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## **XVIII Real estate**

Article 27 of the Mexican Constitution establishes land and water ownership restrictions. The article grants the Mexican Nation ownership of the land and water within the national territory, and provides that the Nation shall have the power to transfer ownership rights to such properties to private individuals, thereby creating private property.

Section 1 of article 27 grants the right to acquire ownership of land and water only to Mexican individuals and companies, and grants the State a discretionary power to grant to foreigners said rights, subject to the condition that the foreigners agree with the Ministry of Foreign Affairs to consider themselves Mexican nationals with respect to the property acquired, and not to invoke the protection of their home governments with respect to the same. If said covenant is breached, all rights to such property shall revert to the Nation (often referred to as the "Calvo Clause"),

Moreover, the aforementioned section prohibits foreigners from acquiring direct ownership over land and water within the "prohibited," or "restricted zone." That is, within a strip of land 50 kilo meter off the coastline, and within 100 kilometers of international borders.

### ***A. Acquisition of real estate by foreigners***

As a general rule, a foreign individual or company may directly own land in Mexico: However, as stated above, foreigners (individuals or companies) may not acquire direct ownership over land or water located within the restricted zone. Although foreigners may not acquire direct ownership in the prohibited zone, they can acquire other rights over real estate in the following cases:

1. A Mexican company with foreign investment up to 100 percent may directly acquire property within this zone to perform industrial, commercial or tourism activities (non-residential). The acquisition must be registered with the Ministry of Foreign Affairs.

2. Foreign individuals or companies, and Mexican companies with 100 percent foreign capital stock, may acquire the rights of use and benefit from real estate for residential purposes, through a trust executed with a Mexican financial institution. The duration of the trust may be up to 50 years, and the term may be extended upon request of any person having an interest in the property.

3. Foreign individuals or companies may lease real estate and other properties in Mexico without limitation.

### ***B. Agricultural, livestock and timberland***

Foreign and Mexican individuals may acquire land for agrarian, livestock and forestry purposes, subject to the restrictions and requirements mentioned above, and the following size limitations:

1. Individual agricultural property generally cannot exceed 100 hectares (247 acres) of irrigated land. One hectare is equivalent to 2.4711 acres.

Land used for the production of cotton cannot exceed 150 hectares (371 acres) of irrigated land, and land used for the production of a very few specialized crops, like coffee, bananas, cacao, and fruit trees, may not exceed 300 hectares (741 acres) of irrigated land.

2. Individual property used to raise livestock cannot exceed an amount of land necessary to raise a maximum of 500 large farm animals, or its equivalent in small farm animals (the Department of Agriculture determines the equivalent for each type of animal).

3. Individually-owned timberland must not exceed 800 hectares (1977 acres).

As a general rule, a foreign company cannot directly own land in Mexico for agricultural, livestock, or forestry purposes. However, Mexican companies may own agricultural,

livestock or timberland, in tracts not greater than 25 times the factor of individual landholdings, regarding each of the three types of uses mentioned above.

A Mexican company owning land must have a sufficient number of individual shareholders or partners to justify its total landholdings. For example, if the company owns 2,500 hectares of irrigated land, and the individual irrigated landholding is limited in size to 100 hectares, the company must have at least 25 individuals as shareholders or partners.

In addition, the capital stock of the company must include a special series of shares or partnership interests, identified with the letter "T." Series "T" shares, or partnership interests, are equivalent in par value to the value of the capital contributed in agriculture, livestock or timberland, or those funds destined for the acquisition of such land, depending upon the value of the land at the moment of the contribution or acquisition. Foreigners, either companies or individuals, can acquire no more than 49 percent of series "T" shares or partnership interests; the remaining 51 percent must be held by Mexicans. In addition, a corporation may issue an unlimited number of ordinary shares through capital contributions, which may be 100 percent subscribed by foreigners. Series "T" shares carry the same rights as ordinary corporation stock shares.

Furthermore, no individual, either directly or through a company, may hold more series "T" shares, or partnership interests, than those equal to one individual landholding. Another option to acquire land in Mexico is through a Mexican trust.

### ***C. Formalities concerning the transfer of property***

It is advisable to carry out certain verification steps prior to the purchase or sale of property. Mexican law also requires that several formalities be satisfied in order to legally transfer real property.

