THE REAL ESTATE M&A AND PRIVATE EQUITY REVIEW

EIGHTH EDITION

Editors
Adam Emmerich and Robin Panovka

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The Real Estate M&A and Private Equity Review

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PREFACE

Real estate investment trusts (REITs) have emerged from covid-19 to face a new reality. Covid's acceleration of a number of key technological trends has changed the way in which we interact with real estate, ushering in an era of increased remote working and online shopping and the adoption of prop-tech into virtually every aspect of real estate. In general, companies with assets that service the digital economy – cell towers, logistics and industrial properties, and data centres – benefited from the pandemic's acceleration of the digital economy, while traditional sectors have had to adapt to the new realities. And the rapid advancement of artificial intelligence promises further change. Additionally, the recent tremors and disruption in the banking industry and the rise in interest rates and inflation, combined with upcoming debt maturities, may portend a volatile period. As always, strategic planning and risk management will be critical to adjust to changing times.

Covid-19 aside, the world is facing a number of macro headwinds that began to rear their heads in 2022, including persistent inflation, a higher interest rate environment, the ongoing war in Ukraine, and considerable turmoil in the banking sector. While there remain opportunities to make strategic acquisitions and investments within real estate, the continued volatility in the near term, and the complex and challenging macroeconomic backdrop will likely continue to have disparate impacts on different subsectors and different geographies within the industry.

Stepping back from recent global events and market dislocations, publicly traded real estate companies and REITs, with help from real estate private equity, have steadily transformed the global real estate markets over the past 25 years. Their principal innovation, and 'secret sauce', has been 'liquid' real estate. Unlike traditional property ownership, equity in publicly traded real estate vehicles is highly liquid, and can be bought and sold in large volumes, literally in minutes, on numerous global exchanges. Indeed, during the pandemic, REITs issued more than US$10 billion in public equity, taking advantage of the massive amounts of liquidity washing over financial markets beginning in the spring of 2020. In 2021, public REITs raised approximately US$27 billion in follow-on equity offerings, declining to approximately US$18 billion during the volatility of 2022.

Publicly traded real estate vehicles now have an aggregate market capitalisation of over US$1.3 trillion globally, including nearly US$1 trillion in the United States and approximately US$130 to US$170 billion in both Europe and Asia. As public REITs and other vehicles have aggregated these properties and grown in scale and sophistication, so too have real estate-focused private equity funds, playing an important role in catalysing hundreds of billions of dollars of REIT and real estate merger and acquisition (M&A) transactions and initial public offerings.

However, despite that massive growth and despite the pandemic, potential growth is far larger both in long-standing REIT markets and in newer REIT jurisdictions, where the trend is more nascent. With increasing development and urbanisation, the world is producing more and more institutional-grade properties, and a growing percentage of this expanding pool – an estimated US$5 trillion and counting – will inevitably seek the advantages of liquidity by migrating to the publicly traded markets. The growth is expected to be both local and cross-border, with nearly 40 countries already boasting REIT regimes. Despite this potential for growth, it remains to be seen whether the ongoing conflict in Ukraine and the associated energy and supply chain disruptions, as well as the rise of populist movements around the globe, will spur a wider backlash against globalisation and cross-border investment.

REITs and other publicly traded vehicles for liquid real estate have grown because they are often a superior vehicle for stabilised assets. Greater liquidity and transparency – and often superior governance – are attractive to investors, resulting in a lower cost of capital and superior access to vast amounts and varieties of capital in the public markets. In addition to cheaper capital, REITs and other public vehicles benefit from efficiencies of scale, sophisticated management and efficient deal structures, to name just a few advantages. With these advantages, the global march of real estate to the public markets seems unstoppable.

This publication is a multinational guide for understanding and navigating the increasingly complex and dynamic world of liquid real estate and the transactions that mostly produce it. The sea change in the markets, sometimes called the REIT revolution, has meant that major real estate transactions have migrated from Main Street to Wall Street. They now often take the form of mergers, acquisitions, takeovers, spin-offs and other corporate transactions conducted in the public markets for both equity and debt. They have grown exponentially in complexity and sophistication, and increasingly represent cross-border multinational transactions fuelled by the now-global real estate capital markets and M&A deal professionals. And they are often intermediated by international investment banks rather than local brokers and financed with unsecured bonds or commercial mortgage-backed securities. In a fair number of cases, they are catalysed by private equity firms or similar actors, sometimes building portfolios to be taken public or sold to public real estate companies, and sometimes through buyouts of public real estate companies for repositioning or sale.

