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COUNTRY PROFILES  
ON  
THE HOUSING SECTOR

**LITHUANIA**



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## **PREFACE**

This study on Lithuania's housing sector is the fourth carried out by the ECE Committee on Human Settlements to analyse housing sector reform in countries with economies in transition. The first focused on Bulgaria and its results were published in 1996 (ECE/HBP/101). The second study, on Poland, was published in 1998 (ECE/HBP/107). The third study, on Slovakia's housing sector, came out in 1999 (ECE/HBP/112).

These country-specific strategic housing sector analyses are intended to assist the Governments of countries with economies in transition in improving performance in this sector. They also aim to provide practical information to those with a special interest in the country, such as international lender and donor organizations, technical assistance agencies, or private sector investors, within and outside the country. The objective is to identify positive trends and problem areas, so as to be able to assess the implementation of national policies and strategies, and the social and economic consequences of housing reform for the population and other major actors in the sector. The studies are the work of international teams of experts. They cooperate with governmental bodies, non-governmental organizations, local authorities and the private sector to mobilize available information sources in the country. An international team of experts also draws up recommendations to guide the housing sector reform towards sustainable patterns of housing development.

The ECE Committee on Human Settlements included the Country Profile on the Housing Sector of Lithuania in its work programme in September 1998. In January 1999, teams of national and ECE experts were formed to carry out the study. The Governments of Bulgaria, Norway, Slovakia, the Russian Federation and the United Kingdom made national experts available for the task. The travel expenses of the experts from countries in transition and from the ECE secretariat were covered by extrabudgetary funds, which had been provided by Finland and the Netherlands. The Governments of Norway and the United Kingdom financed their national experts' participation as their contribution in kind. The successful conclusion of the project would not have been possible without their generous support.

The fact-finding mission of the international team of experts took place from 21 to 24 February 1999, the verification mission from 16 to 19 May 1999. The experts' Lithuanian partners responded to their queries and requests during both these missions.

The long-term development of the Lithuania's housing sector will depend on the further restructuring of its legal, financial and institutional frameworks. Growth and investment in housing can be maintained if the sector becomes sufficiently competitive and attractive. Accelerating the restructuring of the housing sector along market principles is linked to the stabilization of the economy, but also depends on the commitment of the Lithuanian Government to further reforms. Possibilities include the liberalization of public sector rents; competition in the maintenance and management of housing, the establishment of housing allowances and other financial incentives to ensure cost recovery of housing services and more explicit regulation of owner-occupied multi-family buildings.

## 1. Housing reform

Lithuania has become a 'nation of homeowners' due to the mass privatization of public housing. Restitution and land reforms have also been carried out. Housing markets have replaced the previous uniformity of State- controlled house prices. A number of private actors and institutions have become an integral part of the new market system. New types of housing organizations and intermediaries have developed.

The macroeconomic environment of housing seems to be favourable with economic growth, low inflation, and a low budget deficit. Within this context, current housing policy needs to be integrated with policies for the economic development of the country, as well as with social and spatial policies. Two inter-sectoral links are particularly important for the housing sector. *On the demand side*, the impact of household income on the operation of the housing market requires economic and social policies that allow access to adequate housing for low- and middle-income households. Despite overall economic recovery, household savings and purchasing power remain limited. In addition, financial instruments for housing are poorly developed. Small capital markets and the lack of adequate mortgage arrangements further restrict housing demand. *On the supply side*, new policies need to encourage competition in the provision of new housing and in the delivery of housing services. Housing sub-markets (for construction materials, maintenance and management, housing finance) are relatively small, and ensuring healthy competition is important in terms of consumer choice, as well as in competitive pricing.

*Housing reforms need to be considered a political priority.* Current efforts to revise and update the Law on the Provision of Dwellings for Citizens might be an excellent opportunity to follow up with a national housing strategy and action plan facilitating access to affordable housing. In the post-privatization phase particular emphasis needs to be placed on policies and measures that will encourage the maintenance and renewal of the existing housing stock. The lack of appropriate institutional structures to deal with those issues requires the urgent attention of central and local government authorities. The regional administration, as a new institutional structure, needs to acquire a stronger political mandate to coordinate efficiently the activities of different municipalities. This might achieve better use of regional natural, human and economic resources, and ultimately eliminate existing regional disparities.

### Box 1: Housing policy recommendations

1.1 *Housing policy should become a priority. A reviewed national policy should have the following objectives:*

- *To increase the availability and affordability of housing;*
- *To ensure the efficient use and maintenance of the existing housing stock;*
- *To mobilize funds for housing investment;*
- *To increase the share of social housing.*

1.2 *The national housing policy needs to be implemented through a series of actions/programmes/initiatives organized and administered under a national housing strategy. Particularly important elements of the housing strategy should be:*

- *A strategy to involve governmental structures, non-governmental organizations and the private sector in a comprehensive solution to housing problems;*
- *A post-privatization strategy dealing with maintenance and renewal of multi-family housing;*
- *An enabling policy increasing the supply of new housing in the largest cities to counteract housing shortages and to ensure adequate tenure choices;*
- *A more efficient and transparent housing subsidy system that targets the needy and abolishes*

**Box 1: Housing policy recommendations**

*the general 'waiting lists'.*

1.3 *The implementation of a national housing strategy could be assisted through the development of municipal housing policies/programmes. At the local level these policy frameworks should define local priorities and approaches and encourage the diversified supply of housing suited to local housing needs (see box 2).*

1.4 *At the operational level, the national housing strategy should focus on the design and implementation of appropriate financial and legal instruments to put policies into practice (see specific recommendations in boxes 3 and 4). The process of institutional capacity building is instrumental for the success of these reform efforts and needs to be supported through a series of initiatives at the national, regional and municipal level (see recommendations on institutional structures in box 5).*

**2. Existing housing stock and new housing construction**

By the end of 1998 Lithuania's housing stock consisted of 1,306,061 housing units, with an average of 353 units per 1000 inhabitants. Today several indices suggest that urban areas are still experiencing serious housing shortages. This shortage was quantified in 1992 in the 'Bustas' programme at 136,000 dwellings. An evaluation of housing standards in rural and urban areas indicates significant differences. While rural housing mainly requires a massive improvement in public technical infrastructure, urban housing is more in need of quantitative and spatial improvements. Data on the age structure of the housing stock show that nearly three quarters of dwellings in Lithuania were built between 1961 and 1996. Some 80 per cent of these dwellings are situated in high-rise prefabricated buildings with common characteristics, such as: low energy efficiency, neglected maintenance and repair work, and relatively poor technical quality of buildings and technical infrastructure. *The future improvement of housing conditions depends to a great extent on the maintenance and modernization of the existing housing stock.* At the moment there is no systematic and comprehensive analysis of its physical and technical condition and the assessment of investment needed to deal with the maintenance backlog.

*Rapid privatization in the 1990s changed the tenure structure dramatically.* Today Lithuania's owner-occupied sector has a share of 96 per cent. A very small public rental housing sector provides limited opportunities for responding to social housing needs. The operation of the housing market has resulted in a rapid differentiation in house prices on a regional and local basis. Data indicate that the limited housing supply nearly tripled prices in central Vilnius locations between 1993 and 1999, while in the suburbs this increase was only twofold. Prices in Kaunas grew approximately two and a half times, while in Klaipeda due to rapid economic growth prices quadrupled. *New housing construction has declined steadily in the 1990s.* The number of new dwellings per 1,000 inhabitants declined to 1.5 in 1997, which is less than 14 per cent of the housing output during the 1980s. On the other hand, the average floor area of new housing has increased by almost 70 per cent, largely due to a surge in individual housing construction. Individual developers and associations/ cooperatives account for 90 per cent of the newly built housing in the late 1990s.

Lithuania has a relatively high volume of homes per 1,000 residents compared to most other countries in transition. Nevertheless, economic growth and growth in household spending power, the need to replace outworn stock and to address current housing market disequilibria (e.g. family overcrowding in small units), all point to some urgency in increasing new housing output. The current housing development process does not appear to work smoothly, other than in the high-end of the market. It is urgent to develop municipal housing policies that will enable access to housing for lower and middle-income households. New forms of support and a broader variety of tenure choices are necessary for a more efficient housing system.

**Box 2: Existing housing stock and new construction – recommendations**

## Policies on maintenance and renewal

2.1 *One of the highest priorities should be to prevent the further decay and inefficient use of the existing housing stock. Municipalities should take greater responsibility for the organization of maintenance and the renewal of multi-family housing. A comprehensive approach to the problems requires the following major initiatives:*

*The preparation of municipal strategies for housing renewal and improvement;*

*Action plans and a time frame for the modernization of housing and infrastructure;*

*Pilot programmes for priority areas;*

*The development of public/private partnerships to implement housing renewal and improvement strategies;*

*The establishment of earmarked funds for the maintenance of the building stock, particularly in the historical parts of the towns;*

*The preparation of simple-to-apply, practical guidelines on energy efficiency;*

*Methods to increase public awareness and participation in renewal activities.*

## Policies on new construction

2.2 *Municipal land policies need to ensure a steady supply of land for housing in general and for social housing in particular.*

2.3 *The process of land disposal for commercial and municipal housing projects through tenders should be simplified by clarifying the role of the State, county and municipality in decision-making and by making the whole procedure more transparent.*

2.4 *The framework of municipal housing policies should include strategic plans for upgrading and expanding the infrastructure. They should be supported by capital investment programmes and extrabudgetary sources (see box 3 for further details).*

2.5 *Measures for the completion of housing started in 1991/1992 should be taken; one possibility would be to grant construction subsidies possibly subdivide and convert these properties into social rented housing.*

**3. Financial framework**

The Lithuanian Government has taken some significant steps to create a financial framework that will enable its housing sector to operate on market principles. The final goal proclaimed by the Government was to increase the affordability of housing for every household. Financial reforms focused on the transition from a highly centralized and subsidized system of housing finance to a system driven by private initiative and the real cost of providing housing services to consumers. However, there is still no clearly developed systematic policy on the reform of financial mechanisms. Separate, but not complementary, measures introduced by the Government have failed to achieve the expected result.

The Government initiated the transformation of the housing financial framework through the radical restructuring of housing investments. Public investments in housing was cut significantly. Instead, private households have become the main investors using their personal savings. Adequate conditions have not been developed to increase the number of institutional investors and to re-channel their capital into housing. There are no specific financial instruments to encourage private (both individual and institutional) savings in housing. *Attempts to improve the overall investment climate in the housing sector include efforts to develop a system of housing construction finance together with the introduction of mortgage systems.*

A characteristic of housing construction activity during the transition has been the cash-driven construction process with a small share of credit capital. It is possible that good entrepreneurs leave the housing sector for more promising lines of business offering a faster return on capital. It might well be the case that inefficiencies in the construction process due to the lack of development finance, small-scale operations and inadequate equipment also add a premium to the already - high construction costs. Ultimately, these constraints affect the quantity and the quality of new housing supply and make it even less affordable. Other significant constraints in the provision of new housing relate to the lack of funds for technical infrastructure. No significant financial measures have been introduced to enable municipalities to carry out infrastructure development. Strategic plans for the reform of municipal housing finance are non-existent. The dependence of municipalities on central government transfers does not allow them to fulfil their functions in the housing sector.

The mortgage market still needs to be developed, although the initial infrastructure is in place. The Government is directly involved in retail mortgage activity: using proceeds from State and self-government funds for construction, it offers highly subsidized mortgage products. *Commercial mortgage lending is emerging but is very limited mortgage.* Recent Government efforts have aimed at encouraging private mortgage lending through the government-guaranteed mortgage insurance system and proposals for secondary mortgage market development. The final structure and rules for operation and the impact on the budget are still unclear. It has been suggested that these arrangements might replace the existing governmentally subsidized mortgage system.

A system of direct State support in the housing sector was developed at the start of the transition to compensate for the elimination of subsidies and to make housing more affordable to certain groups of households. *It has not been changed since the early 1990s and remains poorly targeted and ineffective.* Despite the legal provisions related to housing subsidies, it is generally recognized that financial support is inadequate to solve the problem of the 100,000 households on the municipal waiting lists. The whole procedure for applying for State support is long and cumbersome. About 50 per cent of the families queue for 6-10 years. In 1997 only about 2,000 out of 104,300 households reportedly qualified. Currently, subsidies are distributed universally and household income is not taken into account. The system of 'soft credits' does not allow subsequent adjustment to the loan. There is no mechanism to reduce State support income level increases, which might be the case for some young families. Recent Government statements indicate the intention to differentiate State subsidies taking into account household's incomes and property.

Within the new market reality, access to housing is particularly problematic for new households and tenure choice is very limited. Only few households are able to rent or purchase new housing at market prices. House-price-to-income ratio in Vilnius was 8.2 in 1998, indicating serious market distortions. *Affordability is the most significant constraint for the efficient operation of the housing market.* Overall the lack of a systematic approach to the reform of the financial framework is a major barrier to further housing sector development. It is important to emphasize that the financial framework must promote the economic and efficient use of physical and financial resources, equity between households and between housing sectors/tenures and transparency of cash flow through the housing system. Specifically, reforms of the Lithuanian housing finance system should seek: (i) to reduce the direct role of the State, (ii) to provide sustainable, market-based finance, (iii) to integrate the housing finance system into national and international capital markets, and (iv) to channel more household savings into housing investment, while also attracting extrabudgetary resources.

**Box 3. Financial framework – recommendations**

Housing finance

3.1 *Commercial lending should become the prevailing form of fund mobilization for construction. Possible directions for improvement include, but are not limited to:*

- *Increasing the supply of construction loans through the improvement of the existing infrastructure for construction lending, including the development of a country-wide real estate market information system, and an independent system of licensed appraisers;*
- *Increasing effective demand through training programmes for inexperienced borrowers (commercial developers, municipal enterprises, households) and education, including proper construction project business plan development, market analysis and the evaluation of possible*

**Box 3. Financial framework – recommendations**

*sources of loan repayment.*

3.2 *Special attention should be paid to new fund raising instruments. The appropriateness of developing housing-related securities such as housing certificates and governmentally supported saving programmes should be considered.*

3.3 *The Government should use the limited budget investments to attract institutional investors in housing, such as private insurance companies, pension funds, investment companies and credit unions. To achieve that goal it is necessary to introduce a variety of investment instruments and to create additional tax incentives.*

3.4 *The Government should focus on expanding the volume of commercial mortgage lending and the variety of mortgage instruments. The following mortgage market refinements should be considered:*

- *The development of banking standards related to mortgage lending necessary for the secondary market development;*
- *The development of title insurance;*
- *A review of double registration (land and mortgage systems) once fully operational;*
- *The development of fuller information systems on real estate markets, valuations and individuals' credit histories;*
- *The development of a private commercial mortgage insurance market.*

3.5 *Recently introduced State mortgage insurance arrangements need to be kept under close and regular review and should be supplemented by a significant or complete reduction in the direct subsidizing of mortgage interest rates.*

3.6 *To increase the affordability of mortgage products, the possibility of exploiting «cash-poor, equity-rich» circumstances should be explored. Existing equity (such as old flats) can be used to underwrite the credit risk, as well as to introduce new types of mortgage products such as “bridge loans” for the reconstruction of existing housing.*

#### State housing support

3.7 *The Government should review the system of housing support programmes including not only direct support for households acquiring housing, but also direct and indirect (including tax benefits) utility and rental subsidies. The expenditures (direct and indirect) should be explicitly defined in the budget.*

3.8 *The general approach should be to completely stop subsidizing producers of housing services and to turn to the direct support of households, reducing significantly the number of households eligible for State support. Housing subsidies should be income-tested, based on the monitoring of household income from all sources including equity (see **box 4** for specific recommendations).*

#### Land and infrastructure provision: financial issues

3.9 *The introduction of a differentiated land property tax based on the market value of land should be considered. The objective should be to facilitate the recycling of land in urban areas with high development pressure.*

3.10 *The opportunities for a discrete use of market land value as a supply-side subsidy should be taken into consideration. The disposal of urban land plots at less-than-best-price as a condition for providing some affordable housing on- or off-site can be a mechanism for delivering non-profit or social housing or commercial housing for future sale with proceeds going to the State or municipality.*

**Box 3. Financial framework – recommendations**

3.11 *Financial arrangements related to the provision of infrastructure need to be reviewed in order to overcome the shortage of funds for new development and improvement. Options to mobilize extrabudgetary sources include:*

- *A review of tariffs for urban services to reflect real production costs and to ensure cost recovery;*
- *Raising funds for infrastructure development projects through municipal bonds;*
- *Introducing development charges/fees that account for a share of infrastructure development cost.*

**4. Legal framework**

*Lithuania has made considerable progress towards the establishment of a legal framework for a market-based housing sector.* Efforts to enable the efficient operation of the market, as well as to encourage private investment in housing, are reflected in the newly adopted laws and regulations. Early reforms have centred on legislation enabling the operation of real estate markets, such as privatization and restitution of housing, lease and ownership of land. The creation of market mechanisms has led to a new definition and protection of property rights in housing, facilities for transferring property rights, the registration of property title and mortgages, the establishment of financing mechanisms, access to reliable information, professional services, etc.

Despite these changes, *the legal framework remains rather vague on the regulation of rights and responsibilities in privatized multi-family buildings, particularly as far as the mechanisms and instruments for financing and organization of repair and maintenance are concerned.* The Law on Homeowners' Associations was an important step towards clarifying and developing property rights, but failed to enforce a workable system in most of the privatized buildings. New owners are unwilling to join homeowners' associations and are unable to bear the full costs of maintenance and capital improvements. Problems are associated with the lack of a legal entity to deal with management and day-to-day operations, with unresolved questions related to ownership of common areas and land, and with the mixed public/private ownership of housing units. The municipal maintenance companies undertake repairs and manage the privatized buildings. As long as the municipal maintenance companies exist in their present form, it will be difficult for other actors to enter the house maintenance and management business. Once privatized, some of the municipal maintenance companies might continue to provide services on a cost-recovery basis. Overall the lack of a clear legal framework for multi-family housing ownership will undoubtedly lead to a further degradation in the quality of the stock. The law needs to be amended to ensure that former tenants assume full responsibility for costs related to their residential property.

Despite changes in financing arrangements for maintenance and renovation (e.g. adjustment of tariffs for services), measures were insufficient to generate adequate revenue. Municipal enterprises play a significant role in the organization and pricing of these activities, and bank lending in this area is insignificant. The costs of energy and utilities seem to cause affordability problems not only to low-, but also to medium-income groups. It is estimated that 30-40 per cent of the households in Vilnius would have difficulties in sustaining their homeownership status, if adequate maintenance was carried out. Meanwhile in the public rental sector, rents account for 1.5 per cent of the average household income. Maintenance fees charged to tenants amount to less than 25 per cent of the actual cost. These low fees contribute to the lack of turnover and investment in public housing. Meanwhile anecdotal evidence suggests that tenants in the private sector spend more than 50 per cent of their income on housing, particularly in larger cities with a significant, by Lithuanian standards, private rental stock. This 'uncharted territory' requires attention and more efficient legislation. *A systematic financial policy in the area of management, maintenance and renovation of private and public housing is long overdue. It might be advisable to introduce a tenure-neutral system of housing allowances that will increase the availability of rental housing and make the sector more transparent.* Practice in other central and east European countries indicates that housing allowances enable the regulation of the sector and eliminate massive tax evasion by private landlords. In the public sector, housing allowances will allow increases in rent revenues up to a certain fraction of the replacement costs. This will enable a more efficient operation and maintenance of the stock.

*New legislation on leasehold arrangements is beneficial for the supply of urban land for new housing development.* These rights, protected by the Constitution, offer a viable alternative to full ownership for public and private investors. They establish clear stipulations on land use and act as an effective zoning instrument. In addition, leasehold provisions generate stable revenue for the State through ground rates related to land values. Finally, leasehold allows developers to direct funds to building production without freezing their scarce capital in land costs. Other measures that might increase the supply of land for housing development relate to municipal land-use plans. An important requirement of the Law on Territorial Planning must be that local governments evaluate the land and housing market situation and formulate their strategies for these areas before the drafting and approval of a master plan. This should ensure that land-use plans become more realistic and not purely normative, as was the practice in the former system. Currently, the lack of comprehensive and reliable information on vacant building lots, unclear ownership status, precise zoning and building requirements are frequently cited problems. Real estate firms provide only partial information on land and house prices, and no institution offers a full database on housing market activity. It should be noted that the development of efficient urban land markets served by planners and real estate professionals is a way to eliminate distortions and inefficiencies in the existing land-use patterns and to overcome shortages of developable land for new housing.

Land taxes are of critical importance, because many of the users who were granted property rights during Soviet times and/or through the Restitution Act were quite often not the best users. Land taxes need to be based on market values. At the moment properties in very attractive locations are reportedly under-taxed and properties in less attractive locations are over-taxed. This system creates distortions and exacerbates misallocation in residential land-use patterns. Furthermore, the existing income tax system does not encourage investment in the purchase or renovation of housing. *Tax incentives might generate a significant pool of private resources for:*

- The purchase or construction of owner-occupied dwellings;
- Building alteration or extension for residential purposes;
- The renovation or modernization of a residential building/dwelling.

Examples of tax deductions include: interest on mortgages up to a certain amount, the allowable amount spent on energy improvement, renovation, capital repair, etc. amortized over a certain period of time. These deductions could introduce more transparency in the renovation/construction business, and encourage taxpayers to invest in new construction and renovation. As the economy stabilizes and interest rates decrease, such investment will gain momentum. The Lithuanian Government might wish to prioritize and phase out some tax deductions (e.g. on mortgage interest for housing purchase), while maintaining others in an effort to attract capital to renovation of multi-family housing and/or private rental housing.

Value-added tax on housing development and improvement is a significant burden, if the funds are not from the State budget. Legislation needs to level the playing field and introduce similar incentives to private investors, homeowners and homeowners' associations. The introduction of a zero VAT rate on housing construction and renovation would also contribute to the expansion of the housing stock and in turn decrease the price of dwellings.

#### **Box 4. Legal framework – recommendations**

##### Regulations on owner-occupied housing

4.1 *The Law on Homeowners' Associations should be reviewed. It needs to be enacted as a framework for the efficient management of owner-occupied multi-family buildings. Particular issues to be addressed are:*

- *The establishment of homeowners' associations needs to be compulsory where 50 per cent or more of the flats have been privatized;*
- *The ownership of multi-family buildings and the land occupied by the building (leasehold or freehold) should be legally regulated as a necessary prerequisite for mortgage lending and the use of land as a collateral;*
- *Owners' maintenance responsibilities, liabilities and rights to carry out modification in their unit should be explicitly defined;*
- *Sanctions against owners not fulfilling their legal and/or contractual obligations, including*

**Box 4. Legal framework – recommendations**

*court procedures, should be specified;*

- *The necessary mechanisms and instruments to organize repair, maintenance and to implement energy-efficiency measures need to be clarified;*
- *Special provisions need to be included for multi-family units without homeowners' associations.*

4.2 *Existing contracts between owners of privatized flats and the municipality need to be reviewed along the following lines:*

- *The management and maintenance functions need to be clearly separated;*
- *The municipality might use its legal power to appoint a manager, but maintenance and repair services can be contracted out;*
- *Charges for such services should be regulated by the municipal board, but paid for by the owners;*
- *Municipal management obligations should be phased out with the establishment of a homeowners' association as a legal entity;*
- *Subsidies for energy improvement, capital repair, the expansion and refurbishment of residential premises need be conditional upon the establishment of homeowners' associations;*
- *In the case of ongoing privatization, sale should be conditional upon acceptance of legally enforceable, realistic obligations for the future repair and upkeep of the housing unit, including proportional responsibility for the common space.*

4.3 *Legislation on mortgages for owner-occupied housing needs to incorporate special regulations for foreclosures/ bankruptcy to protect the security of lenders.*

**Regulations on rental housing**

4.4 *The Civil Code regulating private rental housing should be amended to include the following provisions:*

- *Rental contracts, landlord/tenant agreements, need to be mandatory;*
- *Excessive tenant protection should be urgently reviewed with a view to striking a balance between the rights of tenants and the right of owners;*
- *Tenants in clear breach of general legal requirements, e.g. payment of rent, misuse of the property or vandalism, should be liable in accordance with the tenancy agreement;*
- *Tenants need to be protected against unjustified rent increases, harassment by the landlord and violation of their occupancy rights.*

4.5 *Existing legislation regulating municipal rents needs to be revised along the following lines:*

- *Rents in the public sector need to be differentiated according to location and quality of housing;*
- *Rent levels in municipal housing should at least cover operating costs -- management, maintenance and insurance costs.*

4.6 *The Government needs to consider the development of new legislation that will introduce means- tested housing allowances both in the private and in the public rental sector.*

**Tax regulations**

4.7 *A residential property tax system needs to be introduced. Taxes need to be based on market value to eliminate tax inequities.*

4.8 *The laws on taxation should be reviewed to introduce incentives making private investment in the housing sector financially attractive. Options include:*

- *Tax-deductible interest on mortgages up to a certain amount;*

**Box 4. Legal framework – recommendations**

- *Tax-deductible amounts spent on energy improvement, renovation, and capital repair amortized over a certain period of time;*
- *Income tax benefits for first-time buyers.*

4.9 *The existing law on value-added tax needs to be amended to eliminate tax privileges for private investors using 'soft credits' or State grants for housing construction and renovation. Alternatively, the Government may wish to consider tax exemption for housing construction and renovation that is universally applicable for private and public investors.*

4.10 *The Government might consider granting homeowners' associations in multi-family housing the status of non-profit entities for tax purposes. This might encourage the formation and the operation of a critical element in the institutional structure of Lithuanian housing.*

## 5. Institutional framework

Establishing adequate institutional structures in the housing sector is particularly important. It requires a clear definition of the roles and responsibilities of the major participants, if progress is to continue at a satisfactory rate. Efficient and effective institutional structures are not an expression of bureaucratic traditions. They are, on the contrary, an absolute necessity to address the major social and economic problems and opportunities in the housing sector.

*Political responsibility for housing* should be more clearly visible in Parliament. A clear concentration on major housing policy issues within one parliamentary committee would reflect appropriate political priority, and would increase political efficiency on housing matters. Similarly, *ministerial responsibility* for housing should be strengthened. In particular, the limited institutional capacity of the Housing Policy Division within the Ministry of the Environment is a bottleneck in the institutional transformation of Lithuanian housing. *The new regional administration* in Lithuania should be given a stronger political mandate to play a key role in the coordination of housing and other municipal activities within each region. The present regional administration needs to acquire a clear mandate for coordination and advice on municipal housing policies.

*The municipal level* lacks political and administrative structures with clear responsibility for housing issues. Apart from Vilnius, Lithuania's municipalities have not implemented the systematic structural changes needed for the efficient functioning of a market-oriented housing sector. Vilnius has established political and administrative structures within the municipality and has developed a practical, result-oriented municipal housing policy. This example could be spread to other municipalities. The Healthy City of Kaunas Programme and housing renewal schemes in Telsiai municipality are other *examples of good practice*.

*The private sector* is an integral part of the Lithuanian housing system. The construction and building materials industry have been completely privatized. A variety of organizations and institutions have emerged in the 1990s, representing the interests of producers and consumers of housing. A number of real-estate agencies have established a solid presence in buoyant urban markets. Financial institutions managed to survive the banking crisis and are positioned to assist the operation of the market. Despite these positive trends, there is an institutional vacuum related to the regulation of the housing system. The transformation of national legal and financial frameworks has been somewhat slow and less supportive of institutional changes. Residual structures, a legacy of the Soviet housing system, continue to exist (such as municipal maintenance companies). In some cases State companies, recast as private entities, do not compete effectively in the housing market. Furthermore, the organization of *private owners in multi-flat housing* is considered a major challenge to the further development of Lithuanian housing. Institutionalizing homeowners' associations requires urgent national and municipal actions.

