

SO, YOU WANT TO ADVERTISE AND SELL YOUR MEXICAN RESIDENTIAL REAL ESTATE PROJECT IN THE UNITED STATES – NOW WHAT?

COMPLIANCE WITH THE UNITED STATES INTERSTATE LAND SALES FULL DISCLOSURE ACT AND VARIOUS STATE LAWS

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Successful developers of residential real estate subdivisions ("Projects") located in Mexico often attempt to reach the large market of potential customers located in the United States. Developers will often advertise to these consumers via the internet, e-mail, telephone, direct mail and other forms of communication, but may overlook a very important aspect of a successful marketing plan -- compliance with United States federal and state land sales laws.

Developers in other countries often ignore these laws because they are either not aware of such laws or simply believe such laws do not apply to them. In fact, a developer of a Project located in Mexico that is advertised to Americans must comply with federal and state laws of the United States. If they fail to do so, they may face civil or even criminal penalties, as well as being required to give purchasers the right to cancel their contracts.

DOES MY PROJECT NEED TO COMPLY WITH THE U.S. LAND SALES LAWS?

Within the United States, the marketing, sale (or even leasing) of residential lots, homes or condominium units (regardless of whether the Project is located within the United States) is regulated at the federal level by the Interstate Land Sales Full Disclosure Act and related regulations (the "Federal Laws").

Unless a Project falls within an exemption (discussed below), a developer wishing to market its Project in the United States is required to register with the U.S. Department of Housing and Urban Development ("HUD") and to provide purchasers with a disclosure document ("Property Report") before that purchaser signs an agreement. Developers may not mail promotional materials or even return telephone calls or emails unless the Project is registered.

In addition to the Federal Laws, many individual states have their own land sales laws. State law compliance is discussed below.

IS MY PROJECT EXEMPT FROM FEDERAL LAND SALES LAWS?

A developer offering less than twenty five (25) units or lots as part of a common promotional plan is exempt from both the antifraud provisions and registration requirements of the Federal Laws.¹

A developer offering 25 to 99 units or lots is exempt from registration, but may still be subject to the anti-fraud provisions of the Federal Laws.

If the Project has one hundred (100) or more units or lots (including any other Projects promoted under a common plan), the developer may need to register unless it qualifies for one of the available exemptions. The most common exemption is for a developer to agree to construct and have the units ready for occupancy within two years.²

A Federal Law exemption, however, does not automatically excuse the need to register with individual states (with the exception of the State of Illinois).

¹ The anti-fraud provisions provide, among other things, that it is against the law for a developer to make an untrue statement of material fact or omit material facts or defraud a purchaser. A developer that represents that amenities or utility service will be completed by the developer will be obligated under the anti-fraud provisions to complete such amenities or services.

² Under this exemption a developer may provide a pre-sale contingency period of up to 180 days, but that does not extend the two year period. Instead the developer simply has an option to terminate the purchase contracts during the first 180 days.

STATE LAW COMPLIANCE

Many states within the United States regulate the marketing and sale of out-of-state land to their residents.³ For example, states can require (i) registration of the Project with a state agency, (ii) public offering statements to be given prior to entering into binding contracts or reservation agreements and/or (iii) use of a local broker or agent licensed in the state.⁴

Land sales laws are not uniform and what constitutes sales activities is subject to the laws of the individual state.⁵ Most states have taken the position that advertising via mail, email or even placing a telephone call into a state (even in response to an unsolicited request) subjects the developer to the laws of that state.

The state law compliance process varies from state to state; ranging from a simple two page form to a comprehensive registration application with a state property report similar to the federal registration requirements. A number of states have specific disclosure, escrow and deposit requirements and require financial assurances that promised improvements will be completed.

While registration under the Federal Laws will not necessarily exempt a Project from registration in a state, there are a few states that provide an exemption equivalent to the federal one hundred lot exemption. Most states exemptions based on the size of a Project however are limited to much fewer than ninety-nine lots (e.g., 25 lots).

A HUD registration may, however, help to simplify the state registration process because some states provide a shorter registration process for Projects registered with HUD.

Regardless of whether a Project is exempt from or registered under the Federal Laws, the interstate land sales of each target market state should be considered.

The penalties imposed for violations of a state's land sales laws range from voiding sales contracts and imposing fines to felony criminal charges. A broker's or sales agent's license may also be suspended.

