



The Mexican Trust (*fideicomiso*)

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The Mexican Trust or better known as the *fideicomiso* is a commercial contract governed by Mexico's general law of credit instruments and operations (GLCIO). Like most contracts in Mexico governed by a particular statute, the GLCIO includes a number of mandatory provisions which means they can not be modified or waived, but also allows trusts to include other contractual provisions, making them one of the most flexible types of contracts in Mexico, and one that is widely used for many different purposes.

Generally speaking, the trust or *fideicomiso* normally consists of three parties; the trustor or settlor, the trustee, and the beneficiary, although the beneficiary is not required in some trusts. The trustor or settler can either be an individual or an entity, and it's the party that usually transfers title or management of certain assets, rights and benefits to the trustee, who holds them in trust. The trustee is the party that holds the assets in trust, and the party that is given the responsibility of performing and complying with the specific purposes and goals of the trust. And last but not least, is the beneficiary, which although common, it is not a party that appears in all trusts. The beneficiary of a trust is the party that stands to benefit from the assets and trust, whether its by using and enjoying the assets, by having privileges or special rights to the assets such as a security interest, or by receiving income from the assets, to name a few.

Most trusts require that title to the property in trust be held by the trustee, but that does not mean trustees will consider those assets as part of their net worth or reserves. In fact, Mexico has implemented rules that require trustees to keep separate accounting books for assets held in trust. Other trusts simply require that assets be "affected" or "subject to" the trust, which means that title may remain with the trustor.

Also due to statutory requirements, the trustee must always be a Mexican bank or financial entity, and it must act in accordance with the trust's purpose. Unfortunately, the Mexican "bank" or "financial entity" requirement is probably the biggest reason why trusts are not always viewed as a practical mechanism for some business transactions, as many Mexican banks are either unprepared or unwilling to take on the responsibilities and duties within certain trusts, especially when dealing with personal property.

Like in many other jurisdictions, trusts in Mexico are always created for specific purposes, and trustees are bound and limited to act in accordance with such purposes. However, in practice, trustees usually take a passive role during most of the trust's life, further allowing management and other duties to be taken by the beneficiary or other third parties.

For most trusts to function, there is a prerequisite to transfer certain property to the trustee, for its care and management. Trustees must exercise good faith and shall use diligent and professional efforts to promote and protect the best interests of the assets in trust. Although the trusts themselves will include a purpose and the trustee's duties, trustees are always expected to act as good "father figures".

By law, trusts are considered irrevocable, unless otherwise provided in the trust itself, and also by law, trusts can also hold most types of properties, and rights. When properties and rights are transfer to a trust, the trustor may "hold-back" or "reserve" for itself, certain portions of a particular asset, or only do so under a partial or limited assignment. This means the trustor may also keep and maintain for itself, certain rights over the assets held in trust.

Creation and Formation.- Trusts must be in writing and must be prepared (or amended) following the same formalities required for the transfer of the properties that will be subject to the trust. For instance, if the property to be transferred to the trust is real property, then the trust must be created with the same requirements as when real property is transferred in Mexico. That includes the formalization of the trust in a public deed in front of a Mexican Notary Public. Likewise, if the trust will hold personal property only, then it can be created by means of a private contract and no public deed or Mexican Notary Public may be required for the formation process.

Duration.- Trusts are normally for specific period of time and can not exceed 50 years, except under certain specific cases when such term can be exceeded. Also, there are certain types of trusts that can be extended, for instance land trusts which are discussed below. Furthermore, trusts can terminate under various scenarios including the trust reaching its purpose, when such purpose becomes impossible to satisfy, by agreement of the trustor and beneficiary, or when revoked by the trustor, if the trust allows for such revocation, to name a few. Upon expiration, and unless otherwise provided by the trust, the trust assets or the proceeds thereof will distributed to the beneficiary.

