

Session 5

The Role of Land Banks / Land Funds in the Privatisation Process

I. Summary

The privatisation process is of outmost importance for the development of the rural areas in the SEE/MEE/CIS countries. Germany, confronted with similar problems as the named countries after the break down of the German Wall, founded the BVVG in 1992, a a state owned limited company in charge of the privatisation of agricultural and forestry land in the new federal states. A set of newly decreed laws governed the activities of the BVVG. By selling approx. 0,6 Mio ha agricultural and forestry land as well as 0,04 Mio ha building land and still holding over 1 Mio ha in its portfolio the privatisation activities of the BVVG had and still have a great impact on the development of a land market and on the development of the agrarian sector in general. Through the establishment of a state privatisation agency the following goals were achieved: transformation of the agrarian sector without a large scale break down of farming businesses, the establishment of a competitive agrarian sector, the establishment of a functioning land market, the consideration of structural aims in the rural area in the privatisation process.

The BVVG therefore serves as a model to illustrate the advantages of state intervention into the transformation process of land ownership and land market development. As a consequence, governmental institutions could well be of great relevance for the SEE/MEE/CIS countries. Necessary for their success will be the clear definition of agri-structural goals, a market oriented privatisation strategy, coherent land- and land market laws and efficient and transparent rules of conduct.

II. The Legal and Institutional Structure for the Administration of State Owned Land in Eastern Germany

In order to establish the basic facts for a discussion about the advantages of land banks and land funds it is necessary to describe the legal and institutional structure for the administration of state owned land in Germany with special focus on East Germany.

In Germany there is no such thing as "public ownership". Although the German State owns plenty of real estate of any kind, the legal status of this ownership does not differ from the ownership of an individual that owns some sort of real estate. This is defined in the Civil Code. All owners no matter if public bodies or individuals therefore have the same rights and duties concerning their property.

The Federal State of Germany can be roughly divided into three main administrative layers: State, Federal State, and Municipalities whereby all of these statutory bodies with legal capacity are owners of real estate.

Land owned by the State (Federal Republic) can be divided into two categories: „administrative property“ i.e. property necessary to fulfill administrative functions and „general property“ which is not used for this purpose. It is usually administered by the Regional Finance Offices of the Federal Ministry of Finance. But there are also state owned companies, who do the same for special categories of property, such as „German Railways Corporation“. Since 1990 a new category of federal property exists, namely land formerly owned by the public in the new federal states. This property has at first been administered by the Treuhandanstalt/BvS and later by its successors, among them the Bodenverwertungs- und verwaltungs GmbH (BVVG), in charge for agricultural and forestry land.

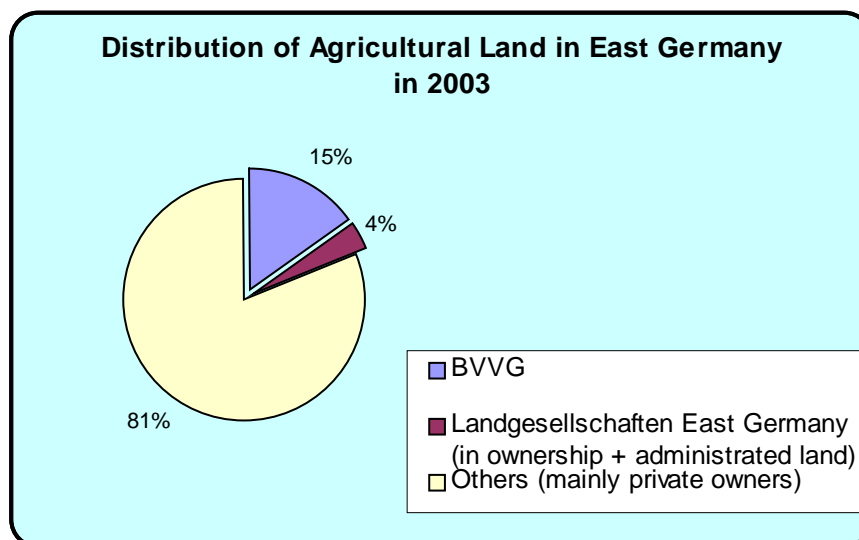
Land owned by the Federal States is usually administered by the Federal State Ministry of Finance and its subordinated authorities such as the Landgesellschaften.

