



# Global Connection

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## SNELL & WILMER OPENS OFFICE IN MEXICO

On October 21, 2008, Snell & Wilmer L.L.P. announced it has opened an office in Los Cabos, Mexico. The office marks the Firm's seventh location, and its first outside of the United States. With this announcement, Snell & Wilmer becomes the first United States-based law firm with a presence in Baja California Sur.

The office is anchored by attorneys Richard Krumbein and Carlos Sugich, with the support of Curt Reimann and Jon Frank from Snell & Wilmer's Tucson and Phoenix, Arizona offices respectively. The group will focus on providing a wide range of transactional and regulatory work to national and international businesses with interests throughout Baja and northern Mexico. As the office expands, it will draw upon the resources of the Firm's over 400 attorneys practicing across the western United States.

Snell & Wilmer's vision for office expansion is to build upon its existing presence throughout the western United States, and to carefully evaluate opportunities that arise in other regions. Mexico continues to emerge as a key player within the global economy. An increasing number of United States companies are establishing operations in this growing marketplace. At the same time, a significant number of enterprises within Mexico are expanding their international business reach. The climate and beaches across Baja and northern Mexico have turned those regions into an increasingly popular destination and focus of international economic development activity, especially from United States-based companies and investors. Active real estate, resort development, and infrastructure enhancement activities make the region a promising market for Snell & Wilmer.

The address of Snell & Wilmer's Mexico office is:

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## NAFTA'S INDIRECT EFFECT ON REAL ESTATE INVESTMENT IN MEXICO

by Carlos A. Sugich and Brynn Hallman



This election cycle has seen much discussion about the North American Free Trade Agreement (NAFTA)

and its impact on labor. Less discussed, although no less important, is the effect of NAFTA on real estate investment. Because NAFTA can open great roads of opportunity in Mexico for investors who know the lay of the land, this article will serve as a roadmap to chart that course.

### Background

NAFTA is a regional free trade agreement authorized by the World Trade Organization. It is divided into Chapters (1-22 plus annexes), each dealing with different areas, such as trade, investment, the environment, and dispute settlement.

Although there are no provisions in NAFTA that deal directly with real estate, NAFTA has had a significant indirect effect on real estate investment in Mexico. NAFTA's policies of trade liberalization, for example, have provided advantages for businesses, consumers and investors of the three signatory states. Furthermore, perhaps the single most important effect on real estate investment is the added confidence and security of investments,

coupled with the availability of neutral forums for the settlement of disputes. Today, buying or developing real property in a NAFTA signatory state is no longer a completely alien transaction.

### Real Estate Service Providers

Among other things, NAFTA affects real estate investment in Mexico through its professional services provisions. Attorneys, brokers, and title companies are all beneficiaries of NAFTA's liberalizing provisions.

- **Real Estate Brokers**

Chapter XII of NAFTA affords National Treatment and Most Favored-Nation Treatment to professionals and service providers of the other states. Real estate brokerage services fall under NAFTA's definition of professional services. NAFTA has eliminated citizenship and permanent residency requirements for the licensing or certification of professional services in each of the signatory states. Through its Federal Trade Commission, NAFTA also provides mutual reciprocal standards for recognizing real estate professionals in the three states.

- **Attorneys**

NAFTA implemented the figure of the Foreign Legal Consultant. Pursuant to NAFTA, each signatory state is required to implement a mechanism to ensure that a national of another signatory state is permitted to practice the law of any country in which the national is authorized to practice law. To this end, several state bar associations in the U.S. have created a foreign legal consultant certification process. Additionally, many law firms have opened offices in each of the three countries solely for the purpose of advising on the law of their national state.

- **Title Insurance Companies**

U.S. title insurance companies now offer title policies for real property located in Mexico, relying on abstracts prepared by local attorneys who

perform a title search and prepare an opinion letter. Escrow services are not used in Mexico; however, they are commonly used in the U.S. and Canada for transactions regarding real property in Mexico.

### NAFTA Chapter XI (Arbitration)

Chapter XI is the Investment Chapter of NAFTA. Section A of Chapter XI establishes a framework for the protection of investors within NAFTA, including rules mandating National Treatment, Most Favored Nation treatment, and general compliance with international law, which requires nations to deal fairly and equitably with foreign investors. Section “B” supplies foreign investors with access to a binding dispute resolution system through international arbitration to enforce the investment protection measures set forth in Section “A”. Arbitration panels are usually composed of neutral arbitrators appointed by the parties and the procedure is governed by UNICTRAL or ICSID rules of arbitration.

