

## **Part Two. CURRENT SITUATION, GOALS AND CHALLENGES IN PARTICULAR AREAS OF THE HOUSING SECTOR REFORM**

The analysis of the framework conditions in part one shows that there are a number of aspects within the Russian Federation's housing sector that need to be analysed in more depth. Although many themes deserve to be studied in their own right, the following are thought to be the most relevant today:

- The management and operation of the housing stock (chapter VII)
- Utilities (chapter VIII)
- Social housing (chapter IX)
- New construction and urban planning (chapter X)
- Land management and real property market development (chapter XI)

For each theme, the major challenges will be identified and analysed in depth. In addition, options for addressing these challenges will be put forward.



# *Chapter VII*

## **MANAGEMENT AND OPERATION OF THE EXISTING HOUSING STOCK**

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One of the greatest challenges within the housing sector is the management and operation of the housing stock, in particular the organization of repairs and maintenance. Free privatization has dramatically changed the ownership structure of the housing stock. However, even today there is no clear understanding of ownership. The concept of private homeownership has been highly devalued, not only by the public authorities, but also by the owners themselves. There is no proper institutional structure for the flat owners and there is a lack of information sources for them in particular in multi-unit buildings. In most cases, they do not have the opportunities and capacity to take decisions on their property.

### **A. The consequences of privatization**

In the Soviet Union all apartment buildings were for rent. The State or State companies owned the residential buildings and the authorities took care of their management, maintenance and repair. Living space in State-owned buildings was rented to citizens for permanent residence. The monthly rent was approximately 1% of the average per capita income of ordinary families.

The privatization policies of the 1990s changed this. The privatization of flats and the switch from tenants to owners was seen as a tool to increase the efficiency of the housing stock management and maintenance. The privatization process has, however, left many questions open. Although individual flats are privatized, the common areas, structures and infrastructure of buildings are not formally privatized. Home ownership is understood to cover only the dwelling.

The privatization policy made it possible for residents to "privatize" their dwellings free of charge. About half the flats in apartment blocks have been privatized. Because the rents in Soviet times were nominal, they did not include capital repair costs and did not even cover maintenance costs. This has not changed. Therefore, privatization does not bring any financial benefit

to the residents. On the contrary, in most cases it increases their financial responsibilities. Consequently, interest in privatization has waned among residents, while the authorities are still promoting it as they hope that privatization will reduce their responsibilities with regard to the huge problems in the housing stock.

Private owners can form a homeowners' association, which in principle can independently decide upon the maintenance and management of the building. But in most cases, some flats in a building are privatized and others not. In such apartment houses it is almost impossible to form a homeowners' association, because the local government, which formally owns the other flats, is reluctant to be part of a private owners' association.

The privatization legislation did not stipulate sufficiently clearly how the ownership of the whole building should be legally determined and organized. At the moment nobody clearly owns the partly privatized apartment blocks and nobody is clearly responsible for them; the buildings are "ownerless". This situation is a serious obstacle to the development of proper maintenance and renovation.

The first priority should, therefore, be to search for efficient patterns of management of apartment blocks in which some of the flats have been privatized. The Government will have to be strongly involved in the development of such patterns. The lack of a tradition in the ownership of buildings and of understanding of an owner's responsibilities makes it difficult to rapidly shift the responsibility for housing and buildings to the individual private flat owners.

### **B. Management of the housing stock**

In the Soviet system there was no clear distinction between ownership, management, maintenance, reconstruction/repair and provision of public utilities for housing. This is generally still the case

today. The same local organizations and authorities can act in all these tasks and take care of all these duties. There is no clear distinction between customer and supplier in the housing sector and a lack of transparency in costs and money transactions. In this kind of system it is almost impossible to measure or assess the efficiency of different actors.

Formally, the overwhelming majority of residential buildings still belong to the municipalities, i.e. public authorities, which delegate their management and maintenance to subordinate organizations - housing maintenance offices (ZHEKi), companies offering customer management services (DEZi), trusts, etc. It has become evident that these are inefficient.

The causes for the current low quality of housing stock management cannot be merely explained by the strong impact of the municipal authorities on customer's service offices (Zheki/ Dezi). There is also a lack of correlation between the results of their activity and their financial remuneration. The fees are hardly related to the services delivered, and increased payments would not necessarily lead to any improvement in service. Another reason for the inefficiency of the customer's service offices and their subcontractors is that their activity can hardly be controlled. There is little transparency, either in financial terms or with regard to the delivery of services.

The lack of explicitly prescribed responsibilities is one of the biggest problems of the management and maintenance system. Up to now housing and public utilities have largely been provided by a monopolistic system, which means that the occupants are unable to reject management services of inadequate quality. Demonopolization of the market would enable them to choose the best company and to be involved in the management of their homes. This is not the case now, as their involvement is restricted to paying for housing services and public utilities.

The current system of payments for housing services is complex (see chap. VIII). Citizens cover only 20-40% of their housing costs through complicated tariff systems, which include a complicated social support system, privileges and subsidies for 60-70% of the population. The remaining housing costs, 60- 80%, are supposed

to be covered by the municipalities, which in general are unable to finance the sector properly even though approximately 60% of their budgets go to housing. Approximately 20% of the costs are not covered at all, which means increasing debts, deteriorating services and dilapidated property. This has already resulted in social problems.

Moreover, despite the lack of income, maintenance enterprises have 5-10 times more personnel than similar West European organizations. This is an indication of their very low efficiency. The households that they serve consume 2-4 times more energy and 50 % more water than generally in the West and there is much waste of material resources. In general, the service providers suffer from poor management. In the Russian Federation it is already understood that maintenance urgently needs more efficiency, better tariff systems and better financial administration. Citizens cannot understand why they should pay more for poor or even deteriorating services.

Compulsory annual financial auditing has been recommended to Russian municipalities and enterprises. The promotion of professionalism in municipal enterprises needs consultant advice in technical and administrative issues, in the promotion of transparency and in developing tariff systems and personnel policies. Although there is a control mechanism through State and municipal housing inspections, which control the quality of public utilities, this is not sufficient, in particular as these inspections frequently also suffer from a lack of efficiency. Compulsory auditing is impossible as there are hardly any qualified Russian auditors. The need for education and training in all aspects of maintenance is obvious and urgent.

As a result of all these difficulties, renovations and repairs in the housing stock are insufficient and the public utilities cannot renovate their infrastructure. Consequently, both the infrastructure and the housing stock are run-down.

### **C. Ownership of the housing stock**

With the transfer of ownership, it was expected that the new private homeowners would take over the management and maintenance of the housing

stock. To facilitate this, the organization of individual owners in multi-apartment buildings into associations was promoted. Those homeowners' associations either take the form of traditional housing cooperatives and housing construction cooperatives (ZhK, ZhSK) or the newly established household associations (TSZh).

In fact, the attempt to organize households through homeowners' associations has not been very successful so far. According to Gosstroy, in 2001, there were only about 5,000 registered TSZhs and about 16,000 registered ZhSK.

Most associations were established in new constructions and in buildings intended for demolition, so the real figures are even more modest. Many of the TSZhs were established artificially, under pressure from local authorities. Many of the associations are kept alive only formally: they have no bank account, no statutes and no board.

The establishment of homeowners' associations is constrained by a number of factors that are difficult to overcome, for instance:

(a) The authorities have not fully transferred the land on which housing has been built to the ownership of condominium households, despite legal obligations to do so;

(b) The authorities have failed to comply with a legal obligation to give State and municipal grants to homeowners' associations to finance maintenance, current repairs and renovations of buildings and to provide utility services, and to compensate for housing subsidies and privileges which had been granted to the owners of the condominium;

(c) The low number or total absence of professional real-estate managers, and the lack of a market for management, maintenance and repair services.

Generally speaking, creating homeowners' associations is burdensome, especially for local authority management companies, but also for the major utility providers, as they have the need to tailor their management and billing systems towards the needs of the new management institutions (see chap. VIII).

It has proved easier to establish homeowners' associations in cases where new blocks of

apartments were developed for sale. Developers and association representatives report that there were no major difficulties establishing the associations and running them. These cases may serve as promising examples, however even here there are problems:

(a) The developers and the construction companies have become the initiators of the homeowners' associations. Due to the huge size of these new blocks, creating a homeowners' association turns into a formal act of collecting signatures rather than involving the owners in joint decision-making. So basically the developer runs the block and applies his management and maintenance solutions.

(b) The practice of forming homeowners' associations in new buildings goes against the main idea of the housing reform to demonopolise housing management and maintenance services. The developer has the obligation to run the building during the warranty period. The developer will, however, also have a major comparative advantage for any future tendering for maintenance and repair work owing to his familiarity with the technical particularities of the block;

(c) The efficiency of a homeowners' association depends on the professionalism of its leaders. Those pre-established by developers are not 'bottom-up' initiatives, rather a quasi-association assisting the developer to meet his business targets. Some of these institutions may turn to be successful in the future, but few are forums for initiatives from owners.

The federal Law on Homeowners' Associations obliges authorities to rethink and to develop new approaches to increasing the role of the owners and their institutional representatives (homeowners' associations). Today, the new owners of the privatized apartments lack any real incentives to take responsibility and form homeowners' associations. There are even cases where the owners may lose certain benefits that are provided only to tenants. Moreover, ownership of the flats is not registered so that they cannot be used as collateral. The newly formed homeowners' associations in the existing housing stock face several procedural difficulties in connection with their establishment, or when they try to run to the block differently than before.

The creation of a homeowners' association entails that full responsibility for upkeep and maintenance rests with the residents. However, the establishment of homeowners' associations requires adequate financial means and organizational support.

In a few cases the regional or local government institutions are making an effort to promote, advise and assist the new owners in creating homeowners' associations. A good example is Moscow's Department of Housing Policy, which advises the owners of the apartments directly and virtually through its website.

In the blocks of apartments where no homeowners' associations are created, the municipal housing companies (DEZi, Zheki) remain in charge of everyday management and repair, but also of channelling the different subsidies. For people living in housing provided by employers it is still possible that the companies' managers run the housing stock too, but there is a tendency to transfer this stock to municipal responsibility.

During the Soviet era, there was a variety of self-help groups and local initiatives, e.g. housing committees (ДОМКОМ). They were based on national traditions of collectivism and mutual support in rural communities and neighbourhoods. All these mainly dealt with regulating the community and setting rules. So there is a tradition of third-sector public movements in the Russian Federation and they have been closely associated with 'collective' homes, including multi-unit buildings, and the need to regulate the living conditions there.

#### **D. Organizing repair and reconstruction**

The Russian housing stock is fairly new, but due to the low quality of construction and poor maintenance it is wearing out quickly. According to Gosstroy, all *khrushevki* will have to be renovated within the coming 10 years. Other large-panel buildings are generally in better condition.

It is important to try to repair the housing stock as economically as possible and prevent its increasing deterioration, the loss of flats and the further lowering of housing conditions. At the

moment it is not economically possible to demolish all older, run-down blocks of flats and replace them with new construction. Therefore, massive economical renovation is necessary to prevent housing standards falling further. In general, costly renovations of the panel block buildings might not always be advisable. If the economic situation of the country gets better quickly, this kind of housing stock will lose its attraction as wealthier people will start wanting better and more individual dwellings and houses and living areas, and will move out of old block buildings.

Reconstruction and renovation of residential apartment blocks seems to have almost come to a halt. Renovation of buildings has shrunk heavily after the break-up of the Soviet Union and has not yet picked up. Renovation of private flats by their owners increased after the 1998 economic crisis, which as a whole was a disaster for the renovation sector.

Statistics and other information on renovation and reconstruction of buildings and flats are very limited. This is probably due not only to the lack of statistics but also indicates that there is little repair and reconstruction. The unclear situation of the ownership of buildings effectively limits all interest in repairs. Federal organizations and some municipalities have made some preliminary plans for renovation and reconstruction work but these have not yet been carried out. How to finance repairs has not been decided. It is, however, evident that private inhabitants or "private owners" are not able to finance renovations directly from their incomes. Private investors are rarely interested in financing repairs, when the incomes of the inhabitants are low or uncertain. So the only possible financier is the public sector, municipalities or the federal Government.

There is a lack of companies specialized in renovation and reconstruction work. There are Russian companies that carry out new construction, and are capable of developing new housing areas. They do not seem very interested in renovation projects, but if municipalities can organize financing, those companies will probably be capable and interested in repairing larger apartment blocks, in the same mass production way as they were once built. For smaller or

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specialized renovation projects more small firms would be needed in the market to increase flexibility and boost competition. There should be free and transparent competition between different renovation companies to improve efficiency and reduce costs. At the moment this is not the case.

When planning and starting the renovation work a technical, economic and social survey of the building stock is needed. Technical surveys of

Russian residential buildings are made both by Russian and Western experts using different methods. According to the Russian system, the condition and standard of an old building is compared to regulations for new buildings. After renovation, the old building should fulfil the standards of new buildings. This principle makes renovation work difficult and expensive and it is, therefore, not used in Western countries, where the original design of the building is the basis for renovation.



