach in the past.

The MEDT proposals provide that objections to the respective lists of land plots may be presented within seven days upon the date of their presentation to the registrars. In our view, first, this issue may need an amendment to be introduced to the Law On Registration, so as the one month given for conducting the registration procedure starts from the date of expiration of this 7 day period, and second, the seven days term is arguably too short for identification of disputed land plots in the list and preparation of well-documented claims. We expect that faced with this short period authorities may make a practice of lodging objections to all properties on entire lists to prevent registration, and then deal with the consequences over a longer period of time. As noted in our initial response to the MEDT Report, additional steps may be necessary to prevent routine objections to lists, such as requiring detailed written objections alleging facts other than mere ownership.

The proposed MEDT amendments to the draft law go further to address a situation we have encountered in many Russian cities in which we had a chance to work, when a property is held in joint or shared interests by state and municipal authorities. For example, separate parts of a single office building may be in the property of federal, regional, or municipal unitary enterprises. Similarly, one part of a building may be occupied by dwellings which are characterized as municipal property, and the other is occupied by an office of a territorial division of a federal agency, a federal body of executive power, or an enterprise which initially was in the federal property (according to the current law the latter is a ground for referring the land plot to the federal property). Except for the case when a part of a building is in the property of a private legal entity, MEDT proposes to allocate the entire land plot to the property of “the body of power of the higher level” – that is to the regional, or federal property, respectively.

While this is a simple, quick and certain resolution to the problem, in our view such situations may best be resolved on a case by case basis, taking into consideration such factors as the priority of the civil rights of the citizens, ownership of the dominant portion of the property, and the relative amounts of past and future investments in the building. It

seems to us a fact that the municipalities are presently carrying all the burden of servicing these buildings. Particularly, in case the building is occupied mainly by dwellings, and some smaller portion of it is federal or regional property, allocating the land to the minority owner could have implications for municipal revenues.

As for land beneath the buildings which are in private property, MEDT reasonably proposes not to delineate the plots under them since they must be re-registered into private property or lease in any case. For MEDT the important steps with respect to such land plots are determining the authority to dispose of the land plot and the distribution of revenues, neither of which require delineation. We agree generally with this direction, but think that in the case of leases it would be necessary ultimately to identify the owner of the land in order to allocate the long term stream of revenues and the reversionary rights to the land. One approach may be to relegate such cases to a lower order of priority, providing a longer term for completion of delineation.

Neither the draft laws nor the proposed MEDT amendments address the case when the privately owned building is located on a land plot on which another building of a federal, regional, municipal, or individual real property owner is located. In this case it may be logical to preserve the currently valid principle, according to which the respective part of the site is ascribed to the federal, regional, or municipal property accordingly depending on which property the enterprise initially belonged to prior to its privatization. In addition, however, the land would have to be appropriately sub-divided and this case therefore raises all of the issues which are currently encountered in the determination of land boundaries between neighbors. The case highlights once again the importance of elaborating more detailed rules for determining land boundaries in privatization cases. (These types of situations may also be good subjects for ADR procedures, as discussed further in this report.)

Another issue with the current legislation on delineation of the state land arises under the more recent Law on the Basic Principles of Organization of Local Self Governance, according to which municipal land should be subdivided between settlements and municipal districts. The MEDT proposals address this issue by providing that the "land plots under the real estate objects, which are in the property of municipal districts, as well as allocated to the bodies of local self-governance of the municipal districts, or to organizations and enterprises established by them, shall be delineated as the property of the municipal districts." Although the municipal districts in their main part are already formed, their real estate objects for the present are usually not identified and registered, and their bodies of self-governance often do not yet exist. Accordingly, one of the major issues for further development of legislation on delineation of the state land may be adjustment to the provisions of the law on local self governance.

The MEDT proposals propose that an alternative dispute resolution (ADR) procedure be applied in the process of land delineation, that the ADR commissions "should be formed by the bodies which have presented the documents for registration of the property rights," and that "decisions of the commission should be made by a unanimous vote" of its members. We agree with the proposed ADR approach to resolution of disputes, but suggest that the rules should be elaborated more thoroughly and follow modern models of third-party arbitration. For example, unanimous agreement is often difficult to achieve, even on small panels of arbitrators. Presumably this proposed ADR is intended to

resolve disputes in a binding manner, and not merely be a mediation or fact-finding procedure. It is a formal proceeding. In that case, it may be useful to look more closely at the current rules of the Law On Third-Party Arbitration Tribunals in the RF (102FZ of July, 2002), which provides a detailed framework for this type of procedure, using either permanent or ad hoc tribunals. Appropriate rules for the land delineation ADR can be extracted from that law, or if the law describes an acceptable procedure the rules of the law can be applied to the land procedure. (Note that it is only the rules that may be applied; the current law does not allow units of government to actually create a third-party arbitration tribunal under the law, or participate in a dispute before such a tribunal.)

*(f) Development of Federal Rules on Settlement of Boundary Disputes for Re-registration Cases*

We have been advised that a significant number of failed applications for re-registration of enterprise land rights involve disputes over boundaries, either between the applicant and the municipality or the applicant and adjoining land owners. We have been advised further that in some cases municipalities are not acting in good faith, and using boundary challenge to delay or deny applications. We have also noted elsewhere the practice of some municipalities of allowing applications only for the land lying under the "footprint" of building, denying the applicant needed areas to support the building or facility. We have no statistical data on this point and so cannot confirm the accuracy of the observations, but to the extent they are true part of the problem may be that the Federal law leaves the decision on setting boundaries to the locality, providing little if any guidance on how this is to be done. The vague provisions of the Land Code dealing referring to areas needed to operate the building and facilities are in retrospect viewed as too vague to be helpful.

**Since the entire re-registration program is a creature of Federal law, it may be useful to develop more detailed regulations and procedures for localities to follow in determining the size and contours of the land that is subject to re-registration. Such a detailed regulation would give flesh to the vague provisions of the Land Code, establish uniform practices and provide grounds to challenge arbitrary decisions of localities.** Establishing uniform Federal rules and procedures would likely only be useful if there was a system for monitoring implementation or a system of administrative appeals. Some principles that could be applied to the boundary determination process, which we have already discussed in our comments on the proposed Federal Law on Cadastre, include:

- In determining the boundaries of the property object the decision maker must consider:
    - existing documents granting title, rights of use or construction;
    - existing surveys and maps of the property, from whatever source;
    - urban planning documents;
    - construction documents and permits;
    - aerial photography;
    - patterns of actual use of the land;

  - the demonstrated needs of existing facilities and operations;
  - such other documents, materials or patterns of use that serve to establish the intentions of the grantors or users of the land or neighboring land.

- In determining boundaries of the property the cadastral engineer should seek to minimize dislocation or disruption of structures, access, infrastructure or patterns of use of the land, and to achieve a fair allocation of land to adjoining occupants.

- Grants of footprints under the building, without more, are presumed to be invalid unless justified by the grantor.

- The applicant can demand mediation by a territorial division of the Federal Agency for Real Estate Cadastre or some other administrative body.

*(g) Encouragement of "Alternative Dispute Resolution"*

The MEDT has asked specifically for our views on application of the principles of "alternative dispute resolution" to boundary and title disputes which may arise in the re-registration process.

Alternative dispute resolution (ADR) is a broad term encompassing many types of procedures. Discussion of the many variants and the highly refined theories of ADR is not possible or appropriate for this long report. Briefly, main types of ADR include voluntary procedures intended to mediate disputes and facilitate solutions by the parties themselves; voluntary procedures intended to have a binding legal effect; and compulsory procedures which may be imposed by law, contract or by court practice, and which may have either binding or non-binding effect.

The utility of ADR will usually depend on the nature of the dispute and the parties. Not all issues are amenable to resolution by ADR. ADR procedures appear to work best in cases where outcomes are highly uncertain for both parties, application of legal principles depends on highly disputable facts, and the adjudicator must exercise considerable discretion in reaching a decision based on concepts of fairness and equity. ADR is not a forum for clarifying and enforcing legal and civil rights. With regard to parties, complex, multi-party disputes may not be appropriate for ADR, and it is a rule of thumb that ADR does not work well where there is a great disparity of power between the parties and one party lacks incentives to cooperate.

