



The Legal 500 & The In-House Lawyer
Comparative Legal Guide
Mexico: Real Estate

This country-specific Q&A provides an overview to real estate laws and regulations that may occur in Mexico.

It will cover the most pertinent issues including ownership structures, restrictions, transfers, taxes and environmental contamination.

This Q&A is part of the global guide to Real Estate. For a full list of jurisdictional Q&As visit <http://www.inhouselawyer.co.uk/index.php/practice-areas/real-estate>



Country Author: Nader Hayaux & Goebel

The Legal 500



Vanessa Franyutti J, Partner

vfranyutti@nhg.com.mx

The Legal 500



Alejandro Rojas V, Partner

arojas@nhg.com.mx

The Legal 500

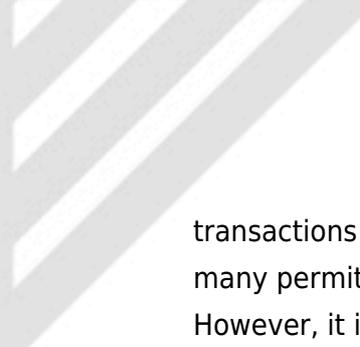


**Fernando Castillo V,
Associate**

fcastillo@nhg.com.mx

1. Overview

Mexico is a civil law jurisdiction; therefore, real estate transactions are subject primarily to the provisions contained in civil statutes. Mexico's federal system is composed of 32 States and several municipalities within each state, and as such, federal and local regulations apply to real property matters. In general, real estate



transactions are governed by local statutes (i.e. Civil Codes of the different States) and many permits related to real estate fall within the scope of the municipal authorities. However, it is important to note that there is an extensive uniformity among the local civil codes and other state-related statutes, particularly covering the conveyance of real property. Finally, Article 27 of the Federal Constitution provides a broad general regime for real estate transactions.

Currently, the real estate market in Mexico offers a wide variety of opportunities for domestic and foreign investors. Increase in funding sources and real estate demand are two of the main reasons for the development of this sector during the last few years. Mexico's legal framework provide for different financial investment vehicles focused on commercial real estate transactions, such as private funds and trusts, as well as capital markets vehicles, such as FIBRAs (equivalent to U.S. REITs) and CKDs (please refer to the answer to question 6 for further detail of such vehicles).

2. How is ownership of real estate proved?

Title to real estate is evidenced by a public deed granted before a notary public and recorded with the corresponding Public Registry of Property ("Public Registry"). Each Public Registry is managed by the local government authority, usually the city or municipality where the real estate is located.

The notary public granting the public deed, which constitutes evidence of title to the real property, delivers the deed to the Public Registry for registration. The public deed is then granted a record number, which serves as evidence of ownership to third parties.

In all States, except Quintana Roo, recording the public deed with the Public Registry has a declarative effect, this is, it evidences to third parties consulting the Public Registry who owns the property. Only in the State of Quintana Roo, however, recording of title is mandatory to perfect conveyance of property, which means that title transfers occur only upon the public deed being properly recorded.

Exceptionally, title to real estate can also be evidenced by judicial resolutions (i.e. adverse possession) or agrarian certificates regarding certain “ejido” land transactions.

3. **Are there any restrictions on who can own real estate?**

In Mexico, foreign individuals and entities cannot acquire direct ownership of land located in a strip of 50 kilometres along the coastline and 100 kilometres along the borders (“Restricted Zone”, which covers almost 40% of the entire national territory).

Likewise, Mexican corporations with foreign investment cannot acquire direct ownership of land in the Restricted Zone for residential purposes. If, however, the land is used for other non-residential purposes (i.e. commercial, industrial, timesharing or tourism activities), the acquisition by a Mexican entity with foreign investment is permitted upon filing a notice with the Ministry of Foreign Affairs.

