

Borrowing Your Way Into Paradise

Real estate loan offerings to help fund the purchase of homes in Baja California

Stories By Lynne Carrier

Like other Americans under the spell of ruggedly beautiful Baja California, Russ Schreier set out to own a vacation home there. He discovered the historic town of Loreto, Mexico, in Baja California Sur, finding his dream lot only a few feet away from the sand and the clear aqua waters of the Sea of Cortez. But buying into the dream brought a rude awakening. “I would have wanted to get a loan on it, but unfortunately none was available at the time,” he recalls. Instead, he formed a partnership to come up with more than \$700,000, the full asking price.

Schreier saw a need. The Del Mar mortgage broker left his familiar world of California home finance and went to work full time in the red hot real estate market south of the border. A year and a half ago, he founded Finance North America and became one of a handful of mortgage brokers and lenders pioneering loan programs for Americans buying property in Mexico.

Lending to American buyers is a relatively new phenomenon in Mexico, where Americans typically pay up front with cash. It comes at a time when the Baja California real estate boom already is in full swing. Dozens of master-planned communities and luxury condo towers are springing up along northern Baja’s Gold Coast. There are no signs of a slowdown. Rosarito Realtor Diane Gibbs says she closed seven real estate purchases in a single weekend last month — and that wasn’t particularly unusual. “Our buyers are getting younger and younger,” she says. “They’re in their 50s now. But they are buying with the idea that they will retire here eventually and realizing that if they don’t buy now, the train might be gone.”

Gibbs, who has lived and worked in Baja since 1988, says her clients usually tap their savings or the equity in their American homes, coming up with the full price through a wire transfer or cashier’s check. But a convergence of factors — among them, rising mortgage and equity loan rates in the United States, higher priced Baja real estate and improving terms for loans on Mexican property — could make loans increasingly attractive for Americans buying homes in Baja.

No Big Banks, Yet



Finding a picture-perfect lot on the Sea of Cortez was easy for mortgage broker Russ Schreier, but securing a loan was not so simple. The solution? Open Finance North America, a lender in Mexico for American property buyers.

Although big, mainstream U.S. banks do not yet lend to home buyers in Mexico, Baja's thriving real estate market is attracting other players. "More and more banks are getting interested," says Julian Myers, an attorney with the law firm Higgs, Fletcher & Mack who specializes in cross-border real estate transactions. "It's working really well."

Baja developers with new luxury projects have begun to offer loan options to potential clients. Among them is the \$55 million, 271-unit oceanfront condo tower being built on land owned by the historic Rosarito Beach Hotel. The condos will be delivered fully furnished when completed in April 2008, and the Rosarito Beach Hotel will offer a service to rent them to vacationers when the owners are not occupying them.

The condo hotel concept is proving popular. Somit Talwar, project manager for the Rosarito project, says more than 100 of the units — ranging from \$175,000 to \$599,000 — have been sold so far. Of the units sold, Talwar says, 90 percent of the buyers have signed up for loans. "I think in the past, people were not financing," Talwar says. "So as a result, the market was not quite as large for us. Not everyone has three or four hundred thousand in cash lying around. Now that financing is available, it has really opened up a huge market. People can afford now to make payments on the loan and buy much bigger homes. Interest rates have gone down, too."

Schreier's Finance North America is providing mortgage services to buyers in the Rosarito Beach Condo Hotel project. He also pre-qualified 70 buyers for loans at the proposed Trump Towers, a similar condo hotel concept with 500 units planned for the coast north of Rosarito. It's not certain whether those qualifying for loans will actually get them when the first units of the Donald Trump-backed project are completed in 18 months. But Schreier adds that the pre-qualification process assures that the option will be available for them.

Schreier explains that terms for obtaining a home loan in Baja are easing, with more American buyers able to qualify. When Finance North America began its Baja lending program through GE Mexico, a financial subsidiary of a global company, only one loan program was offered in Baja. It had a four-year fixed rate followed by a 16-year adjustable rate. The borrower had to put at least 30 percent down, provide detailed income information and have a credit score of at least 720, well above the U.S. average score of 679.

These days, a variety of loan options are available and the terms have improved, he says. A buyer able to provide full income documentation and a high credit score may get an 8 percent loan, fixed for three years, followed by a 27-year adjustable rate. The same borrower could get a 30-year fixed mortgage at 8 percent, Schreier says. The loans may be obtained with as little as 20 percent down. Prepayment penalties have been waived, and loans are available now for buyers with credit scores down to 660.



A condo tower rises from the Rosarito Beach Hotel's complex, which is still family-owned and celebrated 80 years in 2005.

Other mortgage opportunities are emerging in the eastern Baja coastal town of San Felipe, where the proposed Baja Diamante development is beginning construction. The complex will include 4,000 luxury homes and condos to be completed over 10 to 12 years, with sales totaling \$1.2 billion. Single-family villas start at \$255,000, while a 1,780-square-foot, three-bedroom, two-bath unit in a condominium tower overlooking the Sea of Cortez on one side or a Jack Nicklaus-designed golf course on the other will sell for \$345,000.

Kyle Crawford, Baja Diamante's director of sales, says the developers are working with Collateral International, a lender based in Birmingham, Ala. He says that the Collateral loans, offered through Express Mortgage Lenders in Palm Springs, range from 7.5 percent for a 25-year fixed to 6.5 percent for a 10-year loan for buyers.