In the case of application of ADR principles to the issues of re-registration of enterprise land rights, only a few of the issues appear to us to be appropriate subjects for ADR. The main issues arising in re-registration are price, reservations of land for "public use," fundamental issues of entitlement (whether the applicant may legally apply for re-registration), and the size and contours of the land plot. After extensive consideration, it

seems to us that the most likely case for ADR interventions are those concerned with the size and boundaries of land plots, and perhaps some cases of fundamental rights.[4]

With regard to parties, it is our view that ADR is best employed in disputes between private parties, as in a boundary dispute between adjoining land owners. The current rules governing re-registration are so vague and provide the municipalities with so much unchecked discretion that municipalities have little incentive to voluntarily participate in ADR. Even if permitted to choose those cases in which it would submit to ADR procedures the municipalities would probably participate only in the best case for them. However, it is not inconceivable that organs of government can submit to ADR procedures to resolve disputes, and there may be a growing trend to do so on other parts of the world.

The details of our analysis in this question are complex and we considered it best to simply present the main conclusions and recommendations.

- **The proposal for systematic cadastre and registration of titles discussed above is in effect a form of compulsory ADR. The procedure can be considered ADR because it is typically carried out by non-judicial experts who consult with, advice and offer professional opinions to the participants and thereby seek to forestall and resolve possible disputes over titles and boundaries. It is without binding legal effect because land holders are free to lodge court challenges. Nevertheless, the evidence developed in the systematic process will usually be given great weight in a court procedure. It also has the benefit of lower costs and quicker resolution than court procedures. We believe this form of ADR may be most appropriate in high value areas populated by many large enterprise land owners whose claims should be resolved simultaneously but who otherwise have little incentive to participate in ADR procedures.**

- **If adopted, the cadastral surveying methodology proposed by the MEDT in its draft Law on Cadastre, on which we have commented, will implement a form of ADR with respect to boundary disputes. Under that methodology the private sector surveyor will serve as an expert mediator and facilitator among adjoining land owners, registering, responding to and ultimately resolving boundary disputes. Though the decisions of the surveyor will be subject to challenge in court, an attempt will have been made to resolve all issues before that point. Moreover, an expert record and opinion will have been developed to permit parties to assess the merits of their position and whether court action would be a waste of time.**

[4] For example, the price of land has already, in effect, been excluded from ADR under the proposed cadastral valuation procedures on which we have provided comments. Those procedures require a simplified administrative procedure for challenging valuations outside of the court. Since pricing would be based on a simple factor of the valuation, there is no further room for ADR of price disputes.

- **The objective of ADR is essentially to provide a means of dispute resolution that is quicker and cheaper than court action, which given court backlogs can take years to complete. There are many ways to do this, including administrative appeals procedures. In many cases laws require completion of an administrative appeal as a condition of filing a lawsuit in court. We recommend that a new system of administrative appeal for re-registration cases be established to resolve in particular disputes between applicants and municipalities. Even if the cases ultimately end up in court, an attempt has been made to convince the parties of the merits of their positions and an expert factual record and opinion has been prepared, which should be influential in any court case. The outcome of administrative appeals can be negotiated settlements between the parties. Where this administrative appeal should be brought is an open question, but likely candidates would be panels of experts created by the MEDT or the Federal Agency for Real Estate Cadastre.**

- **Some form of ADR could be useful in boundary disputes between private parties. It is in fact used in many places today, and has been used in Russia under several pilot programs sponsored by foreign donors. The UK's Department for International Development (DFID) has conducted a program for establishing third party arbitration commissions in agricultural areas to address land disputes of small-holders. The authors are familiar with a relatively successful third party arbitration program operated by agricultural NGOs in Moldova which have succeeded in resolving rent and other disputes between holders of land shares and operators of corporate farms. It is unlikely that this ADR could be made compulsory. Rather, it would work as an expert mediation or facilitation. However, it is not inconceivable that laws on civil procedure could require participation in an ADR procedure as a condition of bringing a lawsuit on land title and boundary issues. This would require changes to the laws on civil procedure.**

- **Private parties are not likely to seek ADR on their own initiative unless they are aware of its existence and benefits. Nor will they use it if it is costly and not likely to provide the same degree of resolution as a court decision. The most effective way to induce private participation is to make the mediation service available and to educate the public about its availability and benefits. Possible ways to establish the service is to use the personnel of the Federal Agency for Real Estate Cadastre as expert advisors and mediators, as a public service in support of completion of the re-registration program. These services would be part of the usual responsibilities of the cadastre personnel and provided free of charge or for a nominal fee to citizens. (The US Cadastral Survey, responsible for survey of public lands, operates an ADR procedure as a public service to resolve disputes between users of public lands as well as between land users and government regulators. It reviews all legal and title records, holds informal on-site hearings, prepares**

**reports and opinions, negotiates legal resolutions, and provides draft legal documents.)**

- **Disputes to which municipalities are a party are not good subjects for ADR unless the municipalities agree or are compelled to participate. Whether either is likely is not for us to answer. It is possible that even municipalities can be educated to the benefits of quick and low cost modes of mediation in various types of disputes. It is also possible that the amended rules for land re-registration, which we have recommended be prepared as a first step, could require that the parties submit to non-binding mediation procedures before an application for re-registration of land rights is rejected.**

- **Consideration should be given to establishing permanent local commissions that would hear land disputes. These "local land commission" would be both a means of administrative appeal and a means of mediating disputes between private parties. Composition of the commission would be independent experts in land matters.**

- **The present Law on Arbitration Tribunals in the RF (102FZ of July, 2002) establishes rules for creation and operation of permanent and ad hoc third party arbitration tribunals. This is a complex law which creates a formal system of arbitration. It provides for but does not require binding decisions, and allows for enforcement of decisions through normal executive procedures. Its utility in the types of disputes at issue in the present discussion could be limited. For example, a tribunal could not be established under the auspices of a Federal, regional or local government or governmental agency, and it could not hear disputes against administrative decisions, or any disputes involving local government for that matter. At this time there is nothing preventing private parties to use the law to resolve their disputes. However, whether they would actually do so is again a matter of education and promotion? Since MEDT could not itself sponsor or organize a tribunal under the law, its role could perhaps be encouraging and working with likely non-governmental organizations to establish either one or more permanent tribunals under the law to resolve land disputes, or a mechanism for quickly creating ad hoc tribunals as needed, perhaps by creating a list of interested and qualified mediators/arbitrators from which parties could empanel their own tribunal. While this approach may be useful in disputes between sophisticated parties, it is our view that a more informal approach to mediation using available public resources, provided as a public service, could be successful in other cases.**

### 5. Re-registration Procedures and the Roles of Local and Federal Governments

Among the complaints about the land acquisition procedures expressed by businesses in response to the ongoing FIAS surveys of business attitudes and experiences there are the necessity to obtain numerous official approvals; requirements to produce documents not specified in the law; arbitrary bureaucratic behavior; direct or oblique allusions to the

necessity of unofficial payments; and arbitrary interpretation of the legislation. These are essentially issues of process management. We have already expressed the opinion that the rules and procedures for re-registration of land rights have been insufficiently detailed, leaving localities with excessive discretion and ample opportunities to avoid the state policy on re-registration.

The underlying problem may be that municipalities have inherent conflicts of interest in the re-registration process. Surrendering land rights to the private sector deprives local officials of a source of patronage to favored groups and individuals, economic and political control, planning flexibility, and a source of long term rents for municipal budgets (in the absence of a modern system of real property taxation). There is every reason to expect that they would try to avoid or delay this outcome.

**One approach to this problem would be to "Federalize" the re-registration process in an existing or newly created agency of the RF Government.** It is clear that the right or re-registration is a Federal right governed by Federal law. A good indication of that is that in its Draft Law on Re-Registration of Enterprise Land MEDT proposes to establish maximum prices and require that local governments must consider an application for re-registration within 30 days of submission of the application, clearly asserting the Federal prerogative in this sphere. Federalization of the process could also assure greater consistency in policy and implementation. While the MEDT's Federal Agency For State Property Management is a likely candidate for this role, it is not clear to us whether it has sufficient staff or training at present, which could require a significant investment of Federal budgetary resources, and it is possible that conversion to this approach could cause delays and ultimately become a "bottleneck" in the process.