# Chapter VIII

## UTILITY SERVICES

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### Introduction

Tariffs<sup>60</sup> for housing-related services are one of the most widely discussed topics in the Russian Federation today. TV talk shows as well as professional newspapers and journals highlight the different aspects of the new tariff policy and the problems related to it. The main concern is that all residents have to start paying the full cost of the services provided - the principle objective of the national housing reform. Residents, however, fail to understand why tariffs for housing and municipal services (ЖИЛИЩНО-КОММУНАЛЬНЫЕ УСЛУГИ) continue to increase when roofs and pipes still leak, and the municipal management companies cannot repay their debts to the utility providers.

Although the concept of full cost recovery seems normal – the consumer of a service should pay for the service provided – the problem in the Russian Federation today is much more complicated. Housing and community are inevitably handled as one interrelated ‘housing and municipal complex.’ The companies of this complex provide ‘housing and municipal services’, including running the housing stock, maintaining and repairing it, but also utility services and rubbish collection. Today its major problems are related to its inherent contradictions:

(a) According to official statistics, the average resident has a reasonable amount of housing space at his disposal; and most urban apartments are equipped with the necessary amenities (central heating, piped water, electricity, etc.). However, the housing stock and the utility infrastructure are in very poor condition and during the past 15 years no adequate funding has been made available to maintain these amenities. So there is a considerable imbalance between the standard of services provided and the prices/tariffs that households are charged. Consumers do not receive value for money.

(b) Household income is low and neither the households nor the public budgets can afford the prices of the services provided. Continuously

increasing the tariffs will cause a serious crisis both for the providers and for the consumers.

The term “crisis” is now officially used to describe this situation. Professional papers and policy documents list the following priorities to overcome it:

(a) Securing financial stability for the companies providing housing and municipal services;

(b) Establishing market-based instruments for housing and municipal services;

(c) Creating the right conditions to attract investment into these services to ensure their long-term operation;

(d) Encouraging households to take an active part in the management of the housing stock.

### A. Technical condition of utilities

‘Community catastrophe’ – was a common headline during the winter of 2003 in the official Gosstroy newspaper ‘Stroytel'naja gazeta’ (Construction Newspaper). Already in 2002 there had been about 300,000 cases of heating pipes breaking. After the catastrophe of the 2003 winter, the following data were published about the condition of boiler houses. In the autumn of 2002, about 70,000 boiler houses were inspected, but only 76% of these were certified as ready for the heating season. Thus, during the extremely severe winter of 2003, there were 86 major emergencies, with dwellings cut off from heating for more than 36 hours in 38 regions of the Russian Federation. According to the press, in January 2003 heating provision was disrupted in 4,000 apartment blocks, affecting 350,000 residents.

The situation is similar with regard to the water supply. In more than 100 big cities the water supply to residential areas is irregular. On average, in the Russian Federation, 25% of the water supply is lost in the pipes and more than 40% does not meet health requirements. The deficit of water pipeline capacity exceeds 10 million m<sup>3</sup>.

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<sup>60</sup> Tariff: the target price for a service set by the relevant public authority.

According to data of Gosstroy, the rate of physical wear-out of the water-supply networks is 54.2%, of heat-supply networks 56.7%, for electricity supply 68%, and engineering communications in general 60%. About 7% of the district heating networks and 16% of water pipelines need urgent modernization. The accumulated losses within the heating networks, including those caused by the worn-out state of the pipes, equals 30% of the produced heat, which would represent 58–65million tons of fuel a year.

The annual number of accidents per 100 km of engineering communications has increased from 15–20 in the mid-1990s to 70 for water and sewerage networks and to 200 for heat-supply networks in 2000. The European average is three.

In the cities only 30% of sewers are cleaned by municipal sewerage systems to satisfy the norms. The capacity shortage of sewer systems is 9 million m<sup>3</sup> per day (16.5%), about 17% of the networks require major repair; but practically no money is earmarked for these purposes.

From 40 to 80% of the resources of local budgets and a substantial part of the budgets of the “subjects of the Russian Federation” are allocated to housing and municipal services. New housing construction brings losses to cities as every new residential or social building requires additional inputs, deepening the budget crisis.

The following facts further demonstrate the technical situation in the sector:

(a) Between 50 and 60% of the heating and sewage pipes require major repair, the remainder needs to be replaced altogether; 29,000 km of pipes are said to be in a critical situation;

(b) The actual losses of thermal energy and water in the pipelines in some regions are said to be about 55-60%, compared to the normative level of 16%, which is considered to be ‘reasonable’;

(c) The housing stock requires major repair. While the average norm for major repairs is

between 4-6% of the existing stock annually, in reality in some regions in 2002 major repair was carried out only on 0.1% of the stock.

Today not only the professionals but also the politicians on all the levels of government speak about the threat inadequate infrastructure poses to Russian cities and human settlements. The former Prime Minister, Mr. Kasyanov, speaking in the Duma in early spring 2003, analysed the critical break-down in utilities and housing during the winter of 2003 as follows:

(a) One third was the result of major obsolescence, lack of repair and poor preparations;

(b) Another third was due to the non-professional operation of the equipment, i.e. there is lack of professionalism in the sector; and

(c) Finally, the remainder was due to extremely bad weather.

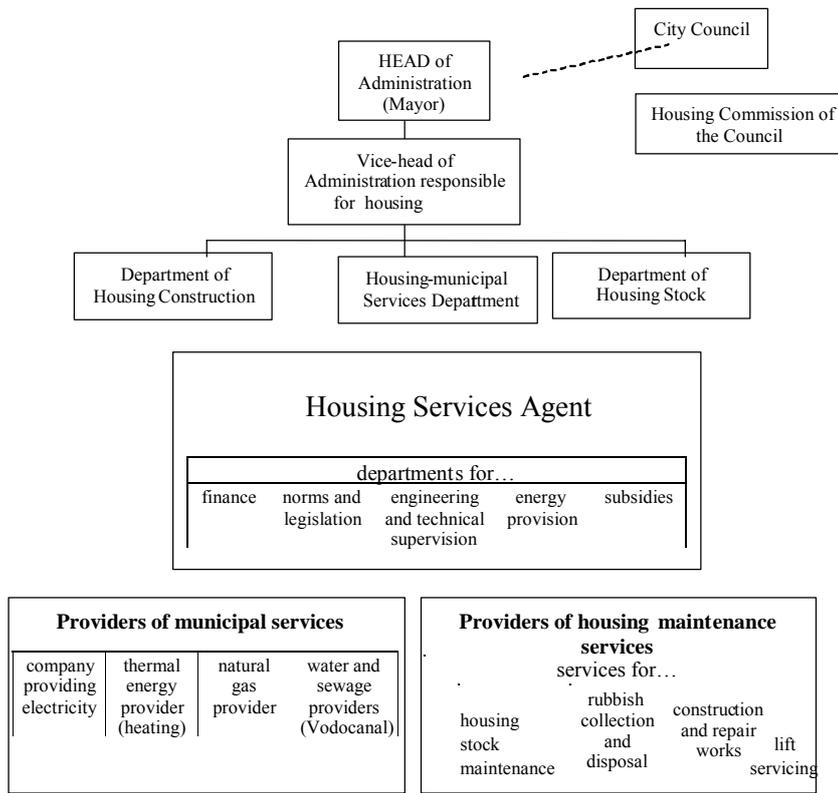
### **B. The system of management**

As described in part one, chapter III, municipalities are still seen as the owners of the dwellings and the municipal companies continue to provide most of the services. There are about 52,000 companies of different ownership with more than 4.5 million staff to provide housing and municipal services, i.e. about 600 m<sup>2</sup> of housing stock per employee. Yet, it is quite difficult to get clear data on how the staff is placed and what the responsibilities are.

The services are generally provided through municipal enterprises for maintenance, heating, water, etc. There are only a few cases where this function is exercised by privately owned management companies. Private management and maintenance companies are said to number fewer than 200. Private companies are more active in providing different maintenance work and repair, but also rubbish disposal services.

The management and maintenance of housing estates is arranged according to jurisdictions, so the service companies have access only to administratively divided markets.

**Figure V. Structure of housing and municipal**



The current system of services gives rise to conflicts of interest. If a household cannot pay for all the services provided, the municipal authorities have to make up for this shortfall. In fact, the municipal authorities should try to reduce the costs of the services so that fewer budget funds will be required for such subsidies. The municipal authorities and relevant managerial structures should strive to reduce the tariffs.

However, the municipal authorities are also the owners of the service companies and they have to pay their staff. Any losses that these companies make are also losses for the municipal authorities and social problems among the staff of these companies are of concern to the municipal authorities too.

personally responsible for the efficiency of their activities and for the expenditures incurred. An audit of heat provision in one of the regions in spring 2003 showed that the municipal ‘heating dealers’ had increased the tariffs for energy 2.5-2.8 times. This is clear evidence that the management system for providing such services lacks any incentive to reduce costs.

Assessments published in professional journals estimate that reasonable management in the sector and an increase in professionalism would cut the cost of utility provision by about 15%. Currently the housing and utilities sector ranks second after construction as the sector with the highest turnover of labour, and data about Moscow have revealed that that about 50% of the posts in the technical maintenance companies are vacant.

### C. Tariff setting

The official price level for housing service provision is termed 'economically fair tariff' (экономический обоснованный тариф). According to Gosstroy, the average is about 22-24 roubles/m<sup>2</sup> for all the housing and municipal

services. In fact, it is approximately 25% higher because of the increasing prices of energy. It is also important to keep in mind that the official tariffs cover only operating and maintenance costs and, in general, do not include depreciation of the housing stock and no funds for repair are collected.

The utility service prices are regulated by all three levels of government. Local governments set prices, tariffs and rates for the municipally provided services. Sub-federal (regional) governments control the delivery of gas, power, heat and water supply by other providers. Moreover, responsibility for setting electric power and (co-generated) heating prices is delegated to special regional power supply commissions. At the federal level, regulation of the housing and municipal services lies with the Federal Power Supply Commission and the State Anti-trust Committee.

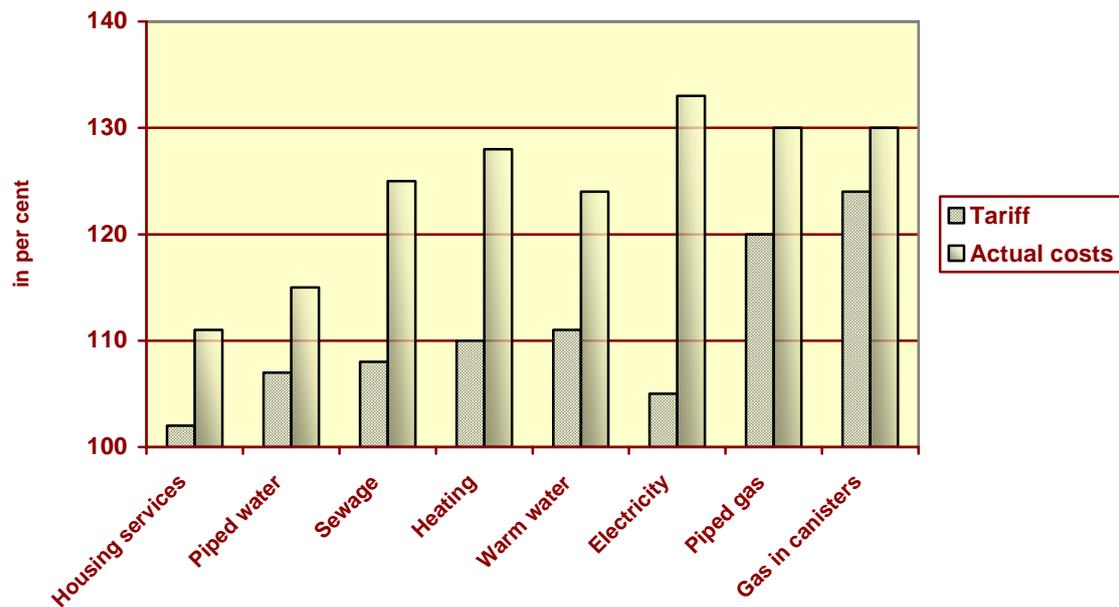
The tariffs for utilities (heating, water, sewage, but also natural gas) are normally calculated according to a standard system. The utility companies invoice the municipal managing company according to the existing norms of consumption or the actual amount of services provided (e.g. the amount of water pumped to the city) which are then multiplied by the economically fair tariff. The municipal management company divides this amount by the number of housing units in its jurisdiction and bills the consumer accordingly.

These schemes date from Soviet times. However, they are seriously flawed, especially because consumption by the final consumer (household) is

not accurate. In fact, except for electricity, there are no accurate figures as metering is very rare. Bills are largely based only on the total water or heat energy produced. They do not take into account whether the consumer has actually used the service, nor its quality.

