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INTERNATIONAL LAWYERS NETWORK



GAMBOA, GARCÍA & CARDONA ABOGADOS
Buying and Selling Real Estate in Colombia

ILN REAL ESTATE GROUP



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KEY FACTS OF REAL ESTATE ACQUISITIONS UNDER COLOMBIAN LAW

1. Standard Forms of Agreements to buy and sell Real Estate:

Despite the existence of several types of agreements to implement real estate transactions in Colombia, the most common forms of agreements used to acquire real estate properties are the promise to sale and purchase agreement and the sale and purchase agreement.

a. *Promise to Sale and Purchase Agreement (Promesa de Compraventa)*

Considering that there are some formalities to acquire real estate properties in Colombia and the need of the parties to be bound by a legal document swiftly, regularly the parties enter first into the promise to sale and purchase agreement (the “Promise”). Under this agreement, the parties set the terms and conditions agreed by them to do the transaction of purchase and sale of the property, and the buyer paid a percentage of the price agreed as a down payment of the transaction. Under the Promise, the seller promise to sell, and the buyer promise to purchase the property when some conditions are fulfilled, usually when a specific date arrived, depending on the complexity of the transaction.

The following are some legal requirements to make valid and enforceable the Promise: (i) the agreement must be done in writing; (ii) the object of the agreement should not be prohibited or invalid by law; (iii) it must include the specific date or condition that sets the date to celebrate the purchase and sale

agreement which must be done by public deed. In relation to this requirement, as stated by case law, it is also necessary to indicate the Public Notary and the time where the purchase and sale agreement public deed will be executed; (iv) the agreement must determine the purchase and sale agreement, in such a way that to proceed with the closing of the transaction, only the formalities or the legal means to transfer and delivery the property are missing.

The last requirement mentioned above, refers to the necessity to include in the agreement on one hand, a full description of the property, among others, its identification name, address, boundaries, registration number, tax identification number and, those of the condominium, if applicable, including the public deeds by means of which the property was submitted to the condominium regime. On the other hand, the price agreed by the parties and its form of payment.

Some conditions are included in the Promise to assure its fulfillment, which means the execution of the promised purchase and sale agreement by the parties, the transfer of the property by the seller and the payment of the price by the buyer. Among others, it is common to agree the inclusion of penalty clauses equivalent at least to 20% of the price, escrow accounts, banking letters of credit or, the indication of the down payment amount as a confirmatory payment or prepaid penalty in case of breach of the



contract by any of the parties, as applicable.

b. Sale and Purchase Agreement (Contrato de Compraventa)

The sale and purchase agreement (the “SPA”) is the regular form of agreement used to acquire real estate properties. When it is preceded by a Promise, the SPA usually replicates the terms and conditions agreed on the Promise, unless the parties agreed to modify some of those terms. Under the SPA, the seller sells, and the buyer buys the property specified in detail in this agreement for the price set therein, just as it was mentioned before in relation to the Promise agreement.

When the SPA is used to instrument a real estate transaction, it must be done in writing by a public deed executed by the parties before a Public Notary. The SPA by public deed itself constitutes only the title by means of which the transaction is done, however, according to Colombian law, in order to transfer the property title to the buyer it is required the registration of the public deed under its registration number at the Registration Office to which the property is linked (according to geographic location). Only when the public deed is duly registered, the property can be considered transferred, and the main object of the SPA is fulfilled.

The same conditions indicated to guaranty the Promise may be included under the SPA. Those guarantees are included to secure, among others, the registration of the public deed, any breach of the contract in relation to its

reps and warranties or the existence of hidden flaws (*vicios ocultos o redhibitorios*) that could not be detected beforehand under a due diligence process but that may affect the property title after its acquisition.

2. Due Diligence:

In order to have certitude about the legal situation of the property at the time of the transaction, it is highly recommended to proceed beforehand with a due diligence process over the property. Such process should include the revision of the property titles, the urban applicable regulations or a land use analysis, when applicable.

a. Revision of Property Titles:

The revision of the property titles is conducted mainly to determine that the seller is the entitled owner of the property and, to rule out the existence of circumstances that affect or may potentially affect the ownership right over that property in case of acquisition (e.g., encumbrances, limitations to the property rights or registered lawsuits). In relation to residential properties, it is important to highlight the existence of some legal figures to protect family housing, such as the Family Housing Assignment (“*Afectación a vivienda familiar*”) and the Unattachable Family Assets (“*Patrimonio de familia inembargable*”) which are indeed encumbrances to the ownership right.