To create this publication, we have invited leading practitioners from around the globe to offer practical insights into what is going on around the conference tables and in the markets in their jurisdiction, with an eye to cross-border trends and transactions. As will quickly become evident, the process of liquefying real estate and transactions involving public real estate companies requires a melding of the legal principles, deal structures, cultures and financial models of traditional real estate, public company M&A and private equity. None of this, of course, happens in a vacuum, and transactions often require expertise in tax, corporate and real estate law, not to mention securities laws and global capital markets. Each of our distinguished authors touches on these disciplines.

We hope this compilation of insight from our remarkable multinational authors produces clarity and transparency in this exciting world of liquid real estate and helps to further fuel the growth of the sector.

Adam Emmerich and Robin Panovka
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Chapter 9

MEXICO

Carlos Ibarra, Alejandra Gutiérrez and Patrick Stockdale[1]

I OVERVIEW OF THE MARKET

During 2021 and 2022, the volume of real estate M&A and private equity (PE) investment transactions increased significantly. However, the prospect of growth for the remainder of 2023 remains uncertain, as the government is focused on austerity and investing in other areas, such as energy (mainly crude oil), social programmes and infrastructure, mainly in south-east Mexico, with projects of potential economic significance (e.g., Tulum International Airport, the Mayan Train and the Interoceanic Corridor of the Isthmus of Tehuantepec). Despite limited support from the Mexican government, the forecast for the second half of 2023 in the corporate and financial sectors seems promising.

A series of circumstances have been paramount in determining the ongoing situation of M&A and PE investment in the Mexican real estate and financial markets. First and foremost, in May 2023, the World Health Organization (WHO) formally ended the global emergency status for covid-19, more than three years after it struck. This has already had a positive impact on M&A and PE investment transactions and going forward, as the Mexican and financial markets worldwide have now started to anticipate potential catastrophic events (mainly derived from covid-19), drastic changes in governmental policy, public spending, their impact on diverse financial market sectors and vulnerabilities.

In 2022, the Mexican GDP grew by 3.1 per cent, as opposed to 4.7 per cent in 2021[2] and the 8.0 per cent fall in 2020 due to the covid-19 pandemic, a sign that the Mexican economy is heading in the right direction. Positive local and foreign investor activity, growing real estate M&A and PE markets, the end of the covid-19 pandemic and the upcoming end of term of Mexican President Andrés Manuel López Obrador's mandate in 2024 are a few key factors that have positively contributed to grow the real estate M&A and PE sectors.

Furthermore, it is important to consider that the ongoing conflict between Russia and Ukraine has continued to cause significant geopolitical and macroeconomic shocks, notably by triggering a sharp rise in commodity prices, which has largely favoured markets and economic activity in the Latin American region, although these benefits may ultimately be offset by some economic and political risks, such as rising inflation, continued supply chain disruptions and a newly elected government in Mexico in 2024.

1 Carlos Ibarra and Alejandra Gutiérrez are partners and Patrick Stockdale is an associate at Ibarra del Paso Gallego.

2 The World Bank in Mexico, consulted on 15 May 2023, www.worldbank.org/en/country/mexico/overview.

II RECENT MARKET ACTIVITY

i M&A transactions

During 2022, 151 new M&A transactions were announced in Mexico, with a total announced value of transactions of US$14.7 billion.[3] By April 2023, nine transactions had been announced in Mexico, a decrease compared against the same period of the previous year.[4] However, the end of the covid-19 pandemic is expected to positively affect this sector going forward, with market lockups ending and negative growth forecasts upshifting within positive parameters. On the upside, foreign transaction data indicates positive growth, showing that, comparing the accumulated value for the January–April period in 2021, 2022 and 2023, the volume of transactions has increased.[5] As per the April 2023 monthly report from Transactional Track Record, during the first quarter of 2023, 99 M&A transactions took place, closing for US$7.718 million. These figures represent a 29 per cent decrease in the number of transactions, with a 33 per cent increase in capital mobilised, compared to the same period in 2022.[6]

The year 2023 promises vast areas of opportunity and growth for companies that are wishing to invest in Mexico, as the second-largest M&A market in Latin America.[7]

ii Private equity transactions

More than US$61.6 billion has been committed to PE transactions over the past 20 years, reflecting a compound annual growth rate of 12.7 per cent.[8] Real estate investment represents a relatively secure way to invest money, providing the investor with a regular income through the payment of dividends. During a time of crisis, it is only logical that investors feel much safer knowing that their money is being managed in a safe environment in comparison with other investment sectors.

III REAL ESTATE COMPANIES AND FIRMS

i Publicly traded REITs and REOCs – structure and role in the market

FIBRAs (equivalent to a REIT in Mexico) allow any entity or person to invest in a portion of real estate, focusing on investments and rights to derive income from the lease of the FIBRA's properties. A typical structure consists of the contribution of real estate assets into a trust, which will retain title to the properties while being managed by a professional property manager. The trust will issue investment-type securities (usually real estate trust stock certificates: CBIs), usually traded on the Mexican Stock Exchange (BMV), the Institutional Stock Exchange (BIVA), or on international capital markets. The resources obtained from the

3 Seal & Associates, M&A Annual 2022, consulted on 15 May 2023, http://mnamexico.com/ma/ma-anual-2022/.

4 Seal & Associates, M&A Abril 2023, consulted on 15 May 2023, http://mnamexico.com/ma/ma-abril-04-2023/.

5 id.