Foreigners who want to acquire rights in real property located within the Restricted Zone may do so through a leasehold interest (as tenants) or through a Mexican trust. The trust is a commonly used vehicle where the trustee (a Mexican financial institution) acquires title to the real property for the benefit of the foreigners (beneficiaries), who are entitled to use, enjoy, occupy, possess and obtain proceeds from the real property according to the terms and conditions set forth in the trust agreement. Mexican trusts created for these purposes may not exceed 50 years, but the term can be extended upon request to the Ministry of Foreign Affairs.

Outside the Restricted Zone, foreigners can directly own real estate subject only to obtaining a permit from the Ministry of Foreign Affairs.

Likewise, religious associations, charities and good will associations can only own real estate that is essential for their specific purpose. Financial institutions are also limited to own direct title to real estate that is essential for their specific purpose.

4. **What types of proprietary interests in real estate can be created?**

Civil statutes in Mexico provide for the following proprietary interests:

Rights in rem

- Fee simple, which grants absolute ownership on real property for indefinite duration (perpetuity).
- Rights which limit absolute ownership on real property:
 - Usufruct, whereby the owner of certain property conveys the right to use and enjoy such property (or part of it) to the beneficiary – “usufructuario” (including everything it may produce). If the beneficiary is an individual, the usufruct may be for a life-time term; for entities, the maximum term is limited to 20 years.
 - Easement, which grants the right to use, enjoy and/or pass through the real property of a third party for a specific and limited purpose, within a part of the property, without owning or possessing it.
 - Mortgage, which grants a lender a security interest in real estate to secure an obligation.
 - Use and occupancy rights (“derecho de uso”), which are similar to usufruct (right to use land) but with no right to benefit from the products of the real property.

Rights in personam

- Leasehold interests (landlord/tenant law).
- Beneficial interests under a real estate trust (the trustee would be the titleholder to the property).
- Other in personam agreements between the owner and the corresponding beneficiary (i.e. commodatum, which is the right to use real property for no consideration).

5. **Is ownership of real estate and the buildings on it separate?**

Real property comprises the land, buildings, constructions and other structures attached to it that, if removed, would damage the property. Thus, ownership of real

estate entitles the owner to everything that the land produces and that is adjoined or incorporated to it, whether naturally or artificially. The legal consequences of building on someone else's property will depend on whether the parties acted in good or bad faith.

Generally, title to real estate is not separate from title to the buildings; they automatically follow ownership of the land. In this regard, land and constructions are recorded together with the Public Registry by means of the public deed evidencing ownership of the real estate. Some States, however, acknowledge in their Civil Codes the right to acquire and register land and buildings separately, according to specific rules that may vary from State to State (i.e. Nuevo León, Morelos, Querétaro, Guanajuato, Jalisco and Puebla). Furthermore, other jurisdictions may allow to waive the inherent right of an owner to own the constructions on their property, in which case, a co-ownership would exist.

6. What are common ownership structures for ownership of commercial real estate?

The most commonly used ownership structures for commercial real estate are:

- Direct ownership by individuals (least common structure due to increased liability exposure).
- Direct ownership through companies.
- Trusts, including specific real estate trusts which rights are publicly traded (e.g. FIBRAs and CKDs).

FIBRAs (fideicomisos de inversión en bienes raíces). Mexican equivalent of REITs (real estate investment trusts) that have become one of the most attractive mechanisms for real estate developers for its tax benefits. Real property owners create a FIBRA by conveying title to a Mexican trust, which, in turn, issues real estate trust certificates in a registered stock exchange providing that the resources obtained from such allocation are used to acquire and develop real estate intended for leasing, based on certain eligibility criteria established under the FIBRA governing documents.

CKDs (certificados de capital de desarrollo). Development capital certificates (known as CKDs) are investment vehicles structured through a Mexican trust which receive resources from the public offering of trust certificates (mainly from pension funds), to finance national infrastructure and real estate projects, as well as to perform investments of private capital in promoted companies.

Sometimes, real estate is transferred indirectly to a buyer through the acquisition of (i) shares or equity interests in the specific vehicle or entity holding title to real property, or (ii) beneficial interests in the corresponding real estate trust.