**Box 5. Institutional framework – recommendations**

***National institutions***

5.1 *Overall political responsibility for housing should be placed clearly within one of the existing parliamentary committees.*

5.2 *The Ministry of the Environment should be given a clear mandate for housing issues, defining its responsibility for overall national housing policies and strategies with a particular focus on issues related to infrastructure provision, rent policies and subsidies.*

5.3 *The institutional capacity for housing issues within the Ministry of the Environment should be strengthened.*

5.4 *The Ministry of the Environment should, as part of the responsibility for a national housing policy, be required to evaluate the existing legal regulations and eliminate gaps and inconsistencies with respect to rights and responsibilities within the housing sector.*

***Regional institutions***

5.5 *County administrations should be given clear responsibility for coordinating municipal policies, programmes and projects in the housing sector. On these issues there should be close cooperation between county administrations and the Ministry of the Environment.*

5.6 *Cooperation between the county governor and municipal authorities on housing and development issues can be strengthened through the establishment of a council cooperating on a voluntary basis.*

***Municipal institutions***

5.7 *To concentrate political responsibility and authority in the housing sector, cities and larger municipalities should establish a housing committee or sub-committee within the municipal council. The committee should in particular advise the council and prepare programmes for investment in land and infrastructure for new housing construction and priority programmes for the renovation of the existing housing stock.*

5.8 *To concentrate administrative authority and responsibility for housing, a department or division should be established within the municipal administrative structure with the following main responsibilities:*

- *To coordinate administrative tasks in the housing sector;*
- *To collect and present comprehensive information on housing problems within the municipality;*
- *To monitor, analyse and report on the performance of municipally owned companies operating in the housing sector.*

5.9 *The present system of municipally owned housing maintenance enterprises should be restructured as quickly as possible and prices for services deregulated. During a transition period an operational service should be available with fees determined by the municipal council. Parallel to the liberalization of prices, an independent regulatory institution should be established to provide independent capital needs assessment on maintenance, repair and improvement services for homeowners' associations to avoid excessive price speculation.*

***Homeowners' associations***

5.10 *The Government should, in cooperation with municipalities, institute a programme of information and operational support for homeowners' associations. This could take the form of regional information centres operated by national or regional umbrella organizations for homeowners' associations, and the dissemination of handbooks on the creation and operation of*

**Box 5. Institutional framework – recommendations**

*homeowners' associations. Efforts should focus on:*

- *Strengthening the management capabilities of homeowners' associations;*
- *The appointment of administrators for privatized multi-family buildings without homeowners' associations.*

*5.11 Energy-efficiency programmes in owner-occupied housing, which are managed by the Housing Credit Foundation, need to be further supported to broaden their outreach to other homeowners' associations across Lithuania.*

**6. Priority of recommendations**

The Lithuanian Government needs to adopt a wider range of strategic approaches to ensuring successful housing reform. It is important to undertake systematic action leading to simultaneous changes in the financial, legal and institutional frameworks for housing. It should be clear that market mechanisms are not the right solution for every housing problem, but the market needs to operate efficiently and effectively to respond to household needs and preferences. Comprehensive reforms, including more efficient forms of State regulation - legal, tax and financial incentives in particular, are required to balance existing market imperfections and to enable competition in the market place.

Learning to use new approaches to achieving housing policy goals will be a gradual process. It needs to build on the strengths of the existing housing system, while overcoming the limitations of current financial, regulatory and institutional frameworks. Change needs to be systematically pursued to ensure better performance, flexibility and accountability of different agents and institutions. While the challenges facing Lithuania are difficult to resolve at any level of government, innovative partnerships and coalitions with local communities, individuals and businesses offer the opportunity of achieving long-term solutions to housing problems. By building upon collaborative approaches, leadership and innovation, the Government needs to ensure that policy intervention is applied to the right problem, in the right way, at the right time. The housing profile has outlined a number of strategies, approaches and tools that, if carefully tailored to different challenges, could result in a more efficient operation of the housing system, fewer subsidies and greater opportunities for the economically disadvantaged. Within that context, the sequence and the scope of housing reform efforts are critical. According to the international team, the following recommendations need to receive priority:

**Box 6. Priorities**

1. *Develop and implement a national housing policy through a series of actions/programmes/initiatives organized and administered under a national housing strategy (1.2).*
2. *Strengthen the institutional capacity and the mandate of the Ministry of the Environment, defining its responsibility for overall national housing policy and strategy (5.2 and 5.3).*
3. *Prevent the further decay and inefficient use of the existing housing stock, particularly with respect to maintenance and renewal of multi-family housing (2.1).*
4. *Improve the regulatory framework for owner-occupied multi-family buildings (4.1).*
5. *Expand the volume of commercial mortgage lending, creating a variety of mortgage instruments (3.4).*
6. *Introduce tax incentives to make private investment in the housing sector financially attractive (4.8).*
7. *Overcome the shortage of funds for infrastructure development and improvement by mobilizing extrabudgetary sources (3.11).*

**Box 6. Priorities**

8. *Develop municipal land policies to ensure a steady supply of land for housing in general and for social housing in particular (2.2).*

9. *Deregulate municipal rents and introduce means-tested housing allowances in both the private and public rental sector (4.5 and 4.6).*

**Lithuania**

**Country profile graph, 1999**

PROFILE FACTOR	PROFILE STATUS				
	Weak				Strong
1. POLITICAL PRIORITY (aggregate value): 1.1 At parliamentary level 1.2 At governmental level 1.3 At local authority level		X X X	X		
2. INSTITUTIONAL FRAMEWORK (aggregate value): 2.1 Parliament 2.2 Central Government 2.3 Regional 2.4 Local authority 2.5 Private sector 2.6 Tenants' and owners' associations		X X X X X	X X		
3. LEGAL FRAMEWORK (aggregate value): 3.1 Law on local authority independence 3.2 Law on real estate 3.3 Law on rental housing 3.4 Law on housing finance and credits 3.5 Law on condominium ownership 3.6 Law on housing subsidies		X X X X	X X X		
4. ECONOMIC FRAMEWORK (aggregate value) 4.1 Investment in housing 4.2 Potential capacities 4.3 Public-sector investment facilities 4.4 Private-sector investment instruments 4.5 Rental policy 4.6 Housing subsidy systems	X    X	X X X X	X		
5. DWELLING SUPPLY AND QUALITY (aggregate value): 5.1 Quantitative supply of dwellings 5.2 Age of dwellings 5.3 Amenities of dwellings 5.4 Repair and renovation 5.5 Energy efficiency 5.6 Land supply for new dwellings	    X	X	X X X	X X	
6. SOCIAL FACTORS (aggregate value): 6.1 Registration of social housing needs 6.2 Policies on social housing needs			X X		



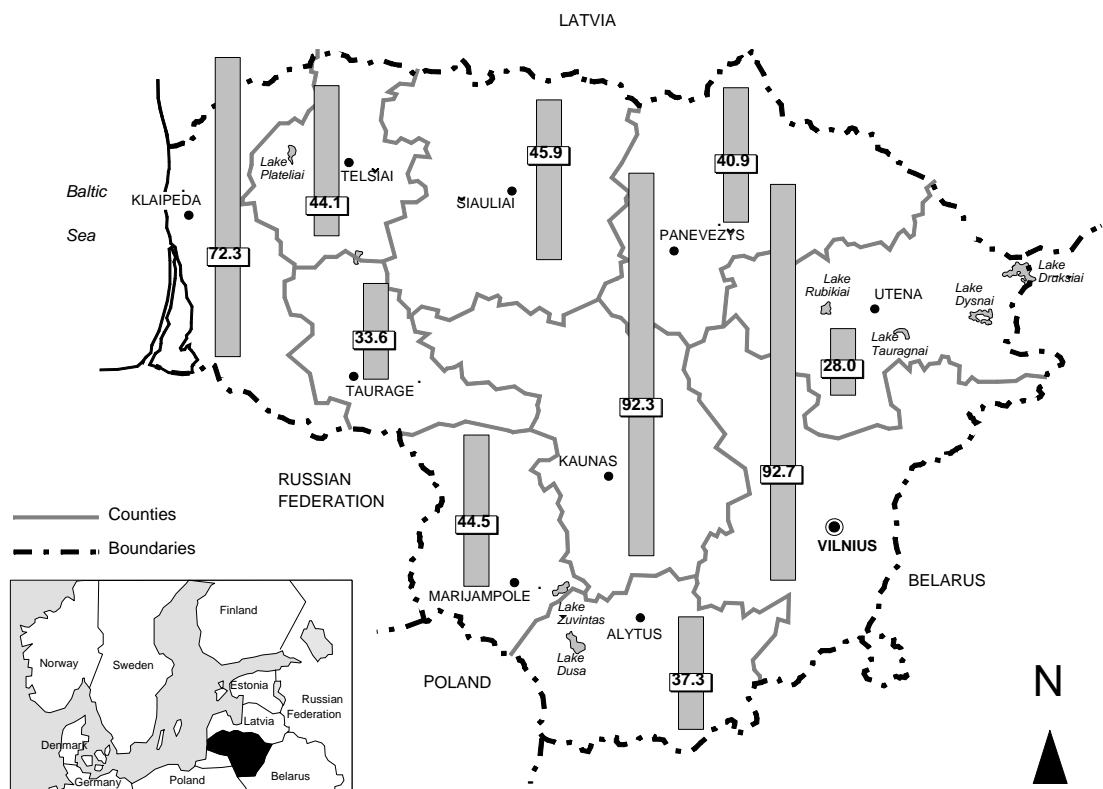
# Chapter I

## FRAMEWORK FOR THE HOUSING SECTOR

This chapter introduces the environment in which Lithuania's housing reform takes place. Apart from general information about the country, it briefly describes the legal and administrative arrangements, and social and economic developments that affect the housing sector. The first section provides an overview of macroeconomic policies, privatization and

economic performance. The second explores urban and rural developments with an emphasis on land restitution and administration, transport development, settlements network, and housing conditions. The third part focuses on housing reforms through national and municipal housing policy formulation. Finally, environmental and health issues are tackled.<sup>1</sup>

**Figure I. Population distribution and density by county, January 1999**



**Source:** Department of Statistics, *Districts of Lithuania, Economic and Social Development*, (Vilnius, 1999).

**Note:** The boundaries shown on these maps do not imply official endorsement or acceptance by the United Nations.

<sup>1</sup> See also United Nations Economic Commission for Europe, *Environmental Performance Reviews: Lithuania* (United Nations publication, Sales No. E. 99.II.E.7), Introduction and chap. 10.

### *Government system*

Lithuania has a three-level administrative system: the Government, an administration of counties (*apskritis*), and municipalities (*savivaldybes*). In 1995, the country re-established ten counties headed by Governors appointed by the Government. Each municipality has a council, elected for a period of two years by direct suffrage. The administrative territorial division of Lithuania includes 56 municipalities (44 districts and 12 cities). The counties are responsible for the implementation of State policies in: social welfare, health care, cultural heritage, environmental protection, spatial planning and land-use reform. The municipalities are responsible for the provision of basic education, primary medical treatment, social care, land-use planning, housing construction and maintenance, municipal services, and public security. In-depth analysis of institutional arrangements affecting the housing sector is provided in **chapter V**.

Local governments draft and approve their own budgets, which include the local sources of revenue (such as notary, real estate and some personal income tax). The councils have the right, within established limits and according to the procedure provided by the law, to establish local dues and to levy taxes and duties. The national budget, representing 23 per cent of GDP in 1998, consists of the State budget and municipal budgets. Parliament adopts the State budget (some 17 per cent of GDP in 1997) and municipal councils adopt municipal budgets (7 per cent of GDP in 1997) one month later. Municipal budgets receive State transfers, though ongoing tax reform aims at increasing independent sources of income for municipalities. The State budget includes allocations for State-supported programmes such as 'Bustas' (Dwelling), while municipal budgets have provisions related to municipal housing. For additional information on State and municipal support for housing, see **chapter III**.

Government reforms in 1998 reduced the number of ministries from 18 to 14, which led to the merger of the Ministry of Construction and Urban Development, responsible for housing policy, with the Ministry of Environment.

### **A. Social and economic transformation**

#### *Demographic trends*

Some 40 per cent of the population lives in the five largest municipalities (Vilnius, Kaunas, Klaipeda, Šiauliai, and Panevezys). The average population density grew from 39.5 inhabitants per km<sup>2</sup> in 1950 to 56.8 in 1998<sup>2</sup>, while the country's population increased by 48 per cent from 2.5 million to 3.7 million over the same period. There are three distinct clusters of counties with different population densities in **figure I**. At the lower end, Utena and Taurage counties have population density of 30 inhabitants per km<sup>2</sup>. The highest densities tend to be in Vilnius, Kaunas and Klaipeda counties with values 3 times higher. The other five counties form a cluster with an average population density of 45 inhabitants per km<sup>2</sup>.

Rapid urbanization has taken place in Lithuania in the past 30 years. The urban population has grown by a factor of almost 3.5 since 1950, while the rural population has decreased by 36 per cent (**table 1**). Migration to urban centres was dominant before 1990. Since 1993, despite the overall population decline, rural areas have gained new residents, which reversed the long-standing migration trends. Emigration from Lithuania has also increased, but less than expected given the domestic economic difficulties.

<sup>2</sup> This compares with 13.5 in Norway, 19.7 in Sweden, 15.2 in Finland, 8.6 in the Russian Federation, 32.2 in Estonia, 38.2 in Latvia, 49.2 in Belarus, 123.6 in Poland, 229.4 in Germany, and 122.6 in Denmark. (1996/1997 data taken from *Trends in Europe and North America, Statistical Yearbook of the Economic Commission for Europe 1998/1999, Geneva, 1999, p.66*).

**Table 1. Migration, 1980-1998**

	<i>thousand inhabitants</i>										
	1980	1985	1990	1991	1992	1993	1994	1995	1996	1997	1998
<b>Net urban migration</b>	<b>29.6</b>	<b>24.6</b>	<b>14.4</b>	<b>-5.1</b>	<b>-29.2</b>	<b>-21.1</b>	<b>-8.9</b>	<b>-9.8</b>	<b>-10.0</b>	<b>-6.5</b>	<b>-1.8</b>
Immigration	116.0	113.4	87.1	63.8	47.0	39.7	43.4	48.8	47.2	47.2	39.5
Emigration	86.4	88.8	72.7	68.9	76.2	60.8	52.3	58.6	57.2	53.7	41.3
<b>Net rural migration</b>	<b>-20.7</b>	<b>-10.8</b>	<b>-2.8</b>	<b>-0.2</b>	<b>7.0</b>	<b>7.9</b>	<b>6.3</b>	<b>8.1</b>	<b>9.1</b>	<b>6.6</b>	<b>2.4</b>
Immigration	59.1	65.0	45.8	38.5	37.7	32.1	31.7	37.0	36.6	34.5	25.9
Emigration	79.8	75.8	48.6	38.7	30.7	24.2	25.4	28.9	27.5	27.9	23.5
<b>Net foreign migration</b>	<b>..</b>	<b>..</b>	<b>-8.8</b>	<b>-8.9</b>	<b>-22.2</b>	<b>-13.1</b>	<b>-2.6</b>	<b>-1.8</b>	<b>-0.9</b>	<b>0.1</b>	<b>0.6</b>
Immigration	..	..	14.7	11.8	6.6	2.9	1.7	2.0	3.0	2.5	2.7
Emigration	..	..	23.6	20.7	28.9	16.0	4.2	3.8	3.9	2.5	2.1
<b>Total migration</b>	<b>..</b>	<b>..</b>	<b>292.5</b>	<b>242.4</b>	<b>227.1</b>	<b>175.6</b>	<b>158.7</b>	<b>179.1</b>	<b>175.5</b>	<b>168.3</b>	<b>135.0</b>
<i>as % of population</i>	..	..	<i>7.89</i>	<i>6.49</i>	<i>6.06</i>	<i>4.70</i>	<i>4.26</i>	<i>4.82</i>	<i>4.73</i>	<i>4.54</i>	<i>3.65</i>
<b>Total population<sup>a/</sup></b>	<b>3,404.2</b>	<b>3,528.7</b>	<b>3,708.2</b>	<b>3,736.5</b>	<b>3,746.9</b>	<b>3,736.5</b>	<b>3,724.0</b>	<b>3,717.7</b>	<b>3,711.9</b>	<b>3,707.2</b>	<b>3,704.0</b>
<i>% change</i>	..	<i>3.66</i>	<i>5.09</i>	<i>0.76</i>	<i>0.28</i>	<i>-0.28</i>	<i>-0.33</i>	<i>-0.17</i>	<i>-0.16</i>	<i>-0.13</i>	<i>-0.09</i>
Urban population	2,074.4	2,298.4	2,526.9	2,557.5	2,568.2	2,549.0	2,533.4	2,526.4	2,518.4	2,534.5	2,525.2
<i>% change</i>	..	<i>10.80</i>	<i>9.94</i>	<i>1.21</i>	<i>0.42</i>	<i>-0.75</i>	<i>-0.61</i>	<i>-0.28</i>	<i>-0.32</i>	<i>0.64</i>	<i>-0.37</i>
Rural population	1,329.8	1,230.3	1,181.3	1,179.0	1,178.7	1,187.5	1,190.6	1,191.3	1,193.5	1,172.7	1,178.8
<i>% change</i>	..	<i>-7.48</i>	<i>-3.98</i>	<i>-0.19</i>	<i>-0.03</i>	<i>0.75</i>	<i>0.26</i>	<i>0.06</i>	<i>0.18</i>	<i>-1.74</i>	<i>0.52</i>

*Source:* Department of Statistics, *Demographic Yearbooks* (Vilnius, 1994-1999).

<sup>a/</sup> Data at the beginning of the year.

An indicator of potential demand for dwellings is the population growth rate. Currently, the country is experiencing a natural decrease in population (**tables 2 and 1**). The highest population increase was in 1970s, followed by a moderate

growth in 1980s. Since 1990, birth rates have declined, while death rates have increased. Birth rates fell particularly sharply in urban areas. Household structure has also changed.

**Table 2. Demographic trends, 1960-1998**

	<i>per thousand of</i>														
	1960	1965	1970	1975	1980	1985	1990	1991	1992	1993	1994	1995	1996	1997	1998
<b>Natural increase</b>	<b>14.7</b>	<b>10.2</b>	<b>8.8</b>	<b>6.2</b>	<b>4.7</b>	<b>5.4</b>	<b>4.6</b>	<b>4.0</b>	<b>3.2</b>	<b>0.4</b>	<b>-1.1</b>	<b>-1.1</b>	<b>-1.1</b>	<b>-0.9</b>	<b>-1.0</b>
Birth	18.1		17.7	15.7	15.2	16.5	15.3	15.0	14.3	12.7	11.4	11.1	10.5	10.2	10.0
Rural						15.6	16.3	15.9	15.8	14.1	12.7	12.2	12.1	12.0	11.8
Urban						16.9	14.8	14.6	13.6	12.1	10.8	10.5	9.8	9.4	9.1
Death	7.9		8.9	9.5	10.5	11.1	10.7	11.0	11.1	12.3	12.5	12.2	11.6	11.1	11.0
Rural	8.9		11.3	12.8	14.7	16.2	15.8	16.0	16.2	18.0	17.5	17.0	16.4	15.8	15.6
Urban	6.1		6.6	6.9	7.9	8.3	8.3	8.6	8.7	9.7	10.1	9.9	9.3	8.9	8.9

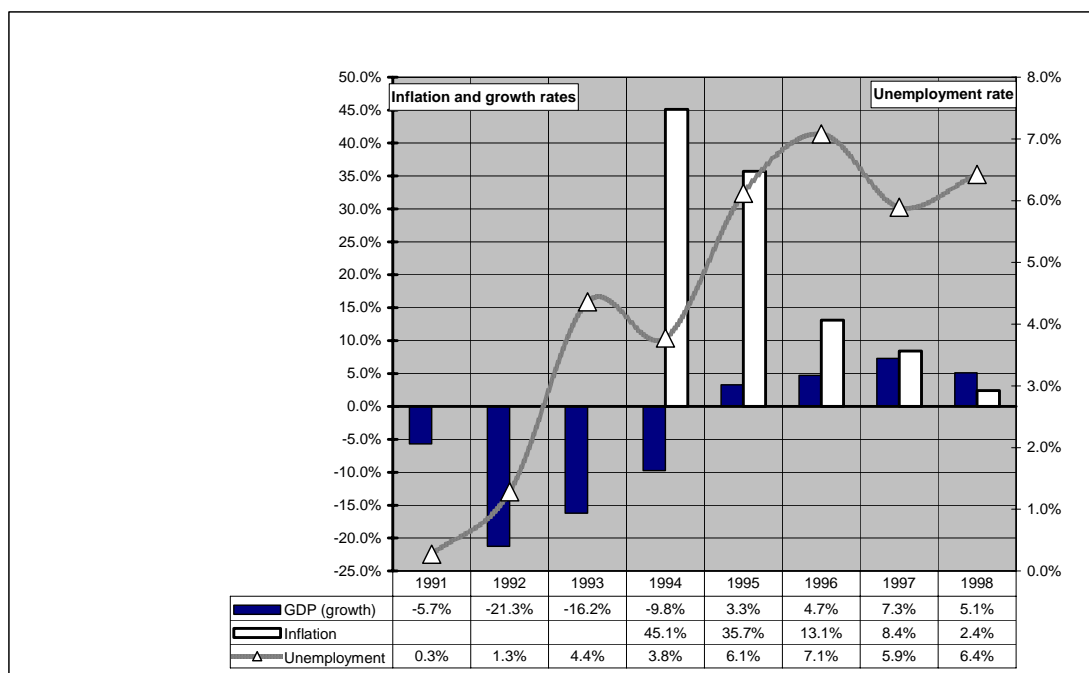
*Source:* Department of Statistics, *Statistical Yearbooks* (Vilnius, 1997-1999).

According to the 1989 population census, there were one million households in Lithuania. Households increased by 10,000 to 11,000 a year in the 1980s, while in 1992-1994 they declined by 10,000. The proportion of single-person households is growing and women account for two thirds of these households. While the divorce rate increased dramatically -- from 35.1 in 1990 to 60.5 per cent in 1997 for new marriages -- marriages decreased from 9.8 to 5.1 per thousand of population over the same period. Women outnumber men, particularly in the post-retirement age group. Experts estimated the number of households at 1.3 million in 1999.

### *Macroeconomic developments*

The Lithuanian economy measured by *gross domestic product* (GDP) is some US\$ 10 billion. In 1998, GDP increased by 5.1 per cent (**fig. II**). The Central Bank expected GDP to grow by 3 per cent in 1999. However, GDP had already shrunk by 4.8 over the first part of the year. The current recession was preceded by economic growth in the range of 3.3 - 7.3 per cent in 1995-1997 due to prudent monetary and fiscal policies.

Figure II. GDP, inflation and unemployment



*Source:* Department of Statistics, *Economic and Social Development in Lithuania* (Vilnius 1998-1999), issues 12,1,2,3,4.

Until 1991, *industry* accounted for 44.4 per cent of GDP (**table 3**), followed by agriculture (16.4 per cent) and construction (5.4 per cent). During the first years of independence, Lithuania's industry suffered the steepest decline in the Baltic region, with production down by as much as 51.6

per cent in 1992. Due to restructuring industry grew by 5.4 per cent in 1997 and by 7 per cent in 1998. Services have increased their share in GDP, reflecting typical transformations to a market-oriented, service-based economy.

**Table 3. Major sectors' share of total output, 1991-1998**

	<i>% of GDP, current prices</i>							
	1991	1992	1993	1994	1995	1996	1997	1998 a/
Industry	44.4	37.5	34.2	27.0	26.1	25.8	25.2	23.6
Agriculture	16.4	13.8	14.2	10.7	11.7	12.2	11.7	10.1
Construction	5.4	3.9	5.1	7.2	7.1	7.1	7.7	7.9
Real estate and financial services	..	..	11.5	11.7	10.5	10.5	9.6	11.0
Services	b/	33.9	44.8	35.0	43.4	44.4	45.8	47.4

*Source:* UN/ECE, *Economic Survey of Europe*, issues: 1996-1997, 1998 No.1, and 1999 No.1.

a/ Preliminary data.

b/ Includes real estate and financial services for 1991 and 1992.

The *main manufacturing sectors* in Lithuania are food-processing, light industry, machine-building, metalworking, electronics, electrical appliances, chemicals, building materials, and energy industries. Manufacturing depends on imports of raw materials. Light industry's modern technology and qualified workforce have created a comparative advantage over other sectors. The electronics and electrical appliances industries have successfully accessed the European markets. The energy sector is undergoing privatization and structural changes.<sup>3</sup> Lithuania is the largest electricity producer in the Baltic region, with 16.8 billion kWh generated in 1996 (Ministry of Economy data). The *construction industry*, mostly privatized, recovered in the mid-1990s with a 6.6 per cent growth in 1997. The construction sector contributed some 8 per cent to GDP in 1998 as indicated in **table 3**.

*Inflation* soared to triple digits in 1991-1993, as the economy felt the combined effects of price liberalization and wage increases aimed at compensating for inflation. In 1998, inflation fell for the fifth consecutive year (from 35.7 per cent in 1995 to 2.4 per cent in 1998<sup>4</sup>). June, August and September 1998 saw deflation rates of 0.5, 0.6 and 0.4 per cent in Lithuania. The current macroeconomic climate with low inflation rates was supposed to encourage investment in housing activities; however, other factors also affect the interest rates for commercial loans (see domestic financial and capital markets below). *Unemployment* reached 7.1 per cent in 1997, followed by a decline to 5.9 per cent. However, in December 1999, it stood at 10 per cent and is expected to be 8.4 per cent for the whole year. Those estimates are based on labour exchange numbers. The labour force survey estimates unemployment at 5.2 per cent above the labour exchange figure (the figure provided corresponds to the latest available survey data, i.e. second quarter of 1999 data).

### *Investment and financing*

*Foreign direct investment (FDI)* amounted to US\$ 700 million in 1996, surged to US\$ 1.04 billion in 1997 and reached a record high of US\$ 1.625 billion in 1998. Sixty-two per cent of FDI capital is of EU origin. In 1996, two important bills were passed to promote foreign investment. Firstly, the land reform bill was enacted in July 1996. It allows foreign enterprises to buy land, so removing a major obstacle to Lithuania's accession to the EU. The second bill allowed foreign banks to operate through branch offices. This facilitates foreign investment operations and meets EU requirements for banking laws.

The economy is suffering a *shortage of capital* to finance investment. Access to international financial markets has improved considerably. Lithuania has an international credit rating of BBB from Standard and Poor's (September 1998) and a sub-investment Ba1 rating from Moody's. As a member of the European Bank for Reconstruction and Development, the International Monetary Fund and the World Bank, Lithuania receives loans for currency stabilization, structural reforms in banking, agriculture, energy and social security. The country also receives grants under the European Union's Phare programmes. Domestic financial and capital markets are critical to structural reforms and to financing economic growth. To fund investment enterprises turn either to the capital market or to commercial banks for loans. Much has been done to push the interest rates on loans down. However, they are still relatively high. In 1996, interest rates dropped to 16 per cent on loans in litai and to 14.73 per cent in hard currency. In 1997-98, the rates plummeted further to 11-13 per cent. Low inflation rates are responsible for these trends. In December 1999, the average commercial interest rate stood at 11.41 per cent on hard-currency loans and 12.98 per cent in litai. Interest rates on housing loans stood at 9.92 per cent on loans in litai and 11.11 per cent in foreign currency, which does not stimulate mortgage markets. The high margin between inflation and interest rates reflects various commercial risks.

<sup>3</sup> Mazzeikiiai refinery (the only refinery in the Baltic countries) was under privatization in October 1999. Also, Butinge oil terminal and oil pipelines have been merged for privatization. The oil terminal started to operate in 1999, marking an important economic restructuring benchmark. Lithuania exports electricity to Belarus, Latvia, and the Kaliningrad region of the Russian Federation. Electricity exports to western Europe highlight EU integration efforts.

<sup>4</sup> Inflation was 6.5 per cent in Estonia and 2.8 per cent in Latvia in 1998.

Sweeping measures were taken to reform the banking sector and to liberalize financial services following the banking crisis in 1995.<sup>5</sup> In June 1996, a law introducing re-capitalization securities was enacted, a condition imposed by IMF in return for a loan to overcome the effects of the banking crisis. The confidence in banks was partially restored after the State increased mandatory bank deposit insurance from 4,000 to 25,000 litai in 1997. The capital market is functioning but volumes are not big; investment funds and private pension funds are just starting to operate. A large portion of stocks is traded directly, indicating poor stock market development and poor liquidity. Enterprises are finding it difficult to raise capital. The public still has not yet acquired a culture of following, understanding and using capital markets as a vehicle for diversified savings. The Government introduced saving bonds in 1999.

#### *Economic policies and privatization*

*Economic reform* was initiated as early as 1987 with the establishment of collective and personal enterprises, although the transition to a market economy started after independence, when the Law on the Initial Privatization of State Property was adopted in February 1991. Prices were liberalized in November that year, triggering inflationary pressures.

Lithuania introduced a national currency, the litas, and established a Currency Board in April 1994. Since then, the litas has been pegged to the United States dollar at an exchange rate of 4 to 1. Two shortcomings of the monetary policy emerged. Firstly, the country's financial dependency on international capital markets increased. Secondly, the strengthening dollar (and consequently litas) against the European currencies hit exports. Importing goods became more profitable than producing them domestically. Thus, incentives for savings and investment became weak. The fixed-rate exchange policy contributed to the slow restructuring.