Municipalities usually have their own property administrations.

Figures on agricultural land in state ownership.

Germany as a whole holds only a small percentage of agricultural land in state or federal state ownership. Due to recent history this is situated mainly in the East German territory.

East Germany	Agricultural Land in Hectar (2003)	in %
BVVG	850.000	15%
Landgesellschaften East Germany (in ownership + administrated land)	212.000	4%
Others (mainly private owners)	4.504.000	81%
Total	5566000	100%



The climate of reform in Germany hasn't left the system of state property management untouched. The Federal state has even proclaimed, that there is no need to keep „general property“ ad infinitum. It is seen as a governmental task to sell „General Property“ if it is not needed in the foreseeable future. As a result the Federal Ministry of Finance currently integrates all state land property into one „statutory body“ – the Bundesanstalt für Immobilienaufgaben BimA. The new federal state, Saxonia, has done the same on the federal state level.

The objective of forming these centralised institutions is to speed up the privatisation of State property to set free desperately needed capital for the state budget.

III. Exceptional Situations call for Special Solutions – The Transformation Process since 1990

The period of 1989/90 and its relevance for East Germany as well as for all other former communist states has been sufficiently discussed. The land and land market situation at that time can be characterised by the following three points:

- Up to 100% of land is state owned or at least state administered.
- The agrarian sector is dominated by collective farm businesses and state farms.
- The landmarket is not yet developed or does not exist at all.

Since then we have experienced a tremendous transformation in the agrarian sector. The transformation process has been marked by three main features:

- The transformation or liquidation of collective farm businesses and state farms.
- The transformation of ownership structure by restitution, municipalisation and privatisation (for money as well as free of charge).
- The development of a new farming and finance structure within the agrarian sector.

The transformation process in the agrarian sector of East Germany required a whole set of new laws as well as the establishment of new institutions.

The most prominent among those institutions since its foundation in January 1990 has been the Treuhandanstalt. The Treuhandanstalt which, as a governmental German Agency received all East German formerly publicly owned property was subordinated to the Federal Ministry of Finance. It was governed by the same ministerial department as other federal enterprises such as German Railways or German Mail. The main task of the Treuhandanstalt became to privatise the received property as fast as possible. The legal basis for the activities of the Treuhandanstalt was manifested in the so called „Law of Trust“ (Treuhandgesetz).

Agricultural and forestry Property with the status „publicly owned“ was given to the Treuhandanstalt on the basis of the 3rd executive order of the mentioned law.

This property encompassed the state farms in its whole, agricultural publicly owned land managed by the collective farm businesses as well as about two thirds of the whole forestry land in the new federal states.

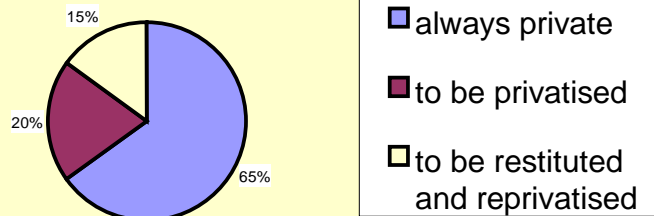
The task of the Treuhandanstalt to transfer public ownership into private ownership covered two main sections:

Property that originated from expropriations before 1945 or after 1949 was to be given back to their former owners through restitution if this was legally and factually possible.

Property originating from expropriations between 1945 and 1949 was to be privatised.

Since the identification of these two sections couldn't be realised in a short time and therefore collided with one of the guidelines of the THA, namely a quick privatisation followed by the subsequent closing of the agency, the BVVG was founded in 1992. The BVVG got assigned all land that had been used for agricultural and forestry purposes at a special reference date, the 3rd of October 1990 (Unification Day).

Categories of Arable Land in East Germany in 1990



Laws governing the operations of the Treuhandanstalt and the BVVG

The **Law of „Allocation of Ownership** regulates the allocation of ownership for real estate and other goods to the different layers of administration, i.e. the Federation, the federal states and the municipalities, as well as to other statutory bodies and the former state farms that have been transformed to limited companies. Governing principle was, who needed the property to fulfil its functions (i.e. military bases for the state and kindergartens, schools etc. for the municipality).

The **Law of Property** regulates the restitution of land towards their former owners, who were expropriated after the 30.01.1933 up to the 8th of May 1945 and after 7th of October 1949 up to the 03.10.1990. Former owners can be the individuals, private enterprises and private foundations.