Real estate trusts became popular in Mexico mainly because of its flexibility as investment vehicles. For instance, by implementing a real estate trust structure, owners and private investors could transfer title to real property and funds, respectively, to develop a specific project, providing for different rights and obligations each of them would assume through their beneficial interests under the trust agreement.

7. What is the usual legal due diligence process that is undertaken when acquiring commercial real estate?

Due diligence process in commercial real estate transactions is usually carried out by counsel acting for the buyer with the support of technical teams in environmental matters. It typically includes an environmental study and a title report. For title reports, a search in the Public Registry is necessary. The search and report product of the due diligence process usually covers the following standard issues:

- Permits, licences and authorizations required for the real estate.
- Material agreements with respect to real property, including project and corporate financing and collateral agreements.
- Limitations on land use imposed by zoning ordinances, urban development regulations, governmental authorities (i.e. concessions, federal zone limitations, etc.), or private agreements (usufructs, easements, covenants, etc.).
- Liens and encumbrances affecting the real property, as well as pending claims against the real property by third parties (generally identifiable through a lien certificate - certificado

de libertad de gravámenes).

- Limitations or requirements according to covenants over real property.
- Agrarian or “ejido” interests (generally identifiable through an agrarian certificate - certificado de no afectación agraria).
- Municipal assessments for public improvements and property taxes.
- Existence of condominium regimes or owners’ associations.
- Rights of third parties in possession (i.e. adverse possession).
- Long-term leases.
- Unpaid taxes and utility charges, fees or rights (i.e. water and electricity).

Due diligence process includes counsel’s opinion on different records and other elements necessary to ascertain any potential risks for the transaction. Moreover, it is appropriate to perform technical assessments on the real estate prior to closing to ensure compliance with Mexico legislation (i.e. environmental, geological, and topographical due diligence). Costs associated with due diligence include notary public fees and costs associated with the appraisal of the property, public registers and archives duties where relevant documents are obtained from.

Due diligence is always recommended for commercial real estate and the forms will vary depending on the characteristics of each transaction; although there are no specific forms, buyers require between 30 and 120 days to carry out the due diligence process.

Sellers of commercial real estate usually provide limited warranties, which are related to: (i) legitimate ownership and title over the real property (marketable title at closing); (ii) absence of liens and encumbrances; (iii) payment of real estate taxes and utility charges or fees; (iv) absence of environmental liabilities; and (v) absence of false statements or material facts. Therefore, buyer’s due diligence process is essential to determine the legal and physical condition of the real estate and assess risks efficiently.

Additionally, under civil law the buyer is protected with a statutory indemnity (“saneamiento para el caso de evicción”). If buyer is evicted due to a judicial decision

arising from a third party claiming superior rights over the land (i.e. absence of seller's title), buyer is entitled to recover damages from seller.

8. What legal issues (if any) cannot be covered by usual legal due diligence?

Under due diligence for commercial real estate transactions, most legal issues are covered. However, environmental risks are often difficult to assess since they require specialized knowledge and government regulation in this matter is vast and complex. Independent environmental law specialists and technical consultants are often involved in this type of due diligence.

Other area of material legal risk, which could have limited coverage by regular due diligence process, is the one related to agrarian property (ejidos); mainly consisting of matters arising from acquisitions through inheritance or from non-visible errors in converting ejido (communal property) land into private property land.

9. What is the usual process for transfer of commercial real estate?

The usual process for a commercial real estate transaction includes pre-contractual arrangements, the purchase and sale agreement contained in a public deed, and recording the public deed with the Public Registry.

Pre-contractual arrangements (heads of terms, letters of intent, term sheets, etc.) may be binding if the parties so provide in the corresponding documents. Arrangements prior to title transfer that are often binding between the parties consist mainly of promises to purchase or sale agreements subject to conditions precedent.

Except in the State of Quintana Roo, title transfer occurs at the moment the parties agree upon the essential elements of the sale (identification of parties, description of real property and price/consideration) and the agreement is formalized before a notary public. For title transfer to be effective as against third parties, the public deed must be

recorded with the Public Registry. In the State of Quintana Roo, however, the record of the public deed with the Public Registry is required for title transfer to occur.