Significant for the purposes of investing in real estate in Mexico, Chapter XI includes a guarantee that states will neither expropriate nor regulate to a degree tantamount to expropriation the private property of foreign investors, except (a) for a public purpose, (b) on a nondiscriminatory basis, (c) in accordance with due process of law, and (d) with payment of fair compensation. This last element, together with the possibility of enforcing its violation through an investor-state dispute mechanism, has had a profound effect on real estate investment in Mexico.

In short, this innovative dispute settlement mechanism in Chapter XI gives Canadian and U.S. investors, whose rights to fair treatment in accordance to international standards have been violated, the right to, after exhausting all local remedies, enforce its NAFTA rights against the Mexican government by means of international

arbitration. Thus, investors that once feared the security of their real estate holdings in Mexico now find comfort in the higher degree of investor protection provided by NAFTA Chapter XI.

### Alternative Financing Vehicles

With the inception of NAFTA, the three signatory states went through several amendments to their domestic laws to implement the provisions of the treaty. For many reasons, but mostly to be competitive with its trading partners, Mexico has and still is reforming its laws to better facilitate NAFTA.

One of the most important areas for developing real estate in Mexico is the area of secured commercial lending. In the past, the legal devices used in secured lending in Mexico were not well-suited to sophisticated financing. Since NAFTA, however, Mexico has reformed its domestic laws and created other financing vehicles to attract credit markets. As a result, interest rates are not as daunting as they once were and financing is available for a variety of real estate ventures.

NAFTA has already facilitated real estate investment in Mexico and will likely to continue in that path into the future, not only because of NAFTA, but also because of steps taken by Mexico in the spirit of NAFTA.

## COMPLIANCE WITH UNITED STATES EXPORT CONTROL LAWS WHEN TRADING WITH MEXICO

by Richard Katz and Brett W. Johnson



When a company exports and imports goods and services between Mexico and the United States, it is

sometimes assumed that the only U.S. regulatory concern is qualifying for duty-free treatment under the North America Free Trade Agreement (“NAFTA”). However, while the NAFTA free trade incentive may be an important factor for deciding to manufacture in Mexico, companies still need to abide by multiple United States export control laws and regulations, which apply to cross border trade with Mexico as they do with respect to any other foreign country. The failure to comply with these regulations may result in penalties which far outweigh any competitive advantage obtained by manufacturing in Mexico under the NAFTA.

U.S. export control laws and regulations are enforced by the Directorate of Defense Trade Controls (“DDTC”) in the Department of State, the Bureau of Industry and Security (“BIS”) in the Department of Commerce, and the Office of Foreign Assets Control (“OFAC”) in the Treasury Department. The Department of State’s export control regulations are called the International Traffic in Arms Regulations (“ITAR”); the Department of Commerce’s export control regulations are called the Export Administration Regulations (“EAR”); and the OFAC controls are generally referred to as economic sanctions regulations. Various trade agreements between

Mexico and the United States (such as the NAFTA) do not supersede these United States export regulations, which are driven by foreign policy considerations and insuring national security.

Many U. S. companies manufacturing in Mexican maquiladoras are defense contractors, that is, they are making products or components on the United States Munitions List (“USML”), which is part of the ITAR. Due to the sensitivity of the technology and related services involved, the U. S. government wants to insure that it has knowledge of all export transactions in this area. In order to legally manufacture items on the USML in Mexico, a U.S. company must be registered with the State Department under the ITAR and must properly license its overseas (Mexican) activities. This might involve specific individual licensing for the transfer of materials, components and/or technology, or the filing of a Manufacturing License Agreement (“MLA”) with the State Department covering all of its Mexican supply activities under a U.S. military program. Foreign nationals involved in the design or manufacture of ITAR-regulated hardware, technology or services must likewise be licensed under State Department regulations.

Many companies fail to realize the need for a license because components and services are being exported to Mexico only temporarily with the finished goods returning to the United States for eventual sale. However, the U.S. State Department is concerned about technology and defense know-how being sent abroad, not just the permanent export of defense hardware. Thus, even temporary exports for production in Mexican maquilas for return to the U.S. are strictly controlled. The penalties for failure to comply with ITAR regulated activity are severe and may even result in criminal prosecution.