Technical Committee.- Depending on the purposes of the trust, the trustee may require either constant or specific supervision and/or direction, or simply certain assistance in satisfying the trust's purposes. This is accomplished by a governing body working in the form of a committee, and its called the technical committee. It is typically appointed at the time the trust is created or when amended. The committee's job or duties can be specific or broad, as determined by the parties creating the trust, or by the parties with authority to appoint and remove members in the committee.

Different uses for trusts:

I Land trusts: Perhaps the most widely known use of a Mexican trust, especially amongst Americans and other non-Mexicans, is the real estate or land trust for the restricted zone for acquiring residential property. Under Mexican law, foreign persons and entities may not own land that is located within the restricted zone, which is an area of 100 kilometers from either border (north or south) and 50 kilometers from the coastline.

These types of trusts are commonly used by foreigners purchasing residential property in tourist destinations like Los Cabos, Riviera Maya, Puerto Vallarta and Acapulco, to name a few.

These trusts can be for a term of 50 years and can be renewed or extended.

The formation process usually takes place by having the seller/developer act as the trustor and by irrevocably transferring title to the property, to the trustee. The trustee then holds the property for the benefit of the beneficiary. The beneficiary will normally have the unrestricted right to enjoy and use the property, as well the benefit of any rental and sale proceeds, if and when the trusts assets are sold, provided the trust allows it.

Before the land trust can be created, the trustee, a Mexican bank, applies for a trust permit with Mexico's Foreign Relations Department (FRD). The application process is relatively simple. Information on the parties and the property is required as part of the application process, together with the payment of an application fee. Under statutory provisions, the FRD has 5 business days to respond all applications, although the term extends to 30 days if the filing takes place at any of the FRD offices located outside Mexico City. Upon the issuance of the trust permit, the parties are then free to formalize the creation of the trust by transferring the real property in front of a Mexican Notary Public.

Like any other real estate transaction, the creation of a land trust will also require the standard due diligence on the property, appraisals, inspections, title searches, the obtaining of certificates of no-liens, certificates of no-debt (on property taxes) and any other customary or statutory requirement under local and state laws for closing on real estate.

Another important feature of land trusts is that they allow the beneficiary to appoint a "substitute beneficiary" at the time of the trust's creation. Upon the beneficiary's death, the substitute beneficiary takes over, as the trust's beneficiary, therefore saving considerable time and money from an otherwise complex probate proceeding in Mexico.

Although the formation process for a land trust may seem relatively easy, and one where little effort is needed, it is advised that beneficiaries negotiate as much freedom and flexibility relative to the assets in trust, and that such terms be clear in the trust itself. Otherwise, the involvement of the trustee will be required, and its is well known that banks can be slow and bureaucratic. Generally speaking, beneficiaries will have the ability to use, and enjoy the property.

However when it comes to renting, managing or making improvements, securing permits, federal zone concessions, and the like, or other more specific actions, unless its negotiated and included in the trust, beneficiaries may find out that they require the participation of the trustee.

Trustees usually grant powers of attorney to beneficiaries to perform such actions, but the granting process takes time, and money, although bank fees are mostly reasonable. Some banks are more flexible than others when it comes to granting powers of attorney and their overall response time, so its important to choose wisely who the trustee will be when the trust is set up.

To sum it up, the Mexican land trust is as safe as the deed to your home in the US or Canada.

Other types of land trusts, including non-business trusts that create certain tax advantages for US companies: Aside from the land trust used by foreigners to acquire residential properties within the restricted zone, there are other types or variations of the land trust. Developers whether acting alone or with other partners in joint ventures, may use land trusts as part of their overall business structure. These land trusts may be required either to segregate ownership of land from a business operation, to satisfy lenders requirements, or to facilitate the ongoing operations with joint venture partners.

Foreign companies investing in land developments throughout Mexico, and not just in the restricted zone, have favored the use of trusts because of certain tax and fiscal advantages. For instance, a US limited liability company may decide to use a trust and become the beneficial owner and lessor of real property located in Mexico. The US company will apply for its tax id in Mexico, and elect to pay taxes on a net basis as provided under the US-Mexico tax treaty.