6 Transactional Track Record, Monthly Report of the Mexican transactional market – April 2023, consulted on 15 May 2023, https://blog.ttrecord.com/informe-mensual-sobre-el-mercado-transaccional-mexicano-abril-2023/.

7 FTI Consulting, Latin American M&A Activity, consulted on 15 May 2023, www.fticonsulting.com/insights/articles/latin-american-ma-activity.

8 AMEXCAP, consulted on 15 May 2023, https://amexcap.com/invest-in-mexico/.

offering will go into the trust. The properties are leased, thereby allowing investors to obtain two potential sources of income: periodical payments arising from the rents; and variable income arising from the appreciation of the properties (i.e., trust corpus).

FIBRAs have various tax incentives; therefore, in addition to compliance with listing requirements and obligations under the Securities Market Law (LMV), FIBRAs are subject to the conditions provided under the Income Tax Law (LISR) regarding trust corpus assets, the purpose of the trust, the distribution of profits and additional reporting obligations, among others.[9]

FIBRAs have performed well since their creation in 2011, showing important profits in 2022 and so far in 2023. Between January and March of 2023, FIBRAs accumulated a return of 9.1 per cent to 261.05 units, despite increases in the reference interest rate, which reached record levels of 11.5 per cent in Mexico, but nevertheless benefited from the demand generated by nearshoring. Their performance during 2023 will depend greatly on various factors (e.g., periodicity of distributions, liquidity, healthy leverage, the level of income or profitability of each property, having a high dividend yield, among others).[10] However, during the first quarter of 2023, industrial FIBRAs accumulated the highest return in the stock market, with Fibra Hotel leading the stock market gains, with a return of 30.71 per cent.[11] The FIBRAs with the highest annual increase or return on real estate trust certificates,[12] respectively, are: FIBRA Terrafina, (22.7 per cent), FIBRA Prologis (18.4 per cent) and FIBRA Uno (12.1 per cent).[13]

By the end of 2022, there were around 16 Mexican FIBRAs[14] specialising in different types of properties, from retail/commercial and industrial, office space, hospitality, energy and infrastructure, mixed-used developments and logistics to learning institutions and mortgages. Most FIBRAs are currently listed on the BMV. However, the relatively new BIVA (launched in 2017) currently has the following five listed FIBRAs:

a FIBRA HD, with 40 industrial, retail and office properties;[15]

b FIBRA Macquarie México, with 238 industrial and 17 retail properties;[16]

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9 LISR, Article 187.

10 D Carolina Soto Cota, *El Economista*, '2022 fue un buen año para las FIBRAs Inmobiliarias, y ¿para el 2023?' 30 December 2022, consulted on 15 May 2023, available at www.eleconomista.com.mx/opinion/2022-fue-un-buen-ano-para-las-FIBRAs-Inmobiliarias-y-para-el-2023-20221230-0055.html.

11 Judith Santiago, *El Economista*, 'Nearshoring da músculo a Fibras; tienen retorno de 9% en Bolsa en 2023', 4 April 2023, consulted on 17 May 2023, available at www.eleconomista.com.mx/mercados/Nearshoring-da-musculo-a-Fibras-tienen-retorno-de-9-en-Bolsa-en-2023-20230404-0122.html.

12 Certificados Bursátiles Fiduciarios Inmobiliarios.

13 Verónica González, *Real Estate Market & Lifestyle*, 15 February 2023, consulted on 17 May 2023, 'Índice de Fibras suma un rendimiento de 13% en 2023', available at https://realestatemarket.com.mx/noticias/mercado-inmobiliario/40571-indice-de-fibras-suma-un-rendimiento-de13-en-2023.

14 Redacción El Economista, *El Economista*, 'Fibras en México, aún en etapa temprana de alcanzar su potencial; en el mundo existen más de 1,000 fideicomisos inmobiliarios', 20 January 2023, consulted on 17 May 2023, www.eleconomista.com.mx/econohabitat/Fibras-en-Mexico-aun-en-etapa-temprana-de-alcanzar-su-potencial-en-el-mundo-existen-mas-de-1000-fideicomisos-inmobiliarios-20230120-0059.html.

