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PURCHASING YOUR DREAM HOME IN MEXICO by Linda Neil Mexico is an exciting place to live for those who are retiring, for those who are working from home on a computer link with their company, for those who are looking for a vacation home or an outstanding investment... above all, for those who dream of a better quality of life! Home... the word represents security and comfort for the majority. All too often the word, when used in conjunction with a purchase of property in Mexico creates stress, worry and, at times has been associated with financial loss. This needn't be the case. Procedures in searching titles and transferring property are similar to those of the United States and Canada. The buyer of a house, condominium or lot in Mexico must ask the same questions, and should receive answers similar to those received when buying a property elsewhere. **RULE NUMBER ONE: SELECT THE COMMUNITY AND THE COMPANY THAT FITS YOU** In considering the purchase of something so important as a home it is necessary to have the right people representing the buyer and his interests. This can be accomplished by first selecting the general area where you think you'd like to live. A review of the local newspaper or telephone directory will give a listing of the real estate companies in the area. Through NAFTA agreements, the Association of Mexican Real Estate Professionals (AMPI), is now affiliated with the U.S. National Association of Realtors (NAR), the Canadian Real Estate Association (CREA), and the International Real Estate Association (FIABCI). These important national real estate organizations are working to achieve standardization of real estate practices and procedures throughout the world. The company you select to represent you in your Mexican property purchase should be a member of AMPI. Not only is the AMPI member company required to operate under a higher standard of care, and to adhere to a code of ethics, but also it may have access to an increasing number of the properties available for sale through computerized data bases. Once the area is selected and a list of the AMPI companies operating there has been obtained - interview the owners and operators of the companies. Ask for references, ask for a professional resume. Interview carefully the persons that most impress you. The person you select should be familiar with area, with basic real estate principles... and should impress you with his or her honesty and drive to find what YOU are looking for. Once you have found the person you feel comfortable with, stick with him or her and let him do his job. The sales person who knows you aren't shopping around will generally work harder to find exactly what you are looking for. Remember, it is your money and your commitment. Do not be pressured by someone who is charming but who does not listen carefully enough to understand YOUR special needs. **RULE NUMBER TWO: EXAMINE THE NEIGHBORHOOD** Once you have selected the right community, an agent with whom you feel comfortable, AND a possible property, check out the neighborhood. Is it new? Is it old? What will it look like 1 in ten years? Are highways or other development projects planned for the future? Where are schools, churches, shopping facilities? Are there homeowner fees for maintenance of common areas? If so, how much are they and when are they paid? Are all the utilities in and paid for? What does the developer have left to do? What building restrictions are there? Are there covenants and conditions registered for the usage of the land?

In many parts of Mexico there is no enforcement of a master plan or building codes. This can affect the changing face of the neighborhood you have selected.

RULE NUMBER THREE:

BUDGET FOR YOUR PURCHASE, CHECK TITLE AND UNDERSTAND THE MEXICAN BANK TRUST (*FIDEICOMISO*)

CLOSING COSTS:

Closing Costs will range from 4% to 30% (yes, 30%!) of the total cost of your property. The higher the price of the property, the lower the percentage of total costs for closing. This is because certain expenses for permits and certificates are fixed, regardless of the value of the property. Costs of transfer include title search, transfer taxes, bank fees, government permits and notary fees. Your seller may assist in some of these; especially those related to title search and insurance. Be sure to get a written estimate so that you will not have unwelcome surprises at the date of transfer of title! While your real estate agent may know the procedure, his or her specialty is to identify the correct property for you and to negotiate advantageous terms for the purchase. The technicalities of the transfer; negotiations for permits, registrations and so forth are generally more objectively and thoroughly handled by a neutral third party who does not have a financial interest in the transaction.

CHECK THE TITLE:

Does your seller have a registered title to the property? Many foreign buyers, in order to avoid the closing costs, or through ignorance, have paid for their property, taken possession of it, and have *never* obtained a registered title! Ask for a copy of your Seller's title documents and reserve the right to examine them prior to the release of any part of your payment. If they are in Spanish have them translated and, if in doubt consult with a neutral third party about their probable validity. It should be added that if the seller has never acquired title to the property he is selling, it can often be remedied. The buyer should be aware of this condition, however, and be certain that the person who accepts his offer is truly the holder of the title. Additionally, he should make arrangements for the additional costs, if any, involved in this double transfer.