**A second and similar approach would be to require that the process be managed by local commissions that are independent of the municipal administration**. This approach has been implemented in land restitution programs throughout central and eastern Europe with some success. An independent commission can act with expertise and objectivity, provided that appointments are made to achieve these objectives. They could provide additional human resources to accelerate processing of applications. Commissions could be established on regional or sub-regional levels to address the needs of the many new small municipalities. One option which could perhaps assure greater independence and objectivity would be ex officio appointments which would include municipal, regional and Federal agencies. Finding budgetary resources to support the commissions would again be an issue, which may depend on the priority that the Federal government sets on completing the process of re-registration. Whether the already established local and regional commissions for property management have the resources, expertise and level of independence necessary to carry out this function may be worth further consideration.

One of the benefits of both the Federalization and the independent commission models is that they would implement a "one-window" facility for processing of applications. One stop facilities have been shown to be highly effective in other spheres of activity,

including registration of real estate titles, land allocation, investment assistance and issuance of urban planning permits.

Federalization or creation of independent commissions would require significant changes in the present administrative arrangements, creation of new institutions, investment of resources, and possibly encounter shortages of available and trained personnel. We are sensitive to the pressures that federalization in particular would place on the Federal budget, and also to the opinion of some commentators that too much authority is presently being centralized in the Federal government. Federalization may therefore be the least attractive option at this time. **A less intensive alternative to both federalization and creation of independent local commissions may be to create a Federal administrative appeals procedure for re-registration cases.** This would leave local discretion and institutions in place, but subject to oversight by administrators with an interest in supporting the policy of re-registration. Whether this would add yet another step and more delay to the process, particularly if court challenges to administrative decisions became widespread, is always a risk. Selection and appointment of the appropriate appeals tribunal also poses a short term challenge, as well as finding resources to support the activities. As with the proposals for ADR interventions, perhaps some of this work could be placed on the staff of the RF Cadastre Agency, who would sit in permanent appeals boards for localities or regions.

As suggested elsewhere in this report, fundamental approaches to restraining inappropriate administrative behavior by local administrations also include further detailing the rules and procedures of the re-registration process, and monitoring local performance by an effective system of data gathering and reporting.

## 6. Compulsory Conversion of Rights

The law requires that enterprises holding rights of land use convert their right to a lease or ownership by January 1, 2006. The original deadline was January 1, 2004, but it became clear that deadline would not be met, partly because of enterprise reluctance to pay high land prices or commit to leases which were viewed as legally inadequate, and partly because of the inability or reluctance of localities to process the conversion requests. It has now becoming clear that the January 1, 2006 deadline also will not be met, for essentially the same reasons, and MEDT is proposing a further extension of the time to January 1, 2008. We believe this is realistic, but that deadline will also be passed if fundamental changes are not made.

The Draft Law On Re-Registration of Enterprise Land put forward by MEDT proposes several steps to accelerate the process of re-registration of rights, including termination of the "right of use" as a legal form of tenure, imposition of administrative penalties on land holders ranging from 200 to 1000 minimum salaries for failure to comply, and mandating that all applications be addressed by local authorities within 30 days.

Business leaders argue that termination of the rights of permanent (perpetual) land use undermines the constitutional rights of the owners of privatized enterprises, since they obtained their property in a package with these land rights. Without offering an opinion

on the constitutional issue raised, we agree that the right of permanent land use is an archaic form of tenure, and it should be eliminated in a market environment.

The intention of MEDT to introduce legal consequences for non-compliance with the re-registration requirement is reasonable, but question whether this once-off penalty in the amount of 200 to 1000 of minimum salaries will compel the larger land holders to rush into significant economic decisions with which they will have to live for a long time.

**Regarding the mandatory time limitation on processing applications, we support the concept but are concerned that with the new Law On the Basic Principles of Organization of Self Government and the appearance of a great number of new municipalities, most of them will not have enough trained specialists to process applications expeditiously.** Judging from past performance, even larger, established municipalities may have a problem meeting the 30 day deadline, and there is of course no administrative sanction for failure to do so. This is again an argument for revising the institutional model for processing of re-registration applications, considering either Federalization, regionalization or some form of independent commissions, all of which could operate on wider areas than individual municipalities.

**Acceleration of the pace of conversion to ownership may be achieved by implementing some of the proposals made by MEDT in its draft law and some of the recommendations of this report.** Acceleration of the overall pace of conversion may depend on whether improvements are made also to municipal leasing practices. It is our conclusion that many enterprises that do not wish to purchase land, or are financially unable to purchase, are at the same time reluctant to enter into leases on present terms and conditions.

Many business enterprises in Russia view a lease as far inferior to ownership as a legal right. In one of the ongoing FIAS surveys of business attitudes and experiences 7.7% of respondents claimed they experienced threats from state organs to terminate rights for leased premises, and this figure exceeded 10% in a number of regions. In one survey only 7.5% of respondents expressed a preference for leasing over ownership. Business representatives have expressed to us not only distrust of the legal security of leasing, but also the fact that over a long term lease they have no protection against unreasonable rent increases. Under current practice land rent increases have been totally within the discretion of localities.

The MEDT proposals in the Draft Law On Re-Registration of Enterprise Land seeks to address some of these issues by establishing a maximum rent of 3% of cadastral valuation and assuring that land holders will be given lease terms of up to 49 years (or less if the land is reserved for future public use or the lessee requests a shorter term). Regarding the proposed 3% lease rate, it does not strike us as exceptionally high, but have no way of comparing it to actual market lease rates today. In many places it will compare very unfavorably with the buyout price of 5% of cadastral value, and land holders should therefore be induced to purchase rather than lease the land. In our view, it is desirable to give land holders the financial incentive to purchase rather than lease the land. In areas in which the buyout price is 20% of cadastral value, a lease rate of 3% is more attractive, but probably still not low enough to create strong preference for lease over ownership.

At the same time, however, the lease rate of 3% is twice the tax rate which would be paid if the land were owned, which gives municipalities a further incentive to discourage or obstruct sale of the land and pressure holders into the higher paying leases. Thus, the proposed lease rate may create conflicting incentives for land holders and municipalities.

These two steps are important, but other steps that need to be taken to improve the quality of leases include:

- **The leasing option does not formally resolve for the land holder the issues of change of use and redevelopment. Under the proposed "speculation tax" the land owner knows that he will be able to redevelop in accordance with current planning rules simply upon payment of the tax, which is a transparent amount. Leasing, on the other hand, gives the lessor complete discretion to deny change of use of the land, and there is no limitation on what that right could cost the land holder. While in practice, changing use under leases has not been a significant problem, and the costs have probably been much lower than the proposed speculation charge, as a legal matter there is no equivalency between the sale and lease options on this important point, and the lease is clearly inferior. Although we disagree with the concept of the "speculation tax," it would seem that to make leasing an attractive option some consideration should be given to how change of use should be addressed under leases, for example by permitting change of use subject to a one-off payment or a limited increase in rental.**

- **Further with respect to change of use of leased land, the leases should provide that lessees are permitted any use which is permitted for the land plot by right under the town plans (not special permit uses), without the need for consent of the lessor. In their use of the land, lessees should be subject only to the general rules of town planning and environmental protection.**

- **Regarding the term of 49 years, we have argued consistently that the emphasis on this term in Russian practice is misplaced, and that there is no reason not to extend the lease term to 75 or even 99 years, or alternatively to require extension of the term unless rejected by land holder. Longer terms are commonplace in other countries, and provide more security to the investor and to mortgage financiers.**

- **Leases issued under the re-registration program should follow a format established by rules. Those rules should prohibit termination of the lease for any reason other than willful environmental degradation and failure to pay rent for an extended period of time, perhaps 2-3 years. Beyond this, termination of the lease should be permitted only on the same grounds that confiscation of the land would be permitted.**

- **The leases should contain an option to purchase which may be exercised by the lessee at any time during the term at a price equivalent to the original**

**buyout price adjusted for increases in cadastral value, with a credit against the buyout price for lease payments already made.**

## 7. Re-allocation of receipts from rents, sales and taxes

An analysis of the history of land privatization in Russia leads to the conclusion that local obstruction of privatization of enterprise land is at least partly based on economic calculations. The allocation of land rents, taxes and sales proceeds to Federal, regional and local budgets has changed frequently, but land rents have usually gone in larger proportion to local budgets while large portions of the proceeds from land sales have been sent to Federal and regional budgets. Although the land tax was characterized as a local tax, it was actually divided among the levels of the budgetary system according to the proportions adopted every year by the laws on federal budget. More importantly, land rents have been within the control of local governments while land taxes, which are substituted for rents if the land is sold, are subject to limitations imposed by Federal law. There are strong indications that local officials believe they would have more control over the long term revenues from land by leasing and collecting rents than by selling and collecting taxes.