One major priority in Lithuania's *fiscal policy* is to restructure the tax system, to minimize

budgetary arrears and to improve the tax administration. The Government strengthened the tax administration by establishing a Tax Police Department and re-organizing the State Tax Inspectorate. Lithuania currently has a personal income tax of 33 per cent and a corporate income tax of 29 per cent. Value-added tax (VAT) is levied at a rate of 18 per cent; excise taxes are applied to petrol, tobacco, alcohol and spirits. Trade taxes play a small role in the tax system, except those on agricultural produce. The tax system is not used to protect domestic industry or the housing sector. In 1999, the Government was struggling to balance the State budget as revenues fell short of projections. Fiscal policy was supplemented with austerity measures and phasing out various hidden subsidies. The 1994 budget earmarked 224 million litai for subsidies. Large amounts were allocated to compensate heating and gas enterprises for preferential tariffs granted to households.

The *Government's economic development strategy* aims at developing market institutions, upgrading the economy's infrastructure. It also aims to integrate Lithuania into the EU political and economic structures. It expects to trigger economic recovery by promoting exports and FDI. Attempts have been made to increase domestic demand. It was hoped that the purchasing power of the population would increase and Lithuanian consumers would buy more goods and services, which could no longer be exported. However, the unexpected recession affected private spending negatively. Unemployment surged, while social benefits were added on top of the fiscal obligations to compensate lost savings. Eventually, the new Government suspended compensation for lost savings to improve the fiscal deficit position.

As an integral part of Lithuania's economic reforms, the *privatization process* was launched in September 1991. The entire process can be divided into three major stages.<sup>6</sup>

The *first stage*, a mass privatisation through vouchers with some cash transactions, covered the period from September 1991 to July 1995. State-owned enterprises, land, agriculture companies and flats were offered in exchange for privatization vouchers (issued in dematerialized form by opening voucher accounts). Over 2.6 million voucher accounts were opened in the banks. Housing privatization accounted for 19 per cent of vouchers at this stage, while about 65 per cent were

<sup>5</sup> In 1995, when the Central Bank imposed tighter control on compliance with the Law on Commercial Banks (January 1995), several major banks collapsed and the country faced a general banking crisis. In May 1996, of the 27 banks licensed in Lithuania, 16 were under suspension or facing bankruptcy proceedings. Today, Hermis and Vilnius banks, out of 11 banks operating, have significant credit resources on hand, while others came out weaker after the crisis.

<sup>6</sup> The analysis in the section draws on information available at <http://www.vtf.lt>

exchanged for shares in State enterprises. The remaining vouchers were used for the acquisition of agricultural enterprises and land.<sup>7</sup> All agricultural land not subject to the restitution claims was offered for privatization. Country-dwellers willing to take up farming had priority in the privatization of the land. Owners of single-family housing were given the same privileges in purchasing built-up residential land in both rural and urban areas. The mass privatization carried out in 1,160 State companies, formerly known as "kolkhozes", resulted in a transfer of 97 per cent of the agricultural assets into private hands. This phase of privatization included the sale of apartments to their tenants. The privatization vouchers were accepted as payment for 80 per cent of the price. Some 95 per cent of the formerly State-owned flats had become private by 1995.

The *second stage*, a privatization through cash sales, covered the period from July 1995 to 1997. Privatization under the 1995 Privatization Law excluded voucher privatization. The methods of privatization were public subscriptions of shares (for small and medium-sized enterprises), auctions (for small enterprises), public tenders (for medium-sized and large enterprises), and leases with an option to purchase. In 1996, 47 entities worth 3.2 million litas were privatized and 272 entities worth 80.9 million litas were privatized in 1997.

The *third stage*, a tender privatization, covers the period from 1998 to date. The Governmental Resolution of 11 February 1997 earmarked for privatization large State-controlled enterprises in the transport, energy and telecommunication sectors. The Privatization Law gave the State Property Fund (SPF) the tasks of holding, using, disposing, and privatizing State-owned property.<sup>8</sup> In 1998, 344 enterprises were privatized, generating 2.3 billion litai. Among the biggest deals are Lithuanian Telecom, Hotel Lietuva and a third of

the oil industry. SPF expects privatization sales to amount to 1 billion litai in 1999.

## **B. Trends and challenges for urban and rural development**

### *Land restitution and administration*

The Government's land policy aims to:

- Accomplish the restitution of land and to implement land reform;
- Stimulate the development of a land market by upgrading the land registration system and creating a mortgage system;
- Levy a real property tax based on market values;
- Create a land information system which will serve both the State administration and the general public for the purposes of land use, physical planning and environmental monitoring;
- Revise the current institutional land administration set-up.

The restitution of ownership rights (or compensation) is at the centre of Lithuania's land reform. Some 2.5 to 3 million parcels have to be surveyed, privatized or leased. The three major types of land being privatized are:

- Agricultural and forest land in rural areas (more than 690,000 people have applied to have their ownership rights in agricultural land restored);
- Allotments of members of gardeners' associations (there are 218,500 such members, they cultivate a total of 21,100 ha); and
- Parcels with housing units and other buildings, mainly in urban areas (homeowners' associations cannot own land).

Land privatization has accelerated due to improvements in the cadastre and land registration systems. Still, the biggest challenge to real-estate registration is the legacy of separated property rights of land and buildings.

### *Environmental challenges*

Air and water quality affects residents' quality of life. Over the past five years, Lithuania has invested in waste-water treatment, but much

<sup>7</sup> About 93 per cent of investment vouchers valued at approximately 10.5 billion litai (US\$ 2.4 billion) were used in this privatization stage. The other 7 per cent (726 million litai) were deposited into private investment accounts to purchase apartments (not yet privatized), agricultural land (maximum 80 ha), land for private use, and plots in collective gardens.

<sup>8</sup> SPF coordinates the privatization process. It organizes privatization of the largest State-controlled enterprises in industry and infrastructure. Privatization of these enterprises is carried out through competitive international tenders prepared and executed by international consultants. Specially appointed public tender commissions carry out international tenders for the privatization of strategic energy, transport and telecommunications enterprises. The commissions determine criteria to prepare privatization programmes reflecting governmental policy and the experience of other countries.

remains to be done to improve the water supply, as water quality still raises some health concerns.

Air pollution in urban areas also tends to be high, due to traffic and weak environmental control over industrial centres. The most important and increasing source of air pollution is transport (responsible for about 70 per cent of emissions). The increase in vehicle use and transport in general has a direct impact on the noise levels in homes and public buildings in urban areas (see below). The energy industry, oil processing, chemical production and the manufacturing of construction materials are the biggest industrial air polluters. The population living near such sources of pollution has been found to suffer diseases such as lung cancer, a high incidence of acute and chronic bronchitis, and pneumonia.

During the winter, the inhabitants of multi-flat houses complain about insufficient heating. Because of bad thermal insulation the temperature is often lower than 15° C. More than 30 per cent of the dwellings are partly damaged by microscopic fungi because dampness accumulates on the internal surfaces of walls, providing conditions for micro-organisms to grow on brick walls. This phenomenon is often found in multi-family houses. Those fungi excrete toxic substances and may cause irritation or asthma and other respiratory diseases, especially among small children.

Air quality is worse in renovated or newly constructed buildings with airtight windows. They rarely have adequate air circulation systems or the systems are often turned off to reduce the building's running costs.

The number of parasitosis cases is increasing. Soil contamination with the eggs of ascarids increased 2.4-fold, with the eggs of toxocaras 2.2-fold, toxocariasis morbidity 9-fold. The number of people infected with toxoplasmosis quadrupled between 1995 and 1997. The growth in parasitosis cases is linked with the increasing number of pets kept in dwellings. The law regulates animal guardianship and keeping, but its implementation is inadequately controlled.

Tobacco smoke is the main lung cancer risk factor and one of the main causes of heart and coronary diseases. Moreover, smoking might cause children's asthma. The Government has set

requirements for smoking areas but smoking is not sufficiently restricted in public places.

Noise comes from transport, the entertainment business, industry, security alarms, neighbours and other sources. Noise measurements in Vilnius have shown that the level of noise was high near streets with heavy traffic during peak hours (between 67-80 dBA and 43-57 dBA). Noise-proofing houses and public buildings did not ensure a decrease in noise to an acceptable level. Recently, noise from show business and entertainment centres has become very problematic, because it is not regulated by the Administrative Code of Law Violations and it is difficult to prevent. Noise produced by various sorts of equipment and its impact on life hygiene is a new problem. There are sorts of equipment that are not suitable for installing in occupied houses because of the high levels of noise produced during their operation. In addition, they often are installed without any measures for noise-proofing.

Population morbidity indicators are not taken into account in territorial planning. The causes of prevalent morbidity and mortality are not analysed in territorial planning, and the elimination of these causes is not foreseen in such plans. The urban infrastructure is developing slower than other elements of territorial planning. That is why local heating systems, water supply and sewerage are planned and built more frequently. However, regulation of ownership and responsibility for the use of infrastructure is not adequate (see **chapter IV**).

The quality of old houses and their environment are deteriorating little by little because of a lack of care and repair. Most dwellings built before 1993 are energy-inefficient. There are major energy losses and the costs of the energy used are increasing. To promote environmentally sound development, the Government is already carrying out an energy conservation programme in the building sector. Although Governmental Resolution No.704 determines which premises are not suitable for habitation, there is no resolution laying down how to help people living in houses that could harm their health or that lack basic amenities who are seeking to improve their living conditions.

The State's Public Health Centre is currently coordinating a national effort to produce a national environmental health action plan. This plan will be a very important policy implementation effort

towards ensuring the right of Lithuanians to a suitable dwelling.

### *Transport development*

Its geographic situation makes Lithuania a bridge between western Europe and the Russian Federation. The country has important transit functions. The railway network (**fig. III**) extends over some 2,500 km, while the paved road network covers 35,800 km. The national road system needs considerable maintenance and investment. In early 1994, the Government approved the National Transport Development Programme up to the year 2010. The development policy for the State transport infrastructure seeks to:

- Integrate the national transport system into the west European transport network and transport service market, and maintain transport links with the Commonwealth of Independent States;
- Harmonize the legal basis for regulating transport activities with EU laws and regulations;
- Create an open transport service market and promote private investment in the sector; and
- Ensure the stability of the transport infrastructure, its reconstruction and development, through public investment.

The Via-Baltica (Warsaw-Kaunas-Šiauliai-Riga-Tallinn) will be based on existing roads through their gradual renovation, the construction of city bypasses, and the construction of bridges and additional lanes. It is estimated that by the year 2000, traffic flows will have doubled. The road network is developing in another direction (**fig. III**): Klaipeda-Kaunas-Vilnius-Minsk (Belarus). The plan is to renew the road surface in certain sections and to construct a bypass around Vilnius. Average traffic intensity has already reached 3,500 to 12,900 vehicles a day and is estimated to reach 5,000 to 18,000 vehicles a day by the year 2000.

### *Settlements network*

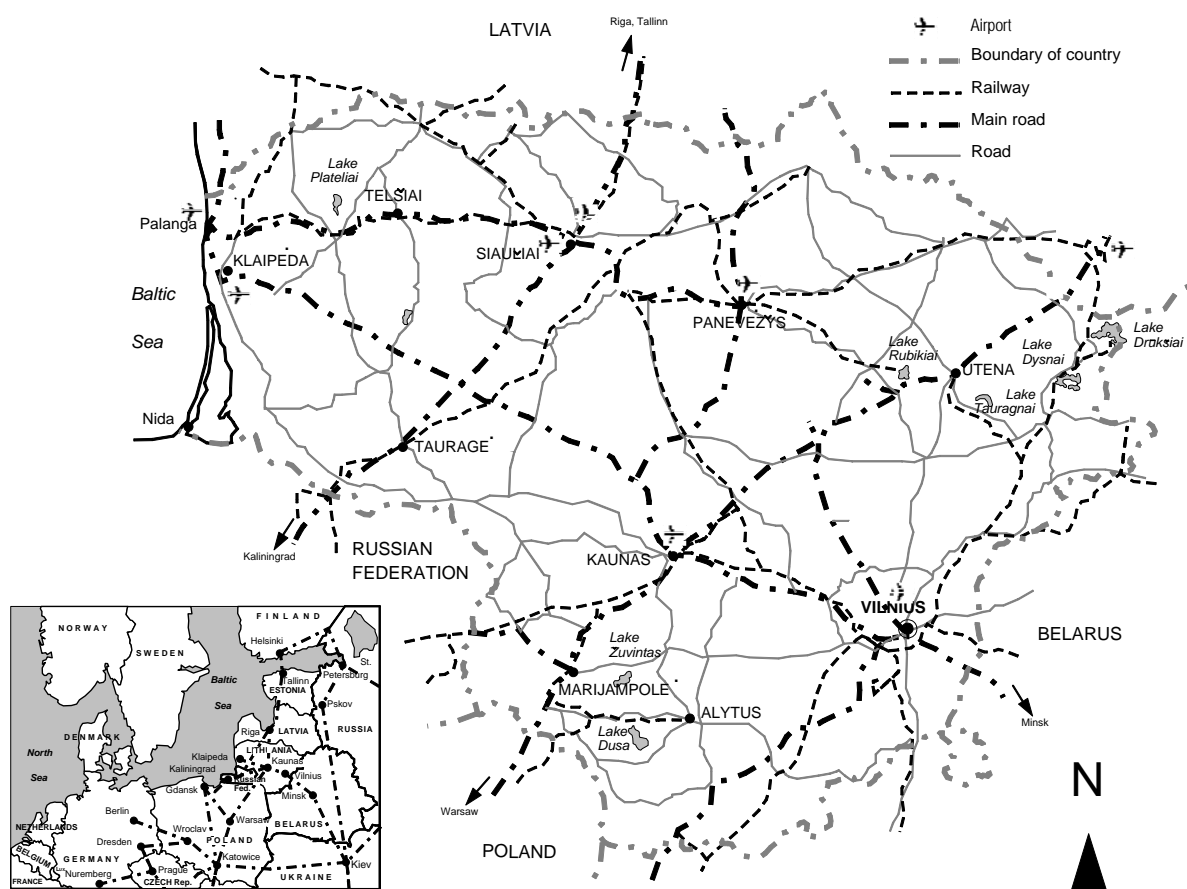
Before the Second World War, there were only two big cities, Vilnius (186,000 inhabitants) and Kaunas (154,000 inhabitants), and one

medium-sized town, Klaipėda (51,000 inhabitants), in what is now Lithuania. At present Vilnius and Kaunas each have a population of over 400,000; Klaipeda, Šiauliai and Panevezys each have more than 100,000 inhabitants. Other large urban centres are Alytus and Marijampole with more than 50,000 residents, while 13 towns fall into the medium-size category of 20,000 to 50,000 inhabitants. There are also 72 small towns and urban-type settlements in rural areas.

Lithuania has a *well-balanced network of human settlements*, which has resulted from the distribution of different functions among urban centres. Vilnius is the historical and cultural centre and the administrative capital. Klaipeda is the country's main port, while Kaunas is the educational, business and trading centre. In rural areas, the system of farmsteads (120,000) that existed before the Second World War was reorganized into collective farms. After 1990, many rural centres started to lose their economic and social importance. Job opportunities in rural areas are rare and some 70 per cent of all unemployed young people live in small rural centres. Consequently, living conditions in rural settlements have worsened considerably. Regional differentiation so far has been addressed by promoting small and medium-enterprise development. As far as housing provision is concerned, much lower growth rates in rural areas reflect the lack of demand and employment opportunities in these localities (see **table 4**). Housing stock characteristics are analysed in detail in **chapter II**.

### *National policies and objectives for spatial and regional development*

In 1995, the former Ministry of Construction and Urban Development drafted a *new national comprehensive plan for the period up to the year 2010*. The document, currently under discussion, defines spatial development priorities, the conditions and instruments for territorial management, as well as actions to implement the plan. Spatial development policy, in more general terms, had already been outlined in the national action plan for 1996-2000 prepared for the United Nations Conference on Human Settlements (Habitat II) in 1996.

**Figure III. Transport networks affecting Lithuania's settlements**

Source: UN/ECE.

Note: The boundaries shown on these maps do not imply official endorsement or acceptance by the United Nations.

**Table 4. Housing stock, 1990-1998**

	<i>thousand dwellings, buildings</i>									
	1990	1991	1992	1993	1994	1995	1996	1997	1998	
<b>Total dwellings</b>	<b>1,159</b>	<b>1,166</b>	<b>1,111</b>	<b>1,204</b>	<b>1,226</b>	<b>1,247</b>	<b>1,270</b>	<b>1,278</b>	<b>1,306</b>	
<b>Annual change in dwellings</b>	<b>14.1</b>	<b>6.5</b>	<b>(55.2)</b>	<b>93.3</b>	<b>22.0</b>	<b>20.8</b>	<b>23.1</b>	<b>8.0</b>	<b>28.2</b>	
Growth rate (annual)		0.6%	-4.7%	8.4%	1.8%	1.7%	1.9%	0.6%	2.2%	
<b>Newly completed buildings</b>	<b>22.1</b>	<b>15.3</b>	<b>12.7</b>	<b>8.2</b>	<b>6.9</b>	<b>5.6</b>	<b>5.6</b>	<b>5.6</b>	<b>4.2</b>	
Urban	17.5	12.8	11.2	7.4	6.1	4.6	4.4	4.4	3.2	
Rural	4.6	2.5	1.5	0.8	0.8	1.0	1.2	1.1	1.0	

Source: Lithuania, Department of Statistics, *Statistical Yearbooks* (Vilnius, 1997-1999).

Note: Data on housing supply in 1993 shows a higher growth rate due to a new definition applied in housing statistics.

In regional policy, the Government's goal is to *minimize the growing regional disparities*. That these exist and are widening is illustrated in **figure IV** with **table 5**. Despite the methodological drawbacks, GDP per capita by region presents a rough picture of how regions are performing. When compared to the average, the data reflects a certain distribution around the average. The United Nations Development Programme (UNDP) developed a regional human development index<sup>9</sup> for Lithuania. When calculating averages and

plotting deviations for both indicators on the graph, one can see that regions differ widely not only in economic development but also in terms of unemployment, morbidity, education, security, etc. In 1998 there was a shift towards a widening gap between the lowest and highest values as far as the average GDP per capita was concerned. The year 1999 was marked by a recession, which makes us expect that the economic situation will worsen further.

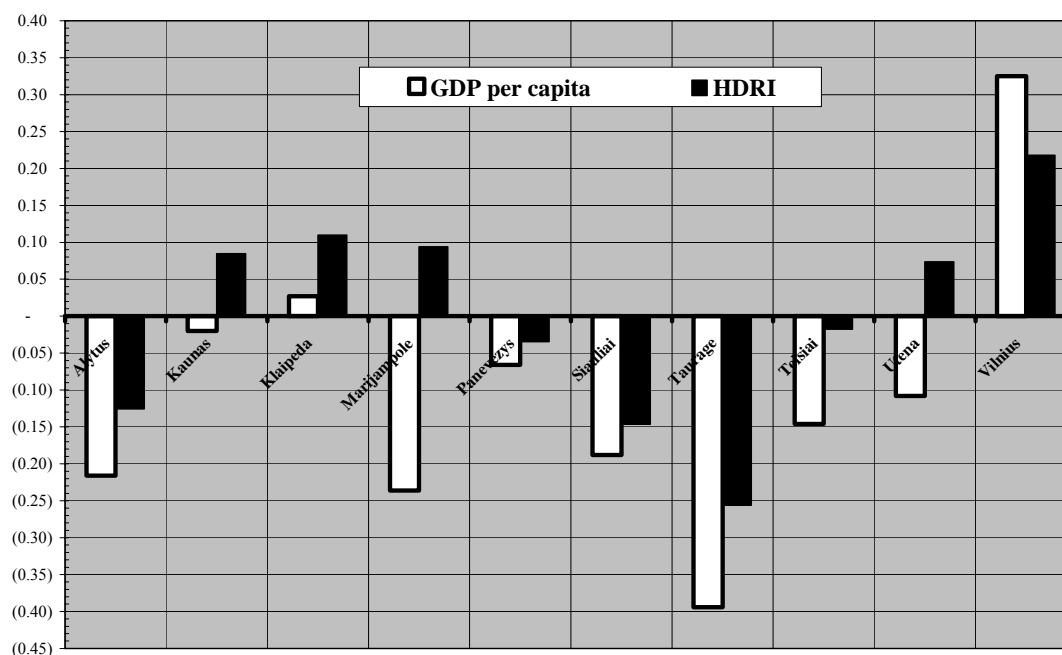
**Table 5. GDP per capita and HDI by region, 1996-1998**

Counties	GDP per capita (th litai)			Compared to average			RDHI	
	1996	1997	1998	1996	1997	1998	1997	1998
<b>Total</b>	<b>8.5</b>	<b>10.3</b>	<b>11.6</b>					
Alytus	7.2	8.7	9.1	0.85	0.84	0.78	0.35	0.36
Kaunas	8.2	10.3	11.4	0.96	0.99	0.98	0.64	0.57
Klaipeda	9.4	11.0	11.9	1.11	1.06	1.03	0.62	0.59
Marijampole	6.7	8.2	8.9	0.79	0.80	0.76	0.67	0.58
Panevezys	8.6	10.4	10.8	1.01	1.01	0.93	0.53	0.45
Siauliai	7.6	9.0	9.4	0.90	0.87	0.81	0.47	0.34
Taurage	6.3	6.7	7.0	0.74	0.65	0.61	0.28	0.23
Telsiai	7.7	9.1	9.9	0.91	0.88	0.85	0.57	0.47
Utena	8.0	9.3	10.3	0.94	0.90	0.89	0.57	0.56
Vilnius	10.0	12.6	15.4	1.18	1.21	1.33	0.59	0.70

**Sources:** Department of Statistics, Counties of Lithuania, Economic and Social Development (Vilnius, 1999). Ernst van Koesveld, Human Development Across Regions in Lithuania, UNDP (Vilnius, August 1999).

<sup>9</sup> The regional human development index (RHDI) is similar to the human development index (HDI) as it also comprises GDP per capita, but it represents longevity and knowledge in another, more direct way. At the same time, the RHDI comes closer to the concept of human development and human security. Apart from the variables selected, the methodologies differ slightly (see Ernst van Koesveld, UNDP, 1999 or <http://www.undp.lt>). The selected variables are GDP per capita, unemployment rate, morbidity by active tuberculosis per 100,000 persons and crime rate per 10,000 inhabitants.

Figure IV. Regional disparities, 1997



**Sources:** Department of Statistics, *Counties of Lithuania. Economic and Social Development* (Vilnius, 1999). Ernst van Koesveld, *Human Development Across Regions in Lithuania*, UNDP (Vilnius, August 1999).

There is a broad consensus on the need for a regional policy and regional development with a multi-sectoral approach to solve problems. Human settlements and housing issues have a role to play here and cooperation and coordination of work between institutions is crucial. The ministry responsible for the coordination is the Ministry of Public Administration Reform and Local Authorities. However, the process of introducing regional development and formulating regional policy is still in its infancy. It lacks a clear legal structure (a regional development law is in preparation) and an organizational structure is yet to be established (council on regional development and national agency for regional development).

Lithuania has many old towns and well-preserved architectural and historic monuments. The goal of the Government is to prepare programmes to mobilize financial resources for renovation and modernization. In urban development, attention is given to the *conservation and rehabilitation of the historical and cultural heritage*. The Government intends to develop programmes and measures to preserve existing

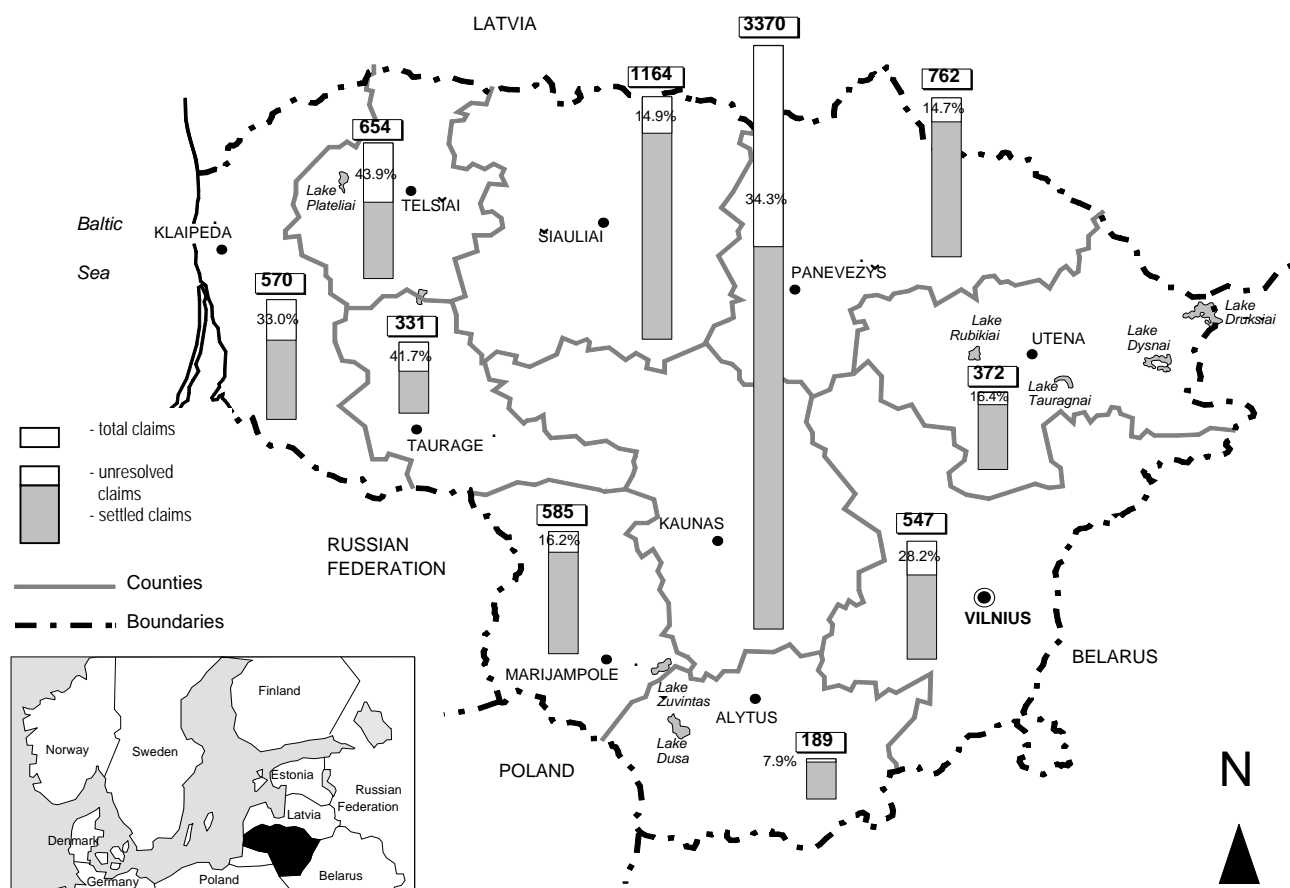
green areas, retain residential functions, and restrict traffic in old town centres. Special efforts have been successfully initiated in Vilnius, which was placed on the UNESCO list of World Heritage Sites in 1995.

### C. Housing reforms

#### *Restitution of property rights to dwellings*

Privatization and restitution are considered the hallmark of the housing reform process. The Law on the Procedure and Terms of Restitution of Citizens' Property Rights to Existing Real Estate (June 1991) is the legal framework to compensate or return real estate to former owners. Since 1991, 8500 applications have been submitted for the restitution of property rights to dwellings. Property rights have been restored to 4600 (53 per cent) owners (see also **chapters II and IV**). Only 978 claimants (or one in five approved claims) have received compensation (payment in cash, forest, another dwelling, or a plot of land). In January 1999, about 28 per cent of applications were still to be resolved (see **fig. V**).

**Figure V. Geographical distribution of claims for restitution, January 1999**



**Source:** Department of Statistics, *Economic and Social Development in Lithuania*, issues 3/1998 and 2/1999.  
**Note:** The boundaries on these maps do not imply official endorsement or acceptance by the United Nations.