UNDERSTAND THE MEXICAN TRUST - *FIDEICOMISO*

Payment of the purchase price is not enough. In order to have a valid ownership interest in the property which you are buying it is necessary to have the title recorded. This puts the rest of the world on notice that the property is yours. If you are a foreign person purchasing property in many parts of Mexico, *including the entire Baja peninsula*, the property will transfer not to your name but to the name of a Mexican bank as trustee for your interests. The Mexican constitution prohibits direct ownership of real property by foreigners in the "prohibited zone", a strip of land thirty miles wide along its seacoasts and sixty miles wide along its borders with the United States and Guatemala/Belize, as well as the entire Baja peninsula. This is the reason for the bank trust, the "*fideicomiso*", which has been established under the guidelines of the Mexican government so that foreigners may be protected in their property acquisitions.

Whether you are purchasing in a zone requiring a bank trust or in an area where title can be taken directly into your name, it is necessary that this transfer take place and your interest registered as soon as possible after the successful conclusion of the negotiations to purchase your dream property. Until this transfer takes place you are vulnerable: the seller may die, the heirs may be unwilling to recognize your rights in the property, you may become involved in a lengthy and expensive probate

proceeding. Meanwhile, your interest may not be recognized by the authorities should you wish to obtain a building permit, by the bank should you wish to borrow money and use the property as collateral or as part of your assets; by the courts should a third party also claim an interest in the land, or, very importantly, should you later decide to sell it.

The prudent buyer of real estate in the United States or Canada would not consider leaving his title "in limbo" in either of those two countries; one should not do so in Mexico either.

The foreigner purchasing real estate in Mexico is buying *personal, not real* property if the acquisition is on the Baja Peninsula, within thirty miles of any coastline on the mainland, or within sixty miles of any border. The acquisition is *personal* property.

How does *personal* vs. *real* affect the foreigner who acquires property under a Mexican bank trust? The effect is negligible. Instead of using the words; "transfer of title" one should more properly say "transfer of trust rights", or, "assignment of trust rights". In practical terms the beneficiary has full control of the property. He may direct the trustee bank to 1.- lease the property, 2.- mortgage the property, or 3.- sell the property. The foreign owner enjoys full rights of usage and may do anything to the property permitted under Mexican law. He enjoys the same rights of dominion as any Mexican citizen who has direct title to the property. He may construct a building, tear it down or modify it in compliance only with the local zoning and planning ordinances or, if applicable, the homeowner's condominium regime.

A permit to acquire the rights in the property must be obtained from the Secretary of Foreign Relations and the terms of the permit form a part of the deed. Currently, the term for a trust is fifty years. Multiple renewals are permitted under the law. By requesting extensions each fifty years a property may be controlled by a family or business entity for generations.

RULE NUMBER FOUR:

INVESTIGATE THE STATUS OF THE CONDOMINIUM REGIME

A word of caution for those who are considering the purchase of a condominium or a lot in a subdivision. Just as in other countries, the unit, or lot must be legally described and an individual property tax number issued. This individual property must be registered in both the Property Tax Office and in the Public Registry of Property. Often, a developer will spend time and energy on promoting the sale of the properties prior to completing the establishment of the Condominium Regime. Until this is completed, legal title to an individual unit or lot cannot be granted since there is nothing to describe! Be sure to investigate the status of the condominium regime prior to completing the offer to purchase!

RULE NUMBER FIVE:

INSIST UPON RECEIVING A REGISTERED TITLE

The purchase/sale document signed by buyer and seller is generally legally valid between the parties to the transaction. It most likely contains the description of the property, the price to be paid to the seller, and any other special terms and conditions. It may be drawn up by the parties, their agent(s), or by a third party. It should be considered as an interim contract, however. Until the final deed is drafted by and signed before a Mexican Notary Public and duly registered, the transfer WILL NOT provide valid notice to third parties. This final deed must be recorded in the Public Registry Office of the municipality in which the property is located. Mexico's land registry system functions in much the same manner as those in the United States or Canada.