The situation is gradually changing. According to the Federal Law No. 120, as of 20.08.2004, "On amendments to the RF Budget Code in Respect of Inter-Budgetary Relations," starting from January 1, 2006 100% of the land tax will go to settlements, municipal regions and town districts. Federal Law No. 111 as of August 20, 2004 "On Introduction of Changes to the Article 60 of the Budget Code of the Russian Federation" provides that starting from January 1, 2006, all proceeds from the sale and leasing of state-owned unimproved land plots located within municipalities and allocated for housing development will go to the local budgets, until the state-owned land plots are delineated by type of owner. This is a clear recognition of the need to financially motivate local authorities' to make land available for development.

In 2005 revenues from rent and sale of leasing rights on land of all categories are divided equally between the regional and local budgets until the land plots are delineated. Revenues from sale of improved land plots under the re-registration program go entirely to the budget of the respective body (federal, regional, municipal budget) that owned the enterprise or real estate object on the land prior to their privatization, and receipts from sale into property of unimproved land plots are distributed 15% to the Federal budget, 35% to the region, and 50% to the locality. All the receipts from rent, sale into property or sale of leasing rights on delineated land go to designated owner.

**To encourage localities to support re-registration, consideration could be given to further amending the federal tax legislation to provide that until delineation of state-owned land property is completed, a greater share of revenues from sale of all categories of land go into local budgets.** A greater share of proceeds not only from land designated for housing development, but for commercial and industrial uses as well, may be justified considering the fact that main bulk of paperwork for land privatization falls onto local authorities, including the cases of privatization of federal land. This objective could also be achieved by adoption of regional regulations according to which a subject of the federation returns to municipal authorities its share (35 percent) of one-time

payments received from investors for the right to lease land of unimproved land sold through auctions. In this case local authorities' share related to one-time payments for the purchased land increases from 50 to 85 percent.

**Still the better approach may be to introduce amendments to the federal law providing for: (1) the revenue from sale into property and sale of leasing rights on unimproved land assigned for production and commercial uses, as well as in the case of unimproved land for housing development, shall go in full into local budgets until the delineation of state-owned land is completed; (2) 50% of the proceeds from the sale of all improved land (occupied by enterprises and building owners) located within the municipalities shall go to the local budgets, until the state-owned land plots are delineated by type of owner.**

## 8. Reservation of land (removal of land from circulation) for future public needs

Major exceptions to the right of re-registration occur when the land is reserved for future public use or located in protected territory. These exceptions can undermine the policy of re-registration, and account for most denials of applications. We have been to cities in which over 50% of the urban territory has been placed in sanitary or water protection zones, and others which routinely designate land for future public use regardless of whether there is any realistic chance within a reasonable time frame of ever actually using the property for such purposes. It is our view that this device is frequently used to avoid the policy of re-registration and maintain municipal control over land markets.

One of the troubling aspects of this practice is that it effectively deprives land holders of a right without compensation. To re-characterize land in this way is equivalent to taking it from its holder, without the obligation to pay the compensation which would be due when any land use right is terminated.

The situation in Russia today differs from that faced in some developed economies, but there are some analogies. In the developed economies, where the state and municipalities own relatively little land, planners on occasion show a future public use of private land in official town planning documents. The implication is that the land eventually will be taken for public use and compensation paid to the owner. However, until that occurs, the owner may be prevented from improving or redeveloping his property under threat that he will not be compensated for those improvements once the plan has been published. In addition, the owner could lose long term tenants who seek other accommodations, or potential purchasers. The value of the land is affected by the cloud of an eventual taking of the land for a public purpose. Ultimately, many of these planned public improvements are not implemented for lack of resources of change or plan, which only increases the damages to the land owner.

The new Planning Code was going to limit the ability of cities to classify land as needed for public use, introducing the provision of Article. 9, Cl. 4.[5] This may be considered as

[5] "It is not permitted to the bodies of the state power and local self-governance to adopt decisions on reservation of land, on withdrawal, including through buy out, for state and municipal needs, as well as on transfer of land from one category to another, in the absence of the documents on territorial planning, except for the cases, stipulated by the federal laws".

a positive step, although we are not quite convinced that it would be effective enough, since there are no requirements to the planning documentation as a prerequisite for making the decisions on land reservation, and criterion of its absence. Actually, in all municipalities may be found some sort of town planning acts, including those which were adopted tens years ago.

Moreover, our main point is that the reservation itself has to be made a legal component of the territorial plans, adopted in the same way as any adoption or change to the plan. The Planning Code does not say that to us - it says that reservations may be made so long as some territorial plans exist. This strikes us as a different requirement, and it says nothing about how the reservation itself is to be adopted, changed, etc.

There are many proposals for attempting to address this inequity by placing limitations on the effects of "reserving" land through planning mechanisms. Those proposals might include:

- requiring that the reservation be approved in the usual way for urban planning documents adopted in conformity with the valid Master Plans, and including public participation and rights of challenge, as stipulated by the Urban Planning Code;
- requiring that the reservation be justified by feasibility and cost-benefit analysis in addition to usual planning concerns;
- requiring that the facility for which reservation is made is included in the capital budget of the municipality, an entirely separate procedure;
- placing limitations on the amount of time land may be reserved without an actual taking of the land and commencement of the improvements;
- permitting land owners to seek termination of the reservation in case of changed circumstances and lapse of time;
- requiring periodic review and justification of reservations;
- mandatory compensation to owners for loss of profits during the period of reservation.

The present situation in Russian is slightly different, in that the land is not yet privately owned when it is "reserved" for a public purpose, but legal rights of use and beneficial rights to acquire ownership nevertheless exist. The similar result in both situations is that the present land holders rights to use and dispose of the land are compromised.

The new Urban Planning Code addresses this issue in a very rudimentary manner by requiring that no local authority may issue a decision on reserving land for public use unless the reservation is included in town planning documents. At most, this provision could make attempts to reserve land on an ad hoc basis more inconvenient, but will not be likely to stop the practice of including large scale reservations in planning documentation without regard to actual need or likelihood of actually proceeding with the public use.

The effect of this practice is to slow the pace of re-registration and investment and limit the development of private land markets. It can contribute to municipal monopolization of land markets, reduction in the supply of land in private markets, and perhaps artificially high prices.

The RF Urban Planning Code addresses these issues in the most rudimentary way. To avoid these results, further steps could be taken to limit this practice. Possible steps that should be considered include:

- **Planning reservations should be permitted only through the usual processes for adopting or amending urban plans.**

- **Reservation of land in planning documents should be supported not just by planning standards, but by budgetary and financial standards. Economic feasibility and cost-benefit analysis should be required to justify inclusion of a reservation in a municipal plan.**

- **Limit reservations to public facilities. Exclude reservations which amount to nothing more than a proposed change from one use to another, such as "industrial" to "residential."**

- **The facility for which a reservation is made should be included in the capital budget of the municipality.**

- **Absence of urban planning documents for the developed area in which the land is located should not be recognized as legal grounds for denying applications for purchase.**

- **Non-conformity of the present use with urban plans should not be recognized as grounds for denial of application for purchase. The land holder should have the same rights as any owner of a building or facility that does not conform with land use restrictions adopted after construction of the facility.**

- **Establish time limits in which the municipality must actually take the land and/or pay compensation to the holder for termination of the right of use. Until there is an immediate cost associated with reservation of land for public use, and in the absence of other effective restrictions, municipal planners have the incentive to reserve too much land. Too much land will be reserved for unrealistic purposes.**

- **Provide that if the land is not taken within a reasonable period, perhaps 5 years, the reservation lapses, the holder's right to re-register the land as property is revived and it may be purchased at the initial re-registration price.**

- **Require periodic review and justification of the planning reservation.**

- **Require compensation for profits lost for denial of the right of re-registration on grounds of reservation for future public use, and develop regulations and formulas for calculating losses to the land holder.**

- **In connection with Federal oversight over the re-registration program, require municipalities to identify and justify all current reservations which can result in denial of a right of re-registration.**

## 9. Monitoring Progress

In our view, and as reported in the MEDT Report, local authorities have been a roadblock to re-registration of land rights. FIAS surveys of the business community in Russia suggest that only one-third of the businesses that apply for ownership of the land succeed. However, official statistics on the extent of the problem are not available. In the course of this project the team attempted to obtain relevant statistics on land privatization in Russian cities, but without success. Only at the regional level, through personal contacts, was it possible to obtain some limited amount of information. In addition, Gosstat may provide some gross statistics on land privatization for a fee, but requires several weeks to do so. And, statistics on land auctions and non-competitive land allocation are not available at all except by direct request to localities, and then only in some cases.