The problem is aggravated by the fact that average consumption data (amounts) are used not only for invoicing of water, but also for calculating the norms of consumption. The national average is about 235 litres of water per resident per day; in 81 out of the 88 regions where data were available these norms were above 150 litres, with 389 litres in Moscow as the absolute maximum. However, the experience of homeowner associations in Moscow shows that it is easy to consume about 40% less than the norm when consumption is metered. So, the norms introduced for consumption are highly overestimated. If metering were more widespread, service provision would be more accountable and excess provision more difficult. For the seven regions where the norms for consumption were below 150 litres, or 27 litres as the absolute minimum, it can be argued that there is either no relevant service available, or the data provided are not fully reliable.

The main housing policy aim today, as mentioned above, is to raise all the tariffs for the services provided to households to cost-recovery levels. According to the comparative data in table xx of official tariffs and actual costs, during 2002 the costs to service providers increased more rapidly than tariffs. The official tariffs for the services that are set by the relevant authorities are much lower than the actual operating costs reported by the service providers.

**Figure VI. Increase in tariffs and costs for services during 2002**

Between 1993 and 2000 there were considerable increases in tariffs and the cost-recovery levels increased from 2-3% to 60-70% on average, not including charges for capital repairs. However, the Russian Federation still has the lowest level of cost recovery in Eastern Europe. Moreover, the service providers have come under increasing financial pressure because tariffs charged to consumers remain highly controlled, while price liberalization in other sectors has raised their costs.

In these circumstances, when tariffs are adjusted by different authorities either on the federal, regional or municipal levels, service providers have no incentive to lower the costs for utilities. If a service provider were to invest know-how and become more efficient at a relatively lower cost, the authorities would lower the tariffs accordingly. Higher operating costs on the other hand imply higher tariffs. Therefore the market is still producer-dependent and companies are interested in showing higher rather than lower operating costs.

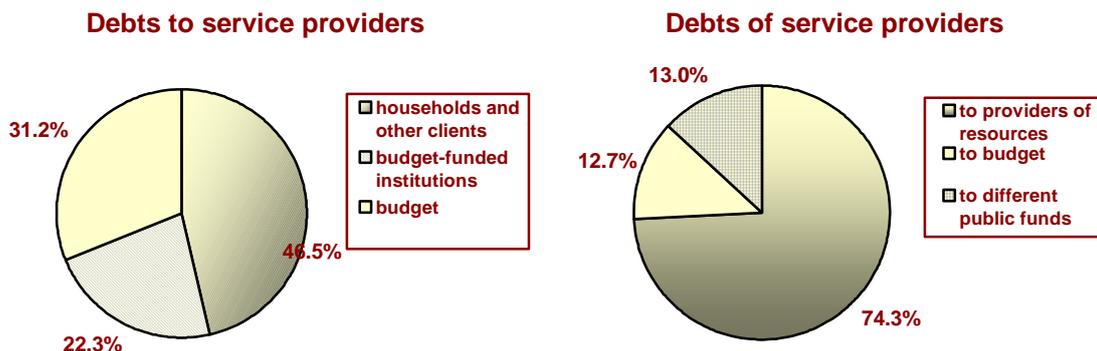
#### **D. Affordability and payments**

Utility bills often go unpaid and debts have mounted. In Moscow, on average, about 80% of

bills are paid on time, 10% are paid late and the remaining 10% are never paid. Currently, residents get bills showing the full costs of services, but they have to pay only about 60% (on average) of these costs. As incomes are too low to meet these costs in full, municipalities are expected to cover the remaining 40%.

Municipal budgets are usually small and housing accounts for about 40-60% of all municipal expenses. In Moscow housing services swallow about one third of the city's resources. As all the tariffs are constantly increasing, municipalities cannot fully compensate for the part that is not covered by households. Consequently municipal maintenance agencies do not have the funding to organize all necessary maintenance works and the municipal housing stock suffers from a lack of repair or/and maintenance. Every month the companies – especially the providers of utilities – are 2.3 billion roubles short: 0.5 billion due to unpaid household bills and the remaining 1.8 billion due to a shortage of funding from the budget.

**Figure VII. Financial situation of housing and municipal service providers**

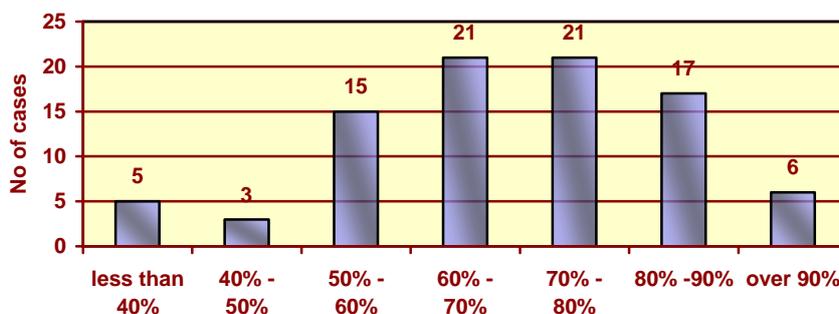


The charts above show the financial situation of the housing and municipal service at the end of 2002. In total, 184 billion roubles were owed to them for delivered but still unpaid services, the debt is 8.7% higher than the previous year. Roughly, half this debt is due by the households and by other clients, the other half is due by the budget. This shortfall in income means that the providers themselves owed 274 billion roubles to their creditors. In 2002, this sum increased by 7.8% compared to 2001.

According to the Gosstroy's monthly journal, the situation is likely to worsen substantially by the end of 2003. At best it will remain unchanged.

Based on data provided by Gosstroy for 2002, the average housing cost per resident was 465.76 roubles per month. However, on average residents paid only 322.01 roubles (69.14% of the sum due). The lowest cost per resident was 244.66 roubles and the highest 2593.28 roubles. This covered from 9.25% to 94.77% of the cost.

**Figure VIII. Cost coverage by region**



On the diagram above, data from the regions for 2002 are analysed to present the average cost covering percentages. The national average for the period was 69.14%. The histogram gives a clear picture of certain inter-regional problems of affordability. The vast majority of regions have a coverage percentage above 50%, but there are problematic regions in the far north and other

regions with severe climatic conditions where the cost coverage percentage is below 50%. Realizing this problem, Gosstroy has initiated a special national programme to resettle households from these regions.

Below is a randomly chosen bill for housing costs for June 2003 in a region where the average

housing cost per resident per month was 414.57 roubles (for 2002) and cost coverage was 56.38%.

In this apartment the household consists of two persons and the floor space is 35.7 m<sup>2</sup>.

**Table 15. Randomly chosen bill for housing costs for June 2003**  
(in roubles)

Item	Rate per unit of measurement	Costs incurred
Technical maintenance	0.51	18.21
Cleaning the stairwell	0.24	8.57
Cleaning the surroundings	0.73	26.06
Major repair	2.56	91.39
Rubbish collection	11.05	22.10
Cold water	78.05	156.12
Hot water	65.43	130.86
Heating	4.04	144.23
Gas	9.30	18.60
Radio	14.00	14.00
TV aerial	36.00	36.00
Total		666.14

From a total bill of 666.14 roubles the household had to pay only 167.77 roubles, so 498.37 roubles were subsidized from different sources. The household's share is only 26.69%. The bill does not include electricity charges.

In early 2002, Moscow's Mayor Yuriy Luzhkov started a 'pilot project'. He called on people with incomes above R 8500 (\$280) per household member per month to pay 100% of housing costs on a voluntary basis. Thousands of families received two bills: a 'voluntary' (full price) bill and a normal bill (about 60% of the full price). Families could choose to pay either of the bills. Only 44 families paid the voluntary bill in January 2002.

### **E. Government initiatives**

To address the problems of the housing and municipal services, the Federal Government initiated, on 17 November 2001, the housing reform sub-programme 'Reform and Upgrading of

the Housing and Utilities Sector in the Russian Federation for 2002-2010'. Its major idea is that the reform of the complex and the relevant services may be successful if two initial preconditions are met:

- (a) Providers have sufficient revenues to cover at least operating and maintenance costs;
- (b) Consumers are willing and able to pay the costs of services they are charged for; consumers will be willing to pay as long as they feel services are priced fairly.

The sub-programme identifies five priorities:

- (a) Increase tariffs to the level of operating cost coverage by 2003;
- (b) Discontinue the current system of privileges and exemptions;
- (c) Establish a system of personalized housing allowances as protection for low-income families;

(d) Creating joint-stock companies for the management and maintenance of the housing stock;

(e) Privatizing utility companies.

(f)

An action plan was established to carry out the measures in three major stages.

Stage one: 2002-2003:

- Draw up an inventory of debts to identify the share and reasons of the debts caused by public institutions, correspondingly due to a lack of funds in the budget; find the resources to payoff these debts, but also introduce measures to receive the due sums from the households indebted to the service providers;
- Discontinue the subsidization of the housing and municipal service sector and introduce market prices for these services;
- Improve the social security system for residents.

Stage two: 2004-2005:

- Develop the principles of competition in the sector;
- Introduce professional management in the complex;
- Create instruments to monitor and regulate the activities of natural monopolies;
- Improve the financial and technical situation of the utility companies by introducing management through concessions;
- Introduce personal housing allowance accounts for all residents.

Stage three: 2006-2010:

- Attract private funding to the housing and municipal services sector;
- Propose instruments to ensure the stability of service providers;
- Make available different banking credits.

However, there have already been delays.

# Chapter IX

## SOCIAL HOUSING

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The cohesion of a society cannot be seen independent from its housing situation. The Russian Federation's economic and social transition during the past decade affected some population groups more adversely than others. To protect the most vulnerable from despair and social isolation, a social safety net is needed and it has to include provisions for those households that are unable to solve their housing problems unaided. This chapter looks at the social housing thematic in the Russian Federation. It first looks at the current situation and the main challenges with regard to housing provision to the socially weak, including the current system of targeting of housing support. It then moves on to describe the impact of transition policies, in particular the large-scale privatization policy, on the capacities of the different actors in the housing sector – public institutions at the different levels of government, condominiums, etc. – to address the housing concerns of the socially weak.

### A. The current situation

Social housing in the context of the Russian Federation today is a complex theme. The first step in any discussion on that topic would need to address the question on what is meant by social housing and what is included in this notion. The present structure of the urban housing market in the Russian Federation is approximately 20% private and 80% multi-flat blocks, predominantly municipally owned. These municipal blocks of flats are in turn split approximately 50-50 between privatized and rented units.

It is tempting to define social housing as rented units within municipal blocks of flats. However, the specific characteristics of Russian privatization and the legal structures for the municipal blocks mean that no discussion of social housing can ignore the privatized flats within these multi-flat blocks.

Firstly, cost-free privatization means that tenure and economic circumstances are by no means consistent. There are many relatively needy - especially elderly - flat owners within the multi-flat municipal blocks. Secondly, since property

taxes and pure rent (Nayem) are both modest, the running costs to both privatized owners and tenants are largely identical, consisting of utility and maintenance charges. In an overwhelming number of cases, the municipality retains responsibility for the structural condition of the block as condominium associations normally do not accept this responsibility even where a majority of the individual flats have been privatized. For these reasons we will refer to these municipal multi-flat blocks as mixed-tenure public housing, of which the rented units – or social housing more narrowly defined – can be seen as a subset.

Russian social housing thus suffers from being a problem within a problem. Social housing cannot be improved without resolving the issues around the municipal blocks - the mixed-tenure public housing. The thrust of social housing policy over the coming decades must be progressively to disentangle social housing from the wider challenges facing mixed-tenure public housing. This is critical in order to allow the State to focus its scarce resources on those in greatest need. In other words, the Russian Federation needs to make the step from providing public housing to virtually all its citizens to targeting specifically needy and vulnerable people or categories of people for social housing.

It is striking in discussions with Russian housing professionals that housing is expressed almost exclusively in terms of surface. There is little focus on dwellings, households or people. Defining the priority target groups for social housing and designing buildings around these people – rather than expecting the people to adapt to a fixed form of housing provision by construction type or tenure – is the long-term future for social housing in the Russian Federation, as in all advanced societies.

Radical improvement can certainly not be achieved overnight. Mixed-tenure public housing exists as a fact. Inevitably much public resource will be diverted away from the specific area of social housing to address the urgent need to maintain the fabric of these buildings which,

whatever their failings, are at present the essential means of delivering housing to the overwhelming bulk of the urban population.

However, throughout the process, the goal of social housing policy, i.e. the creation of rented and other forms of subsidized tenure for specific groups based on economic need or vulnerability with housing designed around their requirements, must not be lost sight of.

The remainder of this chapter reviews in turn the tactical challenges which need to be overcome in the medium term in order to be able to deliver this longer-term vision. The focus will be first on the issue of targeting resources by need, then on how to maximize existing resources in the context of huge maintenance liabilities in the public housing stock, before reviewing the interaction of the various levels of government in the context of social housing.