*National housing policies*

The basis of a housing policy during the transition period was established in 1992, when Parliament approved the 'Bustas' governmental programme. The programme formulated the following principles:

- Gradually move from State housing provision to housing purchase;
- Shift away from uniform housing to individual choice, with the State remaining responsible for providing housing only to socially and economically vulnerable population groups;
- Create favourable conditions for the provision of long-term loans for housing construction;
- Promote housing construction by different types of developers: public, private, and housing associations;
- Create legal and economic conditions for the public housing stock privatization.

According to the 'Bustas' programme, the Government aimed to build 12,000-14,000 housing units annually. In practice, new construction has declined and is way below those targets. Mass privatization of public housing has eliminated the possibility to provide shelter to socially disadvantaged households (see **chapters II and III** for detailed discussion). Overall, the outcome has been rather controversial.

Currently, the Government's goals in housing are to:

- Encourage new construction where individuals finance their housing;
- Create conditions for financial markets to provide long-term financing;
- Differentiate State subsidies to support the most needy households;
- Earmark 2 per cent of the State budget for the 'Bustas' programme; and
- Encourage individuals, homeowners' associations and public enterprises to save

energy by renovating and insulating dwellings.

So far, most of the housing policy measures have focused on the development of effective instruments to make long-term housing loans available to the majority of the population. Such a universal approach requires a stronger banking sector, as well as mortgage institutions. The purchasing power of the population, in the housing markets of large urban centres in particular, remains limited and needs to be increased. This objective appears to be quite complex and can be achieved only in the long term. At present, long-term loans for housing construction and renovation are subsidized by the State and allocated to households who are homeless or have less than 10m<sup>2</sup> per person or who are eligible for social benefits. Some 100,000 households are eligible for State support and are officially registered with local municipalities (see **chapter IV**). Experts recognize that the State is not able to respond to the volume of applications. Therefore, a new edition of the Law on the Provision of Dwellings for Citizens (1992) is before Parliament. The Ministry of the Environment has drafted a housing policy strategy to assist the debate in Parliament. The Government has passed Resolution 794 to appropriate funds for municipal housing for 1999-2000 (see **chapter IV** for details).

Another major problem in the housing sector is associated with the dramatic increase in heating and hot water charges, which has created a considerable burden on households and led to wide dissatisfaction with Government policies. According to the Housing Credit Foundation (HCF), the average household spends about 14 per cent of its income on energy. In response, the Government has established two instruments. First, starting from May 1997, homeowners and homeowners' associations have been able to obtain the necessary technical assistance and loans for the preparation and implementation of energy efficiency projects from HCF.<sup>10</sup> Secondly, subsidy and support schemes for heating and hot water have been introduced. Low-income households are eligible for heating and hot water subsidies if their

heating and hot water bills exceed 25 and 5 per cent of their income respectively. The Social and Labour Ministry estimates that approximately 30 per cent of urban households are eligible for these subsidies.

#### *Municipal housing policy initiatives*

The 'Bustas' programme was the first national reaction to the political determination of the State to withdraw from housing supply. While one of the objectives of the 'Bustas' programme was to facilitate housing privatization, it failed to restrict the conversion of residential into commercial properties and to define maintenance responsibilities for common ownership areas. Currently common areas of ownership are maintained in most cases by the municipal housing maintenance enterprises. Municipalities are concerned with these problems, but have failed to address the issue in a systematic manner.

A municipal housing policy has been developed only for the city of Vilnius. It has four strategic directions: to maintain and improve the existing housing stock, to help people who cannot afford adequate housing, to provide support to meet new housing demand, and a new definition of housing roles and responsibilities. Each direction has its own goals. To maintain and improve the existing housing stock, for example, the municipality aims to privatize its housing maintenance enterprises, to support homeowners' associations to maintain city housing, to carry out housing renovation and energy saving programmes, to set and enforce minimum housing standards, and health and safety regulations. Its Action Plan envisaged two phases: phase 1 for 1998-1999 and phase 2 for 2000-2005. The policy document recognizes that the State, homeowners' associations, individual owners, tenants and private-sector actors must be involved in solving housing problems in Vilnius. A housing division with 20 staff members in the city administration and a sub-committee on housing issues being established by the Council indicate a commitment to institutionalize and implement these objectives.

<sup>10</sup> Five advisory centres are established. Eight schools, 38 homeowners' associations and 20 individual homeowners carried out energy efficiency projects via the Energy Efficiency and Housing Pilot Project. The Project started in 1996 with a World Bank loan (US\$ 10 million) and the assistance of two Netherlands ministries (Ministry of Housing and Urban Development and Ministry of Economics).

## *Chapter II*

# *EXISTING HOUSING STOCK AND NEW HOUSING CONSTRUCTION*

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In the post-war period urban growth in Lithuania was very dynamic. The share of urban population increased from 23 per cent in 1939 to 65 per cent in 1995. Urban growth was the highest in 1966-1970 due to a yearly migration of 57,000 inhabitants from rural to urban areas, which correspondingly led to the depopulation and decline of rural areas. In Lithuania, there are 111 towns (according to the national classification all settlements with more than 3,000 inhabitants are towns). Almost 40 per cent of the inhabitants live in the five biggest cities; 15 per cent of the total population is concentrated in Vilnius. The high level of urban concentration, together with employment restructuring, intensifies regional differences in the demand for and the supply of housing.

### A. The existing housing stock

By the end of 1998 Lithuania's housing stock consisted of 1,306,061 housing units, with an average of 353 units per 1,000 inhabitants and average useful floor space of 21.1 m<sup>2</sup> per capita. However, regional and local differences in housing consumption are significant. In the rural areas, with some 351 dwellings (mainly family houses) per 1,000 inhabitants, there is practically no demand for new housing. In the urban areas, there are, on average, 338 dwellings per 1,000 inhabitants, mainly in multi-family housing estates, with much less floor space per dwelling unit. Though housing construction in Vilnius has increased the number of housing units per 1,000 inhabitants significantly (**table 6**), housing shortages continue to be a major problem. It should be noted that the indicator for Vilnius (333) is one of the lowest of the capital cities of all economies in transition.<sup>11</sup>

**Table 6. Dwellings per 1000 inhabitants, 1980'1998**

	1980	1990	1994	1996	1997	1998
Lithuania	280	310	329	342	344	353
Vilnius	282	271	293	298	299	333

*Source:* Statistics Lithuania, B 902 : Stock of dwellings 1998, Vilnius, 1999.

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<sup>11</sup> According to 1994 data, these figures range from 341 (Riga) to 433 (Prague), while the average for the capital cities of the countries in transition is 383 housing units per 1000 inhabitants. (MRI, 1996).

A comparison of housing quantity in **table 7** indicates certain deficits in the Lithuanian housing stock. The indicator of persons per room, a traditional measure of residential overcrowding, is as high as 1.3. A high value of households per dwelling (1.06) indicates that housing supply is

unable to meet housing needs -- to provide a separate dwelling for every household. Lithuania has one of the most unfavourable quantitative indicators among the economies in transition included in the sample.<sup>12</sup>

**Table 7. Housing consumption in selected countries in transition, 1994**

	<b>Dwellings per 1,000 inhabitants</b>	<b>Households per dwelling</b>	<b>Persons per room</b>	<b>m<sup>2</sup> per person</b>
Albania	219	1.00	2.70	8.0
Bulgaria	405	0.88	1.00	16.7
Czech Republic	397	1.01	1.04	25.5
Estonia	410	1.03	1.18	32.0
Hungary	385	0.99	0.92	32.1
Latvia	370	1.13	1.21	20.9
<b>Lithuania</b>	<b>329</b>	<b>1.06</b>	<b>1.30</b>	<b>19.7</b>
Poland	296	1.06	1.02	18.2
Romania	341	0.95	1.19	17.4
Slovakia	334	1.00	1.14	21.9
Slovenia	338	0.95	1.33	19.0

*Source:* Hegedus, J., S. Mayo and I. Tosics, Transition of the Housing Sector in the East-Central European Countries (MRI, Budapest, 1996).

<sup>12</sup> The figures for Vilnius are even higher; in the public rental sector it was 1.52 person per room in 1994.

Today several indices suggest that urban areas are still experiencing serious housing shortages. Among these indices are the household-to-dwelling ratio; mismatch in the structure of dwellings and households; percentage of urban families living in dormitories and number of applicants on the municipal waiting lists (see **chapters I and IV**). This shortage was quantified in 1992 in the 'Bustas' programme at 136,000 dwellings. Urban-rural inequalities in housing consumption can also be illustrated by data from the 1989 Census, which states that 64 per cent of families in urban areas occupied one- or two-room dwellings. The average size of urban dwellings is smaller (53.8 m<sup>2</sup>) than that of rural dwellings (67.5 m<sup>2</sup>). The rapid growth in the urban population and a very low spatial standard per person adopted in State rental or cooperative housing<sup>13</sup> account for these differences.

From a quantitative point of view, the urban situation has improved slightly since the early 1990s, not so much because of the new

construction, but particularly due to the conversion of former dormitories and non-residential premises to dwellings. For example, new construction added 23,700 dwellings to the existing housing stock, while conversion added another 50,100 dwellings between 1994-1997. Meanwhile anecdotal evidence suggests that many dwellings were converted to commercial or business uses, particularly in areas close to the central business districts of the larger urban centres. There are no statistical data on these changes, nor is it possible under current legislation to prevent such conversions.

Another disproportion can be seen in the structure of the housing stock versus the structure of households (according to the number of household members and the number of rooms in the dwelling), as illustrated in **table 8**. The data indicate that there is a shortage of dwellings with three rooms or more. It seems that new construction has responded by delivering larger dwellings (**table 14**).

**Table 8. Distribution of dwellings and households, 1990**

Households		Dwellings	
Number of persons In a household	Per cent of total	Number of rooms In a dwelling	Per cent total
1	21.5	1	16.8
2	26.5	2	37.9
3	22.5	3	30.5
4	20.1	4	10.0
5 or more	9.4	5 or more	4.8

**Sources:** Ministry of Construction and Urban Development, *Housing and Environment in Lithuania Today, Tomorrow and after Tomorrow*, National Report for the United Nations Conference on Human Settlements HABITAT II, Republic of Lithuania (Vilnius, 1998); Institute of Architecture and Construction, Kaunas, 1999.

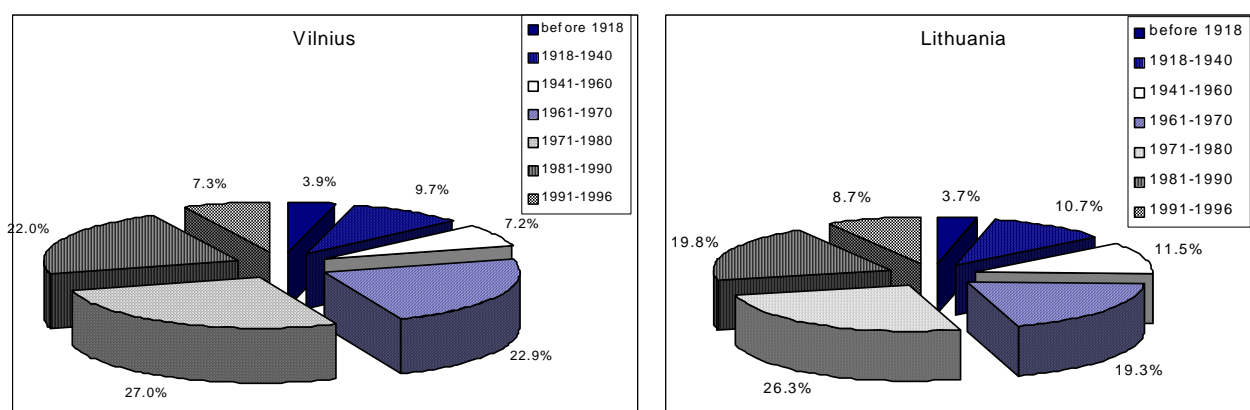
<sup>13</sup> Housing consumption was limited to less than 5 m<sup>2</sup> per person in State rental and less than 7 m<sup>2</sup> in cooperative housing.

### Quality of the housing stock

Data on the *age structure of the housing stock* (fig. VI) show that nearly three quarters of the dwellings in Lithuania were built in the period 1961 - 1996. Only 3 per cent of the dwellings were built before 1918 and another 11 per cent between

1918 - 1940. Due to neglected maintenance this relatively new housing stock requires extensive renovation. According to 1998 data, approximately 105,744 m<sup>2</sup> of total living space in public housing (4.1 per cent of the total housing stock) is considered to be unfit for habitation and will probably have to be demolished.

**Figure VI. Age structure of the housing stock in Lithuania and in Vilnius**



*Source:* Statistics Lithuania, B 902: Stock of dwellings 1998, Vilnius, 1999.

It is difficult to supply complete time series on the *quality of the Lithuanian housing stock*. Available data are rather vague and not consistent, and there is a mismatch in recent official information (e.g. 1993 data reflect the situation excluding privately owned houses in rural areas). Overall, housing qualitative indicators, such as central heating, piped water and sewerage system and bath (or shower), are higher in urban areas (see **table 9**), while the spatial standard is in general more favourable in rural areas. In rural areas only

44 per cent of the dwellings are connected to the piped water supply and 39 per cent have central heating. By contrast, close to 90 per cent of urban housing has access to a piped water supply, sewerage and central heating. While rural housing requires mainly a massive improvement in the public technical infrastructure, urban housing is more in need of quantitative and spatial improvements. In the case of new dwellings, the data indicate a commitment to higher technical standards.

**Table 9. Facilities in the housing stock  
(In per cent)**

	<i>Piped water</i> <sup>a/</sup>	<b>Fixed bath or shower</b> <sup>a/</sup>	<b>Centr al heatin g</b>	<b>Electric ity</b>	<b>Sewera ge system</b>
Total housing stock, 1993 <sup>b/</sup>	58.9	53.8	57.8	100	N/A
1998	72.8	63.0	69.4	100	70.7
Urban housing stock, 1996	90.4	81.9	86.2	100	89.7
1998	89.4	80.7	87.0	100	89.1
Rural housing stock, 1998	44.1	32.5	39.2	100	39.1
Newly completed dwellings, 1993	97.6	96.3	96.3	100	N/A
1994	100.0	97.1	76.8	100	97.1
1995	96.4	94.6	96.4	100	96.4
1996	94.6	92.9	96.4	100	96.4
1997	96.0	95.0	96.0	100	95.0

**Sources:** UN/ECE, *Annual Bulletin of Housing and Building Statistics for Europe and Northern America 1980, 1990, 1991, 1992, 1993* (New York and Geneva, 1995);

UN/ECE, *Annual Bulletin of Housing and Building Statistics for Europe and Northern America 1998* (New York and Geneva, 1999);

*Statistics Lithuania, B 902: Stock of dwellings 1998*, Vilnius, 1999.

<sup>a/</sup> Indoors.

<sup>b/</sup> Excluding privately owned houses in rural areas.

N/A - not available.

When discussing the technical performance of the existing housing stock, it is necessary to keep in mind that in the period from 1960 to 1990 construction was dominated by multi-family high-rise prefabricated housing, which accounted for 80 per cent of the total output. These types of buildings have the following typical problems:

- Poor construction quality, including the technical infrastructure in the buildings (bathrooms, electrical wiring, pipes and plumbing for heating, water and sewage pipes, lifts, etc.);
- Low energy efficiency (the most problematic being lightweight and monolithic panel houses with external walls 30 and 35 cm thick);
- Neglected maintenance;
- High energy losses in the district central heating system and hot water production and distribution.

In Lithuania, another source of housing are garden houses and summer cottages. Gardeners' associations constructed small houses on small plots of land on the outskirts of large cities during Soviet times. Gardeners' associations owned 22,000 hectares of land in 1998, of which 12,400 hectares were privately owned by 185,000 individuals.<sup>14</sup> Though quality is poor, retired people and young families occupy many of these garden and summer houses all year long.

#### *Maintenance*

Lithuania has more than 30000 multi-family buildings, most of which are privatized. However, homeowners' associations manage some 10-15 per cent of them. Maintenance is still a monopoly of the municipal maintenance enterprises (companies), which also maintain the public rental stock. The variety, quality of services and tariffs are

<sup>14</sup> S. Puipa, *Process of the land reform and perspectives in Lithuania* (1998).

established without any adjustment to markets. Rent level and maintenance fees in the municipal rental sector, and maintenance fees in the owner-occupied sector are low, which restricts systematic maintenance and improvement. Consequently, this situation neither stimulates new private enterprises to enter the housing maintenance market, nor promotes competition.

There are no surveys or estimates of the investment needed to repair and improve the existing housing stock. Municipal maintenance companies estimate regular maintenance costs at Lt 0.8 per m<sup>2</sup>, while only about Lt 0.25 is charged per month in the municipal rental sector.<sup>15</sup> Because of the massive need for energy improvement, one of the explicit objectives of the 'Bustas' programme is to reduce energy consumption. The National Energy Savings Programme states that up to 50 per cent of the annual energy consumption could be saved by appropriate measures such as:

- The thermal insulation of the existing housing stock;
- Heat meters and economic incentives for the rational use of heat;
- Improvements in heat supply systems;
- The optimization of energy and fuel distribution.

The cost of thermal insulation improvements of the housing stock was estimated at 22 billion litai (US\$ billion 5.5) in 1992.<sup>16</sup> In response to the challenge new regulations for the thermal performance in housing construction have been implemented, and soft loans for energy savings programme have been made available. The Housing Credit Foundation administers approximately one million litai per year to this end.

It is clear that there is an enormous need for well-organized and effective management and maintenance of the existing housing stock and

preparation of strategies for modernization and renewal. Since a large part of Lithuania's housing stock is energy-inefficient and energy prices are rising, the energy bills of households are increasing.

That leaves fewer resources for maintenance and repair. Therefore, in the current situation effective management could play a crucial role, as could maintenance companies, able to evaluate conditions, set priorities and propose sequence of steps necessary to improve individual cases. The activity of such companies should include also better information and communication with the owners.

## B. Tenure structure and housing markets

### *Privatization of housing*

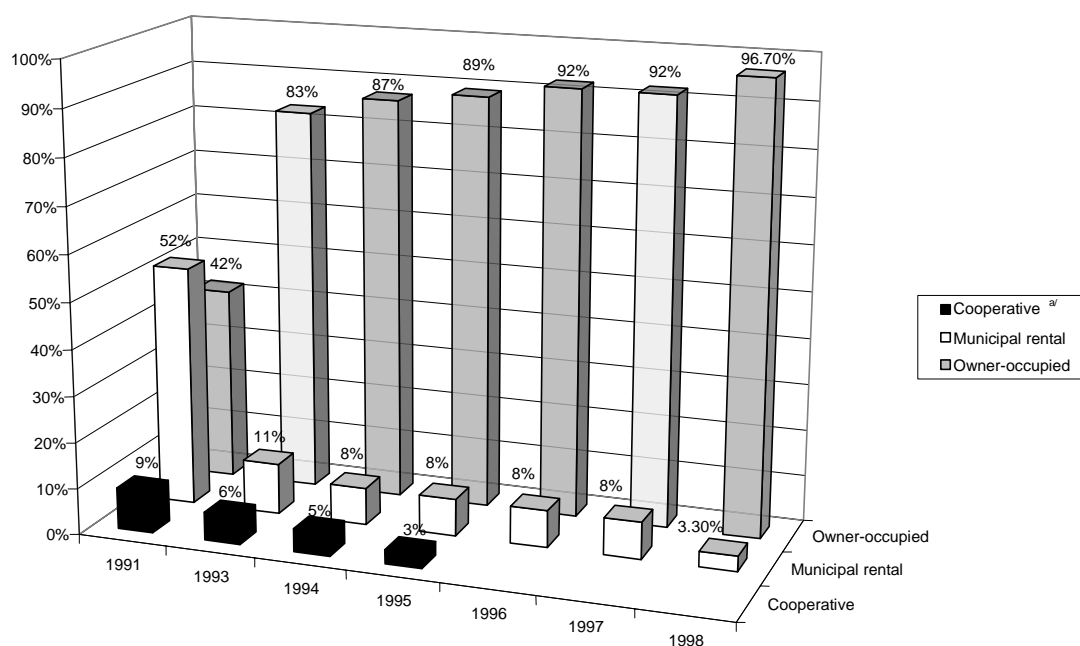
The first step on the way to housing market development was the restoration of the private ownership of housing. Since the legal basis for the restitution of ownership rights to property was established in 1991, 8,500 applications have been submitted. In 1998, 8,727 families lived in dwellings subject to restitution (see also **chapters I and IV**). As far as the restitution of ownership rights to land is concerned, only 12,000 applicants in urban areas received their land back.<sup>17</sup>

Until the re-establishment of independence, about 60 per cent of all dwellings (and about 80 per cent in urban areas) were owned by the State. Today, Lithuania's owner-occupied sector has a share of 96 per cent (**fig. VII**). Privatization was implemented very quickly, resulting in the sale of 532,900 State and publicly owned dwellings. Close to 94 per cent of all requests by tenants to purchase their flats were satisfied. It should be noted that land on which residential buildings were built was not subject to privatization. Dwellings were purchased using 23 per cent cash and 77 per cent vouchers.

<sup>15</sup> Study on Government Assistance Programmes to the housing sector (Vilnius, August 1998).

<sup>16</sup> The latest available update from the Ministry of the Environment in January 1998 suggests that these costs have increased to 20,000 litai per dwelling.

<sup>17</sup> There were 670,000 applications for land restitution in rural areas. By January 1998, 250,000 had been approved. Of the 60,000 applications in urban areas, 12,000 were approved.

**Figure VII. Changing tenure structure, 1991 - 1998**

*Source:* Statistics Lithuania, *Stock of dwellings 1998*, B 902 (Vilnius, 1999).

<sup>a/</sup> According to the new legislation (1995), housing cooperatives had to register as homeowners' associations.

Thus, Lithuania became one of the "forerunners" in housing privatization and, together with Albania, Bulgaria, Hungary and Romania, has an extremely low volume of public housing compared with the 1990s EU average of

approximately 18 per cent. **Table 10** illustrates the privatization trends in selected countries in transition. Additional information on tenure structure in Europe is presented in **annex I**.

**Table 10. Changes in the tenure structure in selected countries in transition (In per cent)**

	Albania		Bulgaria		Czech Republic		Estonia		Hungary		Romania		Slovakia	
	1990	1998	1990	1998	1990	1998	1990	1998	1990	1998	1990	1998	1990	1998
Public rental	35.0	2.0	6.8	7.1	39.0	23.0	65.0	10.0	22.0	5.0	21.4	4.0	27.7	14.0
Private rental	-	-	1.5	3.2	-	10.0	-	-	0.5	1.0	1.0	3.0	-	-
Owner-occupied	65.0	98.0	91.7	89.7	41.0	44.0	35.0	90.0	77.5	94.0	76.1	93.0	50.2	69.0
Co-operative	-	-	-	-	20.0	23.0	-	-	-	-	1.5	-	22.1	17.0

*Source:* UN/ECE - CHF Practical workshop on housing privatisation, Crakow 1999.

The post-privatization phase faces a number of problems. One is that almost all dwellings could be privatized, even those with serious structural and technical problems and those that should be condemned. Another is that low-income households became owners but are not necessarily able to maintain their homes. Many urgent problems are thus ahead in regard to renovation and maintenance. But more importantly, the low share of public housing has left municipalities with no opportunity to provide shelter for socially marginalized households or people with special needs, or to respond to rising homelessness. *Homelessness*, almost unknown in Soviet times, has become one of the most serious problems confronting people going through a difficult time in life. Though there are no official statistics on homelessness in Lithuania, reportedly homeless people were either victims of fraud in the sale of their flats, or lost their dwellings as collateral for loans. Most of the homeless are long-term unemployed and tend to be under the age of 30.<sup>18</sup> Municipalities and private charitable NGOs provide temporary shelters, but a solution to this problem requires a more systematic approach.

#### *Housing and land markets*

Following the restitution and privatization, many dwellings were offered for sale on the housing market. Voucher privatization provided a major boost to housing demand. In 1996, 74,216 sales of buildings and 11,042 purchases of land were registered, while in 1997 the volume of building sales nearly doubled to 148,761.<sup>19</sup> The most active real estate markets operate in the larger cities -- Vilnius, Kaunas, Klaipeda and the sea resort of Palanga. *Housing prices are particularly sensitive to economic crises.* High inflation in 1993, the 1996 banking crisis in Lithuania and the more

recent financial crisis in the Russian Federation considerably affected housing prices. House price differentiation is driven by differences in location, neighbourhood status and quality. Anecdotal evidence suggests that urban location close to the business districts and the old towns with higher-quality dwellings and buildings have increased considerably in price. House prices in these locations are typically 1.5-2 times higher than in other areas. Other parameters that affect house price dynamics are the number of rooms, the design, the layout and the construction system. Smaller dwellings are more expensive per m<sup>2</sup>; in larger units the price per m<sup>2</sup> reportedly decreases by 10 to 20 per cent, particularly in smaller towns, where running costs tend to be a burden on household budgets.

Although there is no comprehensive information on house prices as surveyed by a specialized institution, the available information on market prices for new dwellings (**table 11**) and individual houses (**table 12**), without finishings, illustrates the major trends in regional housing markets. Limited supply nearly tripled the prices of flats in central Vilnius between 1993 and 1999, while in the suburbs they merely doubled. In Kaunas, prices rose by a factor of approximately two and a half, while in Klaipeda due to rapid economic growth they quadrupled. *In the first half of 1999, price variations for flats were significant -- fluctuating from Lt 3,200 in the best locations of Vilnius to 750 in Panevezys.* Inflation and limited supply account for the moderate growth in house prices. However, the use of imported building materials, with better performance and higher prices, also affects house prices. New construction is reportedly 20 per cent more expensive than existing dwellings.

<sup>18</sup> United Nations Development Programme, Lithuanian Human Development Report 1996 (Vilnius, 1996).

<sup>19</sup> A. Bagdonavicius, Real Property Market and Real Property Taxation in Lithuania (Vilnius, 1999).

**Table 11. Market prices of new dwellings in multi-family housing, 1993 – 1999**  
(In Lt per m<sup>2</sup>)

	Vilnius <sup>a/</sup>			Kaunas	Klaipeda	Panevezys
1993	1200	700	400	500	450	300
1994	1300	930	450	600	570	500
1995	1800	1000	500	700	670	600
1996	2000	1200	600	750	850	650
1997	2400	1500	800	800	900	770
1999	3200	1900	N/A	1200	1800	750

**Sources:** Institute of Architecture and Construction, Kaunas, 1999;  
Namū Valda, Summary Information on Real Estate Prices, (Vilnius, 1999).

<sup>a/</sup> Vilnius: central, broader and suburban location.

<sup>b/</sup> Data are only for the period January – June.

N/A - not available

Prices of individual housing show a similar pattern of growing regional differentiation. The preferred type is the traditional single-family home of 100-150 m<sup>2</sup> constructed up to 5 years ago (**table 12**). Prices per m<sup>2</sup> are 1.5-2 times higher than the

prices in multi-family buildings. Data indicate that suburban homes in Vilnius tend to be less attractive. However, this is due to their lack of adequate infrastructure and their problematic accessibility.

**Table 12. Prices of individual houses, 1993 – 1999**  
(In Lt per m<sup>2</sup>)

	Vilnius <sup>a/</sup>			Kaunas	Klaipeda	Panevezys
1993	2900	1600	N/A	N/A	N/A	N/A
1994	3200	1800	800	N/A	N/A	N/A
1995	3500	2000	900	1400	1200	1200
1996	3700	2900	900	1600	1600	1200
1997	4500	3500	1200	1800	2000	1400
1999 <sup>b/</sup>	5800	4700	N/A	2000	3300	1600

**Sources:** Institute of Architecture and Construction, Kaunas, 1999;  
Namū Valda, Summary Information on Real Estate Prices (Vilnius 1999).

<sup>a/</sup> Vilnius: central, broader and suburban location.

<sup>b/</sup> Data are for the period January – June.

N/A - not available.

The house-price-to-income ratio in Lithuania is quite high (see affordability issues in **chapter III**). Because of affordability problems, transactions tend to concentrate on the upper segment of the urban market. Annual turnover in the owner-occupied sector is estimated at 7-8 per cent. The highest demand is for 1 or 2-room dwellings and small<sup>20</sup> individual houses with good insulation and low energy consumption. Extremely large houses with poor thermal performance and inadequate architectural design built in the early

1990s (before 1992) are extremely unpopular and their prices have not moved since 1994.

A *private rental sector*, consisting mostly of privatized dwellings, has developed rapidly in Vilnius and other large cities. The rent is often 40 to 60 times higher<sup>21</sup> than the rent in the public rental sector. Experts estimate that some 5-8 per cent of

<sup>20</sup> Up to 200 m<sup>2</sup> of floor space.