The form of the state statistical review # 3-zem which was amended in June 2005 and which is now called “Land Transactions” contains only the aggregate information on the main types of the land transactions, and does not contain the specific information essential for policy decision making and adjustment of the strategy for the land market development. In fact, this aggregate data is not useful for what we are proposing to do - which is determine local performance in implementation of the law. The existing statistical reporting forms include little if any of the specific data we recommend in this report.

Despite the fact that Federal law establishes the basic civil rights to privatize land and to be treated fairly in administrative procedures (e.g. auctions), there is no requirement that localities report activities on land rights re-registration, and no Federal agency supervises this important national objective. At the same time, greater transparency may be one of the few tools the Federal government has to monitor the cooperation of local governments in implementing these policy objectives. In addition, policy interventions should be tailored to address actual problems. For example, the specific reasons why so many applications for re-registration of land rights are rejected would be important information for policy development.

The question should be asked why the government does not collect and maintain statistical information on this important aspect of state policy. **We recommend that the Federal government establish a more detailed statistical reporting requirement for transactions in state and local land, including the information on applications for acquisition of land, its terms, etc.** The amount or reporting would not be a significant burden on local and regional governments, as many already keep this data for themselves.

There are substantial legal grounds for implementing a reporting system, including general oversight of implementation of the RF Land Code and the law On Local Self-Government; maintenance of the national cadastre; and the continuing Federal legal interest in land prior to completion of the delineation process.

The MEDT, which is now in charge of most issues relating to state property, either independently or in cooperation with Gosstat, would be the appropriate agency to design and implement such a system. The data to be included in the reporting is a matter for development, but should focus on indicators that can monitor local performance in meeting the requirements of the law, including for example:

Re-registration

- number of applications
- land use
- approved
  - (time for approval)
- rejected
  - (time)
- delayed
  - (time)
- reasons for rejection
  - documentation
  - boundary
  - town planning
  - Federal/local land delineation
  - Etc.
- Price
- Amount of land claimed
- Amount of land awarded

Land auctions

number of events
cancelled events
size of land parcel
land use
approximate distance from the center
starting price
sale price
auction period (from announcement until completion of auction)
number of applications
number of disqualified applications
number of registered bidders

# III. Availability of Unimproved Land for New Construction

Re-registration of the land rights of enterprises and building owners is only one of the approaches to creating the private sector land market. Another important issue for improving business access to land is the legislation which defines the types of unimproved land plots which can be sold or leased for development purposes, which is mainly an issue of creating transparent competitive and non-competitive procedures for divesting state and municipal land into the private use and ownership.

## A. Current Law

### 1. The Land Code

In all cases which refer to "prior conciliation" of location the Land Code is interpreted to refer to planning and zoning rules which identify the permitted use of the land parcel and the essential constraints on the type of structure that may be constructed, and the availability of connections to essential utility services. Thus, "prior conciliation " usually can exist only if the locality has comprehensive planning and zoning regulations and transparent, well regulated procedures for obtaining connection rights to public utility systems, all of which are practically non-existent in Russia today. Alternatively, localities may prepare all of the necessary planning documentation for selected land parcels on a case-by-case basis prior to offering them for sale by auction or tender.

Under Article 30 of the Land Code, in cases where "prior conciliation of the location" of the facility to be constructed is not required, the unimproved land plot may be sold as property only through an auction, or the lease rights sold through auction or through direct negotiation. When "prior conciliation" of the location of the facility is required, the unimproved land plot for construction purposes may not be sold as property. It is not specified whether the unimproved land plot may be leased by either auction or direct negotiation, but those possibilities are implied and are in fact the only apparent explanation for these provisions of the Land Code.

Unimproved land plots for purposes not related to construction may be sold into ownership or leased through direct negotiation. Whether such land can also be sold or leased through auction procedures is not specified in the law. In any case, as a matter of practice auctions are not required for this type of land. Moreover, it is unclear what kind of land plots of this category may be allocated into property: many such land plots may have non-capital construction objects on them, e.g. kiosks, temporary awnings for cars *("rakushkas"),* etc.

Thus, the present law provides for mandatory auctions only (1) when land is sold into ownership and "prior conciliation of location" is not required, which is today a very small minority of cases, and (2) when land is made available for housing development pursuant to recent amendments to Article 38 of the Land Code, discussed further below. In effect then, the present situation differs very little from the mechanism of granting construction rights inherited from the Soviet administrative system of land use regulation. Allocation of land plots for construction purposes still relies primarily on non-competitive transfer

into lease,[6] which leaves open the question of favoritism and corruption which has accompanied local land privatization programs since their inception.

## 2. Recent changes to auction procedures for residential land

In late 2004, under the legislative initiative of the RF President to develop and implement a comprehensive set of laws aimed at the formation of an affordable housing market, there were adopted a number of laws to address certain serious issues and problematic situations in the sphere of residential development. The most important changes for purposes of the present analysis arise under Federal Law No. 191 as of 12.29.2004, "On Enactment of the Town Planning Code of the Russian Federation," which amends the Land Code to provide that as of October 1, 2005 transfer of land plots for residential development into ownership or lease are conducted only through auctions (Art. 30.1, Cl. 2). In case of "complex development for the purpose of housing construction" only lease rights may be granted at auctions, and within such "complex development" individual land plots subsequently may be purchased as property upon the completion of construction of utility facilities and cadastral survey.

These newly added clauses to Articles 30 and 38 of the Land Code raise a number of questions deserving of consideration:

- In case of "complex development for the purpose of housing construction" the owner or lessee of land plots is obliged to comply with the established terms of housing construction (Art. 30.2, Cl. 6; Art. 38.2, Cl. 3, It. 8), and the enforcement provisions (Art. 30.2, Cls. 8, 9) stipulate that the rights to the land plots may be terminated in case of "inappropriate accomplishment of the requirements." The term "inappropriate accomplishment" is not clearly defined and could be abused.
- The initial Articles 30 and 38 of the Land Code are concerned with land auctions and tenders, whereas the amendments are concerned only with land auctions. The distinction between auctions and tenders is clear in Russian law, particularly the Civil Code, and they are different procedures. Moreover, simple auctions in cases of "complex development for the purpose of housing construction" may be difficult. Indeed, the new law may anticipate this difficulty when it requires participants in the auction for complex development to present "documents containing the proposals on planning, subdivision and development of the territory." It is unclear why these documents are required and how they are used at the auction if the bids are concerned only with the proposed purchase price, as the legal definition of auction supposes.
- Generally, the "complex development for the purpose of housing construction" is inadequately defined and too simplified. Obviously, this development may be concerned with large territories which would be subdivided and on which several buildings and facilities would be located. It is also most likely that development of such territories will include housing construction as well as social facilities,

[6] Transfer of land plots into lease for real estate development without "prior conciliation of facilities location" without an auction is allowed on compliance with two conditions: 1) the information on availability of such plots is published well in advance, and 2) only one application was submitted after the publication (Land Code, art. 30, cl. 4).

retail trade and other commercial real estate. It is not clear whether competitive allocation of such other territories is regulated by these provisions.