## **B. Main challenges**

Three distinct issues are specific to the Russian Federation when trying to define needy or vulnerable groups for social housing. The first of these is the historically grown notion of collective provision, while the other two relate to the phenomenon of privileges or “mandates” and “poor owners”.

### **1. Collective provision vs. means-testing**

The concept of targeting or means-testing is relatively novel in the Russian Federation. Until a decade ago, collective provision was both ideologically and economically a given. The transition to a market economy has created significant disparities in individual economic circumstances, particularly in Moscow, where there is a sizeable, financially independent middle class, which the city authorities estimate at between 25-30% of the population. Given the present housing structure, the majority of this middle class will still live in mixed public housing. If they have privatized their flats, they will enjoy upside capital appreciation, while the public purse, in most cases, still takes responsibility for the fabric of the building.

This is a powerful example of the opportunities that may exist through appropriate incentives (such as low-cost mortgages) for gradually moving this category into privately owned condominiums and so freeing up social resources.

At present, municipal waiting lists are based on the housing space available to an individual. The primary drivers are not their social vulnerability or income (“means test”).

It can be argued that means-testing is a luxury when the average standard of living across the Russian society remains depressed. However, if means-testing is not introduced, State resources will continue to carry individuals even as their economic circumstances improve. The example of the growing Moscow middle class is telling. The economic policy of the Russian Federation is designed to create such financially independent sectors of the population throughout the country.

It is important that social policies are in place to protect the population in case economic policies are not as successful as quickly as envisaged. It would be strange however to design social policies on the assumption that key economic policies will never succeed.

It can be further objected that means-testing is complicated by the lack of transparency in many individuals’ true financial position. However, means-testing does already apply for social security and other support payments to cover housing costs, so there is no reason why it should not also be adopted as one of the key criteria for allocating social housing.

### **2. Privileges and mandates**

Means-testing in the Russian Federation has a further challenge due to the system of privileges or mandates which grant inter alia priority housing rights to different classes of citizens. The privileges may cover up to 70% of the population and cover an estimated 40% of the population for housing payments alone.

While some of this grouping is consistent with targeting State support to the needy, a

considerable number of beneficiaries are from the relatively comfortable area of the public sector.

The impact of privileges on waiting lists for social housing is dramatic. According to Moscow city, applicants with privileges receive 50% of annual allocations and can expect to be relocated within five years. Other applicants, who may have far fewer financial means, can wait forever.

As a result the waiting lists have lost credibility and many needy people no longer register at all. Therefore, waiting lists are likely to significantly underestimate real social housing needs across the country.

The Russian Federation is actively reducing the number of privileged groupings, but, as yet, no effort has been made to integrate the federal system based on privilege with a more means-tested municipal approach. Even within the municipality, means-testing is incomplete, being based primarily upon dwelling space not financial capacity.

If means-testing is accepted as a guiding principle for targeting social housing and it is also accepted that federal takes precedence over municipal, the following integrated order of priorities for social housing waiting lists emerges:

	Means-tested	Non means-tested
Federal privilege	1	3
Other citizens	2	4

### 3. "Poor owners"

Cost-free privatization has resulted in many property owners who are actually poor. There are a few examples of condominium associations within the public housing sector where the owners had formed an internal and informal social security system to support elderly and poor owners unable to meet their share of the condominium's maintenance bill.

It is therefore possible in Russian mixed public housing to find a relatively comfortable "tenant" living next to an indigent "owner".

It will take many decades to eliminate this mismatch between economic circumstance and housing tenure. The solution requires a systematic long-term effort to incentivize more rational allocation of social housing. Such incentives might be as follows:

Existing situation	Incentive	Desired future situation
Financially comfortable tenant or privatized owner within mixed public housing	<p><b>Positive</b> Subsidized affordable mortgage</p> <p><b>Negative</b> Higher property tax on privatized mixed public sector flats</p> <p>Increased pure rent (<u>nayem</u>) for wealthier tenants in mixed public sector flats</p>	Private owner in real private sector, i.e. directly or through condominium taking responsibility for structural as well as day-to-day maintenance

It is important to note how vital a functioning mortgage system is likely to be to Russian social housing. Without a mortgage market, it is difficult to see how wealthier households within the existing mixed public housing can be enticed towards the real private sector.

Without the ability to focus scarce resources on those in need, it is unlikely that the State will be able to begin a social housing new build programme, which is essential if a real Russian social housing sector is to evolve.

The reason why such new build is critical is the probable unsuitability of much of the existing

Financially comfortable owners/tenants	→	Private sector – either new build or public blocks upgraded to genuine condominium status
Financially needy but able-bodied owners/tenants	→	Existing public housing blocks on rental agreements or other subsidized tenure
Elderly and special-needs owners/tenants	→	New build social housing on rental agreements or other subsidized tenure

It must be emphasized that the shift towards new social housing construction will be gradual and over a lengthy period. Social housing is expensive in terms of public budgetary resources. For example, the capital cost of general-needs social housing in England (where private finance has been available within social housing for 15 years) is borne 50%-60% by the State, whilst for more specialized social housing the share of the State rises to 95% in many cases. At present in the Russian Federation only Moscow city has a substantial “social housing budget” intended to be used to fulfil the needs of applicants on the waiting list.

### C. Financial challenges

#### 1. Public housing blocks

The financial challenges facing the present mixed-tenure public housing system are considerable. The estimated heavy repair backlog across the

mixed public housing for true social housing. For general needs (able-bodied individuals and families), the existing stock, adequately maintained, may provide an attractive long-term solution.

However, for elderly or special-needs tenants, accessibility issues and lack of care and support facilities are likely to be serious impediments to using existing mixed-tenure public housing as a long-term solution.

A possible long-term outcome for the existing mixed-tenure public housing stock is thus:

country amounts to R 550 billion, or twice the annual gross turnover of the housing sector. The situation is deteriorating. Within one district in St Petersburg it is estimated that a 300-350% increase in the heavy repair budget is needed to meet current requirements. In Nizhny Novgorod the demolition/repair of dilapidated/run-down stock is barely 50% of the required level.

The lack of reliable stock condition surveys makes it unclear how accurate the R 550 billion estimate is, but also makes it difficult to predict future trends. There is the clear risk that obsolescence and the underfunding of the past decade will result in the backlog increasing at a greater than linear rate.

Although the current mixed public housing blocks are in many ways far from ideal, they are at present the only means of providing housing to the overwhelming majority of urban Russians. It is therefore imperative that the current heavy

repair backlog should be cleared as the most pressing priority.

## 2. Implicit and hidden subsidies

Some of the backlog can and is being addressed through demolition and re-provision using private finance. The immaturity of the wholesale and consumer finance markets, limited competition among construction firms and the general level of economic wealth will limit the ability of the private sector to respond to the full magnitude of the challenge in a realistic time frame. There are, however, most likely unrealized opportunities for expanding “planning gains” as discussed below.

For the greater part, the State will need to share this burden with the population and this means eliminating a vast array of subsidies, which the State simply cannot afford if the housing stock is to be maintained. These subsidies include:

- (a) Incomplete recovery of utility and maintenance charges including unfunded federal mandates;
- (b) Maintenance charges that often fail to include a portion for heavy repair;
- (c) Pure rent or nayem at miniscule levels;
- (d) Nominal property taxes on privatized flats within public housing blocks;
- (e) Cost-free privatization even on new and recently refurbished properties.

The present economic conditions mean that some people require all such subsidies and most require some subsidy. Hence elimination of subsidy means the elimination of implicit or hidden subsidy, since by definition these are indiscriminate and wasteful. The thrust of all the measures discussed in this chapter is to end implicit and hence indiscriminate subsidy and move towards grossed up charges offset by explicit means-tested and hence targeted support.

Housing is at present an intensely political area, in which the electorate is offered significant inducements by rival parties. Since the costs of these inducements are implicit, the illusion is created of a “free lunch”. In reality what is happening is that current general consumption is being financed by foregone capital expenditure on the mixed public blocks, which house 80% of all urban Russians and which are falling into increasing disrepair.

Two issues are of particular relevance to social housing issues: the lack of pure rental charges and cost-free privatization. But first this chapter discusses the financial challenges condominiums are currently facing.

## 3. Financial challenges facing condominiums

Within recent purpose-built private sector housing, condominiums are potentially highly effective. Household incomes are high and the property maintenance charges should be relatively predictable.

An enormous effort is being made to create condominiums within the public housing sector. Thus far less than 1% of households within the public sector are covered by condominiums. Many of the challenges facing such organizations have already been discussed – tenure/economic mismatches and mixed rental/privatized tenure.

It is questionable if such condominiums will ever be able to make a serious contribution to the heavy repair burden – either the existing backlog or upcoming. Incomes are likely to be weak or at best uneven, whilst the structural maintenance liabilities are not transparent and at worst ruinous. Insurance for the entire block is virtually non-existent.

Creating condominiums in the existing mixed public sector housing blocks may be effective to meet current or day-to-day maintenance. However, few households will want to shoulder the huge potential structural liabilities in large and often visibly poor-quality municipal blocks.

Serious consideration should be given to limiting the liability of public housing condominiums until full building insurance is available. In addition, social security should be available to those condominium members who are truly unable to meet payments.

There are constitutional issues concerning the compulsory memberships of condominiums. It must surely be easier to address this constitutional issue if it is clear that the demands on condominium members within the mixed-tenure public housing blocks are affordable and fair.

This merely serves to emphasize that only the State will be able to finance the bulk of public housing heavy repair. However two areas of subsidy militate against the State successfully shouldering this burden. These are discussed below.

#### 4. Rent charges

Rent in a Russian context hardly deserves its name. Pure rent or *nayem* is estimated at between R 0.1 and R 0.12 per m<sup>2</sup>. Compared to this, utility and maintenance charges average R 24 per m<sup>2</sup>.

The absence of pure rent represents a significant subsidy to tenants but on an indiscriminate and implicit basis. As explained above, there is no automatic link between tenant status and financial means.

The present situation is exacerbated by the fact that service charges rarely provide for a heavy-repair sinking fund. As such, there is no direct correlation between housing charges and the capital costs of providing the housing.

It may seem visionary to discuss pure rent when even utility and day-to-day maintenance charges are still not fully recovered. However, housing is a long-term business and this is compounded by the need to reform the system of housing subsidies and to develop an offsetting social security system - itself a long-term undertaking. It will be difficult to develop and see through the necessary reforms over an extended period of time unless there is a genuine understanding of the long-term goal.

Introducing a pure rent - even if heavily subsidized - that is linked to capital costs, including a real market price for land is also going to be important if rational capital allocation decisions are to be made in respect of new social housing construction. As discussed above, this will ultimately be necessary once initial stabilization of the public housing blocks is achieved.

#### 5. Cost-free privatization

Cost-free privatization has achieved a number of benefits. It has provided the beginnings of a traded housing market, enabled individuals to find

personalized solutions to their housing needs and, through inheritance, begun a modest cascade of wealth across generations. At the same time cost-free privatization has led to confusion of tenure and need. It has significantly reduced the ability of the public sector to offer rented accommodation to those in need and left the public sector in the unenviable position of being responsible for the structural integrity of ageing public housing blocks, whilst the upside capital appreciation of the individual flats is held by individuals.

In Moscow alone some R 2 billion worth of rented accommodation is privatized on a cost-free basis annually. This equates to approximately 225,000m<sup>2</sup> of rental space assuming US\$ 300 m<sup>2</sup> construction cost or almost a quarter of the new social rented accommodation being built each year by the city. The situation in other areas is far worse than in Moscow, as it is one of the very few regions able to construct new social housing at all.

#### D. Municipal, regional and federal responsibilities

##### 1. Roles, responsibilities and interrelations

It is widely acknowledged that the municipal sector is the last area of the economy to begin the transition from the earlier collective command-and-control environment. The guiding principle thus far has been to allow the municipalities and regions to lead on this area under general federal guidance. At the same time, the housing sector has formidable financial challenges and grossing up subsidies as discussed above will inevitably compound the scope of housing-related social security.

It is clear that the Russian Federation will not merely need to be involved in setting overall housing policy but also become increasingly engaged financially if the challenges are to be effectively addressed.

At present social security support is primarily a regional responsibility with limited federal finance estimated at approximately 20% of the total budget cost.

There are also variations in regional support levels, most of which become effective well before the 22% of household income, which is the

federal threshold, as well as differing administrative arrangements. It is open to question whether the regional level is able to carry the financial and policy burden involved.

The relationship between Federation, region and municipalities might best be described as evolving, with a level of tension in the budgetary sphere. There is a real risk that housing and the municipal sector become a victim of this institutional tension.

The Federation has on occasion created expectations – examples being the level of federal privileges and the new programme to clear the heavy-repairs backlog – without matching these expectations with adequate funding.

The present bill on the municipal economy is in fact being delayed, while the financeability of various measures is addressed.