Please see below a table with relevant steps and responsible parties for closing a commercial real estate transaction:

Transaction Steps	Seller	Buyer	Comments
Pre-agreement	<ul style="list-style-type: none"> · Preparation of draft sale and purchase agreement · Negotiation of sale and purchase agreement with buyer · Provide buyer with documents and information for due diligence process 	<ul style="list-style-type: none"> · Due diligence · Buyer conducts a search in public registries. (Please refer to answer to question 7 above). 	<ul style="list-style-type: none"> · No prescribed form of agreement but industry standard terms · Appraisal of the property prior to the transfer agreement
Signing to Closing	<ul style="list-style-type: none"> · Satisfaction of any conditions to closing 	<ul style="list-style-type: none"> · Arrangement of purchase price funding (including any third party debt) · Satisfaction of any conditions to closing 	<ul style="list-style-type: none"> · A deposit of part of the purchase price is typically paid on signing which will be forfeited if the buyer fails to complete sale · Escrow instruments may be used to secure full payment upon satisfaction of conditions to closing
Closing	<ul style="list-style-type: none"> · Repayment of any existing debt and discharge of mortgage (if any) · Execution of transfer agreement 	<ul style="list-style-type: none"> · Execution of transfer agreement · Payment of purchase price 	<ul style="list-style-type: none"> · A notary public must formalize the transfer.
Post-closing		<ul style="list-style-type: none"> · Payment of real estate acquisition and other related taxes · Registration of transfer at the Public Registry 	<ul style="list-style-type: none"> · The registration duties depend on the transaction price and the place where the land is located. Notary publics usually arrange this step

10. Is it common for commercial real estate transfers to be effected by way of share transfer as well as asset transfer?

Yes, depending on the parties' needs and tax circumstances, real estate transactions can take place either through an asset sale or through a share or interest sale (whether

equity or beneficial interest).

11. On the sale of interests in land does the benefit of any occupational leases and income automatically transfer?

Under Mexican civil law, lease rights run with the real property conveyance. In this case, tenant has a right of first refusal in case landlord decides to transfer the real estate over which the lease was created (unless such right is waived), and landlord must give tenant prior notice of the intention to sell in order to allow tenant to decide whether or not the right of first refusal is exercised.

As a general rule, the lease will transfer and subsist in the same terms of the original lease agreement, but now tenant shall pay the rent to the new owner, including unpaid rents. The new owner must notify tenant of the title transfer in order to have the right to demand and collect rent payments.

12. What common rights, interests and burdens can be created or attach over real estate and how are these protected?

Under Mexican civil law, there are specific forms of servitudes that can be created over real state, such as access and water easements, real covenants and easements for utility companies (i.e. power transmission lines). In addition, few States recognize the right to create view easements over real property under certain conditions. In some cases, servitudes must be constituted by operation of law; for instance, in case the land has no access to a public road, the law gives the owner the right to demand before the court the creation of an access easement.

Easements must be recorded with the Public Registry to be effective as against third parties. Easements are in rem rights and, as such, are usually transferred with any conveyance of land.

13. **Are split legal and beneficial ownership of real estate (i.e. trust structures) recognised**

Trusts are structures frequently used for commercial real estate transactions in Mexico; nonetheless, ownership is not split into legal and beneficial title as in common law jurisdictions. Under Mexican law, real estate trusts are agreements under which the owner conveys title to the trustee (a Mexican financial institution), which acquires the real property for the benefit of the parties acquiring a beneficial interest in the trust. The beneficiaries have the rights accruing to them under the trust, which could include the right to use, enjoy, occupy, possess and obtain proceeds from the real property. Moreover, beneficiaries instruct the trustee in connection with the real estate.

However, the only title subject of registration with the Public Registry is the one held by the trustee, which is considered for all legal effects as the sole owner of the real property. In other words, beneficiaries cannot record separately their beneficial rights derived from the trust agreement (some states have allowed for such registrations; however, there is no legal basis for such registrations).