- It is not clear why the method of estimation of the starting price is different for cases of "complex development" and other cases of auction of residential land. In the first case the information in mass media on the auction (Invitation to Bid) contains the information concerning the rent rate and "the starting price of the right to sign a lease," i.e. lump sum exceeding the rent (Art 38.2, Cl. 3, Its. 3, 4), whereas in the second case the starting price is interpreted as "a starting amount of rent." (Art. 38.1, Cl. 7; Cl. 10, It. 5).
- In case of the housing development the information on technical conditions of connection to the engineering infrastructure and connection fees must be included into the package of auction documents. But in most cases the actual technical conditions and connection fees can be specified only upon consideration of a relatively advanced design of the improvements. Until that time technical conditions and connection fees may be considered preliminary in nature.
- The terms, procedures of preparation and holding auctions are in our opinion too simplified and not flexible in respect of the interests of developers. For example, techniques as an option to pay off the purchase price by installments, to compete on the schedule of payments, reasonable pre-qualification procedures for participation in auctions, the concept of the reserve price and the alternative models of bidding, are not addressed at all. We understand that it was the intention of the legislators to exclude the possibility of arbitrary administrative behavior and corruption, but these techniques have proven to be useful elsewhere and may enhance the development of competitive procedures of land allocation, especially in case of commercial development.
- Under the new auction rules, which particularly are intended to avoid speculation, speculation may become the rule rather than the exception. Prohibition of meaningful pre-qualification requirements very likely will permit the winning bidder to flip the contract, without limitation, (so-called "briefcase developers"). So, small groups of favored individuals who have never constructed a house may win the bids in many cases, and then sell the assignment of the contract to actual developers, or bring real developers in on some venture. It is not unusual for a municipality to want to see both prior project experience and financial capability before the applicant would be permitted to participate in the bid.

The recent amendments are concerned only with housing development, were elaborated and adopted in a package of laws on "affordable housing," a significant concern in many places. Nevertheless, the procedures of preparing and conducting land auctions in respect of commercial land development are much the same as for housing development. Moreover, further development of the rules on allocation of non-residential land may be as important since non-residential development may be a source of considerable receipts to the local budgets, creates new jobs, develops co-operating industries and services, and generally stimulates economic growth.

MEDT and Federal Antimonopoly Service (FAS) officials acknowledge the necessity to elaborate further regulations governing competitive procedures for allocating land for

commercial development. An issue has been within which legal act these regulations should be developed. **In our view the recent additions to the Land Code were a departure from the framework concept of that law, and further amendments for the Code may not be necessary. It would be more appropriate to develop details pertaining to land auctions and tenders for housing and commercial development in the "Rules of Organization and Management of Public and Municipal Land Sales and Leases" adopted by the Resolution of RF Government No. 808, as of 11.11.2002, which is discussed further below.**

### 3. Current auction regulations affecting commercial development - Government Resolution 808

Except for housing, the procedures for competitive allocation of land plots used for commercial and other purposes are still governed by the Resolution of the RF Government No. 808 "On Organization and Management of Public and Municipal Land Sales and Leases." Resolution 808 replaced RF Government Resolution No. 2 of 01.05.98, "On Approval of Procedures for Organization of Sales (Auctions, Tenders) of Lands in Urban and Rural Settlements, or Lease of Them, to Natural and Legal Entities." The earlier Resolution 2 provided in our opinion an adequate legal framework for organization of competitive land sales, and slow progress in implementing land auctions was caused by a variety of economic and political factors unrelated to the procedures themselves. However, the more recent Resolution 808 has not only failed to correct some deficiencies of the earlier legal act, but may actually have created new barriers in the development of competitive land sales.

In our estimation, contradictions, ambiguities and simple errors in Resolution 808 which may undermine the efficiency of auction procedures include:

- Bidders are required "to make bids on the amount of rent" rather than a fee for the right to conclude a lease agreement, as it was provided by the Resolution 2. The Rule does not clarify what amount of rent constitutes the starting price: monthly, yearly, or for the whole leasing term, and whether rent bids must be compared using some sort of net present value formula which would allow comparison of streams of payments. The same vague requirement is found in the newly amended Land Code (Art. 38.1). Moreover, it is more logical to set a formula for a long-term lease, rather than to fix its rate for the whole period. Finally, this provision does not anticipate the requirement that the land rate shall not be more than 3 percent of cadastral value of land plot, and how that limitation would affect bidding.
- Resolution 808, Cls. 3–5, has inherited the deficiency of Resolution 2, containing statements about federal, regional and municipal lands, which treats public lands as already assigned to a specific level of public authority. However, since the provisions of the federal law On Delineation of Ownership in Public Lands are not yet implemented, the Resolution in point should rather regulate who will be the seller of a land plot if it is still unclear which public authority it belongs to.
- The rule is concerned with land auctions only, and does not present the procedures for land tenders. Thus, contrary to the Resolution 2, the rules do not

envisage the possibility of making decisions by tender commissions.

- Particularly important is that Resolution 2 directly specified that the established rules covered lands for development, while Resolution 808 remains vague whether its rules cover only lands allocated for development purposes or other lands as well. This is exactly the kind of clarification that is needed due to the lack of clarity on these issues in the Land Code, as noted above.
- From Item 3 of the Rules it appears that the authorized seller of federally-owned lands (although the Rules provides no definitions for such terms as "owner" or "seller") is the Ministry for Property Relations (currently, the Federal Agency), which, in particular, is authorized to "submit offers on organization of competitive sales and terms of bidding to the RF Government", "regulate most essential terms of land sale agreements", and "conclude land lease agreements based on the bidding results". In effect, the functions of the seller and the manager of land auctions are put topsy-turvy when compared with the equivalent provisions of the Civil Code (Arts. 447–448), Resolution 2, as well as the amended Land Code;
- Contrary to the provisions of the Civil Code on holding auctions and tenders (Art. 448, Cl. 1), the rules (as well as the Resolution 2, and the amendments to the Land Code) envisage only competitive sales with an open list of bidders, essentially prohibiting pre-qualification.
- Contrary to the Land Code (Art. 38.1, Cl. 3), the rules permit closed bidding (in envelopes), which is reasonable, particularly in case of competing on the schedule of payments. But at the same time, it stipulates that in case of equal price proposals, the bidder which has presented the bid earlier is declared the winner of the auction. This solution seems illogical, when the actual time of submitting the sealed bid is irrelevant to the objectives of the proceeding and it is a simple matter in this case to ask the competitors to present new bids.
- The rules, as well as the Resolution 2, and the amended Land Code, repeat the faulty provision initially fixed in the Civil Code (Art. 448, Cl. 5), which envisages that the winner shall be defined the same day as the auction takes place. It may be applicable to the auctions, when the only one criteria of the winner is the proposed price, but in fact is not possible in case of land tenders, when a set of non-quantitative proposals may be presented. Such proposals need much more time to be assessed.

**Overall, Resolution 808 presents some problems that may limit the growth of competitive procedures as a land allocation mechanism and needs further amendments and elaboration, particularly in respect of industrial and commercial development, as well as non-construction uses.**

## B. Experience with Land Auctions

Use of competitive procedures for selling unimproved land plots has not been widespread. In some regions and cities (e.g., Samara, Tomsk, most of the cities of

Leningrad Oblast) no land auctions have occurred. In some other RF Subjects and cities (e.g., Moscow, Nizhny Novgorod) auctions are held only for lease rights, and in some cities of this category, land lease rights are auctioned only for short terms (3–10 years for small scale trade and service uses and non-capital construction purposes, such as gas stations, car washes, car services, parking lots, *kiosks*, summer cafes, etc.). Overall, the number of land tenders in the Russian municipalities remains quite small.

Even in Veliky Novgorod, a participant in the World Bank housing development project which emphasized the development of land auction mechanisms, land tenders virtually ceased after the pilot project of 1995–1996. In contrast, the cities of the Saratov Oblast (Saratov, Balakovo) are pioneers in conducting land auctions, selling not only the right to lease, but selling the land plots as property as well. However the land plots are sold there into ownership mainly for building of private dwelling houses, and very seldom for commercial activities. The majority of tenders are still for land lease rights of 5 year duration, and only recently have there been long-term leases of 10 to 25 years.

Only unimproved and unencumbered land plots, which are usually rather rare, are offered for sale in most regions and municipalities. There are only a few cases when land plots with significant encumbrances, for example dilapidated housing needing to move the residents to a new place, which comprise the majority of land plots desirable for redevelopment, are offered at auctions and tenders. It also appears that mainly land plots located on the outskirts of cities are sold by auction, and not the land plots in central municipal districts and other prestigious areas which are of most interest to private developers.

Tender participants in many cities suggest that land tenders still are often preceded by direct negotiations with potential buyers on the price of the land lease rights as well as unofficial payments, after which the tender is organized, in essence, for the specific buyer.

A selective survey of private developers conducted by FIAS suggests that mainly new, truly private sector development companies are relegated to participation in auctions, and that quasi- state or municipal construction companies still typically acquire land through direct negotiation.