Components and technology not covered on the US munitions list under the ITAR may still be subject to export controls under the Department of Commerce's Bureau of Industry and Security regulations (the EAR). The EAR covers both hardware and technology exports which are technologically sophisticated, "dual-use" (civilian and military) or subject to various international controls which have been adopted into the U.S. regulatory scheme. The issue for exporters of high tech components and technology to Mexico is to determine where their items are classified under the EAR and the level of control. The level of control for shipments may be minimal; there may be a general license available, a license exception may apply or no license may be required at all. However, in certain cases, it will be necessary to obtain a specific license from BIS to permit export to Mexico. If a specific license is required, it is critical that the exporter obtain the license prior to shipment. Like the ITAR, penalties for non-compliance under the EAR are severe.

In addition to assuring compliance under the ITAR and EAR, exporters to Mexico must pay attention to OFAC sanctions. While OFAC administers country-wide specific sanctions regimes (Cuba, Iran and other pariah states), it also enforces list-based sanctions directed against specific entities and individuals- drug dealers, terrorists and other parties barred from trading with U.S. persons. Thus, exporters must pay careful attention to the customer and/or end-user of their shipments. Exports to persons on the various OFAC sanction lists are prohibited and can result in penalties and/or revocation of export privileges.

In addition to the United States export control regimes discussed above, U.S. exporters must be mindful and train their salespeople in regard to the Foreign Corrupt Practices Act ("FCPA").

Many United States companies are engaged in developing Mexico's infrastructure or dealing with a Mexico nationalized company (i.e. Petróleos Mexicanos). The FCPA essentially prohibits the bribing of Mexican officials in an attempt to obtain or maintain a competitive advantage (i.e. licenses, government contracts, etc.) in Mexico. Companies engaged in activities involving Mexican government officials, even if the activities are through consultants or middlemen, should train their employees in regard to the FCPA provisions.

Due to the intertwined nature of the Mexican and United States economies and the free flow of goods and services across the border, it is important for companies to remember that United States' export controls must be followed. Proper recordkeeping according to the various regulations, export compliance initiation, and export control training are essential pillars to trade deals in Mexico. A company's failure to incorporate an effective export compliance program into global operations may result in significant penalties and the disruption of on-going operations domestically and abroad.

## CROSS-BORDER LENDING IN MEXICO

by Carlos A. Sugich and Brynn Hallman



With nearly 1.5 million Americans living in Mexico and billions of dollars in U.S.

investment, Mexico is an attractive credit market to U.S. lenders. Various U.S. lenders are funding loans to U.S. companies and individuals doing business in Mexico. Many of these loans are secured by real and personal property in both Mexico and the U.S. These Lenders include national and state banks, REITs,

mortgage bankers, equity funds, hedge funds and pension funds. The following is a brief summary of some of the key legal aspects of cross-border real estate lending in Mexico.

## Background

Cross-border lending in Mexico involves a loan or financing agreement originated in the U.S. regarding a project in Mexico secured by real or personal property in Mexico or both Mexico and the U.S. The transaction is governed by U.S. and Mexican law.

## Mexico Security Agreements

Two security devices are normally used by lenders to secure loans against real property in Mexico: (1) a mortgage or "*hipoteca*," and (2) a Guaranty Trust ("GT") or "*fideicomiso de garantia*."

(1) **Mortgage.** Just like in the U.S. a mortgage is an agreement pursuant to which the lender or mortgagee is granted a lien against real property of the mortgagor to secure a monetary obligation. A mortgage is binding between the parties upon its execution but is perfected against third parties by filing the same with the Public Registry of Property where the real estate is located. A Mortgage must be foreclosed by filing legal action in the competent courts where the real property is located.

(2) **Guaranty Trust.** The GT is the security instrument of choice in cross-border real estate lending mainly because if provided in the contract, the Lender may elect a non-judicial foreclosure or a trustee's sale if the Borrower defaults. Moreover, if, upon foreclosure, the collateral is less than the debt owed plus interest, the beneficiary of the trust can obtain a deficiency judgment subject to certain homestead exemptions. In a standard GT, the trustor/borrower transfers legal title to the property to the trustee as collateral to secure payment of an

obligation in favor of the beneficiary/lender. This means the collateral given in the trust becomes isolated from creditors' claims and the bankruptcy estate.