15 Fibra HD, consulted on 17 May 2023, www.fibrahd.com.mx.

16 Fibra Macquarie Mexico, consulted on 17 May 2023, www.fibramacquarie.com/en.html.

c FIBRA Prologis with 104 manufacturing and 119 consumption properties;[17]
d FIBRATC, which replicates the S&P/BMV/FIBRAS Index, reflecting the performance and operating dynamics of assets classified as FIBRAs;[18] and
e FIBRA Upsite with a portfolio in the Northeast, North, the Bajío region and Central Mexico.[19]

To date, there has been considerable growth in the number of new properties in the real estate industrial sector, greatly attributed to nearshoring, among other reasons. In this regard, 2023 has seen historic advancements in the industrial sector, mostly concentrated in Mexico City and Monterrey, in the state of Nuevo León, the latter being host to the new Gigafactory plant for Tesla. The new Gigafactory for Tesla will be the company's sixth manufacturing plant and third outside the United States; the other two are in Berlin and Shanghai.[20] While commercial and industrial FIBRAs have a positive forecast for 2023, there may be additional challenges this year, since the increase in the reference interest rate of Banco de México, the central bank of Mexico, may affect the prices of securities certificates.

ii Real estate PE firms – footprint and structure

Apart from provisions set forth under the Foreign Investment Law (LIE) regulating, limiting or prohibiting foreign investment in specific areas or matters in Mexico (e.g., the Restricted Zone and 'T' shares for holders of rural land), the main financial regulators for PE funds in Mexico include the following:
a the Mexican Central Bank;
b the Ministry of Finance;
c the National Banking and Securities Commission;
d the National Commission for the Protection and Defense of the Users of Financial Services;
e the Retirement Fund System Commission; and
f the Institute for the Protection of Bank Savings.

In general terms, provisions under the LMV regulate securities offered to the public and also provide specific safe harbours for private offerings of unlisted securities.[21] The specific regulation will therefore be linked to the selected vehicle.

There are several vehicles used for PE transactions, which depend on a variety of factors such as location, subject matter and (mainly) tax concerns. Mexican stock corporations (SAs), which are regulated under the General Law of Commercial Entities (LGSM), and investment promotion companies (SAPIs), which are regulated under the LMV, are commonly used for targeting companies due to their governance and because they are capital-oriented, providing fewer restrictions than partner-oriented entities such as limited liability companies (SRLs).

17 Fibra Prologis, consulted on 17 May 2023, www.fibraprologis.com/en-US.
18 FIBRATC, consulted on 17 May 2023, www.bbva.mx/empresas/productos/inversiones/etfs/etf-fibratc.html.
19 Fibra Upsite, consulted on 17 May 2023, https://fibra-upsite.com/.
20 Mateo Crossa & Nina Ebner, nacla Reporting on the Americas since 1967, 'The Drive Behind Tesla's New Manufacturing Plant in Mexico´, 4 April 2023, consulted on 17 May 2023, available at https://nacla.org/drive-behind-teslas-new-manufacturing-plant-mexico.
21 Further information may be found in Article 8 (Private Offerings) of the LMV.

Trusts are also commonly used in such transactions given their versatility, including the possibility to create different types of beneficiary rights that serve to accommodate waterfall payment structures. Private equity investment trusts (FICAP) are used to improve PE investment in Mexico by allowing investors to participate in non-listed Mexican entities. Furthermore, PE backed buyers typically use special purpose vehicles, which may include limited partnerships, fiduciary certificates of capital development (CKDs), trusts, or even private organisations, to carry out their acquisitions. Rarely does a buyer with a PE backing directly engage in the acquisition documentation. The LISR includes provisions regarding investment thresholds, the purpose of the investment, participation on the board, allocation of remaining funds and distribution of profits and time frames for holding equity.[22]

IV TRANSACTIONS

i Legal frameworks and deal structures

As a general legal statement and by constitutional mandate, the original ownership of land within the Mexican territory belongs to the nation; private ownership stems therefrom.[23] Therefore, there are certain types of properties whose ownership is reserved for the nation, there are other types of properties that may be acquired by private parties freely and without restrictions and, finally, there are types of properties that must be acquired under certain restrictions or with additional legal procedures.

Regarding real estate property, under federal statutory law, there are agrarian community ownership regimes (*ejidos* and *comunidades*) that basically provide the ownership of a land to an agrarian community under a special regime that is different from private property. Under these regimes, the sale of real estate property and the granting of most rights of use are prohibited unless: *ejido* land is converted into private property under certain circumstances and requirements; or private parties enter into an agreement to use *ejido* land subject to certain requirements and conditions[24] regulated by the Agrarian Law.

Since *ejidos* and *comunidades* cover nearly half of the Mexican territory,[25] compliance with federal statutory law governing them is of extreme importance.

Despite this important exception, private real estate property is governed by the Civil Code of each local jurisdiction, but depending on the business plan and the structure decided for the acquisition of the real estate, it may involve additional laws and regulations (federal and local), such as the LIE and the LGSM.