The **Law of compensation** has a special impact on the privatisation activities of the BVVG as it allows certain groups of people to buy agricultural and forestry land at reduced prices (mode of price calculation is ruled in the law). The Law has to be seen in its historical context. It was a political decision, not to reconstitute property from former owners, who were expropriated by decrees of the Soviet Military Administration in the East German Sector during 1945 and 1949. The idea behind the Law of compensation was (besides ruling the monetary compensation for the lost property) to allow the expropriated to purchase a limited quantity of agricultural and forestry land at reduced prices as a kind of evening-up. Besides that, farmers holding a lease contract with the BVVG, who were East German citizens at the 03.10.1990 were also to be benefited through the possibility to buy land at reduced prices. The thought behind this was, to give East German farmers the chance to acquire property. The amendment of the law of compensation in 2000 due to the examination by the EU-commission in 1998 led to some changes in the Law, the most important one: all farmers holding a long term lease contract with the BVVG can purchase a certain quantity of land according to the rules of the Law of compensation. This law was disputed for years and still is, a final decision about its legitimacy by the European Court of Human Rights is still outstanding.

The **Law on “Adaptation of Agriculture”** regulates the handling of collective property, e.g. the collective farms. This law paved the way to transform socialist collective farms into co-operative farms and limited companies, or respectively regulated their subsequent liquidation. It basically opened the way to disentangle privately owned land and inventory

from collective farms and opened up opportunities for the establishment of all kind of new farms: private family farms, co-operatives, limited companies, corporations etc.

IV. The East German Model – BVVG: Agriforest Privatisation Agency and Land Fund

The guiding principles

The management structure of the BVVG is a centralised, the operational structure a decentralised one. The head office in Berlin provides supervision and guides the regional branches. The regional branches sell and lease within comparatively wide limits, that are set by a system of authorisations. There is no direct influence onto the sales and lease process by the federal states or the municipalities. That has ensured an important principle: **Uniform** Privatisation and administration in all New Federal States of Germany on the base of federal laws and regulations.

The BVVG hasn't been established as a part of the federal administration. Though 100% state owned the BVVG has the legal form of a limited company. The limited company BVVG is a service provider for the state that works within limits that have been set by law. The BVVG is supervised by the Ministry of Finance. With the legal status of a limited company it is neither subject to day to day decisions of the administration nor to every day politics. That insured a second important principle: **Independent** privatisation and administration.

With an company portfolio of initially app. 35% of all arable land and a sales market share of app. 70% in East Germany the BVVG became the most influential agent on the East German land market. Information about the methods for lease and sale as well as the results of the privatisation are publicly available, thereby establishing the third principle: **transparent** privatisation and administration.

The BVVG is not part of the public budget. All income out of lease and sale is reduced by the costs of the BVVG and the balance is transferred into the coffers of the Federal Ministry of Finance as a household income position. The BVVG, apart from the legal provisions, is not allowed to subsidise the agrarian sector. The strong link to the Finance Ministry makes sure that the fourth principle is being observed: **Turnover-oriented** privatisation and administration

The rules of conduct for the BVVG and the configuration of the supervisory board and counselling bodies make sure that the BVVG acts in the interest of a balanced development of the rural areas in co-operation with the agrarian administration and elected bodies. That stands for the fifth principle: **Social responsibility**.

The three phases of privatisation

The probably most important decision of the BVVG had been to start the privatisation process with leasing out, regardless of final ownership and sale or transfer back free of charge at a later time. That decision for at first short term and later long term lease policy helped to stabilise the emerging farms. Forests were managed by the forest administrations of the federal states to thereby ensure the proper and legal use of forests. The BVVG therefore had time to establish its ownership and its system of administration. That **first phase** started in 1992 and ended 1996.

The **second phase** has been the sale of land at reduced prices according to the law of compensation. Note that one basic precondition for purchasing agricultural land at reduced price is the status of a long term leaseholder. The basic desired effect was the consolidation of the newly developed farm structure. The predominant sales of large scale forest holdings

(up to 1000 ha) established a strong basis of private forestry ownership that accounts for app. 50% of all forests in Eastern Germany. That phase started in 1996 and will last till 2006.