Unless the deed for the rights of the beneficiary has been recorded, there may not be a remedy for the purchaser who neglected to obtain a registered deed... his interest, his investment, may be lost.

When a foreigner is acquiring residential property for which a bank trust is required, the purchaser should receive a deed which has been signed by the bank trustee before a Mexican Notary Public. This will name the beneficiaries and substitute beneficiaries of the trust in accordance with the purchaser's instructions. A full description of the property must be included, seller's capital gains taxes paid and buyer's acquisition tax paid. These receipts should be included in the deed document which may consist of eight or ten pages, or more. The final page of the document should bear the stamp of the Public Registry, together with Book and Page numbers and the date on which it was recorded. If this stamp is not on the document, the transaction has not been completed, the buyer is not fully protected.

CONSIDERATIONS IF FINANCING YOUR PROPERTY:

Until recently, most homes and condominiums were for sale for all cash or financed by the seller. With the advent of NAFTA however, several mortgage companies have entered the Los Cabos and Cancun, Riviera Maya marketplaces and offer long-term financing for qualified buyers. If you are considering financing your purchase, and are buying in a location where financing is offered, it makes sense to investigate the terms and plans available, select the company of your choice and make lender approval a condition for the purchase.

If the seller will be financing your purchase, request that title be transferred to you and a pledge guarantee contract executed guaranteeing payment. Traditionally, sellers have preferred to hold title to the rights in their name and transfer title to the rights only upon receipt of payment in full from the buyer. Meanwhile, however, the seller may die, may disappear, may go bankrupt... a risky situation for the buyer. The prudent buyer will insist upon a transfer of title and registration of a mortgage or pledge in which he gives his rights in the property as security for payment of the remaining purchase price. In the event of default by the buyer, the seller must conduct a proceeding similar to a judicial foreclosure in the United States and Canada. It is troublesome, as is any foreclosure in any country in the world but not notably more problematical. The registered title and recorded pledge or mortgage provide the buyer a greater comfort level in his investment. The lender also enjoys protection in having his loan recorded and will have an established legal proceeding to follow in the event of default by the buyer.

CLOSING COSTS.... OR HOW TO AVOID UNPLEASANT SURPRISES.

Mexican law says that taxes must be paid on the higher of the following: purchase price OR appraised value. Since many appraisals are lower than the actual selling price your taxes will be considerably lower if the appraisal value is declared. Payment on this basis has taken place for many years in many parts of the country. It is, however, illegal. Should you choose to pay your costs based upon this basis, please be aware that: 1. it is violation of the law and 2. your tax base will be low for declaration of value in the property when you sell it. Furthermore, if you are financing your property through an institutional lender, full value must be declared.

Following is an example of some of the steps involved in obtaining a registered title. The costs for same will vary with the property and a written estimate should always be obtained prior to initiating the process.

OFFICIAL APPRAISAL: The appraisal must be made by an appraiser who is usually an architect and who is recognized as a *Perito Valuador*, Official Appraiser,

by the property tax authorities in the municipality where the property is located. This is required prior to completing any transfer of title. If an institutional lender is involved, a commercial appraisal may also be required.

FOREIGN RELATIONS PERMITS: If the property you are purchasing is already in a trust (*fideicomiso*) you may either: request assignment of the rights to you, or may request a new trust for fifty years. If a new trust, a permit from the Secretary of Foreign Relations is required. Whether a new trust or an assignment of rights, the deed in the new buyer's name must be registered in the National Foreign Investment Registry. When considering a new trust or an assignment of rights, the factors to be considered are: 1. Remaining term of the existing trust - when will it need to be renewed?; and 2.-What are the annual bank fees under the existing trust?

If the permit has an unexpired term of less than fifteen or twenty years and/or the annual bank administration fees are more than \$500.00 U.S. dls., it probably makes sense to obtain the permit for a new fifty year trust with a bank offering more attractive fees.