Besides the relative newness of federal structures, two specific features probably contribute to the present situation. Firstly, there is no single point of responsibility for housing at federal level either in terms of ministry or parliamentary subcommittee. Secondly, there is a lack of transparency in the finances of the municipal economy so that there is more room than usual for argument over the real capacity of lower tiers of government to fund federal initiatives.

If housing is to flourish, the Federation will need to invest heavily as discussed earlier. Whilst it is surely right to encourage the municipalities to take the lead delivery role, the Federation will need to be sure that federal funding is being effectively deployed to meet federal targets.

## 2. Budgetary relations

The present budgeting situation within the Russian Federation is difficult. Of 87 federal regions only 8 are net contributors to the overall national budget.

Within federal regions the major city may itself subsidise the region. Even in a case like Ivanovo, which with average monthly income per head at \$80 is below the national average, a net R 1.5 billion is transferred to the poorer municipalities within the region by the main city. If the city overperforms against budget, this outperformance

is in turn shared with the rest of the region.

This is a complex area. On the one hand, the overall lack of budgetary resource and the economic challenges of non-urban municipalities make significant redistribution unavoidable. Set against this, the present situation offers no incentives to the urban municipalities to outperform, transfers funds away from areas with large housing heavy-repair backlogs and potentially stifles the ability of urban centres to lead the much-needed process of wealth creation.

It is recommended that the Federation should review whether the present redistribution model is aligned to its critical path policy issues. As part of this review, the Federation needs to be clear on the importance that it attaches to the municipal economy in general and urban housing in particular relative to its many competing priorities.

Fragmentation of responsibility for housing is not confined to the federal level. On the ‘subject of federation’ level, an issue such as homelessness can be found in a different department from housing, whilst regular housing management and heavy repair/construction, if in the same department, generally appeared quite distant cousins. It is likely that a stronger holistic focus on housing and a reduction in the autonomy of the various housing committees would be desirable.

It is further evident that, within the federal cities (Moscow and St Petersburg), the districts are essentially administrative only with no independent budgetary authority. Given the size of these two cities, one has to question how effective any totally centralized control can be. Indeed Moscow city has a commitment gradually to empower the districts.

This lack of independent district budgets is particularly relevant in respect of “planning gain” - the social return in terms of cash, new units or housing repair that a private contractor commits to in return for land and planning permission. It is striking that these planning gains are not transparent as a contractor might acquire rights, for instance in a suburb, in return for a cash contribution to the city budget, which might be used in housing elsewhere [or possibly even for another budget line].

As economic prosperity and hence land prices increase, planning gain will become ever more valuable a social resource and it is strongly recommended that such planning gains should be accounted for in the district where they arise and any inter-district budgetary transfers linked to these gains should be fully transparent.

Planning gain is a powerful tool. The typical approach to urban renewal in the United States or the United Kingdom has been to create beacon sites on which landmark buildings are constructed to generate a chain of rising land values. This in turn stimulates further private development with in turn opportunities for planning gain in support of social housing and amenities.

In certain cities there are relatively attractive individual buildings being constructed but generally in sites where there appears little opportunity for further new construction in a similar style. Municipalities probably require training in how to maximize this benefit.

The Congress of Municipalities organizes benchmarking and best practice conferences. However, the federal Government will need to strengthen its own involvement in this area in order to ensure efficient knowledge transfer across the country.

# *Chapter X*

## *NEW CONSTRUCTION AND URBAN PLANNING*

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This chapter aims to analyse current challenges within the system of new construction and spatial planning. Section A assesses practices in new construction, including the organization of the construction industry, trends in the demand for new construction, as well as concerns of construction norms and quality. Section B examines the planning process, which includes policies of land pricing, plan development, the planning environment and permission procedures.

### **A. New construction**

#### **1. Predominant characteristics of new construction**

The Russian Federation with its enormous diversity of climatic conditions, cultural traditions and size of settlements as well as with the naturally diversified availability of natural raw materials suitable for the production of construction materials is strongly predisposed to the development of a highly differentiated construction industry. However, due to the long period of a highly centralized system of governance the Russian construction industry is still dominated by the construction of standardized, multi-storey blocks of flats. Ten years ago only five types of buildings were built. Now architects and constructors enjoy the possibility of more variety in the design of buildings.

With changes in technology the formerly common large-panel buildings give way to more complex construction systems in which concrete (including light concrete), brick and some ready elements of the construction are used. Concrete poured into tunnelled forms is used for the fast construction of housing blocks. A relatively simple and cheap method for the improvement of energy efficiency of buildings has been introduced in Moscow and Vladimir regions. Similarly to the commonly used method of the concrete construction, liquid concrete is poured into a form, which is made of boards. Then the concrete hardens and the form is no longer needed to keep the structure and therefore boards have usually been removed. However, as these boards are made from material

(e.g. prefabricated polystyrene sheets) which has better thermal characteristics than concrete, with the new method the boards are left stuck to the concrete walls for thermal insulation.

The permanent growth of the above type of housing construction is particularly strong in the cities of Moscow and St Petersburg, in the republics of Chuvashija, Adygeja and Tatarstan, in Sverdlov, Novosibirsk, Tomsk, Tjumen, Kemerovo, Nizhny Novgorod, Vologda, Samara and Sakhalin regions, in Primorsky kraj. However, the bulk of new construction still consists of complexes of multi-storey block of flats. Low-rise residential buildings are still a rare phenomenon in Russian cities, let alone detached, single-family houses. The “Kurkino” housing estate in Moscow constitutes an example of recent housing construction. The whole estate is planned for more than 30,000 inhabitants but only a small fraction consists of single-family houses built specially for veterans. Buildings with fewer than 40 flats are considered “elite housing” in Moscow. Relatively smaller buildings are built on sites of historic and cultural importance (e.g. Pushkin near Saint Petersburg) where limits on the height and size of new construction protect the historic townscape.

As described in chapter VIII, the provision with utilities is insufficient, in particular in newly built single-family houses. Out of 22,600 single-family houses built in 2001 only one third (45.7% in cities and 22.5% in rural areas) were fully equipped, i.e. running cold and hot water, central heating, sewerage.

Newly built flats in multi-storey blocks are usually delivered in a very rough, unfinished state apparently to give to the owners the opportunity to complete the flat according to their individual wishes. As a consequence of the poor offer of specialized services, interior work is often done, more or less successfully, by the owners themselves. As a result the final standard of flats varies widely.

The domination of multi-family blocks in Russian cities goes in pair with the domination of large

construction companies on the Russian construction market. This dominance is also closely related to the situation of housing finance described in chapter V. The lack of a secure system of construction finance leads to a situation where banks provide loans for housing construction projects only if they trust the developer, i.e. if they have collaborated with the developer successfully for a long time. This situation favours for large established construction companies that are more or less rooted in the communist era and still accustomed to the style of housing construction of that time. This in turn hinders the development of a more diversified construction industry. This is how a closed circle in the construction industry was created. Large companies prefer to take up large-scale housing projects on empty construction sites rather than small-scale developments within a built urban environment. Local authorities, which usually obtain a share of the newly constructed flats, have little influence on the type and the quality of construction.

Construction companies in the Russian Federation undergo a double licensing procedure. Professionals in the construction industry must have their individual licences certifying their qualifications in construction or design. The company that employs them must have a separate licence for the same work. There is an acute shortage of small or medium-sized companies capable of performing small-scale construction works within built-up areas without excessively disturbing the daily life of the inhabitants of the neighbourhood. This concerns mainly constructions between existing buildings, reconstruction or extensions of existing buildings, major repairs as well as provision of utilities for existing single-family houses.

## **2. Capacity and know-how of the building industry and local authorities**

The capacity and know-how of the building industry and local authorities do not develop evenly in all areas related to housing. In big cities there are many construction companies which use modern construction technologies. However, the progress takes place mainly within the predominant type of construction, i.e. the construction of multi-storey flat-roof housing

blocks on empty construction sites. There is relatively little competition on the construction market. So there is also little incentive to take up innovative projects where new technologies would be accompanied with diversified design, type and scale of construction for the sake of the inhabitants, who would have a wider choice of flats in terms of price and comfort.

Yet local authorities depend on large construction companies to enlarge the municipal housing stock. They are thus unable to stimulate competition on the construction market. Local authorities have little knowledge about and exposure to situations where they are neither the developer nor the constructor but should create enabling conditions and stimulate fair competition among contractors for the benefit of the community.

## **3. The polarization of housing demand**

Figures quoted in chapter II indicate that the current pace of new housing construction hardly exceeds the pace of deterioration of the existing stock. At the same time the average size of newly built flats is increasing. Diverging trends have occurred between the cooperative sector of housing construction (decreasing role) and individually financed construction (increasingly important role).

There is a trend towards polarization of newly built housing stock, as the share of large and small flats in the total of completed flats grows and that of medium-sized flats (i.e. two or three rooms) decreases. This reflects growing disparities in income levels. A relatively small group of rich people creates the demand for large flats (four rooms or more), whereas two other groups create the demand for small flats: those who can afford only the cheapest flats and those who manage to meet their own housing needs and still have some extra money. So they purchase a small flat, which they rent in order to have an additional and relatively secure source of income.

There is one more group of people who need flats, but do not create any market demand because they cannot afford it. They continue to live in the deteriorating stock and wait for their turn in the allocation of a new flat.

Diversified incomes mean that new housing construction should also become adequately diversified. It should meet the growing expectations of the rich and at the same time it should create affordable options to as many people as possible. The more people can afford their own flats, the sooner the municipality will be able to meet the basic housing needs of those households who need assistance.

#### **4. Construction norms and standardization**

Construction norms in the Russian Federation are established on the federal level and the level of the “subjects of the Federation”. Federal norms are divided into:

- (a) Construction Norms and Specifications (SNiP);
- (b) State Construction Standards (GOST);
- (c) Code of Rules for Design and Construction (SP).

Moreover, the “subjects of the Russian Federation” prepare their own regulatory documents called territorial construction norms (TSN) for issues not regulated federally. The State Construction Committee approves and registers these territorial norms. The whole system of construction norms is gradually being updated. Some old norms have already been replaced with new ones, but for other issues norms drawn up in the 1980s or even earlier are still in force. Special attention has been paid recently to energy efficiency. The 1996 Law on Energy Saving tightened federal norms of heat transmission and consequently the “subjects of the Federation” have been introducing territorial construction norms for energy efficiency. However, as stated in chapter III, energy-efficiency standards are still below Western ones.

Russian construction norms are usually very detailed. As regards safety of construction and minimal standards they are usually good. However, because the State was long the only investor, the only developer and the only owner of land and buildings, some norms contain not only safety requirements but also detailed regulations on how buildings and other facilities should be built or designed. Even some recent norms are in the same style, i.e. they contain very detailed indicators leaving little room for individual wishes.

The major problem is not so much the contents of norms but their role, in housing construction. As a result of the lack of competition among builders even in newly constructed buildings, minimal normative values instead of clients’ demands are used as a basis for designing flats. Symptomatically, constructors on several visited construction sites when asked about specific features of the flats under construction assured that they were built in accordance with Russian construction norms. Norms should provide minimal conditions, in particular with regard to safety, whereas competition among constructors should lead to the development of a construction industry oriented towards satisfying consumers’ needs within affordability limits.

Therefore, there is a need to stimulate competition in all branches of the construction industry. Municipalities should focus their efforts on the organization of fair competition in the construction market. Particular emphasis should be put on the competition for municipal housing construction.

#### **5. Quality of housing design**

The economic and social sustainability of a building stock is largely dependent on its design quality. As there is only a limited tradition of diversified housing architecture, a whole new culture will have to be developed. There is a clear need for better design and for further diversification of housing forms to satisfy the needs of a diversified clientele. Builders will have to start listening to the consumers. The scale and size of operations as well as the way in which new collective ownership is organized will strongly influence the character of the new housing stock and hence the whole urban environment. The outcome will depend on the choices made in the near future by a large number of stakeholders, and it will be crucial whether the future users or the producers, developers and big construction enterprises put their stamp on these developments. One can expect that growing demand by the wealthy will lead to a gradual improvement in the quality of design of large and expensive flats. As regards the smallest and cheapest municipal flats built for people on waiting lists, market forces alone will not improve quality.

Therefore, local authorities should pay more attention to the quality of design of the smallest and cheapest category of flats. The smaller the flat, the more carefully it should be designed to make life in it bearable. Even small improvements in design not entailing excessive costs may facilitate significantly the everyday life of people who have to live on a very small area. For instance, the provision of sufficient (not only minimal) width of internal doors enables more flexibility in the location of furniture and this contributes to an efficient use of the floor area.

## 6. Wooden housing construction

There is a lack of statistical data about wooden construction. However, observations in many Russian cities and the countryside suggest that a significant part of the urban housing stock and the vast majority of rural housing are built out of wood. This part of the stock is in particularly poor technical condition, as wooden buildings usually date back to the pre-revolutionary era. Little care is taken of this stock although many of these buildings constitute a valuable part of the cultural heritage. Many wooden houses are still inhabited although they are totally run-down or dilapidated. In many cases, especially if the building is located in the city centre, the only solution is likely to be demolition and relocation of the inhabitants. However, there are several reasons for which this approach should not be applied to the whole wooden housing stock.