A frequent problem still affecting the feasibility of tenders and auctions is the fact that technical information on land plots is often incomplete, and available documentation (in particular dealing with geological conditions, underground communications and utility systems) do not reflect the actual situation. As a result, successful bidders must order many missing or inaccurate documents on their own, and also get the necessary technical specifications themselves, just as they would if the sites were directly allocated without auction. In some cases, inaccuracy of the information provided by municipal authorities, or utility companies (for which in fact no one is liable financially or otherwise) is discovered late in the development process, when the developer has already contracted the elaboration of expensive design documentation, and the works have begun. As a result, the construction costs are often considerably higher than the initial estimate, meaning that too much may be paid for the land. Perhaps most importantly, the winner of the land auction or tender cannot expect the authorities to take into consideration the specific characteristics or difficulty of the project encountered in the course of

construction or look for reasonable compromise between the interests of the city and those of the developer if undisclosed problems are encountered.

## C. Improving the efficiency and transparency of land auction procedures

To facilitate development of competitive land sales and enhance their efficiency we recommend that the following ideas be considered:

- **Now that somewhat detailed provisions have been included in the law for auction of housing land, it is appropriate to develop further procedures for preparing and conducting land auctions and tenders in respect of industrial and commercial uses. Much of this can be accomplished by further development of Government Resolution 808, and does not necessarily need to be done by law.**
- **In our opinion the recent amendments to the Land Code regarding auction of land for housing contain some conceptual flaws and ambiguities that should be resolved before applying these same provisions to allocation of land for other purposes. Some of these issues are discussed elsewhere in this report, and concern in particular the concept of the "complex development."**
- **Consideration should be given to permitting a wider range of concepts and techniques in auction procedures, including an option to pay off the purchase price by installments and to compete on the schedule of payments; reasonable pre-qualification procedures; and the concept of the reserve price.**
- **Elaborate and provide the regions and municipalities with comprehensive Methodological Guidelines on Preparing and Conducting Land Auctions and Tenders, containing detailed comments on the current law on competitive land sales, and recommendations on its application under different local conditions, with a full package of model land auction (tender) documents attached to it.**[7]
- **Introduce into the regulations specific procedures of holding tenders in respect of "complex development" of territories, including land plots with encumbrances − such as items of unfinished construction, dilapidated housing, environmental contamination, etc. In the longer run it is these types of land areas that may provide a great deal of well located and serviced land in urban areas, but which present the most complex problems of development.**
- **Require that the lists of land plots which may be put up for auction or tenders within a year shall be published in the local press. Such an**

[7] The Methodological Recommendations on Conducting Competitive Land Sales (Auctions, Tenders), approved by the Letter of the RF Land Committee No. CC-902, as of 30 September 1999, may be mentioned in this respect. In spite of numerous ambiguities and errors, and the fact that these Recommendations are updated now, its structure may be used as a model in elaboration of the new Guidelines.

**announcement will permit more extensive consideration by potential bidders and allow time to develop and analyze project concepts, obtain financing, establish partnerships, etc.**

- **Consider an amendment to the law stipulating, that the plots unsold during their first auction should be offered through a mandatory second auction, which should be organized and conducted this time exceptionally by specialized non-governmental tender agencies (whose expenses are reimbursed from the final sale price). At present, a failed auction allows disposal of the land through non-transparent, negotiated procedures, regardless of the reasons for the failure. Thus, an auction requirement can be defeated simply by failure to adequately advertise the property.**
- **Until the zoning ordinance is adopted, a realistic list of permitted land uses should be applied in each case, and not a single "targeted use."**
- **The concept of the bids on the amount of rent needs to be clarified in the law, or more preferably, omitted.**
- **All land sales and leases made without competitive auction or tender, without exception, should be based on independent appraisal of market value or market rental, and should not be lower than appraised value. With regard to auction and tender procedures, the starting price should bear a reasonable relation to appraised value. The starting price should reflect the relation of supply and demand on the real estate market, but should be adjusted to reflect legitimate costs associated with the property, including for example the costs of meeting mandatory architectural design requirements (if any are imposed by the city and included in the auction announcement), the costs of the off-site engineering facilities which the city has already provided, and the costs needed for demolition or taking down of constructions which do not comply with the permitted uses of the site and for cleaning the soil to meet the environmental standards established for the appropriate permitted uses. Preferably, the fees for connection to utility services fees should be included into the starting price of the land plot with the guarantees that no additional payments will be required in respect of development and factual connection to the utility services.**
- **The land auction/tender documentation should contain the full and precise information on the adjoining off- and on-site engineering nets, so as the risks may be assessed, and the investment decisions could be made accurately;**
- **Consider clarifying the law to provide that a land plot must be sold as property at an auction or tender unless leasing is justified, and identify specific and limited criteria for offering a lease rather than property ownership. It is our view that the tendency of local administrations to offer land for lease but not as ownership conflicts with the national objective of creating private sector property markets. At this point in development of the Russian land economy, we view land leasing as a poor "second best" alternative which has many potential drawbacks for development of**

**property markets, including continued legal separation of land and real estate rights; greater opportunity for government interference in private economic decisions; misallocation of land through under- or over-pricing and favoritism; administrative complexity; greater opportunity for official corruption; and inferior property rights. In general, we believe there are significant problems associated with government monopolization of any factor of production. We believe that our reservations are also reflected in the attitudes of most Russian business people, who prefer ownership to leasing. All of these can be debated, but our ultimate conclusion is that Russia needs a private land market to serve as a check on the current level of government monopolization, and that market can be achieved only by mandating some level of land sales. This is not to say that there should be no public land ownership or that leasing may not be appropriate in certain circumstances even today, and the emphasis on sales may perhaps be reconsidered as the amount of privately owned land increases and true private markets develop.**

## D. Non-competitive land allocation procedures

Competitive procedures are not necessarily appropriate in all circumstances, and it is likely that targeted allocation of land and property for commercial use will continue at some level. However, direct transactions can be made more transparent, an implied requirement of Land Code for all dispositions of state and municipal real estate.

Articles 31–33 of the Land Code govern the cases when the "prior conciliation of the facilities location" is required, and are therefore concerned with the non-competitive, direct allocation of land plots for development. No changes were made to these articles in the recent Land Code amendments. A detailed commentary on the shortcomings and ambiguities of articles 31-33 could be a subject of a separate report. Most of these problems are already acknowledged by Russian land and legal experts, and so we limit ourselves only to a few comments here.

The main problem with articles 31-33 is that it is unclear, and arguably unjustified, why land plots may be allocated on a non-competitive basis when "prior conciliation of the facilities location" is necessary. The process of "conciliation of location" is an allocation of a land right and should be subject to prior announcement and solicitation of expressions of interest. The usual argument is that conciliation of project location requires too much work, which the municipalities cannot afford and no private investor will do if there is the risk of losing the land to another investor in a competitive procedure. This argument appears to us to be exaggerated, and in fact municipalities frequently prepare the necessary documentation. The amount of information needed to allow competitive bidding for a land plot is far less than usually suggested, and consists of simple parameters such as approximate size of the permitted building , access, permitted uses, red lines, floor area ratio, and infrastructure locations and conditions. Any additional work can be carried out during detailed project development in the normal course of business. There is no need to have highly developed town plans for entire areas as a condition of proceeding with competitive land allocation procedures. We believe

there is a strong argument to be made that land available for development should be subject to public announcement of availability regardless of whether or not "conciliation of the location of facilities" is necessary.

According to the law, "prior conciliation of the facilities location" is not conducted in case the plot is allocated in accordance with the local zoning ordinance. Thus, as zoning rules become common in the Russian municipalities, a requirement of the Law on Urban Planning, the distinction between transactions with conciliation of location of the construction and transactions without such conciliation should be eliminated from the law. Ultimately, then, the practice of "prior conciliation of the facilities location" will be irrelevant, and transfer of all land into ownership or long-term lease at the starting point of the development process will be feasible, not at its end, as is the case now. Whether implementation of zoning ordinances will be accomplished by January 1, 2010, as is presently required under the Law On Urban Planning remains to be seen, particularly considering the large number of new municipalities which would appear under the law "On the Basic Principles of Organization of Local Self-Governance," and which may not have specialists and financial resources to comply with this requirement.