The typical deal structures used by real estate private investors in Mexico to purchase property are as follows:

a direct acquisition, through contractual arrangements that do not constitute a legal entity or a trust (purchase and sale agreements); and

b indirect acquisition, through either (1) corporate structures and legal entities (stock purchase contracts, merger and spin-off restructures) or (2) a real estate private trust.

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22 LISR, Article 192.

23 Pursuant to Article 27 of the Political Constitution of the United Mexican States.

24 Pursuant to Sections IX and X of Articles 23, and Articles 56 and 81 of the Agrarian Law.

25 Registro Agrario Nacional, 'Situación Agraria Nacional al 31 de diciembre de 2022', consulted on 17 May 2023, available at www.ran.gob.mx/ran/index.php/sistemas-de-consulta/estadistica-agraria/informacion-de-interes-nacional.

Direct acquisition through contractual arrangements

Contractual arrangements that do not create a trust or a legal entity are the most common way of acquiring a real property for residential purposes, although not so much for institutional investments. Purchase and sale agreements are governed by the Civil Code where the real estate is located. This type of agreement is binding upon execution in most of the Mexican states, including Mexico City, except for the state of Quintana Roo, where recording with the Public Registry of Property (PRP) is necessary for perfecting conveyance and vesting rights.[26]

Purchase and sale agreements can be executed under different modalities, including:

a title retention or reserve of ownership agreement, when the title of the real property is not transferred until the purchase price is fully paid;

b purchase and sale in instalments agreement, when the purchase price shall be paid in tranches or on a date after the buyer has taken title and possession of the property;

c *ad corpus*, for acquiring the property as a whole; and

d *ad mesuram*, when the purchase price is determined by the surface of the property (price per square metre).

Indirect acquisition through corporate structures and legal entities (stock purchase contracts, merger and spin-off restructures)

The most common corporate structures used in Mexico are SAs, SAPIs, and SRLs, where private investors hold the proportional undivided interest of any real property owned by the company as an indirect right as shareholders or partners.

Indirect acquisition through a real estate private trust

Private real estate trusts are contracts under which the settlors convey ownership of real estate properties to a trustee,[27] with certain purposes for that real property (i.e., its development and sale or lease) for the benefit of the beneficiaries named by the settlor or for the settlor itself. A trust is the most common way of acquiring institutional investments and can be constructed as a pass-through entity for tax purposes or as a tax entity different from the settlors or beneficiaries, and may include a technical committee, which could work like a board of directors of a company. Other benefits of the trust include:

a to the extent that its purpose does not contravene any legal provision, the real estate trust can be adapted to any requirement from the private investors' needs; and

b the real estate title is held by a duly authorised financial institution, thus protecting it against creditors of the settlors or beneficiaries (i.e., there is insulation from bankruptcy).

ii Acquisition agreement terms

Acquiring real property in any location requires an extensive amount of research, planning and preparation, and Mexico is no exception. Hence, certain important aspects must be considered when executing a purchase and sale agreement, a stock purchase agreement or a trust agreement.

26 Pursuant to Article 2549 of the Civil Code of Quintana Roo.

27 A Mexican financial institution authorised to offer trustee services.

Direct acquisition through contractual arrangements

The following relevant matters should be reviewed through the proper due diligence process in a purchase and sale of real estate transaction:

a property title (formalised in a public deed issued by a notary public), duly recorded with the corresponding PRP;
b certificate of non-encumbrances or liens and real folio or chain of title for at least the past 20 years, issued by the PRP;
c all contracts, deeds and covenants affecting the real property; and
d land use and zoning certificates and licences.

It is important to carry out a proper due diligence process before the acquisition of real property or interests thereon, since the National Law of Extinction of Domain allows the government to forfeit or impound any asset in or with which illegal acts have been committed.

In addition, the corresponding agreement should, among others, include representations and provisions in connection with anti-money laundering regulations;

a the covenants and provisions applicable to the property (i.e., condominium codes, environmental and the like);
b the costs and taxes paid by the buyer; and
c written evidence of the co-owners' waiver to their right of first refusal, if applicable.

Indirect acquisition through corporate structures and legal entities (stock purchase contracts, merger and spin-off restructures)

The basic matters to review in a stock acquisition are:

a articles of incorporation and the mercantile folio of the target company issued by the Public Registry of Commerce;
b current by-laws;
c powers of attorney;
d corporate books and financial statements;
e compliance with tax, labour and social security obligations;
f absence of liens over the company's assets; and
g warranties given by the seller to the buyer, such as no reserves of ownership, limitations or claims affecting the company's assets, including real property.

Mergers and spin-offs should comply with procedures set forth under the by-laws and the LGSM and provisions regarding anti-money laundering regulation shall also be observed (e.g., representations and indemnity provisions regarding the legality of the origin of economic resources).