Firstly, it is unrealistic to think that city authorities will be able to provide sufficient new flats to replace the wooden housing stock in the near future. Secondly, many wooden single-family houses have been privatized together with the plots of land beneath them and their inhabitants are often against being moved to apartment blocks. Thirdly, wood as a construction material has many advantages and although there may be a shortage of high-quality modern wooden materials, raw wood is a relatively easily available construction material in the Russian Federation.

Bearing in mind the long period of neglect, simultaneous action in the production of wooden construction materials as well as in design and training is needed.

## B. Spatial planning

### 1. Planning documentation

Spatial planning regulations heavily influence the environment around housing estates as well as the provision of housing. The allocation of land for housing is done in local spatial plans. Hence the importance of spatial planning for housing.

Spatial planning in the Russian Federation is moving from a situation where the State administration was the only actor in the development planning process, i.e. the only landowner, the only developer and the only spatial planner, to one where many actors are involved and there is a need for common rules and for securing a public interest among all other interests.

The new Town Planning Code of 7 May 1998 provides the legal framework for spatial planning. It seems to be a sort of compromise between the old planning system and the requirements of the new socio-economic conditions. Probably due to the transitional situation in many Russian cities and regions, the regulations of the Code are vague in some places. A broad term "planning documentation" is used for a set of documents. Each level of administration has its planning documentation. So two types of documents serve the purpose of spatial planning on the federal level:

- (a) General Settlement Scheme of the Russian Federation;
- (b) Consolidated Urban Planning Scheme, which covers the area of two or more "subjects of the Russian Federation".

The territorial complex urban planning scheme of the development of the "subject of the Russian Federation" constitutes the planning documentation at regional level.

The local level planning documentation contains the biggest set of documents divided into two groups. The first group contains the following urban planning documents:

(a) **Territorial complex urban planning scheme of districts and rural areas.** According to the Code, this scheme should contain, among other items, basic directions for the implementation of government policy on spatial development. It should also contain rough divisions of the territory into different functional zones;

(b) **General plan of urban and rural settlements (Genplan).** According to the Code, this is a basic urban planning document defining the directions and boundaries of spatial development. The contents of the Genplan and the above described scheme overlap significantly. The Genplan is very similar to a spatial development plan of an urban area;

(c) **Draft lines of urban and rural settlements and other municipal entities.** This document is based on Genplan or the complex urban planning scheme. It may be a separate document or small towns and villages it may be incorporated into the general plan;

(d) **Rules for building in territories.** This document should also be based on the general plan or the complex urban planning scheme. It is the only document which, according to the Code, should be a normative local legal act.

The second group contains more detailed documents related to the process of developing land. These are:

(a) **Layout projects.** These are made for elements of the planning structure defined in the general plan. They cover selected parts of urban and rural settlements. They are therefore more detailed than general plans;

(b) **Projects of land subdivision.** These contain the planned subdivision of the area into plots of land. They may be incorporated into the layout project;

(c) **Development project.** This may be prepared by the developer. It covers either the single plot or the area defined in the layout project. Its contents include the exact location of buildings and other structures, number of storeys of buildings as well as other architectural and technical characteristics of planned buildings.

To make the matter more complicated many cities still have old master plans developed during the Soviet era.

Planning documentation provides the legal basis for location decisions. Although only “rules for building” are required to be a local legal act, the general plan (Genplan) is now usually perceived to be the crucial instrument for the introduction of new spatial planning rules. According to the Town Planning Code, the general plan should shape the living environment of settlements in the interest of the population and the State. It should also define directions and boundaries of the spatial development; zoning regulations and rules for the provision of utilities, for the development of the transport network and for basic social services. The plan should also include rules for the protection of the cultural and natural heritage.

Moreover, Genplan is expected to perform several other tasks not explicitly listed in the Code. It should be a spatial reflection and a supportive instrument for the implementation of the city development strategy. It should delineate the economic and functional spatial structure of the city. It should constitute a basis for the spatial allocation of particular land-use types and different forms of landownership. It should also delineate units of the territory for more detailed planning documents.<sup>5</sup>

The general plan is expected to be both a policy document and a legal regulatory document. Moreover, at the current stage of development planning it is also expected to play a distributive role with regard to landownership. This role is performed in several ways. The allocation of land for public roads, social services and other public purposes excludes some areas from privatization. On the other hand, allocations for other purposes (e.g. commercial activities) create demand among potential buyers. The distinction between areas for development and agricultural land also influences conditions of privatization because different regulations apply to the privatization of these two types of land. Finally, it is possible to earmark land in the plan for a particular type of ownership if the city’s strategy foresees this in the general plan. The distributive role is a unique feature of

current spatial plans. The next generation of spatial plans will have to take into account the landownership structure shaped by market forces. Therefore, there is a need to identify now the plots of land that should not be privatized in order to secure public interest (future transport corridors, public open space, etc.). A healthy balance should be struck while doing this.

There is a need to clarify the roles of the different local planning documents in the planning system. To make the system more transparent, policy documents, local legal acts and project documentation should be distinguished as clearly as possible.

## **2. The planning process**

Another set of problems relates to the participation of different actors in spatial planning, especially in the process of plan-making. So far spatial development plans have been prepared by a relatively small group of professionals. This refers not only to old master plans from the Soviet era but also to the new plans under new socio-political conditions. The project of the new general plan of Moscow was prepared in cooperation between planners and a special committee of the city council and then approved by the council without much controversy.

By law, projects for new spatial plans should undergo a public review. The Town Planning Code states that local self-governments should establish their own procedures for project reviews and hearings and that they should also work out how comments should be taken into account. However, it refers only to one planning document, namely the “rules for building”.

A review usually takes the form of a media campaign and a few sessions (each of them lasting several days) to open the project to public inspection and organize public hearings. The experience of the first such public hearings has shown that they are attended mainly by representatives of institutions or organizations with a professional interest in the plan (e.g. utility providers), whereas the turnout of ordinary citizens was relatively poor and even those who attended had little prior knowledge of the subject. The first public hearings did not result in any written remarks. The experience of other countries

in transition suggests that this process might have to undergo further changes.

The spatial planning system should allow for a much more active public involvement. Therefore, further clarification of the planning procedures is recommended. The institutions and organizations that represent the public interest and consequently are obliged to review, to negotiate and to approve or reject the contents of the project within their competencies prior to any public review should be defined. Furthermore, it should be possible for individuals and groups of inhabitants to make applications and remarks concerning the contents of the new plan before the public review. Similarly, there is a need for defining procedures for taking into account written remarks, protests, etc. during the public review.

A well-organized planning process may contribute greatly to facilitating new housing construction. Currently, a municipality can prepare and approve a new plan relatively easily while many potential actors remain passive. However, for the developer obtaining a building permit is usually time- and energy-consuming. Part of this problem should be transferred to the planning stage. Bodies that are now involved in the review of applications for building permits should be more involved in actual planning. This refers especially to the providers of utilities, transport and communication services. The review of the plan should result in a detailed and binding written agreement between the municipality and the utility providers. Rules and conditions for the provision of utilities and services to planned housing estates should be set out in these agreements and included in the plan regulations so as to make the subsequent application procedure clearer and more predictable.

## **3. Land prices and planning gains**

Another challenge is related to the contributions that developers make to the municipality in return for the permission to carry out development. In the case of housing development this contribution usually consists of a certain number of flats that are transferred into municipal ownership. Currently, new developments are usually carried out on land which city authorities rent to the developer for the period of construction. The developer sells the flats and his title to the land

terminates after the completion of the building. If a condominium is formed, it may take over the landownership. According to law, land under housing estates belongs to condominiums. However, no condominium has registered its property rights.

City authorities grant the developer the building permit as well as the title to the land. It is not clear whether the constructor's contributions in kind are made in return for the title to the land or in return for the building permit. However if the privatization of land goes ahead these two things will have to be separated. Issuing building permits will certainly remain in the hands of city authorities, whereas land may be bought and sold freely among citizens.

So the following question needs to be sorted out if the privatization of urban land is to become reality. Is the contribution made by the developer part of the price of land or it is a planning gain? The choice is difficult but unavoidable. Both options have advantages and disadvantages.

If the contribution is included in the price of land, it will be applicable to all cases where the municipal land is sold to the private owner. In such a situation the contribution could also be made in cash, which would allow the municipality more flexibility in spending it, e.g. on the construction of municipal housing or on the reconstruction of the existing stock. However, the land will be sold from municipal ownership only once and any profit will be gained also once.

If the concept of planning gain is applied, it will be up to the municipality to apply it to the particular case or not, regardless of the ownership of the land. The introduction of such an element in the Russian spatial planning system seems reasonable due to the permanent shortage of municipal funds and the considerable need for housing assistance as well as growing income disparities in society. However, care will have to be taken that this instrument is not abused. In addition, this might further complicate the already complicated development procedure and it might even hinder development. Moreover, it is not reasonable to apply the planning gain to small-scale development (e.g. single-family house) or to small construction companies, which are just starting up.

Scrapping the current practice of allocating a certain number of flats to the municipality and replacing it with a system of cash payments seems a better solution because:

(a) There is a need to stimulate the development of new small and medium sized companies offering new products and services on the construction market;

(b) It creates better conditions for fair competition between developers;

(c) It makes the municipality less dependent on the existing big construction companies and gives it more flexibility in planning the use of its housing stock as well as in planning the provision of new municipal housing.

At present, municipalities have relatively little influence on the location and on the quality of new municipal housing. They are dependent on the choices of the large construction companies.

#### 4. The planning environment

The planning environment consists not only of the building but also of its neighbourhood with all its links to the rest of the city and the region. The choice of the location of the first housing estates may affect the safety of the settlement, in particular if the area is prone to natural disasters. Like many European countries the Russian Federation suffered heavy floods in recent years. Moreover, floods have always endangered Saint Petersburg due to its location. The protection of existing settlements requires the construction of protective earth walls, dams, etc. For planning new housing it is certainly better to avoid endangered areas. In seismic areas (the Caucasus, some parts of Siberia and the far east)<sup>1</sup>, the danger of an earthquake should be taken into account in the territorial construction norms and all buildings should be earthquake-proof.

The arrangement and use of green open areas in cities is closely related to the quality of housing and the quality of life. There is usually enough open space in newly built housing estates and efforts are being made to preserve trees and water bodies on construction sites. However, the green space around housing blocks is usually poorly maintained. Moreover, the actual accessibility of open space is difficult for children and the elderly because housing estates are predominantly made

up of 5-storey blocks without lifts (problems for the elderly) and 10 to 20-storey blocks with lifts (problems for children).

Finally, the provision of public transport to housing estates is essential for the inhabitants' quality of life. However, Russian planners are now more preoccupied with the provision of adequate space for garages and parking places, due to increasing car ownership, than with the provision of public transport.

## 5. Permission procedures

### *The general situation*

One of the most important obstacles to construction (including housing) is the complicated procedure of issuing building permits. Russian and foreign sources report that developers who want to construct a building have to spend a lot of time and energy to collect all the required documents, approvals, permissions, etc. This is what prevents small and medium-sized enterprises from getting involved in the construction industry because such companies usually do not have the necessarily administrative staff. The developer is obliged to collect between 40 and 110 partial permissions from different institutions before applying for the final building permit. This seems to take from approximately three months to more than two years. The lack of transparency and predictability of the final outcome makes matters worse.

One should note, however, that this procedure entails not only granting the building permit but also granting the title to the plot of land for the construction. The Land Code (art. 30) specifies two ways of getting the title to the land for construction:

(a) Without the preliminary approval (given by the municipality) of the location of objects to be built: the title may be granted exclusively by means of selling municipal or State-owned land by auction. The purchaser gets the full ownership rights;

(b) With the preliminary approval of the location of objects to be built: in this way only the leasehold may be obtained. This is the case when the developer applies for a specific piece of land where he or she is going to build a specific object. Moreover, a significant part of urban land has

been already privatized together with old wooden single-family houses. One can expect that the very process of land privatization may simplify the procedure to some extent, but this is not enough.

### *The Ivanovo case*

A significant effort to simplify the procedure is currently being made in the Ivanovo region.<sup>3</sup> The municipality of Ivanovo has drawn up suggestions for a new procedure for the preparation of the primary-permission and project documentation for construction. It is based on the "one-door" concept. In the new procedure the municipal administration would take on much more responsibility and would do the bulk of work related to preparing documentation required for building permits. The new procedure would consist of five stages.