**With respect to all non-competitive land allocation generally, we recommend that several points should be considered.**

- **We believe that competitive procedures are not appropriate in all cases, and that the objective is to bring the same level of transparency and protection of the public interest to non-competitive procedures. If competitive procedures become mandatory for all types of land, appropriate exceptions to the mandatory auction rule should be made. Those exceptions should be clear, detailed and easily implemented. For example, an exception could be considered for any land transaction considered to be a strategic importance to the locality, to be defined. Strategic importance can be based, for example, on the size of the investment or importance of the investment in terms of producing long term employment or tax revenues. A determination of strategic importance would be justified in a decision of the local administration. In such cases the transaction would still be subject to the independent appraisal rule, but would not be advertised for expressions of interest. However, the terms of the transaction, including the basis of the finding of strategic importance, would be published.**

- **All land sales and leases, without exception, should be based on independent appraisal of market value or market rental, and should not be leased or sold for less than appraised value.**

- **The provisions of art. 31 of the Land Code on informing the community about anticipated allocation of land plots could be further developed by regulation and made more precise. For example, land available for sale or lease should be subject to public announcement in publications of regional significance, including the location, proposed price, terms and town planning parameters.**

- **The same procedures should be applied to any transaction in which a grant of "conciliation of location" for preparation of a land site is proposed. The right to negotiate a "conciliation of location" should be treated as allocation of a land right in the nature of an option, subject to announcement and solicitation of expressions of interest.**

- **Prior to completion of any non-competitive transaction, the proposed terms of the transaction should be published again for objections.**

## E. Land Allocation and the RF Urban Planning Code

We were asked specifically to comment on the new Urban Planning Code in relation to issues of business access to land. The Code is a large and complex law which is mostly beyond the scope of this project. However, it has always been apparent that planning rules have affected the course of land privatization, and still do today. For purposes of this report there are only a few remarks we wish to make on this topic.

We understand that the new Code is still sharply criticized by architects and town planners, which might be expected for such a complex law. Our view is that the law is generally reasonable and a step forward, but that because of its ambitious scope it will be many years before its provisions are fully understood, and many adjustments may be required. It should be considered a work in progress. Arguably the most remarkable change introduced by the new Urban Planning Code is the compulsory implementation of municipal zoning ordinances (rules of land use and development). We have often expressed the opinion that 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. Lack of transparent zoning regulations vests municipal planning authorities with too much discretion, which has often been abused.

Most importantly for the present discussion, without comprehensive zoning regulations, local authorities may also decline to sell land or offer it through competitive procedures, both of which we view as barriers to access. As noted, in the longer run the current legal concept of land requiring "conciliation of location of facilities" will become irrelevant and should no longer be available to avoid sale of land or use of competitive procedures. Whether this result occurs in the reasonable time frame of approximately 4 years anticipated in the law we cannot estimate. Implementation of comprehensive zoning regulations would also serve to reduce the time and expense of preparing competitive land allocation procedures, which must today prepare plans and specification on a case-by-case basis.

A second point, discussed above, is that the new Code failed to address the issue of reservation of land through planning processes, which can become a major barrier to the re-registration program. We have made suggestions on how that problem can be addressed, but would suggest that it be done through the proposed MEDT Law on Re-Registration, rather than through amendments to the Planning Code at this time.

It would have been preferable if the Code did not try to define the criteria for establishing the boundaries of land plots (Art. 46), but rather left that determination to other laws.

In our view other provisions of the Code do not directly affect access to land for business, though they may affect the costs and duration of the process of obtaining land use and construction approvals, which are also important. For example, the law appears to us to give to citizens and legal entities very broad rights to challenge planning documents and decisions, which may lead to proliferation of lawsuits. Typically, such laws would attempt to limit legal standing to challenge such matters to those persons who can clearly demonstrate direct harm from the decision, and also establish rules of decision that require the challenger to prove that an arbitrary abuse of administrative discretion has occurred. Lawsuits could directly affect the ability to proceed with specific projects, as during the coming years, while comprehensive documentation is being developed, much town planning documentation will be developed for specific sites. However, these and other issues are beyond the scope of this report.

# Annex

## Conditional and Possessory Title under UK Law

(Land Registration Act of 2002)

### 9 Titles to freehold estates

(1) In the case of an application for registration under this Chapter of a freehold estate, the classes of title with which the applicant may be registered as proprietor are-

(a) absolute title,

(b) qualified title, and

(c) possessory title;

and the following provisions deal with when each of the classes of title is available.

(2) A person may be registered with absolute title if the registrar is of the opinion that the person's title to the estate is such as a willing buyer could properly be advised by a competent professional adviser to accept.

(3) In applying subsection (2), the registrar may disregard the fact that a person's title appears to him to be open to objection if he is of the opinion that the defect will not cause the holding under the title to be disturbed.

(4) A person may be registered with qualified title if the registrar is of the opinion that the person's title to the estate has been established only for a limited period or subject to certain reservations which cannot be disregarded under subsection (3).

(5) A person may be registered with possessory title if the registrar is of the opinion-

(a) that the person is in actual possession of the land, or in receipt of the rents and profits of the land, by virtue of the estate, and

(b) that there is no other class of title with which he may be registered.

### 11 Freehold Estates (Effect of Registration)

(1) This section is concerned with the registration of a person under this Chapter as the proprietor of a freehold estate.

(2) Registration with absolute title has the effect described in subsections (3) to (5).

(3) The estate is vested in the proprietor together with all interests subsisting for the benefit of the estate.

(4) The estate is vested in the proprietor subject only to the following interests affecting the estate at the time of registration-

(a) interests which are the subject of an entry in the register in relation to the estate,

(b) unregistered interests which fall within any of the paragraphs of Schedule 1, and

(c) interests acquired under the Limitation Act 1980 (c. 58) of which the proprietor has notice.

(5) If the proprietor is not entitled to the estate for his own benefit, or not entitled solely for his own benefit, then, as between himself and the persons beneficially entitled to the estate, the estate is vested in him subject to such of their interests as he has notice of.

(6) Registration with qualified title has the same effect as registration with absolute title, except that it does not affect the enforcement of any estate, right or interest which appears from the register to be excepted from the effect of registration.

(7) Registration with possessory title has the same effect as registration with absolute title, except that it does not affect the enforcement of any estate, right or interest adverse to, or in derogation of, the proprietor's title subsisting at the time of registration or then capable of arising.

**62 Power to upgrade title**

(1) Where the title to a freehold estate is entered in the register as possessory or qualified, the registrar may enter it as absolute if he is satisfied as to the title to the estate.

(2) Where the title to a leasehold estate is entered in the register as good leasehold, the registrar may enter it as absolute if he is satisfied as to the superior title.

(3) Where the title to a leasehold estate is entered in the register as possessory or qualified the registrar may-

(a) enter it as good leasehold if he is satisfied as to the title to the estate, and

(b) enter it as absolute if he is satisfied both as to the title to the estate and as to the superior title.

(4) Where the title to a freehold estate in land has been entered in the register as possessory for at least twelve years, the registrar may enter it as absolute if he is satisfied that the proprietor is in possession of the land.

(5) Where the title to a leasehold estate in land has been entered in the register as possessory for at least twelve years, the registrar may enter it as good leasehold if he is satisfied that the proprietor is in possession of the land.

(6) None of the powers under subsections (1) to (5) is exercisable if there is outstanding any claim adverse to the title of the registered proprietor which is made by virtue of an estate, right or interest whose enforceability is preserved by virtue of the existing entry about the class of title.

(7) The only persons who may apply to the registrar for the exercise of any of the powers under subsections (1) to (5) are-

(a) the proprietor of the estate to which the application relates,

(b) a person entitled to be registered as the proprietor of that estate,

(c) the proprietor of a registered charge affecting that estate, and

(d) a person interested in a registered estate which derives from that estate.

(8) In determining for the purposes of this section whether he is satisfied as to any title, the registrar is to apply the same standards as those which apply under section 9 or 10 to first registration of title.

(9) The Lord Chancellor may by order amend subsection (4) or (5) by substituting for the number of years for the time being specified in that subsection such number of years as the order may provide.

**63 Effect of upgrading title**

(1) On the title to a registered freehold or leasehold estate being entered under section 62 as absolute, the proprietor ceases to hold the estate subject to any estate, right or interest whose enforceability was preserved by virtue of the previous entry about the class of title.

(2) Subsection (1) also applies on the title to a registered leasehold estate being entered under section 62 as good leasehold, except that the entry does not affect or prejudice the enforcement of any estate, right or interest affecting, or in derogation of, the title of the lessor to grant the lease.