## Documenting Cross-border Loans

In documenting cross-border loans the lender must be aware of the following unique issues not usually encountered in domestic loans:

- **Bilingual Agreements:** Preferably, the loan documents (at least the Note and Loan Agreement) must be bilingual agreements with controlling language and concurrent choice of law and forum selection provisions. This arrangement allows the lender to obtain remedies in both countries.
- **Security Instruments:** Security Instruments for real or personal property are governed by the law where the collateral is located. Instruments such as guaranty agreements, however, may be governed by the choice of law provision in the contract depending on Guarantor's principal place of business or residency.
- **Perfection of Security Instruments:** Perfection refers to the protection a secured party's interest in the collateral against third parties or other creditors of the debtor. For real property, the law of the jurisdiction where the property is located governs. Liens on real property in Mexico are perfected by recording the security instrument with the Public Registry of Property in the state where the real property is located. Liens on personal property in Mexico, on the other hand, may be perfected by delivery of possession of the collateral and/or registration of the security agreement with the Public Registry of Commerce or a "special registry" depending on the nature of the collateral. Perfection of a security

agreement against a foreign borrower in the U.S. is governed by the “equivalence test” set forth in UCC § 9-307.

- **Priority:** Priority refers to the ranking of multiple claims against a transferred asset. Priority is normally accomplished by being the first to perfect a lien by filing against the collateral.
- **Foreign Currency Issues:** Even in dollar denominated loans, the lender should require the borrower to compensate the lender for any loss in the exchange rate in the event of (1) foreclosure or judgments in Mexico payable in pesos, (2) the debtor’s election of its right to pay in pesos, or (3) government controls or restrictions during an economic crisis.
- **Enforcement:** A U.S. lender may want all of the loan documents to be governed and enforceable under U.S. laws; however, the legal system granting rights in cross-border transactions may not be the same legal system in which enforcement occurs. Where title to real estate is in Mexico, enforcement must occur in Mexico.
- **Miscellaneous:** immigration permits, licensing regulations, withholding taxes, jurisdiction clauses, conflict of laws and other issues must be accounted for in the loan documents

Overall, for U.S. lenders contemplating cross-border transactions in Mexico, it is important to understand that certain issues will arise that are not present in domestic transactions. In the end, though, Mexico is a desirable credit market for U.S. lenders because of its geographic location, developments in industry, commerce, and tourism, and the advent of NAFTA.

## GLOBAL CONNECT SPEAKER SERIES

This fall, Snell & Wilmer’s International Practice Group introduced the “Global Connect Speaker Series,” which aims to provide our clients and contacts with an interesting educational experience from a global perspective as well as a forum for networking with others in the community. Attendance to these presentations is open to all interested individuals. If you would like more information on upcoming events in the Global Connect Speaker Series, please contact Kendra Leischuck at [kleischuck@swlaw.com](mailto:kleischuck@swlaw.com).

### Honduran Delegation Visits Snell & Wilmer

On August 19, 2008, the Snell & Wilmer Phoenix office hosted a delegation of approximately 30 individuals from Honduras with the National Law Center for Inter-American Free Trade. In addition to presentations from various Snell & Wilmer attorneys, external Phoenix business leaders were invited to speak to the group. Will Acosta with JP Morgan Chase Bank spoke on the subject of lending in Arizona. Dean Rennell the Executive Vice President of Wells Fargo Bank led the discussion on secure lending from the banker’s perspective. Other areas of discussion included U.S. federal income tax issues for foreign investors, securitization issues, secured lending, and the US filing system. Snell & Wilmer has enjoyed a long-standing relationship with the National Law Center, and we were extremely honored to host this delegation.

## New Babylon

On September 9, 2008, Snell & Wilmer's Phoenix office hosted Phil Allsopp, President and CEO of the Frank Lloyd Wright Foundation, for a private preview of FLW's master plan and designs for the city of Baghdad in the mid-1950s. Wright's designs for this "New Babylon" paid homage to the rich Sumarian, Babylonian, and Islamic heritage of Iraq and were among his last commissions. Attendees had the opportunity to view a small number of these plans and see a preview of the work's spring 2009 exhibition at the Guggenheim Museum in New York City.