<sup>21</sup> Rent levels in Vilnius (according to local experts): one-room flat range from Lt 400 (US\$ 100) outside the centre to Lt 1,000 in the city centre; two- and three-room flats range from some Lt 800 - 2,500 to more than Lt 4,000, respectively.

owner-occupied housing is used as private rental. These dwellings are rarely registered as a revenue property and tend to be rented without a lease. According to real estate agencies, 1-2 room flats in Vilnius and Klaipeda are let within a couple of days; larger flats with 3-4 rooms usually need 2-3 weeks. There is significant demand for single-family housing; it takes only 2-4 weeks to let 3-5 room properties. By contrast, supply exceeds demand for rental housing in smaller towns and remote regions.<sup>22</sup>

*Land markets are a new reality in Lithuania.* The main part of the land market is created by agricultural land transactions; activity on the urban land market seems to be relatively underdeveloped and accidental, concentrated on the largest towns. For example, out of 27,637 private

land transactions in 1998 more than 16,000 dealt with agricultural land. Land price dynamics in the emerging land markets indicate that urban land (in central areas and in suburbs suitable for recreation and future construction) tends to be the most valuable. There are significant differences in land prices between city centres and suburbs and among different towns (**table 13**). As the data indicate, land in central Vilnius has increased ten fold in price between 1993-1999, against 2.5 times in the suburbs. Similar trends can be observed in the second biggest city, Kaunas, and in the port of Klaipeda. In Panevezys (132,100 inhabitants) land prices merely doubled in the same period. Overall, price fluctuations are high, ranging from Lt 600 per m<sup>2</sup> in the best locations of Vilnius, to Lt 8 per m<sup>2</sup> in 1999.

**Table 13. Market prices of land for housing construction, 1993 – 1999**  
(In Lt per m<sup>2</sup>)

	Vilnius <sup>a/</sup>	Kaunas	Klaipeda	Panevezys
1993	60 - 30 - N/A	N/A	N/A	N/A
1994	100 - 40 - 4	5	6	N/A
1995	200 - 60 - 6	5	7	6
1996	270 - 80 - 7	12	10	6
1997	360 - 100 - 10	20	12	8
1999 <sup>b/</sup>	600 - 150 - 10	200 - 80 - 24	360 - 200 - 88	24 - 12 - 8

**Sources:** Institute of Architecture and Construction, Kaunas, 1999;  
Namu Valda, Summary Information on Real Estate Prices (Vilnius, 1999).

<sup>a/</sup> Central, broader and suburban location.

<sup>b/</sup> Data are only for the period January –June.

N/A - not available.

<sup>22</sup> Namu Valda, op.cit.

According to information from the State Land Cadastre and Register, annual turnover on the land market is low, less than 1.5 per cent. This could change in the near future, as one of the important political aims of the Lithuanian Government is to complete the land reform, which would mean going ahead with the mass privatization of the State-owned land. According to surveyors, about 2.5 - 3 million land parcels should be formed to be privatized or leased.<sup>23</sup>

### C. New housing construction

#### *Trends in the provision of new housing*

*New housing construction declined steadily in the 1990s.* The number of new dwellings per 1,000 inhabitants dropped to 1.5 in 1995-1997.<sup>24</sup> As

**Table 14** shows, annual output fell from 22,100 dwellings completed in 1990<sup>25</sup> to 4,500 in 1998.

That is less than 14 per cent of housing output during the 1980s. On the other hand, the average floor area of new housing has increased by almost 70 per cent, largely due to a surge in individual housing construction. New housing is mostly concentrated in urban areas -- between 80-90 per cent of the annual production. While almost 55 per cent of the existing housing stock tend to be 1-2 room flats; smaller units account for 32.2 per cent of the housing built in 1997. Dwellings with 4 or more rooms have doubled their share and form 39.9 per cent of newly built housing. Despite the overall decline, particularly pronounced in 1998, building permits for individual and multi-family housing remained relatively stable.<sup>26</sup>

Table 14. Dwellings completed, 1990-1998

	1990	1991	1992	1993	1994	1995	1996	1997	1998
Dwellings completed (thousand)	22.1	15.3	12.7	8.2	6.9	5.6	5.62	5.56	4.18
Of which urban (%)	79	84	88	90	88	82	79	80	77
rural (%)	21	16	12	10	12	18	21	20	23
Average floor area (m <sup>2</sup> )	65.7	66.3	69.3	74.4	85.5	101.0	112.0	109.0	120
Individual homes' average floor area (m <sup>2</sup> )	104.9	110.0	118.2	133.3	152.0	161.0	180.0	166.0	171.7

*Source:* Statistical Yearbook of Lithuania 1999 (Vilnius, 1999).

<sup>23</sup> Puipa, *op.cit.*

<sup>24</sup> The comparable figure for western Europe is 3.5 - 6.6.

<sup>25</sup> In 1980s, annual production ranged from 28,200 dwellings (1984) to 32,100 (1987).

<sup>26</sup> Building permits for residential buildings issued during the period 1995-1998: 1,581; 1,530; 1,996; 1,452.

*Uncompleted housing* amounts to 23,000 dwellings across Lithuania. Local experts estimate that approximately 90 per cent of these individual homes are located on the fringe of large cities. Some of these projects were initiated on a speculative basis by developers in 1991, who were then caught in rapidly escalating construction costs in 1992-1993. In some cases, individual owners were also unable to secure financing, or municipalities were unable to service the areas as planned. It is difficult to find a suitable financial and technical model for the completion of these

projects, due to their size, layout and lack of adequate infrastructure.

*Construction costs* rocketed in 1992 and 1993. This surge was more or less correlated to changes in the consumer price index. It has been suggested that construction costs increased much more than input costs -- labour and building materials. Though data indicate that income is growing faster than inflation or construction costs, new housing continues to be a privilege for high-income households (**table 15**).

**Table 15. Construction costs, inflation and income, <sup>a/</sup> 1991-1998**

	1991	1992	1993	1994	1995	1996	1997	1998
Construction (total)	100	1184.2	486.9	184.0	125.4	116.8	109.8	104.2
Housing construction	100	1282.7	473.7	187.9	121.4	115.4	110.9	102.7
Inflation	N/A	N/A	N/A	145.1	135.7	113.1	108.4	102.4
Average income	N/A	N/A	N/A	200.6	124.7	100.8	117.4	114.1

*Source:* Institute of Architecture and Construction, Kaunas, 1999.

<sup>a/</sup> Compared with the same period of the previous year (previous year = 100).

N/A: not available (in 1993 national currency was introduced).

Land is another constraint for the provision of new housing. According to real-estate agents, demand for urban land for housing construction is limited. The availability of serviced and developable land for individual housing is problematic. Land for multi-family construction is usually leased for 99 years. Municipalities are responsible for providing the technical infrastructure, but because of scarce budgetary resources their hands are tied. According to developers in Vilnius, there is a certain backlog in the preparation of master plans. Often developers have to finance detailed zoning plans, and this further increases development costs.

#### *Actors in the provision of new housing*

One of the objectives of the 'Bustas' programme was to construct 220,000-240,000 housing units during the 1992-2005 period, which

translates into an annual construction of approximately 18,000 housing units. The programme also set a target of 1,200 dwellings per year for families on benefits. Previous discussions on trends in the production of new housing indicated that reality fell short of expectations. More importantly, the lack of an adequate new housing supply has fuelled speculation and has made housing less affordable to middle- and low-income households.

The introduction of market principles has brought new actors into the real estate markets. As illustrated in **table 16**, a substantial part of new dwellings since 1993 was completed in the private sector. Individual developers and associations (or cooperatives) account for 90 per cent of newly built housing. In 1996, the share of public housing output was as low as 4.4 per cent (some 250 dwellings).<sup>27</sup> This is a radical departure from the situation during

<sup>27</sup> It was 20 per cent, 31.7 per cent, 31 per cent and 29 per cent respectively in Albania, the Czech Republic, Estonia and Bulgaria in 1996.

Soviet times, when the public sector acted as the dominant developer and producer of housing. There are practically no institutional investors in the Lithuanian market. Developers are typically private construction firms, attracting potential clients

before starting to build. Speculative house-building is non-existent. Multi-family housing is often built by 'construction associations', which following completion register as homeowners' associations.

**Table 16. Housing construction according to type of developer**

	1993		1994		1995		1996		1997		1998	
	Units	(%)	Units	(%)	Units	(%)	Units	(%)	Units	(%)	Units	(%)
Public sector	2677	(32.6)	1231	(17.8)	700	(12.5)	249	(4.4)	382	(6.9)	500	(11.9)
Joint-stock companies	502	(6.1)	281	(4.1)	500	(8.9)	185	(3.3)	66	(1.2)	1786	(42.9)
Cooperatives/ construction associations	2834	(34.5)	1976	(28.7)	2181	(38.9)	2854	(50.8)	2732	(49.1)		
Individual developers	2170	(26.4)	3352	(48.6)	2209	(39.5)	2334	(41.5)	2380	(42.8)	1890	(45.2)
Other developers	32	(0.4)	57	(0.8)	10	(0.2)	2	(0.0)	2	(0.0)	N/A	
<b>TOTAL</b>	<b>8215</b>	<b>(100)</b>	<b>6897</b>	<b>(100)</b>	<b>5600</b>	<b>(100)</b>	<b>5624</b>	<b>(100)</b>	<b>5562</b>	<b>(100)</b>	<b>4176</b>	<b>(100)</b>

*Source:* Ministry of Construction and Urban Development, Housing and Environment in Lithuania Today, Tomorrow and after Tomorrow, National Report for the United Nations Conference on Human Settlements HABITAT II, Republic of Lithuania, (Vilnius, 1998).

*Note:* Data for 1995 and 1998 supplied by the Ministry of the Environment, Vilnius, 1999.

In summary, Lithuania has a relatively high volume of homes per 1000 population compared to most other countries in transition. Nevertheless, economic growth and growth in household spending power, the need to replace outworn stock, cope with future demographic changes and address

current housing market disequilibria (e.g. overcrowding), all point to some urgency in increasing new housing output. The current housing development process does not appear to work smoothly, other than in some parts of the high-end of the market.



# Chapter III

## FINANCIAL FRAMEWORK

Lithuania's housing sector is well into the process of transition: the housing stock is largely privatized, some new types of housing organizations and intermediaries have developed, and there are certain arrangements for trading and mortgaging residential property. However, new housing construction is in the doldrums and arrangements for housing capital reinvestment and maintenance (not least those needed to improve the stock's energy efficiency) are patchy.

This chapter covers housing investment and financing of housing provision. A special emphasis is placed on the development of mortgage infrastructure and mortgage products that enable the operation of the housing market. In addition, it explores changes in housing demand, focusing on housing costs, affordability, housing subsidies and allowances.

### A. Housing investment and financing of new housing construction

#### *Housing investment*

In 1993-1998, the absolute level of investment in housing almost doubled (in current prices), as private individuals became the main contributors to the investment process, particularly following privatization and the elimination of restrictions on private construction. However, housing investment decreased within the portfolio of total investment from some 23 per cent to 7.4 per cent in the 1993-1998 period, as in most countries in transition, due to the collapse of public investment in housing (see **table 17**).

**Table 17. Housing investment, 1993-1998**

Type of investment (in current million litai)	1993	1994	1995	1996	1997	1998
Capital investment	1160	2311	3163	4380	5488	6834
<b>Total investment in housing or residential buildings</b>	<b>266.2</b>	<b>465.3</b>	<b>503.0</b>	<b>570.3</b>	<b>560.5</b>	<b>507.5</b>
- share of total capital investment	22.9%	20.1%	15.9%	13.0%	10.2%	7.4%
<b>1. Public sector investment</b>	<b>79.1</b>	<b>74.0</b>	<b>44.8</b>	<b>36.9</b>	<b>44.6</b>	<b>86.6</b>
in residential buildings						
- share of total investment in housing	29.7%	15.9%	8.9%	6.5%	8.0%	17.1%
<b>2. Private investment</b>	<b>187.1</b>	<b>391.3</b>	<b>458.2</b>	<b>533.4</b>	<b>515.9</b>	<b>420.9</b>
<b>Occupiers' assets</b>	<b>175.5</b>	<b>361.1</b>	<b>429.0</b>	<b>511.1</b>	<b>505.9</b>	<b>394.4</b>
- share of total investment in housing	65.9%	77.6%	85.3%	89.6%	90.2%	77.7%
<b>Other sources of private investment in housing</b>	<b>11.6</b>	<b>30.2</b>	<b>29.2</b>	<b>22.3</b>	<b>10</b>	<b>26.5</b>
- share of total investment in housing	4.4%	6.5%	5.8%	3.9%	1.8%	5.2%

*Sources:* Statistical Yearbook 1999 (Vilnius, 1999);

Data supplied by the Institute of Architecture and Construction, Kaunas, May 1999.

*Private individuals' investment in housing almost tripled in the period 1993-1997. Yet, recent data reveal that there are warning signs that should be addressed. First, the absolute amount of private and other investment started to decrease in 1997. Second, private individuals made 90 per cent of total housing investment in 1997, which indicates that housing is not considered attractive by institutional investors. During the reforms, conditions have not been secure enough to attract potential institutional investors. The housing market remains in the hands of owner-occupiers, which makes it difficult to raise the capital needed to increase housing production, especially when average household income is still very low (see*

*below*). The data confirm that the *significant increase in individual housing investment has been unable to compensate for the shortage of other sources*. Consequently, housing's share in total investment has nearly halved.

In the period 1990-1994, new housing construction decreased by 70 per cent (**chapter II, table 14**). Such falls have been common to all countries in transition (50 per cent on average), but in Lithuania the change was much more dramatic. Construction output grew by 6.6 per cent in 1997 (**chapter I**), mostly due to State investment, but its share of GDP remains relatively low, as shown in **table 3 (chapter I)**. Forecasts by the Institute of

Economics and Privatization show construction increasing to 7.8 - 8.2 per cent of GDP by 2002. The housing sector is not viewed as a major economic force in the Lithuanian economy.

*Financing land development and housing construction*

Although not in physical short supply, the housing land market is developed. Land transactions after privatization doubled in 1997, but the sales of land parcels only account for 1.34 per cent of the total number of transactions (building sales represent 14 per cent).<sup>28</sup> Complexities arise from local, county and State involvement in the disposal of public land. The process of land acquisition by legal entities is not clear and transparent, although the tender procedure is used for these purposes. There are further complexities in developing leased land. Nevertheless, the active privatization of the housing stock and State-run industries means that attention is now focused on State-owned land. The State is about to privatize much of its land holdings and this offers a number of opportunities.

*There is also very limited financing available for housing land acquisition and development.* There is no banking lending system for the process, although land, with all future modifications, can be pledged. The major reason is that banks do not consider undeveloped land as being sufficiently liquid collateral. On the other hand, there are few commercial enterprises that specialize in financing land development and the demand for such loans is very limited.

At the moment municipalities are responsible for infrastructure development, but budget restrictions impose severe constraints. Local governments are heavily dependent on central government transfers with very limited opportunity to generate revenues of their own. Overall, the lack of adequate land development financing leads to a significant shortage of land parcels with developed infrastructure available for sale. In 1998, the Ministry of Finance proposed the Lithuanian Municipal Development Programme to assist in the development of a system of municipal investments in infrastructure and municipal services and so support the reform of local government finance.

The programme seeks to provide training, technical assistance and investment support to about 40 of the 56 municipalities by the year 2002 using lines of credit provided by foreign and international financial institutions. Subprojects funded through the Municipal Development Programme will focus on infrastructure loans that can be repaid through user fees. In most cases the municipal enterprise will be the final borrower, and the municipality will guarantee the loan (in accordance with the Law on Municipal Borrowing).

The Law on Municipal Borrowing specifies the following conditions:

- Outstanding debt principal cannot exceed 20 per cent of annual revenues. In exceptional cases the Ministry of Finance may allow an increase up to 50 per cent;
- The annual borrowing limit of a municipality is 10 per cent of annual revenues, including a 5 per cent limit on short-term borrowing;
- The annual debt service related to borrowing cannot exceed 10 per cent of annual revenues;
- The municipality or its enterprise should contribute at least 10 per cent of the total cost of the investment and project preparation costs.

Shortages of affordable and accessible housing construction finance are manifested in recent trends in the sales of new housing, escalating construction prices, a reduced volume of housing production, as well as an increasing number of uncompleted dwellings. *Existing arrangements for new construction finance are still far from efficient and new construction finance continues to be a problem.* Significant changes have taken place in the financing of residential construction during the period of transition. The Government's policy focused on defining its new role from a major developer and supplier of new housing to enabler, providing State support for new construction financed through personal savings. Housing finance reforms centred mainly on:

<sup>28</sup> Data provided by the State Cadastre and Register, Vilnius, May 1999.

- Re-allocating responsibilities from the State in housing construction finance;
- Establishing extrabudgetary State and self-government support funds for construction;
- Reducing significantly the direct finance of construction through both the State and municipal budgets.

The reduction in direct State financing was supplemented with a governmental programme for subsidized construction financing ('Bustas'). Housing construction associations (cooperatives) and individuals on the waiting lists could apply for a 5 per cent interest rate construction loan over 25 years, interest-free for 3 years and with a 80-90 per cent loan-to-value ratio. The subsidies are paid from the General Support Fund raised from revenues from housing privatization, land sales and the State budget. Municipalities also created their construction funds, which get 10 per cent from the State fund resources. This programme is expensive to the Government and in 1996 amounted to approximately 3.4 per cent of the central Government budget.<sup>29</sup>

*The availability of cheap financing from State funds and tax privileges made the provision of new housing through construction associations (cooperatives) particularly attractive until 1995. Most of the funding designated for low-interest loans was assigned to these organizations. During 1993-1995, they received 129 billion litai in low-interest credit. After that, existing cooperatives were re-registered as housing construction associations to complete the construction process. Subsidized construction finance is no longer available to housing construction associations and supports only the completion of housing.*

Lithuania's current system for construction finance has the following basic characteristics:

- Informal financing of construction by private individuals is the predominant form. It relies on small, personal savings, sometimes organized into mutual forms of finance, such as construction associations. This leads to an unprofessional approach to financing where owners become 'self-developers' with little opportunity to effectively manage the risks associated with the development process;
- Development companies sometimes organize future buyers into associations, supplying them with building and developer services, which allows some tax advantages and easier access to public funding;
- Limited direct State financing of the construction of public housing and for target groups, with plans that municipal financing should make up not less than 15-20 per cent of construction investment;
- Low levels of commercial construction finance available to those able to manage effectively development and construction risks, to improve construction technology, and develop the construction industry through competition.

The last point is illustrated by information presented in **table 18**. The value of total housing loans to the value of all outstanding loans in both commercial and government financial institutions in the fourth quarter of 1995 was 12.5 per cent. In September 1999 it decreased to a mere 3.5 per cent. A network of temporary subsidiary companies also undertakes some of this activity.

<sup>29</sup> Staff Appraisal Report Republic of Lithuania Energy Efficiency/Housing Pilot Project, The World Bank, 1996.

**Table 18. Loans for construction <sup>a/</sup>**  
(In thousands of litai)

	Loans for construction	All loans	Share
I quarter, 1995	328,847	3,639,296	9.0%
II quarter, 1995	351,192	3,643,122	9.6%
III quarter 1995	380,761	3,676,331	10.4%
IV quarter, 1995	387,072	3,107,937	12.5%
I quarter, 1996	390,400	2,875,211	13.6%
II quarter, 1996	393,721	2,828,685	13.9%
III quarter 1996	402,174	3,005,328	13.4%
IV quarter, 1996	334,769	3,041,866	11.0%
I quarter, 1997	131,286	2,844,587	4.6%
II quarter, 1997	115,751	2,656,901	4.4%
III quarter 1997	116,313	2,831,685	4.1%
IV quarter, 1997	128,474	3,231,757	4.0%
I quarter, 1998	100,112	3,338,776	3.0%
II quarter, 1998	129,447	3,455,029	3.7%
III quarter 1998	140,533	3,671,283	3.8%
IV quarter, 1998	140,387	3,993,875	3.5%
I quarter, 1999	149,344	4,577,258	3.3%
II quarter, 1999	188,913	4,968,634	3.8%
III quarter 1999	180,880	5,097,243	3.5%

Source: Bank of Lithuania: Statistics – Loans by Economic Activities, <http://www.lbank.lt>

<sup>a/</sup> Data refer to end of period.

In summary, *Lithuania at the moment has a limited capitalized and institutionally backed development sector with little support for entry-level firms.* Housing development remains fragmented.

## B. Factors affecting demand for housing

### Savings

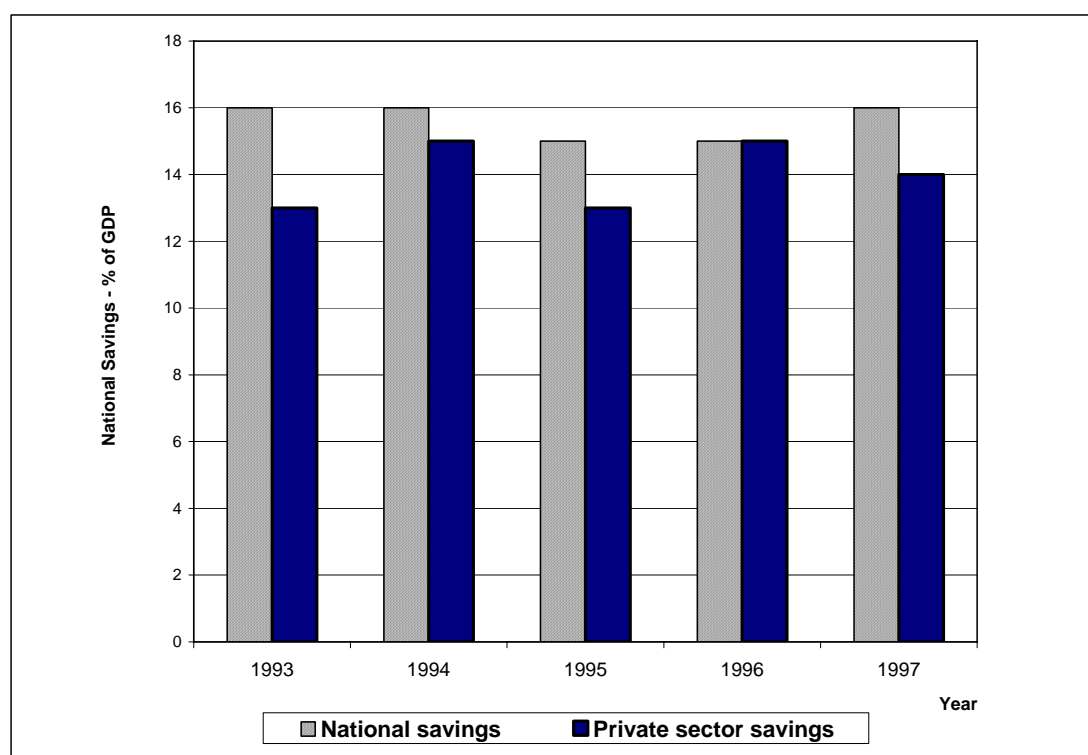
Like other countries in transition, Lithuania started its economic reforms without sufficient local financial resources and savings. At the end of 1997, bank deposits equalled 5.9 billion litai, of which

private account deposits stood at 2.2 billion litai. Foreign currency deposits equalled 2.3 billion litai and stood at 39 per cent of local and foreign currency deposits. The banking sector has not accrued sufficient savings, especially for long-term lending. With a predominance of short-term deposits, bank deposits comprise only 15.4 per cent of GDP. In more successful economies in transition they stand at 30 per cent.<sup>30</sup>

During the transition the Government has failed to develop efficient tools to prompt growth in national and private sector savings, which remain low (see **fig. VIII**).

<sup>30</sup> United Nations Development Programme, *Lithuanian Human Development Report 1998* (Vilnius, 1998).

**Figure VIII: National savings  
(In per cent of GDP)**



*Source:* United Nations Development Programme, *Lithuanian Human Development Report 1998*, (Vilnius, 1998).

The situation with respect to household savings is similar, though it might be considered better in terms of total savings and investments' share of household income according to data<sup>31</sup> in **table 19**. Policies need to be developed to attract private savings and investments into the housing sector. Specifically, there are no financial instruments, such as housing, municipal or private developer government-guaranteed bonds, notes or

other housing-related securities, which could become an attractive savings instrument for channelling funds into housing construction or purchase. Investment funds designed for equity investment do not appear to operate due to the lack of an adequate legal base and unfavourable tax treatment. Furthermore, credit unions (or savings and loan financial institutions) do not yet play a significant role in the financial market.

<sup>31</sup> The data provided in the table 19 are not official and are used for illustration only. To collect data, the Institute uses expert opinions instead of a household budget survey. It should be interpreted with care. The author preferred the data for two reasons. Firstly, the shadow economy exists, only part of the population declares its income and consumption expenditure exceeded the disposable income per capita in 1997-1998. Secondly, the official statistics do not yet show income from savings and investments.

**Table 19. Monthly household income, 1st half of 1998  
(In litai)**

Indicator	City	Town	Rural
Household income	2,186	1,635	996
	100%	100%	100%
Household savings	313	204	110
	14.3%	12.5%	11.1%
Household investments	264	164	80
	12.1%	10.0%	8.0%
Household savings and investments	577	368	190
	26.4%	22.5%	19.1%

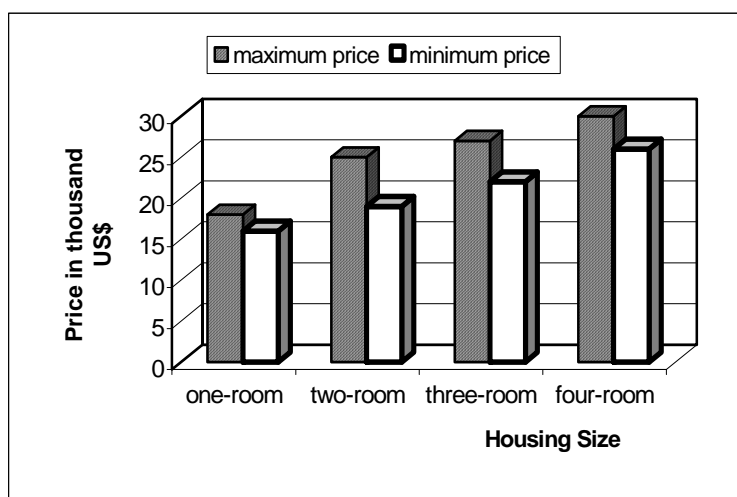
*Source:* Lithuanian Free Market Institute, *A Survey of Macroeconomic Variables in Lithuania 1998/99* (Vilnius, 1999).

### *Incomes and affordability*

Following a dramatic fall at the start of the transition, personal income experienced some positive growth and adjustment. Monthly disposable income started to increase and in 1997 equalled 368.92 litai per household member. In general, household income has also increased, however salaries vary significantly and roughly 8 per cent of the employees in 1997 had a monthly salary above 1,500 litai.<sup>32</sup> Income inequalities remain relatively high. The Gini index, which reflects the extent to which the distribution of income among individuals within an economy

deviates from perfectly equal distribution, was 0.31 for Lithuania in 1997. In eastern European and the Baltic countries the index fluctuates between 0.25 and 0.34.<sup>33</sup> Consumption inequality in Lithuania is increasing also. According to the 1998 Lithuanian Human Development Report, as many as 37.2 per cent of households with three children or more are poor; and more than a quarter of the rural population is impoverished. The incidence of poverty among those with primary and secondary education is six to seven times higher than among those with a tertiary education.

**Figure IX: Prices of standard flats in Vilnius, 1998**



*Source:* Data supplied by the State Land Cadastre and Register, May 1999.

<sup>32</sup> According to the Housing Credit Foundation, Vilnius, May 1999.

<sup>33</sup> United Nations Development Programme, *Lithuanian Human Development Report 1998* (Vilnius, 1998).

*Despite positive trends in income growth, house purchase remains unaffordable for a large number of Lithuanian households.* Calculations based on household income and savings data in **table 19**, as well as house price data, show that it will take 10 to 14 years of saving to become a flat owner in Vilnius. The estimate reflects the situation in the first half of 1998 and is based on the assumption that the average household with an average income will be purchasing a standard 2-room flat in Vilnius. As the available data suggest, there is a significant variation between the maximum and minimum price of units with different sizes (see **fig. IX**), however, house-price-to-income ratios remain high. Clearly, most new households will not be able to purchase housing without mortgage or other support. It should be noted that house purchase assistance must be carefully targeted. Given the mass privatization of the housing stock, most existing households wishing to move will have an asset to sell or rent out to generate net income. This needs to be factored into any assessment of affordability.