14. **What are the main taxes associated with commercial real estate ownership and transfer of commercial real estate?**

Taxes payable with respect to a commercial real estate transaction include the following:

- Real Estate Acquisition Tax (impuesto sobre adquisición de inmuebles). Any irrevocable conveyance of title over real estate is subject to this tax and the rate varies depending on the State, usually between 2% to 3% of the highest between the appraised cadastral value and the purchase price.
- Value Added Tax. This tax has a rate of 16% and applies to the acquisition of buildings, constructions and improvements over commercial real property.
- Income Tax. Seller is responsible for the payment of the corresponding income tax derived from the real estate sale. Base and rates for the payment of income tax will depend whether the seller is an individual or entity, as well as on the seller's place of residence.
- Real Estate Tax (impuesto predial). This tax is paid each year (periodically) by owners of

real estate, depending on the value of the property.

- Recording Duties. Public Registry duties depend on the value of the transaction and the place where the real estate is located, although some states have caps to these duties.
- Appraisal Fees. In commercial real estate transactions, an appraisal has to be made for tax purposes and generally a broker or certified appraiser charges between 1% and 2% of the transaction value as appraisal fee.
- Notarial, Brokerage and Legal Fees. These additional fees vary widely depending on the characteristics of a particular transaction.

15. **What are common terms of commercial leases and are there regulatory controls on the terms of leases?**

Landlord/tenant law for commercial leases in Mexico provides for the following general terms:

- Lease agreements are governed by Civil Codes; however, parties may freely discuss and set forth terms and conditions to regulate the landlord/tenant relationship, except for specific statutory rights that cannot be waived or amended to protect tenant's interests (i.e. rent reductions for inability to use the leased premises due to force majeure or acts of God).
- Security deposits between 1 and 3 months of rent are customary in commercial leases in order to secure tenant's obligations under the lease agreement.
- Landlords usually require a guaranty to secure compliance with the lease agreement's obligations, particularly timely payment of rent. The guaranty is often provided by surety bonds or corporate guaranties from tenant's parent companies.
- Tenants have the right of first refusal in case landlord decides to convey the real property to any third parties. This right may be waived in the lease agreement and such waiver is customary in commercial leases.
- Generally, rent is fixed according to a specific amount negotiated by the parties; however, some commercial leases may adopt a variable formula to compute rent based on tenant's turnover and other variable factors, depending on the purpose of the leased premises. Rent is also usually indexed from year to year.
- Eviction procedures generally take longer than in other jurisdictions because the landlord/tenant laws tend to protect tenant interests. In the event of default under the lease agreement, landlord has the right to initiate the eviction procedure, but tenant is

entitled to raise a defence that may delay the eviction procedure.

- In market standard terms, sub-leases and lease assignments are permitted without landlord's prior consent only with respect to tenant's affiliates or related parties, provided that the guaranties granted are kept under the same terms. In order to sub-lease or assign a lease agreement to unrelated third parties, it is common that landlord must grant prior written consent.
- Tenants of commercial leases are usually responsible for costs related to the leased property, including full repairing and insuring costs. Furthermore, usually any refurbishing or conditioning of leased space must be paid by tenant, approved by landlord and will, at the end of the lease, benefit the landlord.
- Most Civil Codes establish a maximum term for leases depending on the use to be given to the leased premises. Commercial and industrial leases, generally, cannot exceed 20 years (this term may vary according to the state the land is located).

16. **How are use, planning and zoning restrictions on real estate regulated?**

In general, municipal authorities have jurisdiction over urban development and land use by enacting zoning plans and ordinances. A specific municipal agency is in charge of imposing and supervising compliance with planning and zoning restrictions.

Moreover, Federal and state governments can also intervene through their respective legislation setting standards as to the use that may be given to specific areas; for instance, there is a general statute that applies to all the different levels of government (Ley General de Asentamientos Humanos, Ordenamiento Territorial y Desarrollo Urbano) which is adopted, regulated and applied specifically by each state. Besides, Federal, state and municipal authorities may also provide limits to land use through the enactment of several environmental regulations.