## FONATUR

As the destination of choice for nearly 20 million tourists each year, Mexico offers a wide variety of opportunities for investment. On October 9, 2008, Snell & Wilmer's Phoenix office hosted Mario de la Vega, Deputy Executive Officer of Development for FONATUR (Mexico's National Trust Fund for Tourism Development). Over the last 30 years, FONATUR has been Mexico's premier developer of Intergrally Planned Resort destinations. Mr. de la Vega presented to

attendees the opportunities available in Mexico as well as provided a preview of upcoming projects of this leading development agency.

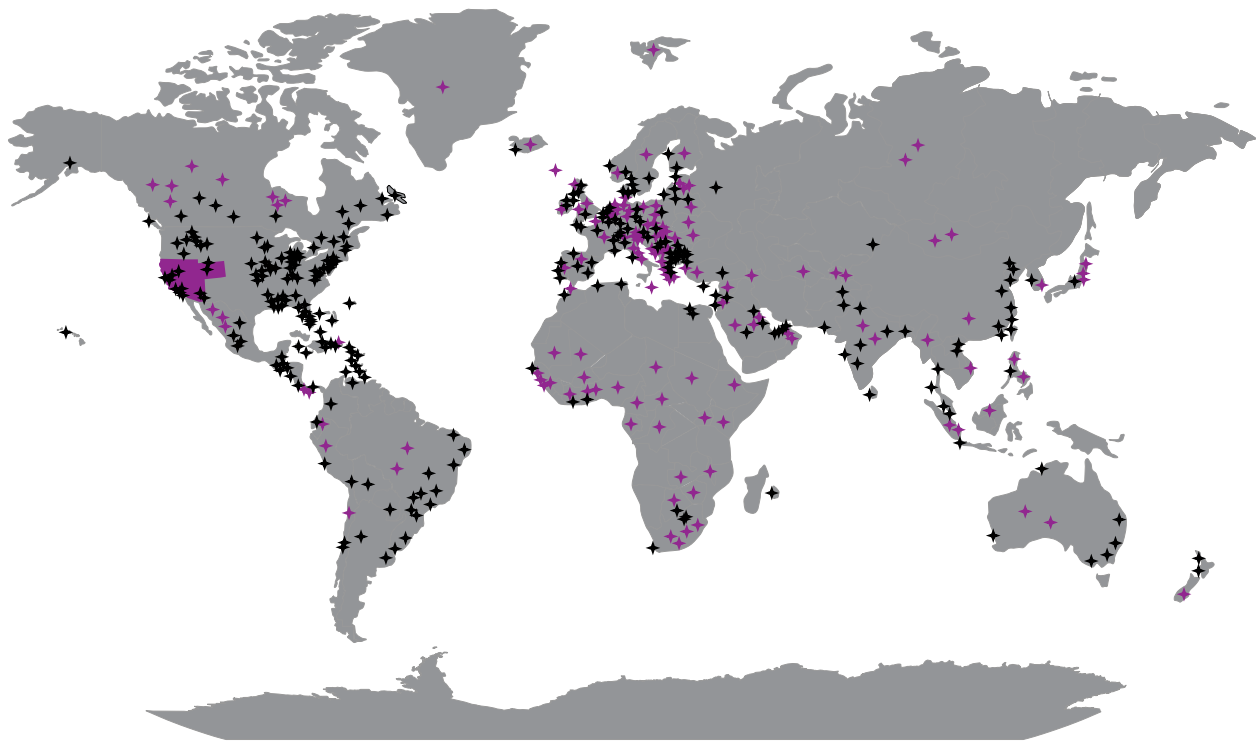


## International Trade Forum

Snell & Wilmer's Phoenix and Tucson offices and the State Bar of Arizona International Law Section invited guests to a special forum discussing the government's and non-governmental organization's efforts to develop international trade opportunities in Arizona. Presenters included Eric Nielsen, Director of the Arizona U.S. Export Assistance Center U.S. Department of Commerce; Don Maxwell of the City of Phoenix; Karla Teixeira of the Arizona Department of Commerce; and Kevin O'Shea, Deputy Director of the National Law Center for Inter-American Free Trade and Co-Chair of the Arizona District Export Council's Trade Policy & Legislative Affairs Committee.



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