While new households clearly face affordability problems to access the homeownership market, housing costs in the public rental sector appear to be modest. According to time series data presented in **annex II**, rental housing is more affordable and on average housing costs -- rent together with utilities (fuel, electricity and gas) -- have fallen and constitute 14.4 per cent of total household expenditures. In 1998 these costs were higher for urban households -- 15.0 per cent -- and relatively lower -- 12.4 per cent on average --

for rural households. Local experts indicate that, for some groups, housing costs might be as high as 30 per cent, mostly due to increasing utility prices.

Fees for hot and cold water and sewerage increased 14- fold in 1993-1998; heating costs 6.8- fold; gas and electricity 2.6- fold. It is estimated that about 20 per cent of the households in Vilnius have difficulties in covering utility costs, and if adequate maintenance were to be carried out up to 40 per cent of homeowners might have financial difficulties sustaining their status.<sup>34</sup> It has been suggested that official statistics related to income are not reliable and should be interpreted with caution.

#### *Housing subsidies, taxes and allowances*

The Lithuanian Government is under pressure to balance its budget and reduce public spending. Public financial support for housing is limited, although different types of direct and indirect governmental support related to housing have been introduced during the period of transition (**table 20**). Governmental Resolution 794 of June 1999 indicates a commitment to distribute funds from the General Fund for Housing Construction and Acquisition for the period 1999 - 2000 and to establish municipal housing funds. The aims of these funds are: (i) to promote the construction of new residential buildings; (ii) to facilitate the modernization of existing municipal housing; and (iii) to assist the purchase of dwellings at market prices.

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<sup>34</sup> Vilnius Municipality, A housing policy for the city of Vilnius. Proposal, p. 6.

**Table 20. Main support schemes, 1997**

	Type of support	Financial source	Amount allocated in one year (million litai)
<b>BUSTAS</b>	Subsidy element of soft loans	Extrabudgetary fund	17.7
<b>Heat and hot water</b>	Subsidy	National budget	230
<b>Energy saving</b>	Subsidy element of soft loans	World Bank loan & Lithuanian counterpart funding	1 (approximately)
<b>Support for municipal housing acquisition</b>	Grants	National budget	10 (in 1998)
<b>Indirect support for municipal services</b>	Hidden subsidy		250 (approximately)
<b>Indirect support for tenants in public rental housing</b>	Hidden subsidy		375 (estimate)

*Source:* Danish Ministry of Housing and Lithuanian Ministry of Construction and Urban Development, *Study on Government Assistance Programmes to the Housing Sector* (Vilnius, August 1998).

Though rents in public sector housing remain very low, rental subsidies are slowly shifting away from general support (available irrespective of income) towards personal, means-tested support. According to a draft law, 135 litai per person per month is the basis for calculating rent allowances. For households earning less than twice this amount per person, rent allowances are paid irrespective of the rental sector. However, rent allowance schemes are complex and have perverse incentives (including unemployment and poverty traps, the need to encourage households to find the lowest rents and the need to integrate with other welfare benefits). Similar observations can be made concerning energy cost allowances (especially the need to encourage households to use energy more efficiently) - a much larger subsidy in Lithuania, as energy costs have risen much faster than rents and are reaching world-market levels.

Property taxes can have a number of aims, including the raising of revenue (possibly earmarked for particular uses), the promotion or reduction of demand, or the promotion of equity. In Lithuania, the main taxes affecting housing include a tax on developed land, value-added tax on construction, a capital gains tax, and corporate taxes on developers, private landlords and homeowners' associations. These, and relief when offered, have a

significant impact on the housing market, but this appears uncoordinated by the Government. For example, VAT is not levied on construction renovation or insulation work or the design of houses and flats funded from the State or municipal budgets. Furthermore, VAT may be reimbursed, but only to those entities that have registered as VAT payers with the State Tax Agency. Usually, physical persons or construction associations are not on the Register of VAT payers. Therefore, the VAT they pay may not be reimbursed.

### C. Mortgage markets

#### *Financial institutions and mortgage market infrastructure*

*One condition of mortgage market development - macroeconomic stability - has been met.* In addition, Lithuania has positive economic growth, strict control over its public expenditure, low inflation and short-term currency stability. In this environment real interest rates are becoming positive whilst nominal interest rates are falling to levels where it becomes possible for potential mortgagors to afford the use of mortgage instruments and to service the mortgage with their incomes (see **table 21**).

**Table 21. Average nominal interest rates and inflation  
(In per cent)**

Indicators	1993	1994	1995	1996	1997	1998	1999
Inflation			35.7	13.1	8.4	2.4	N/A
General government securities		21.43	27.48	20.46	8.90	11.18	11.87
Time deposits <sup>a/</sup> in:							
Litas	90.40	48.43	20.05	13.95	9.01	7.44	8.07
Foreign currency	23.58	24.91	15.97	9.36	6.43	5.05	6.38
Loans <sup>b/</sup> in:							
Litas	91.82	62.30	27.08	21.56	14.39	12.21	9.92
Foreign currency	68.70	51.98	26.93	21.63	12.39	10.28	11.11

*Source:* Lithuanian National Bank, January 2000 <http://www.lbank.lt>

<sup>a/</sup> Data for 1997 and onwards refer to time deposits for 2 and more years. Data before 1997 refer to shorter maturity time-deposits.

<sup>b/</sup> Data for 1999 refer to housing loans while the rates for other loans were slightly higher: 13.09% in litas and 11.46% in foreign currency.

N/A – not available.

*A second important condition of mortgage market development - strong financial institutions - is in its infancy in Lithuania.* The structure of credit institutions has developed (**table 22**). At the same

time the State increased bank deposit insurance from 4,000 to 25,000 litai. Total borrowing from foreign financial institutions recently doubled.<sup>35</sup>

**Table 22. Credit institutions, January 2000**

Type of institution	Number of institutions
Deposit money banks	10
Other banks	2
Foreign banks branches	3
Foreign banks representative offices	4
Credit unions	33

*Source:* The National Bank of Lithuania, Credit institutions, <http://www.lbank.lt>

<sup>35</sup> Sources of information: LB: Statistics – Loans by Economic Activities, <http://www.lbank.lt>; United Nations Development Programme, *Lithuanian Human Development Report 1998* (Vilnius, 1998).

The financial system is slowly becoming stronger. The banking sector started to recover in 1997 after the 1995-1996 crisis. The assets of commercial banks by the end of 1997 comprised 8.3 billion litai and increased by 40 per cent over the year. In 1999, the consolidated assets of banking institutions including commercial banks, foreign bank branches and credit unions reached nearly 12.5 billion litai. Services rendered grew by 18 per cent. The volume of loans grew 2.1- fold. However, relatively weak and inefficient private commercial banks continue to operate in the market. The Bank of Lithuania has not taken adequate action to speed up re-capitalization of these banks. They do not have sufficient funds to grow. Only two commercial banks have significant funds, the largest has assets worth some 2.5 billion litas, but is still oriented towards commercial lending. Commercial banks operate on a very short-term deposit base. Time deposits exceeding 6 months constitute only 12 per cent of the total deposits made. The majority of terms of deposit agreements vary from less than one to three month<sup>5</sup>.<sup>36</sup> There are no specific housing savings banks/mortgagees and inter-bank lending is insignificant.

A major reason for the slow development of the banking sector is that most banking assets still belong to the State. By the end of 1997, close to 50 per cent of all banking assets were State-owned. During the reforms, three State banks were poorly managed and funds from the State budget (loans received on behalf of the State and privatization revenues) were used to cover the losses in the operation of the State banks. Despite political approval, the privatization of the State banks was postponed.

Traditional long-term investors in the mortgage market, such as private pension funds and life insurance companies, are also poorly developed, thus limiting the availability of long-term resources. A law on pension funds is under discussion in the Seimas. Its adoption may stimulate the development of long-term financial instruments. At the moment the major sources of long-term money are the State budget, an extrabudgetary Supporting Fund and governmental external debt. Long-term private sector debt does not play a significant role and in 1997 it was only

4.6 per cent of total external debt. Another financial institution that usually plays a major role in the financial markets are investment funds, but they are non-existent in Lithuania. Several joint-stock investment companies were reorganized into controlling investment companies, but they are very small and limited in their investment policy. Their number is declining.

The weakness of the banking and capital markets has hindered the development of a secondary mortgage market. Such a market can encourage the operations of the primary mortgage market by improving liquidity and diversifying risk. A stronger, more widely based set of financial institutions is also likely to allow longer-term and more varied (e.g. fixed rate, capped, discounted) mortgage products to be developed. However, a mortgage securitization system is currently being proposed. The basic objective is to assist the Lithuanian financial sector and capital markets to adopt the European Union's legislation and to support integration into the single market of the European Union. Within this context, Government policy relating to mortgage market development should be refined.

*The third condition of mortgage market development - its infrastructure elements - has begun to take shape in Lithuania.* With the privatization of the nation's housing stock, a real estate market has developed with the sale, re-sale and purchase of housing. The liquidity of the real estate market increased with the growth of new players such as real-estate agents and certified independent surveyors. Lithuania has a Central Real Estate Register and 15 regional offices. From April 1998 to March 1999, 28000 real-estate objects were registered as collateral valued at 7.5 billion litai, while loans granted were valued at 5.5 billion litai.<sup>37</sup>

In summary, many of the foundations of a mortgage market are in place - strengthening economic fundamentals, an improving banking sector and a real-estate market. Furthermore, the Lithuanian Government has indicated its intentions to expand mortgage lending. An agreement between the Danish Minister of Economic Affairs and the Lithuanian Finance Minister has been concluded with the aim of strengthening the mortgage lending system.

<sup>36</sup> Data supplied by the Housing Credit Foundation, Vilnius, 1999.

<sup>37</sup> <http://www.lrytas.lt>

*Mortgage products*

The Lithuanian Government is directly involved in retail mortgage activity offering subsidized mortgage products. This practice prevents the development of commercial mortgage lending and restricts its efficiency in terms of all-in costs and affordability to consumers. The Government continues to finance mortgages while commercial mortgage lending is just emerging. In short, the presence of the former may be hindering the development of the latter. So *the existing mortgage lending system consists of two separate sub-systems operating on different principles*. The first is through the State support programmes based on non-market principles and the second is from commercial banks based on commercial principles.

A hybrid system, using Government guarantees, is in the offing.

In 1992, the Law on State Support for the Provision of Dwellings for Citizens was adopted. Residents can apply for a subsidized loan for the acquisition or construction of a house or flat. The main characteristics of the loans offered through the State programmes are presented in **table 23**. As discussed in section B (housing subsidies), these loans have highly subsidized interest rates and the Government pays part of the principal. They are available only to a limited number of people within the target groups. The General Fund for Housing Construction and Acquisition has approximately 300 million litai and does not make a profit.

**Table 23. Terms of mortgages through the «BUSTAS» programme**

<b>Commercial banks</b>	Savings Bank (former State bank) Vilnius Bank
<b>Interest rate</b>	5% annual rate; the difference with the market interest rate charged by the commercial bank is covered by the Support Fund.
<b>Other terms</b>	No interest for families on social benefits; 20% discount on principal for orphans; 10% discount on principal for families with disabled members; interest and discounted part of principal are covered by the General Support Fund.
<b>Maturity</b>	Up to 10 years for the purchase of a dwelling; up to 12 years for the construction of a dwelling (Savings Bank only).
<b>Currency</b>	Litas (Savings Bank only); US\$ (both banks)
<b>Loan-to-value ratio</b>	Banks grant a loan up to 90% of the pledged property market value; the down payment varies from 10% to 30% of the dwelling value.
<b>Required income level</b>	Vilnius Bank: monthly mortgage payments shall not exceed 40% of family's net income; and 500 litai per family member shall remain after monthly payment on the loan. Savings Bank: monthly mortgage payments shall not exceed 40% of family's net income
<b>Repayment</b>	Vilnius Bank: monthly annuity repayment, monthly grace period. Savings Bank: dwelling purchase loan – up to one year's grace period; construction loan - 3 years' grace period for principal with quarterly payments; interest on both products paid monthly the month after the loan is granted.
<b>Collateral and insurance</b>	The dwelling shall be pledged and insured; life insurance for 30% of the mortgage.

In 1997, only 1,380 households were granted privileged loans through the State programme. Yet, nearly 8 per cent of all residents (some 90,000 households in urban areas) are registered for State support and it takes six to ten years to receive a loan. There is also a high drop-out rate between initial expressions of interest and mortgaging. Funds allocated for this purpose from the State budget were insufficient even to meet the needs of those on benefit. The programme envisaged the construction of 65,000 flats between 1995 and 2000, or 13,000 per year. Meanwhile, during 1996-97 only approximately 11,000 flats were built.

A *government-guaranteed mortgage insurance system is being developed*. In 1999, the Housing Loan Insurance Company was registered with 7 million litai of capital and 95 million litai allocated for the purpose of eligible loans insurance. Mortgage insurance will be provided if the following conditions are met:

- Loans must be for house purchase, construction or renovation;
- 10 – 20 per cent down payments;
- 15-year maturity loans;
- Insurance premium paid up-front by the Government, with insurance fund taking 90 per cent risk and the bank 10 per cent;
- Principal and interest payments not exceeding 40% of household income.

In short, if households meet the eligibility criteria of the scheme and of the bank, then Government-backed insurance will be forthcoming. Households on the waiting lists will be eligible for Government-guaranteed mortgage insurance. The scheme is a welcome development, but a number of issues need to be monitored:

- Whether cost-to-value differences impede applicants;
- Whether Government, particularly the Ministry of Finance, is content to have an open-ended scheme, not cash-limited;
- Whether relatively low down payments impede the development of savings, sound credit histories, and wider mortgage market development;
- How far the availability of Government insurance impedes the commercial, including risk appraisal, approach of the banks.

There may be other means to stimulate the effective demand for mortgages. Part-buy, part-rent schemes and/or equity share schemes may allow some middle-income households to purchase housing at a modest cost to the public purse. However, they are inherently complex and may require further legislative change.

**Table 24. Commercial mortgage financing offered by the major banks**

Interest rate	9.5-13.5%
Term	No-longer than 10 years
Currency	Mainly in US\$
Size of a loan	70% of a dwelling's market price
Required income level	Monthly mortgage payments shall not exceed 40% of borrower's income
Required income for mortgage: Loan size – 100,000 litas Interest rate – 11% Term – 10 years	Net family income should exceed 3,500 litai

*Source:* Data supplied by the Housing Credit Foundation, Vilnius, May 1999.

*Commercial mortgage lending is not well developed.* At present, only three commercial banks offer residential mortgages, although other commercial banks occasionally offer limited mortgage funds, often to their own employees. One foreign financial institution (the Baltic-American Enterprise Fund) has also started a mortgage programme lending US\$ 5 million in residential mortgages.<sup>38</sup>

As in many countries in transition, the mortgage instruments offered by commercial banks are expensive in terms of high interest rates and short maturity. They are affordable only to high-income groups as indicated in **table 24**. Usually the loan is denominated in a foreign currency because the local currency is considered to be overvalued. This currency risk further increases the borrower's risk and correspondingly leads to a low volume of mortgage operations in the private banking sector. Long-term residential mortgage lending is still considered by the private banking sector as particularly risky. To compensate, the banks have significantly increased their margin over the cost of funds they use to finance mortgages. The margin between the interest charged and one-year deposit interest rates varies between 5-8 per cent. In a well functioning housing market, the value of this indicator should be positive but with the housing loan rate only modestly higher than the cost of the funds (on average 1.5-2 per cent).

In summary, the risks associated with mortgage lending remain high and the private banking sector remains a reluctant mortgagee, preferring to lend to larger legal entities. *Indeed, although housing has been largely privatized in Lithuania, housing finance has not.*

#### **D. Financing of maintenance and renewal**

##### *Maintenance and renewal of multi-family housing*

Much of this previous analysis concentrates on increasing the development and financing of new housing production. However, even in periods of rapid expansion of the housing stock, the management, repair and improvement of the existing one remains central. Three factors compound this importance in Lithuania:

- Lithuania's housing stock expanded rapidly at particular periods in the 1960s, 1970s and 1980s using particular building forms and methods. These properties will age and suffer the same elemental failures at the same time;
- Multi-family blocks of flats, requiring special management and maintenance arrangements for common parts and common services (compared to single-family dwellings), dominate the housing stock;
- Mass privatization of the stock in the early 1990s was undertaken without a robust legal and regulatory framework. However, tenant/landlord relationships have to be replaced by client/contractor relationships with related organizational and financial changes.

First, there is a need for accurate information on the conditions of the housing stock. An accurate sample survey is a first step towards assessing current conditions and disrepair, the timing and the extent of future repair and improvement requirements and the costs.

Second, there is a need to examine ways of increasing the funding for house repair and improvement. Specifically, the following might be explored:

- (a) The provision of 'sinking funds' built up over time to cope with future major repair expenditure;
- (b) The need to develop home improvement equity loans;
- (c) The need to develop some form of home improvement subsidy arrangements for the most intractable cost-over-value cases, particularly for those households on low incomes.

Third, and given the number of owners in individual multi-family blocks, there is a need to bring them together as single purchasing 'clients'. There has been some success in promoting homeowners' associations. These offer a range of benefits in the management, maintenance and improvement of multi-family housing. However,

<sup>38</sup> Data supplied by the Baltic-American Enterprise Fund, Vilnius, 1999.

only 4,500 have emerged so far. There appear to be a number of financial and other means to further expand coverage through:

- (a) The proposed legislative changes which do not require homeowners' associations membership but do require all households to abide by the decisions of properly constituted homeowners' associations;
- (b) Tax incentives for homeowners' associations, perhaps through tax relief to individual households for sinking fund or other maintenance contributions;
- (c) Making energy efficiency or other home improvement grants and subsidies dependent on the existence of a properly constituted homeowners' associations. The Energy Efficiency Housing Pilot Project of the World Bank offers grants and loans via homeowners' associations for energy efficiency improvements. Some 30 homeowners' associations have been sponsored in an 18-month period;
- (d) Making the payment of fuel subsidies dependent on the presence of a properly constituted homeowners' associations;
- (e) Making property maintenance subsidies, now available through municipalities and municipal maintenance companies, payable directly to homeowners' associations.

#### *Maintenance and renewal of public housing*

There are no available data on income and expenditure in public housing. However, following mass privatization the stock apparently contains older and often sub-standard units, scattered through different multi-family buildings. Low rents -- from 0.2 to 1.7 litas per m<sup>2</sup> per month -- do not allow cost recovery of management and maintenance work. The deficit between actual income and required expenditure is currently being managed by simply not carrying out the long-term maintenance work required. The backlog of repairs and improvements in public housing is increasing. While public-sector rent adjustment appears to be long overdue, it can be questioned whether it is appropriate to require the current tenants of public housing to bear all the costs of the mistakes of the past. There is uncertainty about their willingness and ability to do so.

A broad way forward for addressing the above gap between current income and required expenditure for maintenance and renewal is to gradually liberalize rents. Basic rent fees should take into account the depreciation from the updated procurement price of the flat, repair work and maintenance, and management overheads. Simultaneously with the first adjustment of the rent fees, it is necessary to provide subsidies for households with a low income.

#### *Expanding rental housing*

There will continue to be a number of new households unable to become owner-occupiers. Intervention, through some form of subsidy, will be required. This subsidy could be provided to increase the already, extremely high levels of owner-occupation. However, such an approach imposes high repair costs on households with low incomes, and may prevent reinvestment in the existing stock reaching sustainable levels.

*An expanded and more vibrant rental sector is required.* Any successful rental housing system should offer choices to households and a coherent rent structure and be regulated. This would allow landlords to be properly capitalized. In addition, the rental system needs to have revenue streams, covering at least operating costs, that is management, maintenance, and insurance costs. Within these broad parameters, a number of models, or more likely a number of combinations of models, are possible:

- The continuation and re-expansion of municipal rental housing;
- The design and promotion of a non-profit (or non-profit distributing) housing for rent sector (possibly community-based and/or aligned with expanded homeownership associations and/or municipal maintenance companies, once outside the municipal sector);
- The expansion, and where necessary the licensing and regulation, of the private, profit-making, rental sector.

In relation to these options the State will need to examine:

- 
- The form of subsidy (capital or revenue; to producer or consumer, i.e. whether in the form of general – ‘bricks and mortar’ - or personal subsidies);
  - The extent to which subsidy is to bodies outside public finance controls, which can lever private finance;
  - The transfer of risk from State to private and independent sectors;
  - The degree it wishes to regulate organizations operating in a subsidized market.

It is not possible to fully consider all these options in this report. However, they do need the attention of policy makers, landlords and financial institutions if the sector is to play its full role.



# Chapter IV

## LEGAL FRAMEWORK

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### Introduction

Developing an adequate legal framework for the housing sector is one of the major tasks in the transition from planning to markets. Lithuania has made significant progress in establishing the key legal documents that enable the operation of housing markets. At the risk of over simplifying an apparently very complicated process of legal adjustment, major acts affecting the housing sector are identified in **figure. X**. The analysis focuses on major changes introduced in the legal framework that affect owner-occupied and rental housing, as well as the development process. Special emphasis is placed on legal reforms affecting the financial aspects of housing – subsidies, taxes and credits.

An important act for the housing reform was passed in 1992. The Law on the Provision of Dwellings for Citizens sets the framework for transition from a centrally planned to a market-based housing system. According to the Law, each citizen has the right to housing, either through homeownership (new construction or purchase of existing housing on the market), or through renting from municipalities or other legal entities. The number of houses or flats, as well as their size, is not limited. Citizens may build their own house/flat, or establish a housing construction association, which operate according to municipal by-laws. Restrictions on private ownership have been abolished. Citizens are allowed to own, dispose of, rent or mortgage their residential property. Furthermore, limitations on mobility in larger cities, including Vilnius, have been abolished.

The housing registration system has been revised. Previously registration was linked to housing need based on housing consumption lower than 5 m<sup>2</sup> per member of the household. Waiting lists for housing provision were drawn up in State enterprises, organizations and cooperatives for housing construction. At the end of 1987, 143,700 applications from families and individuals were registered. According to the Law on the Provision

of Dwellings for Citizens, municipalities must maintain a register of households in need of housing. The waiting lists in early 1995 included 98,500 households (**table 25**), 92,500 in urban areas, 6,000 in rural areas. By early 1999, there were 104,972 households on the waiting lists. Estimates suggest that social support might be extended to 10 per cent.

Other important regulations for the housing reform are the Lithuanian Civil Code and the Housing Code approved in Soviet times. At present, a new law on housing is under preparation. Interviews with ministry officials indicate that regulations related to housing ownership, management and operation are also being prepared.

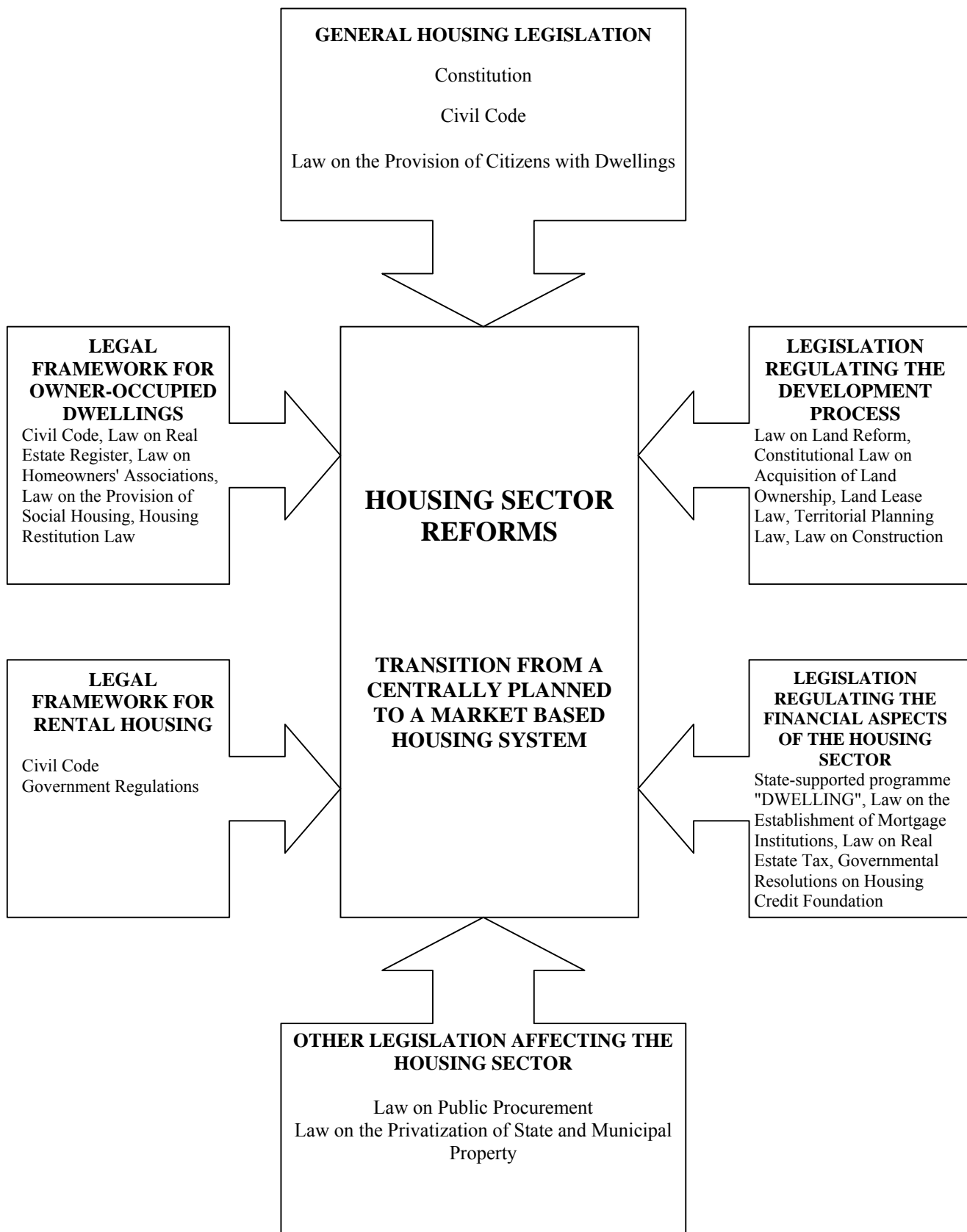
### A. Privatization and restitution

The Law on the Privatization of Dwellings (1991) gave citizens the right to “privatize” municipal or State-owned rental housing. Privatization was implemented very quickly, with 77 per cent of the housing stock being transferred to sitting tenants by early 1995. Buyers could proceed in the following ways:

- Buy making a single cash payment;
- Buy using vouchers for up to 80 per cent of the price;
- Buy in instalments, with a minimum down payment of 10 per cent of the price.

By 1996, 22.6 per cent of the dwellings were privatized through cash payments and 76 per cent through vouchers. The 'right to buy' had to be requested before 1 July 1998. It should be noted that *privatization legitimized existing housing inequalities*. Some of the residents were entitled to “privatize” a room in a hostel, while others had the chance to privatize good-quality, spacious flats. In other cases, the new owners acquired a liability rather than an asset, given the massive need for investment in repair and renovation.

**Figure X. Housing legislation**



A law on the order and conditions of restitution of real property was passed in 1991 and went into force in June. The Restitution Law returned nationalized property to the former owners or their heirs (see also **chapters I and II**). It also specified payment of compensation (cash, vouchers or real estate) if the enforcement of property rights was physically impossible. Land within Vilnius is restituted within a limit of 1 ha. *The implementation of restitution has been problematic*. In 1998, the rights to residential houses were restored to 4,565 claimants out of 8,544 (or 53 per cent). Eviction of tenants in these properties normally causes tension. By 1999, there were still 7,727 households that had to be evicted, while 2,973 tenant families had been relocated.<sup>39</sup> Resolution No. 805 (October 1992) on the Housing Programmes for Tenants of Dwellings Returned to Their Owners provides the legal framework for solving these problems. During 1994, 6.2 million litai were allocated to provide alternative housing to tenants affected by restitution, supplemented by 9 million litai in various forms of targeted assistance. In 1998, 21 million litai were allocated for evicted tenant families. In all 51.4 million litai have been spent since the adoption of the Law.