#### **1. Verification requirements**

Prior to any sale, all individuals or companies, either Mexican or foreign, desiring to purchase real property should verify: (i) that the seller is the owner of the property; (ii) the absence of any liens on the property. If the property is mortgaged, the lien will follow the property, and therefore, the new owner may have the risk of forfeiting such property if the seller defaults on payment obligations; (iii) the existence of any easements on the property, either by law, or by agreement between seller and his neighbors; (iv) that the land involved is not considered "agrarian property" (*ejido*). If the land is classified as agrarian, it must be transformed into "private property;" (v) the status of administrative permits such as "water concessions," or "Federal Maritime Zone Concessions;" (vi) the existence/non-existence of toxic traces in the soil; (vii) that the use regulations allow the use intended for the property; and also (iv) the prospective buyer should verify that the seller has paid the Real Estate Property Tax and water fees for the previous five years.

#### **2. Legal formalities**

Except for very low cost acquisitions, sales of real estate will not have effects before third parties unless they are executed before a Public Notary, in a public instrument recorded in the public registry of property.

#### **3. Immigration status of the foreigner**

All foreign individuals (with the exception of travelers in transit), independent of their immigration status, may acquire real estate in Mexico directly, or acting through an attorney-in-fact, without the need of a permit from the Ministry of the Interior (which was

required in the past), Moreover, foreign individuals can carry out any other act of ownership of real estate without a permit from immigration authorities.

#### ***D. Taxes***

Both the seller and purchaser are liable for taxes upon the purchase and sale of real estate located in Mexico.

##### **1. Income tax**

*a)* If a non-resident individual or company is the seller, the sale of real estate located in Mexico will be subject to a 25 percent tax on the gross amount of the operation, as a final payment.

*b)* However, non-residents who conclude the sale through a public deed may choose to pay a 29 percent tax on the net profit obtained (28 percent in 2007 and subsequent years), Net profit is calculated on an adjusted original cost basis, which includes permitted inflation accounting. The Public Notary is responsible for calculating the income tax and including it in the public instrument. The Public Notary must also collect the payment of the tax from the party, and pay the tax to the Ministry of Finance within 15 days following the execution date of the public instrument.

*c)* The Tax Code considers that a transfer of property has occurred when a trust is created where the grantor designates or agrees to designate a beneficiary different from himself, and does not reserve the right to reacquire the property placed in trust; or if such right was reserved, where the beneficiary loses the right to reacquire the property from the trustee.

In addition, when the beneficiary assigns rights granted, or gives instructions to the trustee to transfer the property to a third party, a transfer of property is considered to take place upon the issuance of said instructions or upon the assignment of rights. The foreigner will be subject to the payment of an income tax according to the aforementioned terms.

*d)* If a non-resident is the purchaser, the tax authority may make an appraisal, and if the value of the appraisal is greater than the purchase price by more than 10 percent, the purchaser will be required to pay a 25 percent tax on the difference between the two amounts. The taxpayer shall pay this tax within 15 days following the notification.

*e)* Income generated by non-resident lessors of real estate in Mexico is subject to a 25 percent income tax on gross receipts. The lessee shall withhold the tax and pay it to the tax authorities.

##### **2. Real Estate Acquisition Tax**

Individuals or companies purchasing real estate, consisting of land and its structures located in Mexico, as well as the accessions related to the land and structures, are subject to the payment of a Real Estate Acquisition Tax calculated at a variable rate between 2 percent and 3.7 percent, which must be applied to the value of the property when located in the Federal District, or the applicable rate in other states.

Purchasers of real property, irrespective of the nature of their operations, must pay this tax. For example, the tax must be paid whether the acquisition is completed through a purchase and sale agreement, a donation, a trust, a merger of companies, split-off, or a payment in kind.

##### **3. Value-Added Tax**

VAT shall be paid by the purchaser of structures or constructions at the rate of 15

percent, calculated on the amount of the operation, which usually includes taxes, other fees, interest, or any other expenses. No VAT is triggered on the sale of land used for any purpose, or on constructions used for residential purposes. In the event that only part of the construction is used for residential purposes, VAT will not be paid on the residential part.

The Mexican notary issuing the transfer document will require a qualified appraisal for tax purposes. Usually, he will obtain certificates of no encumbrance at the Public Property Registry, and certificates by tax authorities, demonstrating that real estate taxes are duly paid. For the transfer to be valid against third parties, the final deed should be registered at the Public Property Registry.