One criticism of loans offered on Mexican property is high closing costs. Sticker shock is in store for buyers used to American lending practices. On a \$300,000 Baja property, total closing costs could be as high as \$23,000, Crawford says. These costs would include a Mexican 2 percent acquisition tax based on the assessed value, fees charged by a Mexican notario, up to \$6,000 for a title insurance policy, \$1,700 for a permit from the Mexican Ministry of Foreign Affairs and other lesser charges.

Nevertheless, Crawford notes these expenses have to be weighed against the bargain prices American buyers get on premium properties in northern Baja. And Talwar notes that over time, low property taxes compensate for the sizable up-front closing costs. How low? Rosarito Realtor Gibbs says the value of her Baja home has appreciated to about \$500,000, but last year, her property tax bill was \$91. Even in big, new luxury projects, developers say that property taxes on a \$300,000 unit could be less than \$300 a year.

As lenders test the waters in Baja, questions remain whether these programs will expand as new major players enter the picture.

Some developers express doubts.

Gabriel V. Robles, president of the Baja Resort Developers Association, says he is not sure that loans will catch on in a big way, although he's optimistic about the future of Baja real estate. He predicts that the sellers will benefit from the vast wealth of American baby boomers, who can afford to pay the full price from their U.S. home equity, stock earnings, retirement funds and inheritance money. "How deep the market is for all-cash buyers is hard to say, but I imagine it's pretty deep," says Robles.

Baja Diamante's Crawford also is skeptical about rumors that big American banks might jump into the Baja real estate scene. "They make great promises, but sometimes you don't hear from their representatives again," he says. "It's not an easy process. It's harder work than it is for them to do a loan in the states. So the ones that are down here doing it, they are busting their butts to earn their money."

Lenders and brokers currently in Baja, however, foresee growth in demand — even for loans with higher interest rates and closing costs than in the United States — when buyers clearly understand the benefits. Most important, they say, is that the loan process can help protect buyers from the higher risks of investing in a foreign real estate market with complex and unfamiliar rules.



Gabriel Robles of the Baja Resort Developers Association anticipates boomers with cash will be more prevalent in the booming Baja market than those needing loans.

Left to their own devices, Americans sometimes lose their shirts in Mexico.

“The reason is that when they go into the market, they do things that they wouldn’t do in the States,” says attorney Myers, who notes 70 percent of his new clients are coming to him with real estate problems. “And in setting up their deals improperly, they’re getting themselves into trouble. . . . people are signing deals on napkins over a few margaritas.” At the outset, buyers should hire an attorney, he says, check the fine print in title insurance policies and make sure that their deposit funds are held in a legitimate escrow account.

Schreier says buying Mexican property with the help of a loan adds a layer of oversight. Even wealthy buyers who could buy expensive Baja real estate with cash have begun to opt for loans. They know the lender has a vested interest in closing a deal that will hold up over time. “They’re using it almost as an insurance policy because they know that they are getting free and clear title on the property and we’re going to do the due diligence on it,” he says.

Also, he sees drawbacks in stripping large chunks of equity from an American property to buy at full price in Baja. “I hate to say it’s risky,” he says. “But you’re buying property in a foreign country utilizing all the equity from your house in the United States. Is that what you want to do?” Also, buying in Mexico with U.S. home equity has limited tax advantages, he says, because tax deductions would be available only on interest up to \$100,000. Obtaining a separate loan for a second home in Baja, however, may provide higher deductions for some buyers, he adds. Those who would benefit, he says, are property buyers having less than a total of \$1 million in loans for their primary residence and second home and are not affected by the alternative minimum tax. He recommends that buyers check with a tax accountant.

Schreier believes that more investors and lenders will take part in the Baja real estate boom — either directly or in the secondary market — as they see that loan yields are higher in the Mexican market and that American property buyers in Baja have good track records. As an example, he says that of 60 loans that GMAC made in Mexico around the year 2000, only one went into default — and in that case, the borrower died.

Another plus for lenders is that Americans buy and sell Baja property through a fideicomiso, a Mexican bank trust that holds title to property. Fideicomisos are ubiquitous in Baja, since Americans cannot hold direct title to property within 31 miles of the coast and 62 miles from Mexican borders. Schreier insists that his American clients buy property through a

fideicomiso trust on any loan in Mexico, even in parts of that country where Americans can directly own property. That’s because under the fideicomiso arrangement, the lender becomes the first beneficiary of the trust, while the borrower takes second position. If the homeowner stops making payments, the lender can take over the property and resell it.

Given the advantages for lenders and U.S. buyers in Mexico, he sees a bright future in Baja for all types of real estate loans, from individual and construction loans to loans that allow full-price buyers to pull equity from their Baja property. Although Americans don’t always understand the culture of Mexican real estate, he notes, they do understand the American culture of credit. “We finance our homes, our automobiles, our educations, our weddings, our dinners,” he says. “We finance everything. That’s what we want to do.”



Although Mexico's casual lifestyle beckons, attorney Julian Myers warns American real estate buyers interested in Baja to take the time to secure proper legal and financial advice before pouring that first celebratory margarita.

Property buyers in Baja are also keeping a watchful eye on emerging loan programs and the influence that might have on property values.

In 2005, Russell Hamilton of Solana Beach purchased a home in the Loreto Bay development in Loreto in the southern Baja peninsula. The developer gave him interim financing at 7.5 percent for three years, long enough for the home to be built. Now, Hamilton is concerned that the red-hot market in Baja California Sur might stagnate or even drop if reasonable loan programs aren't available when his interim financing expires. "I didn't plan on selling my place," he says. "But seeing that the loan programs are just now getting started makes me question whether I should keep it not." He's taking a wait-and-see approach. "I have a year to make a decision."

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