The most common permits and licences required for real estate developments are the license for land use or zoning certificate (licencia de uso de suelo), environmental and construction permits. Operating licenses and liquor licenses may also be required.

17. **Who can be liable for environmental contamination on real estate?**

Under Mexican environmental laws and regulations, owners and any possessors of real estate are jointly and severally liable for soil pollution and other environmental issues, irrespective of any claim they might have against the polluter. Owners and possessors must carry out, jointly and severally, the remediation activities (i.e. clean up) necessary to prevent pollution of the property.

Conveyance of polluted real property requires previous authorization by the Federal environmental agency (SEMARNAT) and any environmental authority shall request remediation from the owner (seller), possessor or buyer, even if the environmental issue was caused by a third party. Although the parties may agree and distribute environmental risks under the transfer agreement, governmental agencies are entitled to bring actions against either party (and other possessors or third parties) for remediation of the land.

Environmental liability is not limited and, therefore, buyers have to undertake comprehensive studies and due diligence to the land's environmental conditions before closing the transaction.

18. **Is expropriation of real estate possible?**

Yes, Federal and local governments, through the executive branch, have the constitutional authority to expropriate and take private real estate for public use. An expropriation must be accompanied by payment of "just compensation" to the owner. In practice, courts have limited compensation to the property's fair market value.

The most common uses of property taken by expropriation are for roads, railways, pipelines as well as the development of infrastructure and public utilities. Expropriation is not very common given the fact that the government usually negotiates easements or sale of land with owners.

19. Is it possible to create mortgages over real estate and how are these protected and enforced?

The most common forms to structure a secured financing for real estate in Mexico are: (i) mortgages, and (ii) security trust agreements.

The mortgage agreement has to be granted before a notary public and the public deed recorded with the Public Registry, in order to perfect the security on the land.

Upon default of the borrower's obligations under the financing documents, the mortgagee/creditor has the right to initiate a foreclosure proceeding in the form of a special summary judicial procedure (juicio especial hipotecario) to enforce the mortgage. In general, the court orders a public auctioning of the real estate to use the proceeds to repay and satisfy the loan in benefit of the creditor. Only under certain circumstances, the court may allow the mortgagee to retain the land in satisfaction of the debt.

20. Are there material costs associated with the creation of mortgages over real estate?

Creation of mortgages over real estate involve notary public fees and legal fees, as well as Public Registry duties to record the public deed. These costs vary depending on the characteristics of the transaction and the place where the property is located.

Mortgages do not involve any tax payments, except for the applicable taxes on interests paid by debtors to creditors under the relevant loan that is secured by the mortgage.



Is it possible to create a trust structure for mortgage security over real estate?

21. Yes, the security trust offers some advantages over the mortgage, particularly

regarding the out-of-court foreclosure procedure. Security trusts are commonly used in loan transactions where not only the land is given as collateral.

The security trust also has to be granted before a notary public and the public deed recorded with the Public Registry in order to perfect the security on the land.

Title to real estate to secure the loan is conveyed by the owner (settlor/debtor) to the trustee (Mexican financial institution), which holds title for the exclusive purpose of securing compliance of the obligations under the financing documents. Upon an event of default, trustee shall follow instructions given by creditor (beneficiary, usually a collateral agent in syndicated loans) to enforce the security.

22. **What is the main legislation relating to commercial real estate ownership?**

- Federal Constitution
- State Constitutions
- Federal and State Civil Codes
- Federal and State Civil Procedures Codes
- Commercial Code
- Agrarian Law
- Foreign Investment Law, and its Regulations
- National Assets Law, and its Regulations
- General Law for the Prevention and Integral Management of Waste, and its Regulations
- General Law of Equilibrium and Environmental Protection, and its Regulations
- General and Local Urban Development Laws
- Local Condominium Regime Laws
- Local Planning and Zoning Ordinances, Land Use and Construction Regulations
- Forfeiture Laws and Regulations