1. Preparing primary-permission documentation. Two slightly different sub-procedures are proposed at this stage depending on whether preparing documentation includes the preliminary approval of the location or not. In both cases the first steps are the same. The developer applies to the municipality. Then the department of architecture and urban planning the department of land resources consider the application and decide which sub-procedure to apply. Preparing the documentation without the preliminary approval of the location would be applicable to areas which are to be sold or rented on a tender basis and where sufficient and valid planning documentation exists. The second option would be applicable to all other cases. In both sub-procedures the municipal administration carries out the necessary preliminary urban planning works and land subdivision.

2. Specification of technical conditions. So far getting permissions and information about conditions under which the new construction can be connected to infrastructure networks has been the most troublesome part of the procedure for the developer. According to the Ivanovo procedure, obtaining all these permissions and conditions would be the task of the department of architecture and urban planning. It would be done on the basis of an agreement between the municipal administration

(the department of architecture), the developer and organizations managing infrastructure networks.

3. Preparing project documentation. This part of the procedure would follow only after the preliminary decision of the executive body of the municipal government. Depending on which of the sub-procedures listed in point 1 is applicable, it may be either the decision on “allocation of the plot for development” or the permission “for implementing a project on the plot of land sold or rented on a tender basis”. Preparing project documentation is the task of the developer. The project itself must be executed by a licensed professional.

4. The approval of the project documentation. According to the proposal from Ivanovo, the project documentation should be approved by the department of architecture and urban planning as well as by the civil defence body and several other institutions.

5. Issuing the building permit. Finally, when all previous conditions are fulfilled and finance for the construction is secured, the developer may apply for a building permit. The permit is prepared by the department of architecture and urban planning and signed by the head of the municipal government.

### ***Further possibilities for easing the problem***

This effort to simplify the building permit procedure is certainly worth further development

and wider dissemination. There are also other opportunities for smoothing the procedural path for new housing construction:

(a) Extend the range of construction works for which no building permit is needed and introduce a notification procedure for minor construction works;

(b) Abolish double licensing of construction companies and retain only personal licensing;

(c) Coordinate spatial planning and environmental impact assessment (EIA) procedures;

(d) Involve the institutions issuing partial permissions into the planning process.

### **6. The need for an active land policy**

The apparent lack of discussions around the approval of new local spatial plans as well as the long permit procedures reflect the predominantly passive attitude of Russian local authorities to land management. It seems that their attitude to land is driven mainly by an instinctive fear of selling land into private ownership. Local authorities prefer to offer all kinds of leaseholds rather than full ownership rights. This situation must be changed if municipalities want to facilitate housing development.

Municipalities should work out and implement comprehensive land policies as a chain of concerted actions comprising: planning; land subdivision; provision of roads and utility networks; land privatization and development control.



# *Chapter XI*

## **LAND MANAGEMENT AND REAL PROPERTY MARKET DEVELOPMENT**

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Housing policy cannot be seen independent from the availability of land. This chapter therefore gives an overview of recent developments in the Russian Federation's land market and real property system. Section A presents the basic government objectives with regard to land and real property development. Section B discusses recent reforms regarding land and real estate ownership and management, while section C reviews trends in the housing market.

### **A. Government objectives**

A dynamic, viable and a well regulated market in real property (land, commercial and residential buildings, and farms) plays a critical role in developing business and in raising living standards. The main function of a real property market is to enable the efficient and optimal use of land and real property resources. A viable, functioning real property market enables the economy to use its existing potential in the most efficient way by channelling resources to their best use. The Government of the Russian Federation's strategic goal in its land and real estate policy is to create the right conditions for the efficient use and development of real estate in the interest of society at large, private entities and individuals.

*The State Mid-term Programme for Socio-economic Development of Russia for 2003-2005* (15 August 2003) contains a special chapter on the development of infrastructure for the land and real estate market. The Government envisages abolishing the State's monopoly on land through three measures: (a) the transfer of ownership of land to the owners of the buildings and enterprises located on them; (b) the demarcation of land rights among different levels of government, including transferring the ownership of land within municipal boundaries to the municipalities; implementing legal zoning; (c) the privatization of land parcels and real estate units on them as unified objects. These measures are intended to increase the supply of real estate, promote the creation of new real estate and encourage a more

efficient use of real property through market transactions. A higher market supply is essential for the development of the production capacities of goods and services, lower cost for users and owners, and meeting the housing needs of the population.

On 21 April 2003, the Constitutional Court decided that a dishonest seller could not dispute in court a real estate transaction, if he had infringed the law in the course of the transaction. Until then if a court ruled that one of the transactions in a property deal had been invalid, all the consequent transactions related to it had to be reconsidered. As a result many honest buyers were deprived of their homes though they could not have known about past irregularities. The Constitutional Court admitted that these court practices were unfair and did not protect the rights of the honest buyer.

### **B. General review of the reform of land and real estate ownership and management**

The policy pursued by the Government has led to a wide distribution of landownership. Approximately 50 million people and legal entities have acquired private ownership rights in land and by the end of the 1990s some 129 million hectares, or 7.6% of the country, was privately owned. Most of this land is agricultural and located in the regions with the most favourable climate and good soil. Some 92.4% of the land is in State or municipal ownership. Given the size of the country, the size of its population and its climatic conditions, it can be concluded that the Russian Federation's land privatization potential has diminished. Available data indicate a falling demand for land among individuals. The further transfer of land from the Government to private businesses will mostly be in cases where the latter are already occupying State land. At present, in the Russian Federation, there are about 5 million transactions with land plots registered annually. By 2002 the State cadastre valuation of all agricultural land had been completed and in settlements more than 40% of land had been assessed.

To support the transition process, the Government has concentrated on developing land market infrastructure mechanisms. By the end of the 1990s, the land cadastre system and the system of real property rights registration were operational throughout the country. Two government programmes support the real property market by emphasizing the need to establish efficient coordination between the cadastre and the real property rights register. The Federal Target Programme for the Development of the Automated System for the Maintenance of the State Land Cadastre and State Registration of Real Property Units for 2002–2007 concentrates on the development of the unified real property cadastre and is supervised by the Federal Land Cadastre Service. The Federal Programme for the Development of the System of State Registration of Real Property Rights and Transactions is carried out under the Ministry of Justice. Both programmes are in the initial stage of implementation. In addition, the Mid-term Programme of Social and Economic Development of the Russian Federation for 2002-2004 identifies the development of the State land cadastre as a basis for the unified system of registration of real property units, and as one of the main land policy issues. The uniformity of the land cadastre system creates a potential for the development of a viable real property market.

In recent years the following major legislative acts on the land and real estate market have been adopted: *the Land Code, the Law on Land Management and Land-use Planning, the Law on the Attribution of Public Land, the Law on the State Land Cadastre and the Law on Registration of Real Property Rights and Transactions*. These laws and others recent legislation have ensured the allocation and transfer of land into private ownership. They have also established a framework and defined procedures for the operation of the real estate and land market. However, the legislative framework for transactions in land and real estate needs further improvements. In particular, transactions (transfer of property rights) need to be more transparent and a comprehensive, unified system for transactions in real property units needs to be set up. The privatization of land on which enterprises and commercial buildings are constructed has not succeeded and only 0.5% of land in cities is in possession of legal entities, because the owners of

enterprises want a second stage of free privatization and are not willing to buy the land. According to the law, land under housing condominiums belongs to the condominiums, but in fact property ownership rights were never registered. From a housing market development perspective, adopting a new housing code (the existing Housing Code dates from 1983) is a priority, since the right to housing should be treated both in a public and in a housing market context.

The institutional set-up for land administration in the Russian Federation reflects historical and political developments. Some institutions were set up in the late 1920s, but in the early 1990s their functions were modified. A number of new institutions and functions have been created in the area of real property rights. As the reform is only a few years old, it is no surprise that there are conflicting goals, overlapping responsibilities and fragmentation of services.

The land cadastre and the building register are not integrated into a unified real property cadastre. The records are still kept by separate agencies without any exchange of information. At the local level, there are three organizations involved in real property and real property rights registration. They differ in their historical background, the way they are organized, their technical procedures and their level of computerization.

*Cadastre chambers* operate under the *Federal Land Cadastre Service*. They were established in the late 1990s but existed earlier as part of the land committees. Since the beginning of 2000 four compatible software products have been developed and certified, and they are now widely used by the cadastre chambers throughout the country. These systems cover both geographical and textual information on land.

*The Russian Technical Inventory (Rostechinventorizacija)* replaces the *Bureaux of technical inventory*, which were municipally owned companies under the limited supervision of the *State Construction Committee (Gosstroy)*. They were established some 75 years ago to monitor real property within the general policy of State control. They had developed their own identification system, usually based on addresses. They held comprehensive technical information on buildings and apartments in so-called technical

passports, which the client was required to obtain at the time of transaction. These databases also keep records of rights to real property objects attached to land parcels registered before 1998 (in 1998 rights registration was transferred to the Ministry of Justice). In September 2003 the *Gosstroy* abolished the Bureaux and from 17 September 2003 their functions and databases were transferred to *the Russian Technical Inventory*. However, at present, there are plans to abolish *Rostechinventorizacija* and to transfer its functions for valuation and real property inventory to the *Federal Land Cadastre Service*. Starting from 1 October 2003, all real estate units are given federal inventory numbers and the unified state register of all real estate in an electronic format is to be put in operation.

*Rights registration chambers.* The right to property, restrictions on these rights, their origin, transfer and termination are governed by the *Civil Code*, and the *Law on the Registration of Real Property Rights and Transactions*. These rights are subject to State registration in the unified State register of rights held by rights registration chambers. Although registration of real estate rights and transactions is governed by federal legislation, the chambers were established in 1998-2000 by regional authorities. The Ministry of Justice does not have direct control over them. It only appoints registrars in regions and provides methodological support for their operation.

In the Russian Federation, a real estate market as a major instrument of economic development has not been established yet. It is possible to indicate only that there is an irregular development of some of its elements. A comparatively fast market development is evident in the housing sector, while the commercial real estate market is weak and the industrial real estate market is almost non-existent. This could be explained by the fact that real estate owners do not have rights to land and insufficient security of tenure. At the same time, it should be noted that the rental market for commercial buildings is well developed and is on the rise. The rental land market (for 5-49 years) is also quite developed, in particular in major cities (Moscow and St Petersburg). Land for development is still mainly supplied through administrative methods and decisions.

Although the legal framework necessary for a functioning urban housing and real estate market is largely in place, there are still two major legal bottlenecks that prevent it from operating efficiently: (a) the division of real property ownership between the Federation, the regions and the municipalities is unclear and unregulated; the situation in Moscow is most complicated and there are no transparent schemes and normative acts to divide real property between the city and the federal level; and (b) there are no clear and transparent rules for the privatization of municipally owned land.

There is also a lack of clear land policy, in particular in the municipalities. Land policy refers here to the entire complex of socio-economic and legal prescriptions that dictate how the land and the benefits from it are to be allocated. A balance must be struck between the exploitation, use and conservation of the land as a resource in order to obtain the necessary level of sustainable development for sensible and orderly city development.

### **C. Trends in housing market development**

Since the early 1990s, the Russian housing market has developed substantially. The main elements of the legislative basis have been established; the major elements of the housing market infrastructure has been set up; general information on market prices, as well as terms and conditions for real estate transactions are publicly available; more people can now afford housing. Market allocation of housing has increased sharply during the transition. The percentage of households that used market methods to obtain new dwellings increased from 43% in 1992 to some 70% in 2002. Those that received their flats through municipal waiting lists decreased from 40% to some 15% during the same period.

The social profile of a typical homebuyer has changed. During the early years of the housing market development buyers used to be mainly the very rich, so-called new Russians. Now most are middle-class buyers who want to trade up. Despite all these developments, there are no new financial mechanisms for acquiring housing on

the market. Because of a very low level of income, few people are in a position to take out housing loans under existing terms and conditions. Adequate forms of borrowing have not been developed so far. Experts estimate that not more than 10% of households can afford to buy a flat on the market, and improving housing conditions still remains a dream for most Russians.

The financial crisis of August 1998 was a heavy blow for the housing market in the Russian Federation. Its impact was not so strong in some cities where the prices for housing were based on dollars (Moscow, St Petersburg, Nizhny Novgorod, Rostov-on-Don, port cities like Kaliningrad, Vladivostok, Khabarovsk and some regional centres near Moscow). The crisis strengthened the differentiation of cities in terms of housing prices. In cities with dollar prices, prices on the housing market went down by 35% – 50%. In the other cities, housing prices fell by a

factor of 2.5 – 3. Housing prices in most cities dropped from US\$ 300 – 500 to US\$ 100 – 300 per square metre of total floor space.

However, since the financial crisis, housing prices on the primary and secondary housing markets of most cities have recovered both in roubles and in the dollar equivalent. Especially high market prices were registered in major cities, regional capitals with good potential for economic growth, financial and cultural centres, in towns that attract a large number of migrants, in resorts and regional oil and gas centres in Siberia and the far east. Housing is the cheapest in small towns (except in the region of Moscow and St Petersburg), as well as in the former industrial cities, especially those located in areas with an unfavourable climate. By the end of 2002 the urban housing market had fully recovered, and in 2003 prices rose above the pre-crisis level (see also table 16).