Indirect acquisition through a real estate private trust

Typical details that a private real estate trust must provide are as follows:

a the parties involved;[28]
b corporate governance provisions that the agreement may foresee;

28 The selection of the financial institution to be appointed as trustee is crucial, given that only a few of them have the sophistication, agility and responsiveness for transactional matters.

c the moment of acquisition of the real property (before or after the execution of the agreement) and the designated beneficiary party;

d whether there will be financing to acquire the real estate in order to comply with the guaranty trust provisions under the General Law of Negotiable Instruments and Credit Transactions;

e the type of trust that will be required; and

f the location of the real property to determine if it should be converted into a restricted zone trust as per the LIE provisions. The Mexican Constitution states that foreign nationals cannot directly own real estate located within 100 kilometres from the borders or within 50 kilometres from the beaches (the Restricted Zone).[29] Thus, in the by-laws of a Mexican company or trust agreement, foreign investors must subject themselves the *Calvo* clause[30] for holding title in such a company or trust,[31] and to obtain a permit from the Ministry of Foreign Affairs, as a general rule.

iii Hostile transactions

Hostile takeovers are allowed under the LMV. However, Mexico has a relatively small number of public companies and high shareholder concentration, which tends to discourage hostile takeovers. There have only been two hostile takeover attempts in the country's history.

It is important to consider that the Mexican Supreme Court declared in 2015 that any clauses in a company's by-laws intended to prevent or restrict hostile takeovers must comply with Article 48 of the LMV to be lawful. In publicly traded companies in Mexico, this is essentially always the case.

iv Financing considerations

The attraction of real estate investment resides in the various ways such operations can be financed. Traditional ways to finance real estate projects are as follows.

Bank loans

These provide the necessary capital to grow the real estate operation in exchange for interest and often other fees that add to the overall cost of the loan.

Investments funds or crowdfunding

Crowdfunding or investment funds allow small and medium-sized investors to participate in all kinds of projects, increasing the range of possible investors for a particular operation. Furthermore, this type of funding allows for continuous entry of capital and has proved to be highly transparent in its operational procedures.

29 Pursuant to Article 27 of the Political Constitution of the United Mexican States.

30 Comprising (1) acknowledging and being subject to Mexican laws and Mexican courts' jurisdiction; (2) refraining from invoking the protection of their foreign governments with regard to the interests that they acquire in Mexico; and (3) being forewarned that a breach under the foregoing Covenants 1 and 2 will result in the forfeiture of the interests that they had acquired in favour of the Mexican nation.

31 If a real estate trust or company asset is located within the Restricted Zone, the trustee or company must file and obtain the corresponding permit issued by the Ministry of Foreign Affairs for converting into a restricted zone trust (foreigners are not allowed under any circumstances to hold a property title within the Restricted Zone).

FIBRAs

As previously discussed, this is a relatively new way of investing capital in real estate that has proved to be a safe and profitable alternative for investors to receive a stable income with relatively little effort, since the trustee or manager of the FIBRA and real estate, usually a banking institution or an expert in the subject, registers it in the stock market and issues CBIs to attract investment capital from investors, and the investors benefit from the dividends. In brief, the investors enjoy the benefits of this mechanism without having to deal with the management of the property.

Fiduciary certificates of capital development

Fiduciary certificates of capital development (CKDs) are used to finance a range of development and construction projects with potential profitability. Few investors can invest in CKDs owing to the high amount of capital that is needed to participate in such mechanism. As a result, ordinarily, pension fund institutions (AFOREs) invest in CKDs.

CKDs operate as follows:

a the entity that needs funding has present or future assets, resources or rights, which are contributed into a trust. The trust (usually managed by a bank or an expert real estate manager) issues stock certificates through the stock market to attract investment capital from investors. In order to achieve the aforementioned, CKDs must be issued through public tenders, and registered with the National Registry of Securities (RNV), while possessing the authorisation for the registration and offering, by the National Banking and Securities Commission (CNBV). The offering must be carried out in an authorised stock exchange, as the BMV or BIVA;

b the development is completed with the funds; and

c the trustee or manager periodically sells the property to pay the investors.

Fiduciary investment project securitisation certificate

Fiduciary investment project securitisation certificates (CERPIs) and their issuance proceeds are destined to finance projects, as well as to invest in shares, partnership interests or the financing of corporations, either directly or indirectly through one or more investment vehicles.[32]

CERPIs must also be registered with the RNV, authorised by the CNBV, listed in the BMV or BIVA and issued through restricted public tenders.

v Tax considerations

In real estate property transactions, the main tax consideration is deductions (diminishing the taxable gain in transactions). This applies for direct and indirect acquisitions, either through trusts or mergers, if the latter are considered as taxable events (which is the main legal implication to avoid and will be explained in the next section).