The trust will also provide that the beneficiary will be entitled sign lease agreements relative to the assets in trust. These non-business land trusts also allow the beneficiary to enter into construction, management, development and marketing agreements with third parties, further enhancing the investment structure and control of the development.

In addition to any tax advantages that these companies receive in the US, some of the advantages in Mexico include that the US company will not have pay withholding taxes on interest payments, and will be able to take depreciation on 100% of the value of improvements built on the site.

II Administrative trusts: These types of trusts will generally revolve around the administration and management of certain assets, and in certain instances, provide for payment and distribution features.

They can either be used by individuals as part of an estate plan, or by corporations as ways of managing their assets. Companies use these types of trusts to manage pension and retirement plans.

The creation and formation process for most administrative trusts is no different from the process discussed above. In other words, the creation process is driven by the type of assets being managed. If its real assets, the creation is more formal with the participation of a Notary Public, and if its personal property, its much simpler.

These types of trusts are also commonly used by municipalities, states and even the federal government, to manage all kinds of resources for different types of government programs. They can range from trusts for education purposes, all the way to trusts that manage and run infrastructure and development projects.

III. Guaranty trusts: Guaranty trusts are fairly new to Mexico. New legislation was enacted in 2000 introducing guaranty trusts as another structure to secure collateral, furthermore, the new legislation was clarified in 2004 removing many of the doubts and confusions created by the initial legislation.

Guaranty trusts present many advantages to lenders and secured parties over other more traditional types of guaranties for instance mortgages, for several reasons. First and foremost, title to the collateral is with the trustee (and not with the debtor, under a standard mortgage), and secondly, in the event of a foreclosure, special summary and out-of-court proceedings are permitted, which are aimed at streamlining the entire foreclosure process.

Guaranty trusts are being used to secure collateral in all kinds of loans issued to Mexicans and to non-Mexican borrowers. These types of trusts typically have two types of beneficiaries, type A which are usually lenders (Mexican or foreign), and type B which are usually the borrowers who will have restricted benefits under the trust, primarily to use, develop, enjoy and profit from the property in trust and its uses.

Once the loans are paid off and there is no need for the collateral to remain in trust, these trusts provide that type A beneficiaries disappear and remove any restrictions imposed on type B beneficiaries, affording full unrestricted rights and benefits to the properties in trust to type B beneficiaries.

Guaranty trusts have substantially impacted Mexico's otherwise limited and expensive Mexico based lending industry, specifically from the consumer / borrower's perspective. They have become the favorite guaranty vehicle for foreign companies and foreign banks lending into Mexico and taking collateral in Mexico. Before the existence of the guaranty trust, foreign companies and foreign banks lending into Mexico and taking collateral in Mexico were very reluctant to participate in those markets. They faced much greater exposure and lengthy and unfamiliar judicial foreclosures under more traditional guarantees like mortgages.

IV. Investment trusts: These types of trusts are generally advertised and used by the banking and financial markets industry as an investment tools. The scope of investment trusts may vary substantially from trust to trust, depending on the market that its designed for, but the goal or purpose is almost always the same, to serve as an investment vehicle for the beneficiaries.

V. Conclusions: The Mexican government has done an impressive job, yet to be completed, by amending and introducing legislation that allows a greater and well accepted use of the Mexican trust as a common tool for the community as a whole, whether on a personal or on a business level.

Banks have also done their part, although because of their greater participation as trustees in Mexican trusts, they are held to different standards. The more common the trust becomes, the more banks will become comfortable with the way it works. Training and support of their trust departments should greatly contribute to the success of the Mexican trust.

If you read this entire article, next time someone says *fideicomiso*.... you will know what they're talking about.

This article is designed to provide information regarding the subject matter covered and is not to be considered as legal advice by the authors. Each case should be reviewed on an individual basis.

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