**Table 16. Prices on the secondary housing market December 2002 (in bold cities of particular concern for this study) (in US\$/m<sup>2</sup>)**

City	Average price	City	Average price
Moscow	1096	Nizhny Novgorod	365
St Petersburg	641	Tomsk	313
Ekaterinburg	519	Astrakhanj	286
Novosibirsk	470	Ivanovo	260

### Moscow

To understand housing market development in Moscow, it is necessary to look at the city's economic and political role in the Russian Federation. Moscow produces some 80% of the country's financial turnover, and attracts some 40% of foreign investment. Moscow has close bilateral economic and social relations with other "subjects of the Russian Federation" and even with other States, which leads some analysts to say that Moscow is developing into "a State within a State". The city's budget for 2003 stipulates 293 billion roubles income and 315 billion roubles expenditure. The city can afford to run a 22-billion-rouble budget deficit because it is a big trade, industrial and financial centre, and tax revenues in 2002 increased by 40%. This financial basis makes it possible for the city to undertake huge investment programmes, mainly

construction, including housing development programmes. Housing development is a priority in the city's investment programmes. In the next eight years it plans to build some 36.5 million m<sup>2</sup> of new housing and demolish 5.6 million m<sup>2</sup> of derelict housing. In 2003 it planned to build 5 million m<sup>2</sup> of housing (up from 4.5 million m<sup>2</sup> in 2002). The city will finance only 1.6 million m<sup>2</sup>; the rest will be financed from private sources.

Moscow is undoubtedly the leader in the Russian real estate market. In the early 1990s, realtors estimated that Moscow's housing market represented up to 75% of the whole turnover of the Russian housing market. The number of sales on its primary market has been steadily increasing: from 8,800 housing units in the mid-1990s to about 30,000 by 2002. In 2002, prices increased by 17% compared with 35-40% in 2001. However, in the first half of 2003 alone,

prices increased on average by 15%. A new frame residential building costs about US\$ 900-1000 per m<sup>2</sup> (without internal walls in the dwelling, equipment and finishings), while the cost of construction is only about US\$ 250 per m<sup>2</sup>. In a brick residential building prices are as high as US\$ 1,400-1,700 per m<sup>2</sup>. In the elite housing sector in the city centre prices range from US\$ 3,000 to 10,000 per m<sup>2</sup> (profits in the elite housing sector can be as much as 1,000%).

The price also depends on the stage of construction at the moment of the purchase. So-called shared participation (*dolevoe uchastie*) in housing investment has grown rapidly (16,000 dwellings in 2000, 14,000 in 2001 and 19,000 in 2002). Agreements are concluded by private individuals who acquire new dwellings at the project stage or before their completion. The price of a dwelling in a finished building can be twice as high as at the initial construction stage. One of the main reasons why such type of acquisition is more favourable than taking out housing credits from banks is the fact that, with a bank credit, borrowers have to declare their income. With the present state of the labour and taxation legislation, most people and companies prefer not to do that. However, this system of new housing construction is based not on legal regulations, but simply on people's trust in investment companies. This type of acquisition is not defined in the Civil Code and courts are not willing to consider cases where individual investors lose their money.

Some analysts consider that there is a clear

relationship between the prices on the housing market in Moscow and the world prices for oil with a two or three month time lag. If world oil prices go up, so do housing prices and vice versa, particular for elite housing units. People who work in the oil and gas industry consider Moscow real estate as a good investment. Experts estimate that some 75% of housing in Moscow is bought by non-Moscovites, mainly people from gas and oil regions. In the Moscow region this figure is 40%. Most of these new dwellings go to the private rental sector, which in Moscow has increased to 20% of the total housing stock.

Another reason for the growth in demand for housing is the drop in the dollar. Many people kept their savings in dollars, and when the dollar went down they switched to investments in housing. However, some experts consider that the housing market in Moscow is overheated and the prices could tumble since the difference between construction cost and price is 4-fold, as a result of favourable world oil prices. This situation is also aggravated by the fact that most of the new housing is bought not for meeting housing needs but for investment purposes with the prospect of reselling in the future.

The total number of transactions concluded on Moscow's secondary housing market has remained stable in recent years at 70,000 – 80,000 per year. According to some estimates, starting with 1994 its turnover was worth US\$ 4 to 5 billion. The dynamics of average house prices on the secondary market of Moscow in 1990-2003 is presented in table 17.

**Table 17. Average house price on the secondary housing market in Moscow, 1990-2003 (in US\$/m<sup>2</sup>)**

Date	Average price	Date	Average price
12/1990	107	12/1997	950
12/1991	270	12/1998	890
12/1992	480	12/1999	710
12/1993	752	12/2000	720
12/1994	1121	12/2001	930
12/1995	1217	12/2002	1096
12/1996	1105	03/2003	1148

Prices on the private rental housing market went up too. The rent on a one-room flat of good quality is about US\$ 350 per month, while for a three-room flat it starts at US\$ 500 per month. Rents in the elite housing sector range from US\$ 1,000 to 20,000 per month depending on location and quality. The greatest demand is for elite dwellings with 130-160 m<sup>2</sup> of floor space. Normally these dwellings have two or three bedrooms and two bathrooms. On the market of villas outside Moscow, the greatest demand is for villas with a rent of US\$ 1,500-3,000 per month.

### St Petersburg

Until now, prices in St Petersburg have been half those in Moscow. The demand for housing has not been so high as in Moscow, and in St Petersburg there is no strong correlation between world oil prices and prices for housing. Investment in housing comes mainly from the city budget rather than from the country's oil and gas regions. As there is less speculative investment, real estate market legislation is better developed than in Moscow and the number of transactions in relation to the total housing stock in St Petersburg

is higher than in Moscow (4% and 3%, respectively), although the city attracts fewer people from other regions.

The city's unified geo-information system in an electronic format is open to the general public. This system contains information for potential investors about specific areas in the city intended for particular types of development, information on particular development projects and reference information for developers. During the past two years major investments (US\$ 3 billion) have come to the city in preparation for its 300th anniversary celebrations.

The average price of a new dwelling (without finishings and equipment) is US\$ 500-600 per m<sup>2</sup> of total floor space; however, it is expected that by the end of 2003 the upper limit will reach US\$ 700 per m<sup>2</sup>. As in Moscow, most new dwellings (more than 90%) are built with partial investments from future owners (payment to the general investor, at the initial stage of construction, of some 10-20% of the total price of the dwelling). The dynamics of prices on the secondary market is given in table 18.

**Table 18: House prices on the secondary market in St Petersburg (in US\$/m<sup>2</sup>)**

Number of rooms	August 2002	August 2003	Increase in prices since August 1998 (percentage)
1	599	790	170
2	546	708	112
3	512	668	84
4	493	647	67
5	496	652	64
6	498	657	86
7 or more	547	660	57

### Nizhny Novgorod and its region

In the early 1990s Nizhny Novgorod, as well as its region was a pilot area and a leader for many market-oriented reforms. It enjoyed considerable financial support and investment, both domestic and foreign, to carry out these reforms. At the time, many construction projects were realized. However, since the financial crisis of 1998, the city's economic and financial regeneration has rather slowed and the local economic situation remains stagnant.

In 2002, in Nizhny Novgorod, housing construction accounted for 198,000 m<sup>2</sup> down from 223,000 m<sup>2</sup> in 2001. In the whole region of Nizhny Novgorod, construction stood at 496,000 m<sup>2</sup> and 525,000 m<sup>2</sup>, respectively. In housing construction the region ranks 15<sup>th</sup> among 89 Russian regions ("subjects of the Federation"). The share of individual housing construction in 2002 increased to 40% of all new housing, and in the first half of 2003 it was 56%. Individual housing construction is mainly carried out with partial investment from the future owners, as is the case in Moscow and St Petersburg. Developers indicate that the absence of clear rules for the allocation of sites for housing construction is a major obstacle to housing and real estate market development.

There is a need to have efficient and transparent procedures for the local authorities to examine, approve or reject urban development projects. Such procedures should be based on the "one-door" principle, where one unit in the municipality has overall responsibility for a coordinated approach as well as for final decisions on project proposals. The necessary documentation to be provided by the developer should be clearly defined, and should vary in complexity depending on the size of the project. A reasonable link should also be established between the time and cost for project evaluation and the final approval or rejection of a project proposal. The present situation, where the cost of the documentation can amount to 15-20% of a project's total cost and approval procedures can take up to three or four years, is not conducive to an emerging urban real estate market.

Today, the lack of good laws is not the principal reason for the lack of sound land-use plans in

urban municipalities. The main problem is that the responsibilities for planning procedures, planning and building permits, implementation and control both at the federal and at the municipal levels are not clearly distributed. A legal clarification of these issues with principles and guidelines on practical planning procedures and flexible rules on implementation at municipal level is urgently required.

### Ivanovo

The city of Ivanovo and its region are considered to be one of the most depressed areas in the Russian Federation. For several decades in the Soviet period the city was a centre of textile production, which was almost the only economic activity in the region. During the transition this branch of the economy was in great crisis, as was the city. Nevertheless, the city and regional authorities are optimistic about the future: the city is only 319 km from Moscow and there is a good potential for tourism development. In the historical areas of the city there are many traditional wooden houses and, if renovated, these could be of interest to tourists and bring related investment and services. In view of the poor financial situation of most inhabitants, the housing market is very weak and the Russian Guild of Realtors has no members from Ivanovo.

An analysis of the supply on the secondary housing market indicates that modern dwellings accounted for 50%; dwellings built in 1970-1980 represent some 27% and 50-storey block housing of the 1960s 16%. The price of these housing units ranges from US\$ 290 per m<sup>2</sup> for dwellings of a better standard to US\$ 200 per m<sup>2</sup> in the housing stock built in the 1960s. New housing units of very good quality (elite housing) costs US\$ 450 per m<sup>2</sup> (without finishings and equipment). The cost of construction is about US\$ 200-250 per m<sup>2</sup>, which means that the profits of the developer is 2-3 times lower than in St Petersburg and Moscow.

### **D. Market operators and customer requirements**

#### *Organization of realtors*

The Russian Guild of Realtors started its activities in 1992. Its members are 1500 legal persons

(brokers, developers, appraisers, etc) and 43 professional organizations working not only in the Russian Federation but also in other members of the Commonwealth of Independent States (CIS), Poland and Bulgaria. The aim of the Guild is to promote a real estate market in the Russian Federation through the creation of an effective system to increase the quality of brokers services and the development of legislation and a business environment. It has an educational and training centre. The Guild is very active in regional housing market development. Following the recommendation of the Guild and the prevailing practice, the system of licensing of realtors was replaced by a voluntary certification scheme. It is expected that, with this innovation, realtors' services will be subject to a qualitative assessment.

The Russian Guild of Realtors and regional guilds of realtors are involved in the implementation of different governmental housing programmes. In the Russian Federation, there is considerable internal migration, related to the economic and social transition. The Government initiated a number of housing programmes to provide social support to young families, families of former servicemen as well as pensioners moving from the north of the country to regions with more comfortable climate and living conditions. The participation of realtors in these programmes helped to channel government funding from the construction of new housing to the secondary housing market, which increased the efficiency and flexibility of these programmes. Steps were taken to establish an information system on the price of housing, employment opportunities in different regions and cities. This helped migrants to make a better choice about where to live. However, this system needs further development into a nationwide database on the real estate market.

### ***Housing market and customer orientation***

In comparison with the housing units built in 1960s-1990s, the housing quality of new flats has increased dramatically in terms of average space, internal design, finishings and installations. This is

partly explained by the fact that the market of building materials is now flourishing mainly due to the import of building materials and equipment from western countries and the orientation of the new housing market towards expensive, private housing units.

However, the high cost of new housing units is not a guarantee of quality of construction and related services. Most construction companies which work in all segments of housing construction economize on their workforce, project design and construction materials. Immigrants from Central Asia or Ukraine, with little or no qualifications, are often used as a cheap source of labour by both Russian and foreign construction companies. Sometimes developers deliberately increase the number of stories in new buildings (by lowering the ceilings of all stories compared to the original project), agreements signed with the city authorities are not strictly followed, and, as a result, the new owners receive housing units that do not fully meet their expectations. In cases of "shared participation", there can be problems with the registration of the property rights.

In Moscow, the housing market is oriented towards elite, high-rise construction (25-30 stories), which in many instances takes place very close to existing housing. As a result, such construction decreases the quality of life in the neighbourhood from an environmental point of view and also in because the existing engineering and social infrastructure was not designed for such residential density. The market price of housing in the existing buildings goes down by 20-30%. Another problem is that there is a lack of normative documentation, qualification and experience among construction companies for the construction of such buildings. Many experts doubt that the geological conditions in Moscow are suitable for such high-rise mass construction development. The future attractiveness of such housing estates is questionable, considering that they may not be safe and that people's general preference is for low-rise residential buildings.