The deductions stated in the LISR are as follows:

a the proven acquisition cost (PAC), which is what the seller paid for acquiring the real property. The PAC can be determined in two different ways:
   - if the property title is dated before 2014, the PAC is proven by the property title; and

32 Pursuant to the General Provisions applicable to Issuers of Securities and other Participants in the Securities Market, more commonly known as the Sole Issuers Circular.

- if the property title is dated after 2014, the PAC is proven by the tax electronic invoice that was issued by the seller's grantor or by the notary public that drafted the property title;

b investments made in construction and improvements to the construction. These amounts must also be depicted and updated in the same terms as the part of the PAC reflecting the construction;

c expenses pertaining to notary public and appraisers' fees as well as taxes. These relate to the issuance of property titles and appraisals as well as local taxes related to the transmission of real property; and

d commissions paid by the seller in connection with the selling or acquisition of the property (i.e., fees paid to a real estate broker).

Indirect acquisition through corporate structures and legal entities (stock purchase contracts, merger and spin-off restructures)

The key issue in indirect purchases through corporations or legal entities is to avoid a taxable event in the merger of two corporations to acquire realty owned by the acquired entity. To do so, the acquirer must ensure that the merger is not considered as a sale for tax purposes.

Under the Tax Code, an acquisition through a merger will not be considered as a sale when the following requirements are met:

a the notice of merger stated in the Tax Code's Regulations must be filed with the tax authorities;

b after the merger, the outstanding corporation or legal entity must continue to do the same business activities as the corporation that was acquired for at least one year; and

c the outstanding entity must file all the corresponding tax returns and notices that the acquired corporation or legal entity was obligated to file.[33]

Indirect acquisition through a real estate private trust

Regarding indirect acquisitions through trusts, there are two main issues to consider:

a when the conveyance of property through the trust is considered a taxable event for federal and local taxes; and

b whether the trust is a pass-through entity for tax purposes.

In the matter of conveyance of property through the trust, as a general rule, this will be considered as a taxable event for income tax purposes if the settlor designates a different person as beneficiary or loses the right to reacquire the real property (i.e., with no reversionary rights).[34] Therefore, careful consideration must be taken when drafting the trust agreement to avoid an early triggering of the income tax.

This rule is only applicable for income tax purposes. Local real estate acquisition taxes have their own set of rules regarding the moment when a transfer of property through a trust is a taxable event. It is important to bear in mind that these taxes do not tax the income or gain of taxpayers but rather the conveyance of real estate property itself. Therefore,

33 Pursuant to Article 14-B of the Federation's Fiscal Code (Tax Code).

34 Pursuant to Article 14 of the Federation's Fiscal Code (Tax Code).

additional analysis must be made on a case-by-case basis to determine if and when such taxes are triggered, as each scenario varies depending on the state or municipality where the land is located.

Finally, it is important to distinguish if a trust is considered a pass-through entity or not to determine if such trust will be considered as a taxpayer for income tax purposes. Trusts will only be considered as pass-through entities when they receive passive income rather than income that derives from business activities.[35]

vi Cross-border complications and solutions

Mexico does not tax foreign nationals in particular and does not have a tax similar to the United States' Foreign Investment in Real Property Tax. Constitutional restrictions and structure vehicles for foreign investments are discussed above in Sections III.ii and IV.ii. Mexico has signed treaties to avoid double taxation with almost every country in the world, including Australia, Brazil, Canada, China, Germany, Hong Kong, Israel, Japan, the Netherlands, Russia, Spain, the United Kingdom and the United States.

V CORPORATE REAL ESTATE

Covid-19 has changed the way corporate real estate operations are conducted. For an entrepreneur or a seasoned company owner, the importance of owning a workspace or office has lessened due to the home office trend. During 2020 and 2021, businesses developed new working practices to operate with some sort of normality while ensuring safe distancing among their employees. As such, the concept of home office and hybrid working models has since been implemented, and many companies have opted to eliminate or reduce their workspace.

As previously mentioned, the FIBRA model remains a popular and relatively stable option for investments owing to the security and transparency that this type of model provides to any individual. Nevertheless, FIBRAs' corporate real estate operations keep facing challenges due to scenarios caused by the pandemic (e.g., decrease, renegotiation and termination of corporate real estate lease agreements, decrease of investment for development of office space, among others) which despite being formally over, are still taking a toll on corporate real estate day-to-day operations.

Operating company and property company (opco and propco) deals are still new to the Mexican corporate real estate market and are not normally executed as in the United States. Such investment structure is normally used in the commercial, office and hotel sectors, which are still majorly controlled by the FIBRA model.