## B. Owner-occupied housing

### *Housing markets and real estate registration*

A number of changes in the legal framework facilitate the operation of the real estate market. There are no restrictions on any Lithuanian or foreign entities owning and purchasing real estate, including residential properties. However, ownership of real estate is separated from ownership of land - the property right to buildings does not itself create the property right to land on which these buildings are located. According to article 255 of the Civil Code, contracts for the sale and purchase of buildings must be concluded in writing and must be certified by a notary. The following main documents should be presented to the notary:

- The original documents of the initial acquisition of the building;
- The inventory file of the building (the legal registration of the building will be carried out only after its technical inventory);
- Different certificates on building issued by the State enterprise of Land Cadastre and Register (one is issued as permanent

evidence of ownership and the other is issued for certain transactions with the property (sale, rent, etc.) and is valid for 15 calendar days);

- The purchasing company's registration certificate;
- The decision of an authorized governing body of the company to purchase the building;
- The power of attorney issued by the company to the person signing the contract to sell or purchase the building.

The last three items apply only to sales or purchases of buildings where at least one party is a company.

In September 1996, the Law on the Real Estate Register was adopted. It came into effect on 1 April 1997 and was amended in October 1997. It specifies that the ownership and other property rights (except mortgages) become officially enforceable after their registration with the central data bank of the Real Estate Register. The State Enterprise of Land Cadastre and Register manages the Register.

The following are registered there:

- Plots of land, buildings, flats in multi-storey houses, other premises and engineering equipment which are registered with the National Inventorization, Projecting and Service Bureau;
- The rights to manage the real estate, including the rights to rent it long term (more than three years), rights of use, easements (except those specified by the Planning Law);
- The restrictions on rights to real estate - repossession, restrictions on changing its main purpose, insolvency of the owner, a condition not to transfer the real estate to a third person;
- The obligations of the owner of the real estate - e.g. repayment of debt for the purchased property.

The right to register real estate and the above-mentioned rights is conferred on natural and legal persons purchasing or acquiring the rights to use real estate according to Resolution No. 85 of 22 January 1998<sup>40</sup>. The register is open to the public,

<sup>39</sup> Department of Statistics, *Statistical Yearbook of Lithuania 1999* (Vilnius, 1999).

<sup>40</sup> Rights of ownership and other rights registered with the Register on Data of State Land Cadastre and State Inventorization, Projection and Service Bureau remain valid until they are registered with the Real Estate Register.

and every person in accordance with the specified legal procedures can have access to real estate information.

New regulations enable the exchange of data of the Real Estate Register and the Mortgage Register. Credit institutions having registered a lien on real estate (mortgage) submit the registration data to the Real Estate Register.

#### *Management and maintenance of owner-occupied housing*

New legal acts regulating the operation, maintenance and renovation of privatized residential houses and flats were approved in 1993. *The Law on Homeowners' Associations (1995)* sets the framework for the division of responsibilities in multi-family buildings where ownership was transferred to the sitting tenants. This act gave cooperatives the opportunity to register as homeowners' associations, which essentially eliminated cooperative ownership in Lithuania. The establishment of associations in privatized buildings is not compulsory. Research indicates that less than 10 per cent of multi-family housing stock in Vilnius has homeowners' associations. Interviews with the Housing Credit Foundation and the Vilnius Associations of Homeowners suggest that many organizational, social and financial challenges persist in the implementation process. More specifically the post-privatization stage is marked by several major problems:

- 'The right to buy' has drastically reduced the supply of social housing;
- Municipalities have failed to control the conversion of residential into non-residential space;
- Ownership rights and management structures for the common elements in multi-family housing - land, recreational and parking places, engineering systems - have not been defined;
- Ownership of land and buildings is separated -- land is owned by the State, while flats are private;
- The administration of newly privatized multi-family houses is still in the hands of municipal enterprises, which is not the most efficient way of administration;
- Due to the lack of funds, maintenance and management is carried out by municipal maintenance companies in an ad hoc manner;

- The decision-making power of homeowners' associations is restricted by

the unequal financial status of households in one building.

Revised draft legislation governing the homeowners' associations will remove some constraints, but some of the main problems are related to attitudes, lack of information and experience, and low incomes of new owners. People are generally not prepared to assume responsibility for common areas, despite the need for substantial renovations to heating systems, roofs, windows and doors in most of the multi-family housing stock. It is critically important to develop a significant number of well-managed, democratically functioning homeowners' associations, which undertake energy-related repairs and take out-and-repay-small loans. This will require developing a new capacity in both the private and governmental sectors.

Municipal housing maintenance enterprises still have a monopoly on the management of the privatized housing stock. Vilnius has 20 such enterprises, each of which was granted a monopoly in one city district (see **chapter V**). These enterprises perform three main functions:

- The collection of some municipal taxes and verification of subsidies;
- The collection of monthly charges on behalf of utility companies;
- Limited repairs and upkeep.

*Resolution No. 1300 adopted in 1995 sets the standards for operation and the tariffs charged for the maintenance and management of residential buildings.* Tariffs can be locally adjusted. In Vilnius fees reportedly range from 0.50-0.60 litas per m<sup>2</sup> per month. Provisions exist to establish a reserve fund for capital repairs. Annual contributions are expected to be 0.5 per cent of the value of the dwelling. (High inflation in 1992 eroded the funds and the system is not operational at the moment.) According to the Law on Local Government, maintenance of multi-family buildings needs to be organized by the municipal enterprises. Prior to privatization tenants signed a contractual agreement with the municipalities in that regard. However, if a homeowners' association is established, residents have the right to choose any company to provide the services. Often private firms have no guarantees for the contract work and de facto choices remain limited to the municipal enterprises.

### C. Rental sector

The Civil Code regulates property relations, objects of public and private ownership, objects of municipal ownership and the implementation of both State and municipal ownership rights. Its chapter 13 deals specifically with municipal housing and landlord-tenant agreements. Tenants of municipal housing have the right to sublet residential premises. Changes in the legal basis of public rental housing have been insignificant. Although subsidies for the maintenance of State-owned housing were abolished in 1992, rental fees for State-owned dwellings increased insignificantly. According to Resolution No. 1432 of December 1997, municipalities determine the rent, which fluctuates between 0.16 - 0.25 litas per m<sup>2</sup>. Rent for State housing makes up only 1.5 per cent of the average household income. In most cases, rental units are dispersed in the now privatized municipal housing stock. Maintenance companies charge marginal fees for upkeep (Resolution No. 704, 1992) and reportedly resort to patchwork maintenance and emergency repairs.

Some regulation of private renting, though rather vague, does exist. The Civil Code specifies that private property can be rented without any restrictions on rent levels. Leases are drawn up, provided that the property is rented for a year or longer. Both parties need to give three months' notice in the case of a non-fixed term agreement. Termination of a lease for non-payment is enforceable through the courts.

### D. Legislation regulating the development process

#### *Landownership*

The Law on Land Reform (November 1991) enforced a process for land provision, restitution, privatization and compensation. The Government adopted the Resolution on the Nominal Price of Land, Forest and Water Reservoirs, outlining conditions and prices for State procurement. The Resolution also outlined a procedure for the valuation of land and the payment of compensation. Furthermore, *the right for expropriation of privately owned land was limited*. The State could sell agricultural and urban land to private citizens. Members of collective garden associations were allowed to purchase land for residential construction. The principal statutes for land use in urban areas were defined in the Resolution on the Process of Sale and Rent of Non-

agricultural Land (February 1992). The Resolution provided for the purchase of plots designated for economic and commercial activity.

*The Resolution on the Renting of State Land was passed on 13 March 1992.* Lithuania's land reserves are divided into privately and publicly owned land. Land users can be organizations and legal persons (or entities) using public land on a leasehold basis. Owners of cooperative houses or multi-family homeowners' associations do not own the land on which their housing is built.

In June 1996, article 47 of the Constitution was supplemented with provisions that allowed municipalities, other national entities, as well as foreign entities engaged in economic activity in Lithuania, to acquire plots of land for non-agricultural activities. According to the Constitutional Law, foreign entities registered and doing business in Lithuania and foreign legal entities having established, for business purposes, affiliates or subdivisions without the status of a legal person in Lithuania, as well as Lithuanian entities (municipalities, Lithuanian enterprises having the rights of legal persons, etc.) are entitled to acquire land necessary for the operation of buildings for their direct business activities.<sup>41</sup> The Constitutional Law on Subjects, Procedure, Terms and Conditions and Restrictions of the Acquisition of Land Plots established the procedures for land acquisition. *Entities may acquire plots of land owned by private persons by buying or and exchanging them; State-owned or municipal land may be acquired by public sale and purchase with or without an auction or tender.* Legal entities do not have the right to own land. A new resolution will eliminate that restriction and will encourage legal and physical entities to purchase rather than lease land in a competitive tendering process.

The practical implementation of these legal provisions was facilitated by Resolution No. 1423 (December 1998) on procedures for landownership permits. Entities may file applications for non-

<sup>41</sup> With respect to foreign entities the following conditions apply: (1) the foreign enterprise is registered in a member State of the European Union, or in a State which is a party to the European Agreement with the EU and the member states thereof, or a member of the Organisation for Economic Co-operation and Development or a member of the North Atlantic Treaty Organization; (2) the foreign State of registration (residence, control) provides equal rights to Lithuanian entities, i.e. the rights are applied on mutual basis; and (3) the foreign enterprise has the main place of business in the State of registration, lasting for at least 5 years.

agricultural plots, which are, according to the detailed plans, approved under the procedure of the Law on Territorial Planning, designated for the construction of residential, industrial, commercial or other primary business activities. It also prescribes the validity of permits in case of land acquisition for the exploitation of existing buildings or new construction, as well as appeal procedures.

#### *Land lease*

According to the Law on Land Lease, Lithuanian and foreign natural and legal persons are permitted to lease land. The owners of private land and the possessors of State-owned land are entitled to lease land to natural or legal persons. The right of possession of State-owned land is vested in State institutions (county governors being the main possessors), municipalities, State authorities and State enterprises financed from the State budget. Land leases are to be concluded in writing.<sup>42</sup> A notary must confirm the lease agreement of the private land concluded for a term exceeding three years. A plan of the land approved by the county Governor's administration, or a land map (scheme) in the case of a short-term lease (less than three years), constitutes an obligatory part of any land lease.

The parties to the agreement determine the period of a private land lease. This period for State-owned land is determined by the county governor's administration and may not exceed 99 years. Both private and State-owned land may be sub-leased, but only with the permission of the lessor. State-owned land may be leased with or without holding an auction, particularly in the case of leases to owners of existing buildings and structures. Auctions for the lease of State-owned land are held by the county governor's administration or by the mayor for land leases for a period up to 3 years. Resolution No. 205 (February 1999) determined the tariffs and the methodology for assessing land

<sup>42</sup> The standard terms of a land lease are:

- place of the object of lease, data of the State Land Cadastre and the Real Estate Register describing the leased land;
- the period of lease and the main land use;
- the terms of the use of buildings and constructions on the plot, other engineering installations and communications on the leased plot;
- the use of the underground, mineral and natural resources (except amber, oil and quartz sand);
- the special terms of land use (protection of cultural heritage and nature objects);
- restrictions on land use and easement;
- the terms of land rent payment and responsibility for violation of the lease agreement.

values in different locations. The rate is 6% of the potential sales price.

The Law to Amend the Law on Land Lease (March 1998) approved a new wording. By Resolutions No. 938 and 939, the Government changed the procedure for the payment of land lease tax, but the tax rates determined in 1996 are still valid.

#### *Planning*

The Law on Territorial Planning (December 1995) regulates different aspects of territorial planning and the inter-relationship between legal entities, individuals and public authorities involved in this process. It defines the main levels of spatial planning -- *territorial, specialized, master planning and detailed planning*.

The Government, public authorities, the county governor, municipalities, natural and legal entities organizes the preparation, coordination and approval of planning documents. Together with the landowners and users engaged in an economic or other activity on the planned territory they also implement them. Territorial planning aims to:

- Form an adequate and healthy environment for living, work and recreation;
- Establish a policy for the development of residential areas and infrastructure;
- Protect and rationalize the use of natural resources, land and cultural heritage;
- Harmonize the interests of natural and legal entities, the public, municipalities and the State regarding the use of the territory;
- Promote investment in social and economic development.

The following levels of territorial planning can be distinguished: (1) *national* (territorial plans approved by the Seimas and the Government); (2) *county* (territorial plans approved by the county governor or by public authorities); and (3) *municipal* (territorial plans approved by the municipality).

*Master plans* are the major documents for territorial development.<sup>43</sup> They define land uses, investment priorities and the regime of economic, social and construction activities, as well as the use and protection of natural and cultural assets. Special emphasis is put on residential development. Operative planning establishes a data bank of territorial planning information to monitor investment, changing economic and social needs and impacts occurring during the implementation of the master plan. It allows for constant revision of programmes and action plans. Operative planning serves as the basis for formulating changes in the master plan and in a manner prescribed in paragraph 4 of article 23 of the Law on Territorial Planning.

*Detailed plans* are documents that specify restrictions on land uses and activities, construction and development requirements and land easements.<sup>44</sup> Detailed planning is mandatory if one of the following actions is envisaged:

- Construction, reconstruction or demolition;
- The development of land;
- The expropriation of land for public needs;
- The use of mineral resources, a change in the use of water resources;
- A change in land use, or land area composition;
- Changes in the purpose of buildings and structures.

*Article 25 sets the guidelines for public participation in territorial planning and ensures its transparency.* General, detailed and special territorial planning documents must be submitted for public discussion. The general procedure includes open discussion of the plans within the community, wide dissemination of information, and exhibition of materials. Organizers are required to send a written notification to land and real estate owners whose property status might be affected by national, county or municipal projects. Special provisions ensure the transparency of approved master plans. The municipal board (mayor), the

county governor and the national Government must present reports on the territorial planning activity and its results.

The Code of Territorial Planning Regulations is a system of statutory acts, regulations, technical standards and requirements. The elements of the system are adopted by the Government, individual ministers or other public authorities. They lay down the basic functional and special requirements for environmental and heritage protection, technical, architectural and urban planning.

#### *Building regulations*

A comprehensive Construction Law (September 1996) established the basic requirements for buildings, their inspection, planning, rehabilitation, repair, use and demolition. It also clarified the rights and responsibilities of all parties in the construction process, including State institutions. Certification requirements were established for persons involved in planning, design, technical supervision and construction. Since July 1997, the Law has also established building product certification procedures and imposed mandatory compliance with established standards and other requirements. *The implementation of the Construction Law was overdue.* The lack of regulation has created numerous problems and uncertainties for both the investor (or purchaser of services) with respect to the cost or quality of construction and the construction firms as far as responsibility for material or project defects is concerned.<sup>45</sup>

A system of technical norms and regulations for the construction process has been established. The system contains close to 20 documents related to the design and construction of buildings with responsibilities assigned to Government institutions and organizations regulating various aspects of the construction process. It follows the principles and requirements of EU Directive 89/106/EEC. *Priority is given to the harmonization of regulations and certification procedures with EU standards.* The normative technical documents for construction are obligatory (approved by the Ministry of Construction and Urban Development as well as the Ministry of the Environment). Standards, construction regulations

<sup>43</sup> The following may be the subject of special planning: (1) Lithuania's land stock, including forest land, and water resources; (2) social, cultural, economic activities on the territory under planning; (3) infrastructure; (4) protected territories, their systems, natural and immovable cultural heritage.

<sup>44</sup> Subject of detailed planning may be: (1) land plots and forest property; (2) territories of towns, townships or their parts; (3) village territories.

<sup>45</sup> V. Vaitas, Construction and construction materials industries in Lithuania (World Bank, Washington D. C., 1998).

and recommendations for construction prepared by various organizations and enterprises are recommendatory.

A building permit is issued upon presentation of the construction design, prepared on the basis of detailed plans, which are proposed by a professional architect. Changes in the zoning and revisions of the master plan might be difficult and take more than six months. However, all procedures for the issuing of building permits were simplified (particularly for small houses) in 1999.

### **E. Legislation regulating the financial aspects of the housing sector**

The legislation concerning various types of financial activities has been developed in Lithuania, although to different degrees in various sectors. Perhaps the most advanced legislation can be said to exist in the banking sector, with insurance regulation and supervision practices somewhat lagging behind. The Bank of Lithuania has sub-legislative powers in its field of competence. The Law on Insurance (July 1996, as subsequently amended) regulates the insurance business. With respect to investments by an insurance company, the legislation is detailed. A general requirement is that investment in Lithuanian assets should make up at least 50 per cent of the total investment portfolio, and that authorized capital may be invested only in (i) State and municipal bonds, (ii) real estate and (iii) bank term deposits. Government Resolution No. 739 (June 1998) prepared the basis for the establishment of a Mortgage Insurance Company in May 1999. The Company is owned by the Ministry of Finance and will insure the subsidized or 'soft loans' issued to young families on the waiting lists.

The Law on the Bankruptcy of Companies (No. VIII-270) regulates the bankruptcy procedures of companies registered in Lithuania. The legal definition of a bankrupt company is somewhat unclear -- the company is deemed insolvent when its financial liabilities exceed its assets. In addition,

the legislation does not deal with individual bankruptcy, nor does it apply to individuals who cannot honour their obligations.<sup>46</sup>

### *State support for housing*

The Law on the Provision of Dwellings for Citizens specifies alternatives to State support in the provision of housing. Support is limited to citizens who lack adequate housing. Priority is given to households with special needs: orphans, the handicapped, the chronically ill, the elderly, and single parents.

State support may be provided in one of the following forms:

- Credit with low interest;
- Access to municipal rental housing;
- The 'right to buy' municipal or State rental housing in instalments.

State support per household member is equal to the building cost of 18 m<sup>2</sup> of residential space. Information provided by the Ministry of the Environment indicates that most households (80 per cent) eligible for State subsidies wish to have access to low-interest credit for housing construction. Approximately 15 per cent would like to rent municipal housing, and only 5 per cent would like to exercise 'the right to buy'. Experience suggests that only 4-5 per cent of the eligible households might be able to qualify for mortgages or construction credits with subsidized interest rate. The Ministry intends to revise the system and eliminate the waiting lists, which by mid-1999 reportedly had 104,260 households on them. Data in **table 25** reflects the mismatch between demand for State support (measured by the number of applicants) and the actual potential of the programme to provide soft loans or access to municipal rental housing. Future *changes in the Law on the Provision of Dwellings for Citizens will allow only low-income households and/or socially vulnerable people to apply for municipal housing.*

<sup>46</sup> KPMG, 1998.

**Table 25. Applications and granted State support within the framework of the Law on the Provision of Dwellings for Citizens, 1993 - 1999**

	1993	1994	1995	1996	1997	1998	1999
Total number of applicants on the waiting lists (on 1 January)	91,828	98,490	98,461	97,355	96,661	104,260	104,972
- Applicants for soft loans (total, on 1 January)	73,189	77,959	78,727	80,849	82,146	90,001	89,813
- Successful applicants for soft loans	25	740	970	969	1380	1249	N/A
- Applicants for municipal rental housing (total, on 1 January)	12,630	15,060	14,608	14,110	14,005	14,259	15,159
- Successful applicants for municipal rental housing	846	650	636	624	615	973	N/A

*Sources:* Statistical Yearbook 1999, Vilnius, 1999; Statistics Lithuania B 903, Vilnius, 1999.

*Note:* N/A- not available.

In special cases, support is provided to cover utility costs. For example, the Social and Labour Ministry administers heating subsidies. In 1994, financial resources were allocated from the State budget to cover arrears for municipal services for families on low incomes. Other forms of targeted State support for housing investments, subsidies and credits are identified in the following normative acts:

- 'BUSTAS' State-supported programme, approved by Resolution No. 562 of 17 July 1992;
- Law on the Provision of Dwellings for Citizens, 7 April 1992, No. 1-2455;
- Law on the Procedure of Using Grants and Other Compensation for Covering Credits for Cooperative and Individual Dwelling Construction and Other Costs, 16 May 1991, No. 1-1334;
- Resolution No. 101 (13 February 1992) on the Support Funds of the Lithuanian State and Local Self-governments for the Construction of Houses and Flats and for Preferential Credits for Citizens in 1992-1995;
- Resolution No. 311 (30 April 1992) on the Support for Dwelling Construction Cooperatives;
- Resolution No. 383 (25 May 1992) on the Use of the Resources of Citizens for Dwelling Construction;

- Resolution No. 422 (2 June 1992) on the Approval of the Rules on the Preferential Credits for Dwelling Construction.

#### *Legal basis of the mortgage system*

The Law on the Establishment of Mortgage Institutions was adopted on 16 October 1996. These institutions started their activities in July 1997. Consequently, the legal registration of property liens with the local divisions of the administration of the county governor, the State Bureau of Inventorization and Projection, the Road Police and the Ministry of Transport has been prohibited. These institutions had to transfer information regarding liens on property to mortgage institutions.

The Law provides for the following types of mortgages: ordinary, consolidated (i.e. several assets are mortgaged), in favour of a third party (i.e. assets owned by someone other than the borrower are mortgaged), maximum (i.e. secures the obligation up to a certain agreed limit), joint (several assets owned by several persons are mortgaged), and conditional (i.e. the validity of the mortgage depends on a certain event or condition). The regulations specify that the mortgagee has the right to full satisfaction of his claim from mortgaged property with priority over other creditors. If the right of ownership to mortgaged property is passed to another person, the new owner

assumes responsibility for the mortgage. Properties are mortgaged through contracts between the creditor and the owner of the property or at the unilateral request of the owner of the property. The mortgage agreement or unilateral request of the owner has to be written on a special standard form (mortgage bond), certified by the Notary Public and registered in the Mortgage Register.

The Central Mortgage Office gathers data on mortgaged property, manages the archive of the central mortgage register and transfers data to other State registers.<sup>47</sup> A different procedure for satisfying claims resulting from pledge agreements has been adopted depending on the date of the pledge agreement. Claims of creditors relating to pledge agreements made before 1 July 1997 are dealt with by the district court, while creditor claims relating to pledge agreements made after 1 July 1997 are settled with mortgage institutions (art. 5). If several liens on the same property had been registered before 1 July 1997, the information transferred to mortgage institutions needs to maintain the sequence of priorities. Creditors wishing to change the sequence of priorities may apply to the courts in accordance with the legal procedure.<sup>48</sup>

From March 1998, amendments in the Law on the Establishment of the Mortgage Register set June 1998 as a deadline for the transfer of all lien agreements to the mortgage departments.

### Taxation

At present residential properties are exempt from tax. Furthermore, *real estate tax* is not levied on real estate owned by:

- The diplomatic and consular services of foreign States (on the basis of reciprocity);
- Companies in free economic zones;
- Agricultural companies;
- State and municipal institutions.

A municipality may decide that a company is exempt from real estate tax or that the tax should be reduced. Article 6 of the *Law on the Real Estate Tax of Companies and Organizations, approved in January 1997, provides the framework for establishing the tax value of real estate*. A subsequent government regulation facilitates the implementation. The State Inventorization, Projection and Service Bureau evaluates the real estate of companies and organizations. The taxable value of real estate is the replacement value reduced by 50 per cent. The concept of replacement value is defined by resolution No. 440 of 28 March 1995. The methods of property evaluation were approved by Government Resolution No. 244 (14 February 1996).

Law No. 1-935 -- Tax on Inherited or Donated Property – entered into force in January 1998. In November 1998, the Government passed Resolution No. 1330, which partly amended procedures for the calculation of the taxable value of inherited or donated personal and real assets and the valuation of assets using market prices. The taxable value is capped at 70 per cent of the market price. Taxes vary between 10 to 25 per cent of the property value. Furthermore, properties with average market prices of 45,000 litai are considered luxury property and declaration is compulsory.<sup>49</sup> Properties inherited from or donated by close relatives are exempt from tax.

Government Resolution No. 980, which in part amended Resolution No. 603 of 3 August 1993 on the Land Tax, was adopted on 31 July 1998. Land tax is charged according to the data disclosed in the Real Estate Register.

The Law on Value-added Tax, introduced in May 1994, increased the tax burden by 18 per cent. However, VAT is not levied on construction, renovation, insulation work, the design of dwellings, or engineering. Other legislation affecting the housing sector is listed in **annex III**.

<sup>47</sup> In December 1998, the Minister of Justice adopted Order No. 207 on the Procedure for the Change and Deletion of Data on Lien Agreements Recorded in the Database of Mortgage Register. Furthermore, Order No. 227 of the Minister of Justice established the fees for information presented by the Central Mortgage Institution to interested parties.

<sup>48</sup> In June 1998, the Civil Code was supplemented by article 57-1, which specifies that a transaction violating a creditor's rights, may be annulled.

<sup>49</sup> According to Resolution No. 3 of the Commission for the Evaluation of Property, dated 24 July 1998.

# Chapter V

## INSTITUTIONAL FRAMEWORK

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### Introduction

Transformation of the housing sector from a centralized to a market-oriented system requires specific conditions to be successful. One condition is the existence of well-structured institutions operating efficiently within and between the public and private sectors. If the necessary institutions are not in place, the transformation of the housing sector will slow down, and may even stop. In North American and west European countries the establishment of such institutions has taken a long time. Even in these countries, however, one can find large differences in the structure of these institutions, and in the distribution of responsibilities between them. In all these countries, however, the existence of such institutional structures is seen as vital for the formulation and implementation of housing policy at all levels.

In Lithuania, as in all the countries in transition, establishing adequate institutional systems in the housing sector is of particular importance. There is a lack of experience throughout the public and private sectors on how to establish and operate a well functioning housing sector. Solutions to housing needs require fast identification of problems, bottlenecks and opportunities, as well as a clear definition of the authority and responsibility of the main participants. Satisfactory institutional structures are therefore not an expression of bureaucratic traditions. They can be perceived as an example of a dynamic and forward-looking approach to addressing major social and economic problems and opportunities within the housing sector.

#### A. National institutions

The Constitution defines Lithuania as an independent democratic republic. It defines and limits the power of the State, as this power belongs to the Seimas (Parliament), the President of the Republic, the Government and the courts.

#### *Parliamentary institutions*

According to Parliamentary Statute, the Seimas has a number of committees with responsibility for specific fields of policy.<sup>50</sup> Responsibility for housing is today split between four separate committees (**fig. XI**):

*The Committee on Health, Social Affairs and Labour* has a responsibility to prepare draft laws and legal acts regulating employment, labour relations, social care and the provision of living space, and to provide recommendations related to these draft laws and legal acts to Parliament.

*The Committee of Budget and Finance* and *the Committee of Economics* have no explicit responsibility for housing, but have a fundamental impact on the housing sector, as they are responsible for financing housing programmes.

*The Committee of Public Administrative Reform and Local Authority of Affairs* has an indirect impact on the housing sector due to its important role in structuring and implementing the ongoing administrative reforms in the public sector.

#### *Governmental institutions*

The Government of Lithuania consists of a prime minister and 14 ministers appointed and dismissed by the President, with the approval of the Seimas. The ministerial structure was reorganised in 1998. Before this reorganization the main responsibility for formulating and implementing housing policy lay with the Ministry of Construction and Urban Development. As part of the reorganization of 1998 this Ministry was dissolved and major parts of its housing responsibility were transferred to the new *Ministry of the Environment*. However, defacto responsibility for housing in Lithuania is today distributed among a number of ministries, reflecting the distribution of housing responsibilities between the parliamentary committees (**fig. XI**):

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<sup>50</sup> Responsibility for central housing issues such as privatization and the restitution of the housing stock is placed within the Seimas committee structure.

The Ministry of the Environment:

- Proposes legislation on housing;
- Proposes State strategies and programmes on housing;
- Participates in and adjusts draft legal acts prepared by other ministries, government bodies, county governors, etc., related to housing.

The Ministry of Public Administration Reforms and Local Authorities formulates and regulates State and local authority policy on housing and the provision of municipal services (including specific services to the housing stock).

The Ministry of Finance is responsible for:

- Financial State programme supporting housing;
- Funding municipal housing programmes;
- Obtaining and administering international loans for the housing sector;
- Promoting organizational structures among private owners of multi-family buildings and estates.

The Ministry of Economics is responsible for economic State programmes related to housing.