The **third phase** will be characterised by the large scale sale of land at market price on the then fully developed land market. Even though the BVVG already sells real estate at market prices, this has been predominantly building land. The percentage of agricultural and forested land sold at market value by tender or limited tender has been comparatively small. That phase will start in 2006 and be finished app. 2014 – 2016, the assumed closure date of the BVVG. There will then be no need for a East German land fund, because the free land market then regulates the transfer more effectively than any state agency could.

A BVVG balance in figures

Portfolio 2004

0,85 Mio. ha agricultural land under lease
0,30 Mio. ha forests
4,00 Mio land plots

Sold since 1992

0,22 Mio ha agricultural land
0,38 Mio ha forest
0,04 Mio ha building land
515 state farms sold or liquidated

Allocated, restituted and reprivatised free of charge since 1992

2,55 Mio ha agricultural land, forest and building land
Revenue for the state budget app. 2.200.000.000 Euro

V. Assessment of the East German Model – Pro's and Con's

Twelve years of land market development and BVVG-land funds can be put into one phrase: predominantly success and so far little need for basic amendments.

To underline that statement please note the following „pro“ points:

- The model BVVG as a limited company of the Federal Ministry of Finance is a success against all conflicting interests of the federal states and the Ministry of Agriculture. The model has relieved the state of potentially controversial tasks on the disputed field of property relations.
- The transformation of the agrarian structure did not result in a large scale breakdown of farms – the proper land use has always been maintained – the agrarian sector is one of the most competitive sectors of the East German economy
- The transfer of more than 50% of all agricultural land in Eastern Germany happened without large scale political and social friction – an example for a successful balance of interests
- The BVVG has been crucial for the establishment of a transparent and functioning land market. Especially the BVVG introduced lease and sales prices, evaluation methods, model contracts and tender based sales procedures set the rules for the emerging market.
- Structural goals for the rural development were considered in the privatisation process

On the „con“ side are some points that aren't all in responsibility of the BVVG:

- As stated before the law of compensation had to pass an examination through the EU-commission in 1998 and as a result was amended in 2000 because of two basic

breaches of EU-law: - discrimination on the field of market access and unfair competition because of the high level of subsidy. As a result not only East Germans and former owners were eligible to buy land at the reduced price but every EU-citizen, given they held long term leases for agricultural land with the BVVG and were willing to shift their residence near their farm business. The level of subsidy had to be reduced along the EU-lines to app. 35 % of the market value. In result of this procedure the BVVG was not allowed to sell land by means of the law of compensation between end of 1998 and amendment in Sept. 2000, which in consequence slowed down the privatisation process.

- The complexity of the governing laws and regulations are also a reason for the quite lengthy and expensive privatisation process.
- The concept of the BVVG – work fast and you'll be closed soon“ certainly has some negative aspects for the long term motivation of its workforce too. It might become interesting how that will influence the speed of the sales process in the near future.

VI. Conclusions for the Establishment of Land Funds and Land Banks

The central problem of the agrarian sector in the SEE/MEE/CIS countries is the too little and too slow inflow of investment into farms and the processing sector. One important reason for the reluctance of banks and investors is the absence of a functioning, transparent and legally reliable land market for lease and sale and the inadequate protection of the land market by state and state regulated institutions.

A working land market is so important in these countries because the restitution towards former owners and the distribution of land among the rural population has led to a widespread fragmentation of land ownership. Besides most SEE/MEE/CIS countries still keep a large proportion of agricultural land and forests in state ownership. That is mostly due to the lack of ultimate allocation of ownership or the lack of effective privatisation programmes. Moreover most countries have imposed restrictions, e.g. no sales at all until a set date, maximum size of holding, no sales to foreigners etc.. This basically means, that a large proportion of land is not at the disposal of a national land market.

The resolution of an unclear and often economically unfavourable ownership structure and usage pattern is inevitably connected with often prohibitive costs for the involved landowners and farms. That calls for a systematic exertion of influence by the state in order to improve the land market conditions. It includes the necessity to “deprivatise” non viable land plots and redistribute them by following agri-structural goals. One could well call that path the „grand detour“.

A viable path seems to be to develop a long term strategy for rural areas, accompany that by the ratification of appropriate land ownership and land market laws and to round it off by an effective state land management institution.

Stefan Kresse

Katja Dells

Hans-Egbert von Arnim

Berlin, 5th of March, 2004