VI OUTLOOK

Despite being formally over, the covid-19 pandemic deeply impacted most sectors of the Mexican and world economy and will continue to impact consumers' habits for the years to come, with some analysts predicting that despite current economic gloom, spending will increase, with a few reservations where consumers accumulated sizeable reserves, and by the second half of 2023, it is expected that household cash flow will increase. Although consumers will continue to show prudence, having money and savings in the bank will encourage them

35 Pursuant to Article 13 of the LISR.

to make larger purchases.[36] This goes to show that society is being forced to adapt to the new normal and rethink products, services and supply chain structures. Therefore, the main trends and developments in the industry will be market-driven practices aiming to reconcile with changing demands and consumer habits to succeed in this new normal.

To some, 2023 will be no different from previous years, as the lingering effects of covid-19, the ongoing war between Russia and Ukraine, inflation and a looming risk of recession are still rather fresh. These factors continue to exert pressure on the real estate sector's activity, especially in the production and marketing of, and access to, housing.

According to the new president of the National Board of Directors of the Mexican Association of Real Estate Professionals (AMPI), 2023 will experience a slight rebound of around 1 per cent for the real estate industry, in all its different segments. This, of course, remains to be seen.[37]

Major real estate companies and co-working providers are now looking to re-adapt or even redesign their spaces with health and safety measures, a reduced number of meetings and controlled access to their facilities. Developers are also rethinking the allocation of spaces and open areas.

Sustainability trends are also noteworthy. By 2022, Mexico ranked seventh in the list of the top 10 countries and regions for leadership in energy and environmental design.[38] Responsible investment is also gaining strength through more objective environmental, social and governance (ESG) investments. As a global trend, most of the largest corporations follow the Global Reporting Initiative standards. Even *afores* (pension fund institutions) that have stringent investment restrictions are now encouraged to take ESG data and policies into consideration.[39] Furthermore, in 2015, Nacional Financiera SNC, the development banking institution, issued the first Mexican green bond – the first in Latin America to obtain climate bond certification – for several sustainable energy projects. This was followed by Mexico City's New International Airport (NAICM) Trust's issuance of green bonds to build a new airport,[40] although the project was subsequently cancelled.

By the end of 2022, there was less demand for green bonds in Mexico than in previous years as businesses decided to issue sustainable bonds with both environmental and social

36 Forrester Contributor, *Forbes*, 'How will consumer behavior change in 2023?', 3 November 2022, consulted on 19 May 2023, available at www.forbes.com/sites/forrester/2022/11/03/how-will-consumer-behavior-change-in-2023/?sh=bba6074143fe.

37 Samanta Escobar, *El Economista*, 'Cuáles son las amenazas para el sector inmobiliario en este 2023', 16 January 2023, consulted on 19 May 2023, available at www.eleconomista.com.mx/econohabitat/Cuales-son-las-amenazas-para-el-sector-inmobiliario-en-este-2023-20230116-0052.html.

38 Deisy Verdinez, *USGBC*, 'The Top 10 Countries for LEED demonstrate that green building is a truly global movement', 7 February 2023, consulted on 19 May 2023, available at www.usgbc.org/articles/top-10-countries-leed-demonstrate-green-building-truly-global-movement.

39 Diario Oficial de la Federación, Disposiciones de Carácter General en Materia Financiera de Los Sistemas de Ahorro para el Retiro, 18 September 2019.

40 Mexico City's New International Airport.

benefits. Additionally, 80,983 million Mexican pesos has been raised through the BMV through the joint issuance of 19 theme bonds, including two issuances of green debt, six each of social and sustainability bonds, three of sustainable bonds, and one of a blue bond.[41]

To support and grow the green bond market, the BMV and BIVA permitted green bond issuance and collaborated with the CBI and significant institutional investors. For BIVA, 35 per cent of all long-term corporate debt placements in 2023 will be accounted for by regulations and ESG bonds. To collect information on green, social, sustainable, and sustainability-related bond issues in Mexico, BIVA introduced the BIVASG platform, the first of its type in the Mexican stock market, offering details on laws, ESG standards, sustainability reports, and other matters. This approach should be commended as it will support and guide more businesses towards the adoption of ESG standards.[42]

41 Judith Santiago, *El Economista*, 'Bonos Verdes cerrarán con ligero crecimiento el 2022:CBI', 23 December 2022, consulted on 19 May 2023, available at www.eleconomista.com.mx/mercados/Bonos-verdes-cerraran-con-ligero-crecimiento-el-2022-CBI-20221222-0086.html.

42 Judith Santiago, *El Economista*, 'Bonos ASG serán el 35% de todas las emisiones de deuda en Biva en 2023', 15 February 2023, consulted on 19 May 2023, available at www.eleconomista.com.mx/mercados/Bonos-ASG-seran-el-35-de-todas-la-emisiones-de-deuda-en-Biva-en-2023-20230214-0095.html.