The present fragmented responsibility for national housing at the political level, and the similar fragmentation at the executive level between various ministries, prevents proposals for a coherent national housing policy. The lack of such an overall policy also leads to uncoordinated and therefore probably inefficient use of available policy tools within the legal, financial and economic fields. Moreover, the organizational structure with specific responsibilities for housing in the new Ministry of the Environment, which is

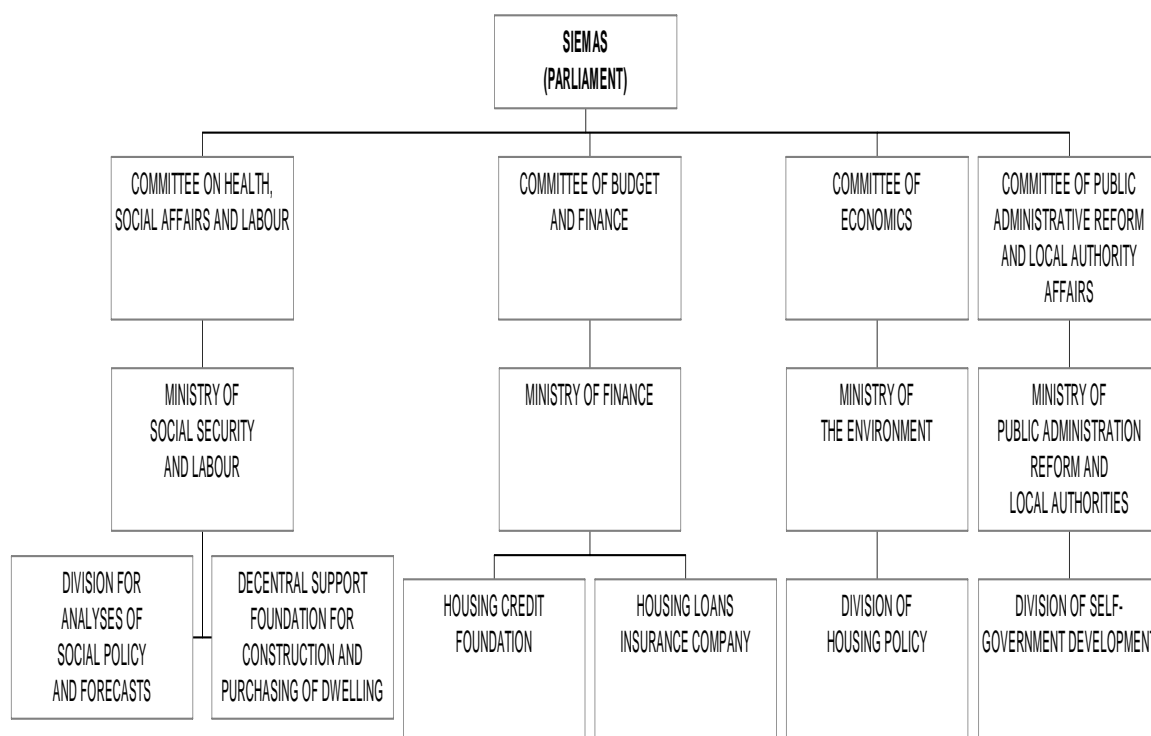
the Government's centre for housing policy, has a limited capacity. The Housing Policy Division within the Ministry has a staff of four professionals.

## **B. Regional institutions**

The local authority reform of 1994 divided the country into 10 counties. This is the highest territorial administrative unit. A county is not an independent, self-governed unit. The administration of counties is organized by the Government according to the Law on the Territorial Administrative Units of the Republic of Lithuania and Their Boundaries (1999) and other relevant laws. The major role of the county administration is to act as an executive, coordinating branch of the Government in the implementation of State policies. The Government appoints county governors. Their tasks, defined in article 5 of the Law on the Territorial Administrative Units, are:

- To implement State policies and programmes;
- To coordinate the activities of government institutions at county level;
- To coordinate local authorities in their implementation of regional programmes;
- To propose county development plans, strategies and programmes.

The county governor has, according to article 8 of the Law, considerable responsibility and powers with respect to land-use planning, urban development and special programmes, such as housing, at the county level. He or she has specific responsibilities for the organization and participation in the development of general and special planning documents for the county, as well as for the provision of recommendations for the preparation of general and special national plans and programmes.

**Figure XI: Governmental institutional structures responsible for housing at the national level**

The Government's administrative system at county level therefore does not replicate the fragmented responsibility for housing issues that characterizes the national institutional structure. Although housing is not specifically mentioned as a responsibility of the county governor, his and her general responsibility for proposing and implementing State policy and programmes clearly also covers housing. The county governor's would therefore be a suitable and powerful State function to encourage and coordinate local authorities in drafting local housing programmes. Such local programmes could, by screening and coordination at county level, form a solid base for the drafting of national housing programmes.

### C. Municipal institutional structures

The Law on Local Self-Government (1994) states that municipalities are entitled to carry out activities and initiatives, and take decisions permitted under the Constitution and other laws and regulations. Problems considered important to the municipal constituency and which do not fall within the competence of State institutions are also the responsibility of the municipality. Articles 4, 5, 6, 10 and 12 of the Law on Local Self-Government define the institutional structure of a local authority as follows:

#### Elected *representative institutions*:

- The Municipal Council
- Committees, commissions and other appropriate bodies.

#### *Executive institutions*:

- The Mayor
- The Executive Board (not compulsory)
- The administration
- Chief executives of districts ("Seniunijos")

The Law grants specific power and responsibility for housing issues to the Council (art. 15) and the Board (art. 18).

#### The Council:

- Forms committees and approves their recommendations;
- Establishes prices and rates for services rendered to residents by municipal enterprises: electricity, central heating, gas and hot and cold water;
- Approves plans and programmes for the development of the municipality.

The Board:

- Executes the decisions of the Council;
- Analyses and prepares proposals for general long-term development programmes covering social, cultural, economic, investment and other areas;
- Organizes the construction and use of residential premises;
- Organizes the renting and sale of municipal housing property according to the law, maintains and supervises lists of inhabitants waiting for State housing support.

The rights of municipalities are therefore extensive. Within these rights there seems to be no significant restrictions on the way local authorities handle the housing sector. First, the law obliges municipalities to define and act on problem areas of importance to their residents (e.g. housing). Second, municipalities can independently decide on the structural way in which they address housing politically (committee structure), and choose the administrative instruments (administrative structure). Third, municipalities are free to cooperate with the private and non-governmental sectors.

Two significant operational factors, however, limit municipalities' freedom to act in the housing sector -- the setting of rental fees for housing and the privatization of the housing stock. Both are today decided at State level -- rent levels are determined by governmental decree, and privatization policy is decided by Parliament. The setting of fees for rental housing has important social and economic consequences for tenants, the municipality and the State. The ability to exercise some flexibility is, however, considered to be an important part of efficient municipal housing policy. Although privatization of housing in Lithuania must be considered, in practical terms, to be completed, the privatization law is still in force. In theory the remaining municipally owned rental housing could still be privatized, provided that the application is submitted before the deadline. Such privatization would have serious consequences for the provision of social rental housing. It can be argued that the privatization of municipal housing stock has gone too far already and has resulted in a

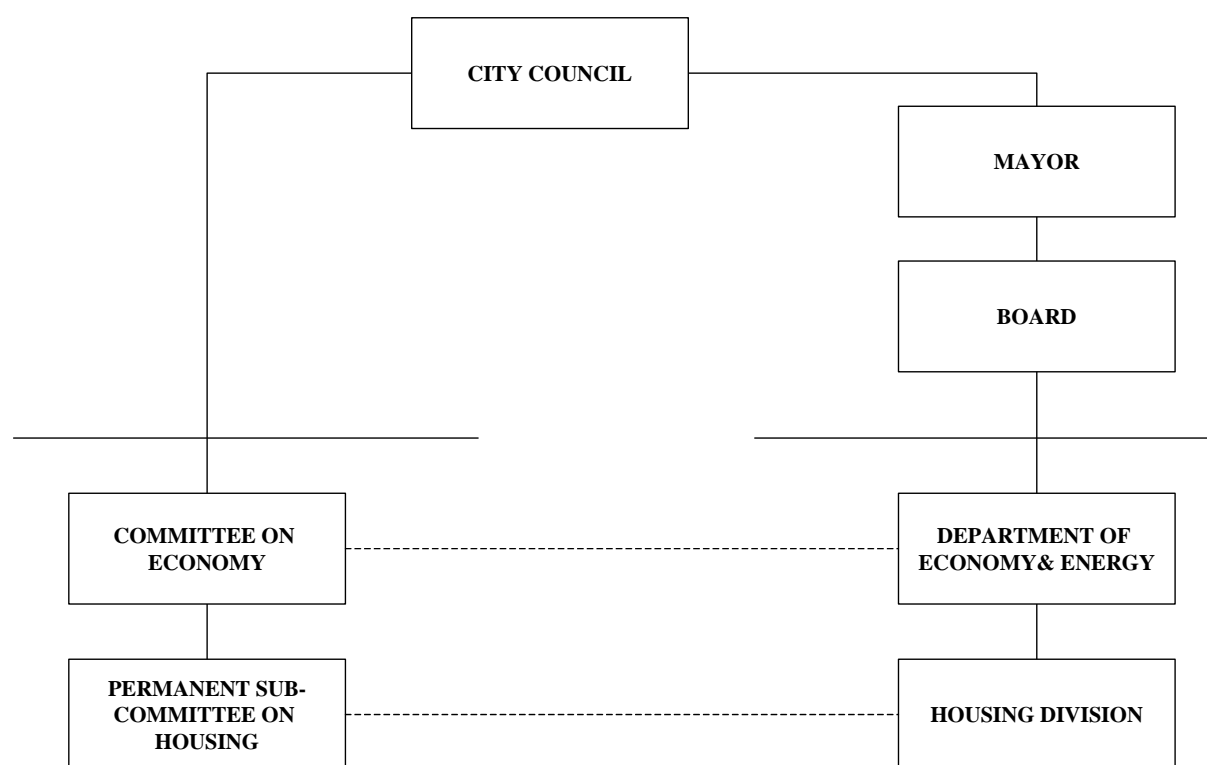
share of public rental housing which is too low to meet the needs. It is therefore considered important to maintain the number of municipally owned housing units and to consider alternatives for its growth.

It should also be noted that the Government is in the process of privatizing State-owned property. A considerable part of this property has been administered and maintained by the municipalities, and in many cases constitutes an important element in their long-term strategy for land-use development. Such properties, currently transferred to the State Property Fund for privatization, might be essential for the strategic economic development and well-being of the municipality. The policy needs to be reviewed.

#### *Municipal political institutions*

Apart from the capital, Vilnius, no Lithuanian municipality today has a permanent committee or sub-committee with specific overall responsibility for housing. Such responsibility is normally distributed among a number of committees. As a consequence of this fragmentation, the Council is ultimately responsible for housing. Yet, as the Council is not presented with an integrated policy approach to the whole field of housing, its ability to effectively carry out its responsibility is very limited. A major bottleneck for the accelerated development of the housing sector is the lack of political priority given to housing at the municipal level. This is reflected in the weak political/ administrative institutions responsible for housing at the municipal level.

Vilnius represents a significant, new and positive trend in upgrading housing issues at the municipal level. In 1998, the city established a permanent sub-committee with overall responsibility for proposing housing programmes for Vilnius and implementing the Council's decisions on such programmes. The City Council, as part of a fundamental revision of housing policy, passed a resolution on a city housing programme. As a basis for the implementation of this programme, the city gradually changed both its political and administrative institutions for housing (see **fig. XII**).

**Figure XII: The city of Vilnius - political and administrative responsibility for housing****POLITICAL***Municipal administrative institutions*

Municipalities do not have specific administrative units with overall responsibility for housing. The exception is the capital, Vilnius. The lack of specific and clear administrative responsibility for housing issues is a fundamental problem. The present administrative structure prevents the development of comprehensive analyses of local housing issues at the municipal level that will facilitate political debate and decision-making related to housing progress.

Larger towns have neighbourhoods or districts (*Seniunijos*) with local administrations, led by a *chief executive*. He/she is appointed by the mayor and is responsible to the Board. The chief

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executive has particular powers and interests in connection with neighbourhood housing issues. A particular feature of municipal housing institutions in Lithuania is the existence of municipal housing maintenance enterprises. Such enterprises are remnants of the former Soviet period. They were specifically established for the maintenance and the repair of the municipal building stock and public areas. Their main functions are: (a) the administration of multi-family houses; (b) the maintenance and repair of housing stock; and (c) the cleaning of public areas and maintenance and repair of public buildings. They function as municipally owned monopolies within municipal districts. In Lithuania's major cities the situation today is presented in **table 26**.

**Table 26: Municipal housing maintenance enterprises in major cities**

City	Number of enterprises
Vilnius	22
Kaunas	3
Klaipeda	12
Siauliai	5
Panevezys	2
Alytus	1

In theory, the housing maintenance enterprises are subordinate to the municipal administration. In practice, they report to the Department of Economy and Energy. Often the chief executive of the district has real responsibility and power to direct their operations. *The present combination of privately owned housing and Soviet-type monopolistic institutions is considered to be a major problem for the establishment of housing management institutions both within municipalities and within the private and non-governmental sectors.* In particular, these enterprises restrict institution-building in privatized multi-flat housing and prevent the emergence of private-sector services. Currently the housing maintenance enterprises are subject to restructuring and privatization. Vilnius, for example, is preparing privatization and restructuring plans as part of its housing programme. Klaipeda is also working on privatization options, while Alytus privatized its largest housing maintenance enterprise as early as 1994.

#### D. Private-sector institutions

##### *The construction and building industry*

The construction and building industry has undergone major changes as a consequence of the Government's programme of "voucher privatization". State-owned construction

companies, numbering 474 and employing 113,000 people at the end of December 1991, were reduced to 40, employing some 6,000 people in 1998 (**table 27**). In 1998, 98 per cent of the construction companies were private. These privately owned entities accounted for 94 per cent of the value of construction contracts, and employed 95 per cent of construction sector employees in that year. It has to be mentioned that many construction companies had contracts outside the country, particularly in the period of Russian army relocation in 1993-1995. For example, those contracts were 18 per cent of within-country volume in 1995, but foreign construction dropped constantly, coinciding with financial crises in the region, to 3 per cent in 1998. Even then, 80 per cent of those construction works were carried out in the Russian Federation.

At first the average number of employees in private construction companies increased to meet demand for foreign construction and fill niches in the domestic market. Then it (**table 27**) decreased, indicating productivity and efficiency efforts. The public construction companies are bigger on average, but they too are undergoing downsizing. Overall, Lithuania has a private construction sector able to function in a competitive manner in the face of the major challenges presented by the maintenance and repair of existing housing, as well as new housing construction.

**Table 27. Construction companies, 1991-1998**

	1991	1992	1993	1994	1995	1996 a/	1997 a/	1998
Number of enterprises, as of 31 December								
Total	1286	1074	1259	1628	1879	1982	2031	2136
State-owned construction companies	474	313	189	133	42	52	40	40
Share (per cent)	36.9	29.1	15.0	8.2	2.2	2.6	2.0	1.9
Privately owned construction companies	812	761	1070	1495	1837	1930	1991	2096
Share (per cent)	63.1	70.9	85.0	91.8	97.8	97.4	98.0	98.1
Average annual number of employees, thousand								
Total	174.4	169.4	126.8	110.9	114.7	119.1	118.7	118.2
State-owned construction companies	161.8	98.1	39.1	17.3	10.2	11.8	9.8	5.7
Share (per cent)	92.8	57.9	30.8	15.6	8.9	9.9	8.3	4.8
Privately owned construction companies	12.6	71.3	87.7	93.6	104.5	107.3	108.9	112.5
Share (per cent)	7.2	42.1	69.2	84.4	91.1	90.1	91.7	95.2
Volume of work done on the territory of Lithuania (current prices), mil. <sup>b/</sup>								
Total	3621	27497	809	1502	1866	2023	2619	3389
State-owned construction companies	3470	17298	248	251	181.7	242.3	153.8	212.4
Share (per cent)	95.8	62.9	30.7	16.7	9.7	12.0	5.9	6.3
Privately owned construction companies	151	10199	561	1251	1684	1781	2465	3177
Share (per cent)	4.2	37.1	69.3	83.3	90.3	88.0	94.1	93.7
Ratios:								
Number of employees in private firms	15.5	93.7	82.0	62.6	56.9	55.6	54.7	53.7
Number of employees in State firms	341.4	313.4	206.9	130.1	242.9	226.9	245.0	142.5

**Source:** Department of Statistics, Statistical Yearbooks of Lithuania 1997 and 1999.

a/ In 1997 enterprises are distributed into sectors by share of authorized capital that belongs to the State (up to 51%).

b/ Prices for 1991 are provided in roubles, for 1992 in talonas and for 1993-1997 in litai. Also in 1991, the average number of employees' figure is an expert estimate.

The data show that the private sector dominates the market. It has enormous potential as it functions in a strenuous financial environment (see **chapters I and III** for interest rates on commercial loans). It is essential that other actors and institutions should also be able to function competitively.

The parallel increase in private-sector construction and building companies has also led to institutional organizations within this sector of the economy. The main professional and organizational structures are listed in **table 28**.

### *The private service sector*

The traditional professions within the building and construction sectors have already established national organizations: the Association of Lithuanian Engineers and the Association of Lithuanian Architects. Within the property transaction and valuation sector there is an emerging professional service, also organized at national level. Two organizations are thought to play a significant role: the Association of Lithuanian Property Surveyors and the Association of Real-estate Companies. Due to the existence of municipal housing maintenance enterprises, private sector management in housing is limited and geographically concentrated in Vilnius, Kaunas, Klaipeda and Alytus.

**Table 28: Private sector interests: major professional and organizational structures**

<b>Organizational structure</b>	<b>Members</b>
Association of Lithuanian Builders (Lietuvos Statybininku Asociacija)	93 <sup>a/</sup>
Association of Building Industry (Statybos Industrijos Asociacija)	37
Association for Sitica materials	7
Association of roofers	50
Association of producers of windows and doors	22
Association of Vilnius construction and repair companies	30
Association of Lithuanian Engineering	..
Association of Lithuanian Architects	..
Association of Lithuanian Property Surveyors	160
Association of Real-estate Companies	17
Association of Medium and Small Real-estate Agencies	18

<sup>a/</sup> Includes most large construction companies.

### *Financial institutions*

The Lithuanian banking sector contains 12 commercial banks organized in the National Association of Lithuanian Banks. In addition, three foreign banks have branches in Lithuania: the Polish Kredyt Bank, the French Société Générale and the German Norddeutsche Landesbank Girozentrale; and another four foreign banks have representative offices in the country. Lithuania also has 33 credit unions, mostly based on commercial and professional interest groups. (see also **chapter III**.)

### *Private owners and tenants*

Both private and public sector tenants do not seem to be represented through national institutional structures. Housing cooperatives have a tradition in Lithuania as one of the alternative tenure forms during the Soviet period. In the post-privatization phase, however, cooperatives were legally required to register as homeowners' associations. It would be worth while considering whether cooperative ownership could re-emerge and gain political support and credibility in the market-oriented housing sector of Lithuania.

The private ownership of multi-flat housing is legally regulated as 'Bendrijos' and can be managed through homeowners' associations. As discussed in **chapters III** and **IV**, establishing such associations is proving difficult. The lack of practical experience with private ownership over the past 50 years, combined with the existence of municipal housing maintenance enterprises, is considered to be a major barrier to the creation of

these important private sector-housing institutions.<sup>51</sup> A growing consensus seems to be emerging on the need to accelerate the institutionalization of homeowners' associations. The problem needs to be addressed by an integrated programme of legal changes, economic incentives, institutional changes and practical assistance and advice.

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<sup>51</sup> The Lithuanian Government, in cooperation with the World Bank, has established a programme for encouraging and assisting homeowners' associations through its pilot project on energy efficiency in the building stock.

## Annex I

## Tenure structure in the European Union, mid-1990s

Country	Tenure form (% of housing stock)			
	Owner-occupied	Social rental	Private rental	Other
Austria	41	23	22	4
Belgium	62	6	30	2
Denmark	56	21	19	5
Finland	61	20	8	11
France	54	17	21	8
Germany	38	26	36	
Greece	70	0	26	4
Ireland	81	10	9	
Italy	67	7	21	5
Luxembourg	67	2	31	
Netherlands	46	41	13	
Portugal	66	4	28	2
Spain	76	2	16	6
Sweden	43	22	18	16 <sup>a/</sup>
United Kingdom	66	24	10	
EU	56	18	21	

*Source:* Boelhouwer 1997; CECODHAS 1995; Oxley 1996.

<sup>a/</sup> Cooperative sector.

**Household expenditure patterns  
(Deciles)**

Deciles	Year		All household	I	II	III	IV	V	VI	VII	VIII	IX	X
Total consumption expenditure	1998	Lt	426.8	135.1	199.5	247.6	292.5	335.2	380.6	438.8	516.2	642.2	1080.3
	1997	Lt	382.6	118.3	176.9	219.2	257.3	295.7	340.1	391.4	458.5	564.1	1004.6
	1996	Lt	348.1	105.6	160.7	199.0	235.7	273.5	313.9	364.2	428.9	530.6	920.7
	1995	Lt	243.4	93.8	112.3	135.4	153.4	159.4	173.2	189.2	219.9	250.9	379.4
Consumption expenditure in cash	1998	Lt%	354.9/100	94.4/100	144.3/100	193.1/100	230.9/100	272.2/100	314.3/100	366.1/100	433.3/100	543.8/100	956.4/100
	1997	Lt%	311.3/100	85.6/100	133.9/100	169.6/100	198.8/100	237.4/100	271.0/100	318.2/100	374.9/100	464.0/100	859.4/100
	1996	Lt%	274.7/100	77.6/100	120.5/100	152.9/100	185.4/100	212.7/100	248.2/100	293.4/100	346.5/100	431.6/100	764.2/100
Food	1998	Lt%	146.8/41.4	54.8/58.0	77.7/53.8	100.9/52.2	114.0/49.4	132.4/48.6	146.4/46.6	165.6/45.2	185.9/42.9	219.9/40.4	270.0/28.2
	1997	Lt%	138.6/44.5	51.9/60.6	76.2/56.9	95.6/56.4	107.7/54.2	124.1/52.3	137.2/50.6	156/49.0	175.9/46.9	197.6/42.6	263.9/30.7
	1996	Lt%	128.2/46.7	49.5/63.8	72.8/60.4	86.9/56.8	103.7/55.9	117.8/55.4	131.2/52.9	151.5/51.6	169.6/48.9	195.4/45.3	246.9/32.3
	1995	Lt%	109.6/45.1	61.7/66.2	73.2/65.2	88.0/65.0	98.5/64.2	85.4/59.9	105.5/60.9	113.7/60.1	126.0/57.3	139.8/55.7	168.1/44.3
Expenditure by households/individuals by deciles on rents, fuel and power	1998	Lt%	51.4/14.5	12.6/13.3	22.8/15.8	39.6/15.8	36.8/15.9	40.9/15.0	48.2/15.3	56.3/15.3	64.2/14.8	75.8/13.9	126.2/13.2
	1997	Lt%	45.7/14.7	12.0/14.0	20.3/15.2	26.5/15.6	31.1/15.6	37.2/15.7	42.9/15.8	47.7/15.0	56.7/15.1	67.5/14.6	115.2/13.4
	1996	Lt%	40.1/14.6	10.6/13.7	18.1/15.0	23.8/15.6	29.5/15.9	32.7/15.4	37.3/15.0	40.9/13.9	47.8/13.8	63.0/14.6	112.9/14.8
	1995	Lt%	38.4/15.8	10.0/10.8	14.7/13.1	20.0/14.8	22.7/14.8	25.8/16.2	26.0/15.0	27.5/14.5	32.3/14.7	34.1/13.6	60.3/15.9
Urban household rents, fuel and power	1998	Lt%	62.0/15.0										
	1997	Lt%	54.7/15.2	21.5/18.2	30.7/17.7	39.3/18.4	40.8/16.6	46.4/16.7	53.3/16.6	56.6/15.8	64.8/15.3	74.8/14.5	118.9/12.6
	1996	Lt%	46.8/14.8	15.3/15.9	26/17.6	32.6/17.7	35.1/16.5	38.4/15.8	42.3/14.8	46.1/14.0	54.4/14.2	65.3/14.1	112.3/13.7
Rural households rents, fuel and power	1998	Lt%	29.3/12.6										
	1997	Lt%	27.0/12.8	5.0/8.5	8.3/9.4	10.4/9.5	13.1/10.2	15.8/10.5	17.7/10.4	29.8/14.0	29.2/11.7	43.1/13.0	98.6/16.0
	1996	Lt%	25.3/13.9	3.9/7.9	6.4/8.6	8.7/9.6	11.3/10.5	12.9/10.3	16.6/11.0	20.7/11.6	28.5/12.7	35.2/12.8	109.4/19.9

Source: Statistical Yearbook of Lithuania, 1999.

### Annex III

#### *Law on Public Procurement*

The *Law on Public Procurement* (January 1997) regulates public purchases of goods, construction work and services financed by State or municipal budgets. The Law also covers contracting and leasing agreements. The Law is applied if the amount of a public procurement exceeds 25,000 litai. If the amount of goods and services does not exceed 150,000 litai or the value of construction work does not exceed 500,000 litai, the purchaser shall be entitled to make purchases only from companies registered in Lithuania. The Law on Public Procurement contains the following options: (i) open tender; (ii) closed tender; (iii) two-stage tender; (iv) competitive negotiations; (v) price inquiry; and (vi) purchase from a single source.

Pursuant to item 2.1 of Government *Resolution No. 956* (September 1997) on the Conclusion and Implementation of Contracts on Construction Work, the former Ministry of Construction and Urban Development issued *Order No. 266* (December 1997), approving the amended regulations on construction work. The regulations of the contract on construction work specify the order of preparation and implementation of contracts between the participants in the construction process - the clients and the executors (contractors). The regulations apply if the construction is financed from public funds (funds of the State or municipal budgets, State social security and other State funds, charity and other support received on behalf of State institutions, loans received on behalf of or with the guarantee of the State, funds of State or municipal companies).

*Resolution No. 956* provides that architects and contractors for constructions paid for by State funds shall be selected according to the order established by the *Law on Public Procurement*. Agreements on projection and construction are made according to the regulations regarding construction agreements and normative construction documents confirmed by the Ministry of Construction and Urban Development. Projection, construction and repair works are paid at market prices.

#### *Privatization of State and municipal property*

The new *Law on the Privatization of State and Municipal Property* was enacted on 4 November 1997. In addition, a number of legal acts related to privatization were adopted, including the *Law on the Primary Privatization of State Property* (February 1991) and the *Law on the Privatization of State and Municipal Property* (July 1995).<sup>52</sup>

A State Property Fund has been established to manage, use and dispose of securities and other assets transferred to it by the Government under the right of trust. It was established after the liquidation of the Lithuanian State Securities Fund and the reorganization of the Lithuanian State Privatization Agency. The State Property Fund, by its functions, is one of the most important privatization institutions.

Pursuant to the newly adopted Law on the Privatization of State and Municipal Property and *Resolution No.1427*, the preparation of assets for privatization was approved. The Resolution also specifies that the Lithuanian State Privatization Agency, the ministry, municipality or any other State or municipal institution that manages, uses or disposes of State or municipal property under the right of trust shall transfer these functions to the State Property Fund.

By *Resolution No. 1148* (September 1998) the Regulations on the Privatization of Shares of Companies that are Significant Objects of Infrastructure or Dominating Objects of Branches of the Economy were amended. The State Property Fund acquired the right to implement and monitor privatization procedures. It can request information about the reliability of potential buyers and strategic investors and approve or reject them. Moreover, the amendments specify that the Fund may negotiate with the selected winner of the tender the improvement and/or revision of the proposed terms.

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<sup>52</sup> Privatization programmes announced before the enforcement of the new law, i.e. 1 December 1997, are still implemented according to the Law on the Privatization of State and Municipal Property of 4 July 1995.

A number of resolutions were adopted by the Government regulating different ways of privatization:

- *Resolution No. 1128* Rules of the Privatization of State and Municipal Property by Open Tender;
- *Resolution No. 1129* Rules of the Privatization of State and Municipal Property by Open Auction;
- *Resolution No. 1132* Rules of the Privatization of State and Municipal Property by Direct Negotiations.

#### *Municipal loans*

Documents regulating the procedures for municipal use of bank credits and loans:

- Financial indicators of the municipal budget for 1998 approved by the Law on the Approval of Financial Indicators of the State and Municipal Budgets for 1998 (December 1997);
- *Resolution No. 492* (April 1998) concerning the Draft Preparation of Financial Indicators for the State and Municipal Budgets for 1999;
- The procedure for the calculation and transfer of State subsidies to municipalities and municipal budget revenue sources is regulated by the Law on the Methodology of Municipal Budget Revenue (July 1997);
- The procedure for the municipal use of bank credits and the taking-out and granting of loans is regulated by *Resolution No. 511* (April 1998);
- The procedure for municipal use of foreign loans taken on behalf of the State or State-guaranteed loans, and the procedure for municipal borrowing from foreign countries is regulated by *Resolution No. 1200/8* of the Government and the Bank of the Republic of Lithuania (October 1997).

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