WHEN SHOULD I START THE COMPLIANCE PROCESS?

To determine an appropriate timeline for a HUD registration, a developer should count back from the date the developer wants to start marketing in the United States. As a general rule, at least six months should be allotted to prepare and obtain acceptance of a HUD registration.⁶ Remember, this is only to comply with the federal registration process. State registrations can take anywhere from one to nine months, depending on the target market states.

As long as the developer is only taking non-binding reservations, the developer does not need to register with HUD at that point. That being said, developers should consider registering with HUD even if not yet required to do so because the HUD filing will make it easier to register in individual states. In fact, many states allow registration with an abbreviated filing together with copies of the HUD filing. This type of piggy-backing of registrations can result in substantial savings by avoiding duplicative filings in each state. The legal fees associated with the HUD filing typically range from \$15,000 to \$20,000 and the legal fees associated with filings in each state are generally \$2,000 to \$4,000.

WHAT IF I FAIL TO COMPLY WITH FEDERAL AND/OR STATE LAW?

³ Many developers in Mexico market their Projects in California. To comply with California law, all advertising literature that will be distributed to California residents or otherwise distributed within the State of California (including the developer's website) should contain the following disclaimer in at least 10 point font in capital letters:

WARNING: THE CALIFORNIA DEPARTMENT OF REAL ESTATE HAS NOT EXAMINED THIS OFFERING, INCLUDING, BUT NOT LIMITED TO, THE CONDITION OF TITLE, THE STATUS OF BLANKET LIENS ON THE SUBDIVISION (IF ANY), ARRANGEMENTS TO ASSURE SUBDIVISION COMPLETION, ESCROW PRACTICES, CONTROL OVER SUBDIVISION MANAGEMENT, RACIALLY DISCRIMINATORY PRACTICES (IF ANY), TERMS, CONDITIONS, AND PRICE OF THE OFFER, CONTROL OVER ANNUAL ASSESSMENTS (IF ANY), OR THE AVAILABILITY OF WATER, SERVICES, UTILITIES, OR IMPROVEMENTS. IT MAY BE ADVISABLE FOR YOU TO CONSULT AN ATTORNEY OR OTHER KNOWLEDGEABLE PROFESSIONAL WHO IS FAMILIAR WITH REAL ESTATE AND DEVELOPMENT LAW IN THE COUNTRY WHERE THIS SUBDIVISION IS SITUATED.

⁴ For example, in California merely "soliciting prospective purchasers" for compensation is an activity for which a California real estate broker's license is required.

⁵ For example, simply emailing information to a New Jersey resident who has requested information from a developer's website, is prohibited in the State of New Jersey.

⁶ The developer will need to time to compile and prepare the large amounts of information requested about both the developer and the Project. Once all the information is compiled, the HUD application process itself can take an additional sixty (60) days or more. HUD must respond to an application with thirty (30) days but typically will request additional information or clarifications. This can result in forty-five (45) days or more for an approval.

The Federal Laws are designed to protect U.S. consumers from fraud and abuse. Failure to comply may lead to civil and criminal penalties in addition to giving purchasers the right to cancel their contracts.

Civil liability under the Federal Laws may include monetary damages, specific performance or any other relief that a court deems equitable (such as damages equal to the difference between the purchase price and the fair market value of the property, plus interest, court costs, attorneys' and appraisers' fees and other costs and expenses such as the cost of travel to and from the Project). The developer may also face penalties of \$1,100.00 per violation up to a maximum of \$1,100,000.00 per person, per year.

Criminal liability for violations of the Federal Laws may include misdemeanor and felony charges against the developer, its directors, officers, agents, employees, and sales agents and fines of up to \$10,000.00 and/or imprisonment for up to five years.

If the developer fails to deliver a required Property Report to the buyer prior to such buyer's execution of a purchase contract, the buyer will be granted a two-year right to revoke the purchase contract.

CONCLUSION

Given the impact of these federal and state laws, it is important to adequately plan for compliance issues. The developer should allow ample time for such compliance and should engage an experienced team (including legal counsel and others knowledgeable with regard to the specific issues) early in the planning stages. This will enable the developer to coordinate its marketing plan with federal and state laws to avoid unnecessary delays, civil or criminal penalties and/or having to cancel contracts with customers in the United States.