NOTARY FEES - The Mexican Notary Public is an attorney who has practiced his profession for at least five years and has been appointed by the governor of the state in which he is practicing. His duties and obligations include; drafting of the deed, calculation of seller's capital gains taxes and buyer's acquisition taxes and to "give faith" to the validity of signatures. The persons signing before him must prove they are who they say they are. Because the responsibility and potential liability for the actions of the Mexican Notary Public are considerably higher than those of Notaries Public in the U.S. and Canada, the notary's fees will also be substantially higher than those charged on the other side of the border. These fees are based upon a rate schedule reviewed and approved annually by the College of Notaries Public and are tied to the amount declared in the property transfer.

I.V.A. - The Impuesto Sobre Valor Agregado (I.V.A.) is a value added tax which is charged on all services. It is 10% of the value of services provided on the Baja Peninsula and 15% for services provided on mainland Mexico. Many trustee banks are headquartered on mainland Mexico, thus the I.V.A. charged on their services will be 15%. IVA taxes must be paid on services provided by the Notary, the appraiser and any other professionals whose services you use

BANK ADMINISTRATION FEES: If title to your property is in a bank trust there will be annual fees for the administration of same. Over the past few years there has been a substantial decrease in annual fees and it makes sense to shop around for the most favorable rate for the property being purchased if a new trust is contemplated. If an assignment, new rates may possibly also be negotiated. Traditionally, trustee banks have not sent annual statements. It is important to request a statement from your trustee bank at least ninety days prior to the anniversary of the trust and pay on time to avoid penalties, or to contract with a company providing this payment service.

TITLE SEARCH AND INSURANCE: A title search is always a worthwhile investment. An investigation will generally indicate the registered owner, the chain of title, and will indicate liens, if any, against the property at the time of the investigation.

Title insurance, issued when the new deed is registered, guarantees the marketability of the property and is a requirement by most institutional lenders. There

are currently three US title insurers offering policies on Mexican properties. In the event there is a problem with title, the insurer is obligated to defend the owner's rights in the property and/or indemnify the owner against financial loss. Investment in a title policy puts the financial risk on the insurer, not the buyer who may not be able to defend the property as well as a major insurance company.

PROPERTY TAXES: are a municipal tax and income benefits the municipality. Typical rates for residential dwellings is 6.5 (pesos) per 1,000 and 13 per 1,000 for properties destined as rental units. Vacant lots are rated at 26 per 1,000 with an increase of 2.6 per annum for each year there is no construction declared on the lot. Maximum amount is 52 per 1,000. Valuations for property tax purposes are generally made every two to three years or at the time of sale of a property. Property taxes must be brought current prior to transfer of the title.

ACQUISITION TAX: The acquisition tax, or transfer tax, is generally paid by the buyer. It is currently 2% of the declared value of the property in most parts of the country.

CAPITAL GAINS TAXES: A foreigner who sells property in Mexico is liable under special rules, much like the United States, for the payment of the I.S.I.R. (*Impuesto Sobre la Renta*) which is the Mexican equivalent of the Capital Gains tax. Liability is either 20% of the declared value of the transaction or 33% of the net value, taking into consideration the length of time held, the improvements made, commissions paid and other allowable expenses. The formula is complicated and the tax should be figured both ways and confirmed by the Notary Public who will be having the documents recorded and making the tax payments. This is a seller tax and title cannot transfer to the buyer under this tax has been paid.

SETTLEMENT FEES: Attorneys and Notaries Public often oversee parts of the previously described required steps to a transfer. The buyer, however, usually has to do certain of his own legwork and can certainly do so if he has a good command of the Spanish language. Unless the buyer has a lot of time to spend on the activity, it may make sense to hire a company whose sole purpose is to supervise and coordinate the permits, tax payments and other myriad of details so necessary to obtain full legal right to the property being purchased. Fees for these services will vary with the value of the property and the complexity of the situation. It is important to always request a written estimate of all the expenses prior to beginning the transfer!

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Linda Neil is founder and CEO of the settlement company®, consultants and land use professionals specializing in legal and tax matters affecting real properties in Mexico. The company provides escrow services and supervises the transfer of titles on Mexican properties located anywhere in the country. Ms. Neil, a California-licensed real estate broker with 30 years of experience in Mexican real estate, is a member of AMPI, NAR and FIABCI. For further information on these subjects, e-mail: info@settlement-co.com.