The aforesaid revision refers to those legal acts in relation to the property that are duly registered under the registration number of the property, which are reported under a no liens’ certificate (*certificado de tradición y*



libertad). Such certificate should have an issuance date no longer than ten previous days and, in any case, before the execution of any agreement, a new one should be requested and revised to prevent the appearance of recent unknown acts registered after the completion of the due diligence process.

Depending on the criteria used by the legal expert in charge of the due diligence, the revision could refer to the registered acts of the property since the beginning of the transference chain of the property, the last twenty years, or the last ten years. However, such acts that are part of the titles chain referring to encumbrances and property limitations, that have not been duly cancelled or those that reveal some inconsistencies under the certificate, must be revised in detail.

Some other documents are revised under this part of the due diligence process. For instance, proof of payment of property taxes at least of the last five years, its cadastral certificate to verify and compare the information of the property based on the information managed by the public entities.

b. Urban or Land Use Analysis:

An urban or land use analysis pretends to verify, according to the applicable urban law, which kind of constructions can be built on the real estate property or which limitations are imposed over the property in relation to its development or use destination. If this analysis is performed over a property that has already a building, it will determine if the construction complies

with the planning regulations applicable at the time of its construction and if the building can have its current or intended destination.

Some of the documents revised in this due diligence are the construction permits and all the urban licenses and urban legal documents of the property, as well as its specific applicable regulations.

3. Forms of Ownership in Colombia:

In Colombia, the ownership is the legal right of a person to use, enjoy and dispose over a thing (including real estate properties), without violating the law or the rights of other people. Nevertheless, there are some special forms of ownership in Colombia that are relevant to mention herein.

a. Fiduciary Trust Property:

A fiduciary trust is a legal vehicle whereby a settlor transfers the property to a trustee in exchange for fiduciary rights. Usually, but not always, the settlor is at the same time the beneficiary of the Trust. This legal vehicle is usually use for the development of construction projects, but it can also be used as a form of simple ownership. Trust property simplifies the transfer of real estate assets, as the seller is able to assign his fiduciary rights to the buyer by a private agreement, without granting a public deed. It also represents a guarantee for real estate transactions, as the trust property is managed by a trust company that must fulfill fiduciary obligations.



b. Real Estate Investment Funds and Private Equity Funds:

A real estate investment fund is a legal and financial vehicle (mutual fund) which mainly invest in real estate properties, in order to generate long-term income and asset valuation which become financial returns for its investors. The real estate investment funds are managed by professional and its investors have their investment represented in participation titles of the fund. The real estate investment funds are highly regulated by the Colombian financial authorities.

c. Condominium Regime:

There is a special ownership type called Condominium Regime (*Regimen de propiedad horizontal*) in which exclusive property rights over private property and co-ownership rights over common areas of the property concur, to guarantee the security and peaceful coexistence of the co-owners. This kind of ownership is very usual in the residential or commercial buildings. The main purpose of this type of property is the maintenance of the common areas of the housing or retail project. It constitutes a limitation to the ownership right and generates to the owners of private properties the obligation to contribute to the maintenance of common property areas, through a monthly administration fee which is paid to the condominium administration.

d. Joint Ownership:

Joint ownership consists of two or more people owning the same property. This

joint ownership is allocated in each person according to the percentage determined in the public deed by means of which they are acquiring the ownership right over the property. If it is not indicated in the public deed the participation percentage of ownership to which each person is entitled of, it is understood that the ownership right is distributed in equal percentages.

e. Usufruct:

There is an ownership retaining usufruct, that consists in the kind of ownership in which the owner conserves the right to dispose over the property but not the right to use and enjoy the property, which are given to another person. The usufruct title is an example of this ownership form.

f. Rural Property:

In relation to rural property is important to mention that the acquisition of these kind of properties must consider the accomplishment of legal requirements related to the statutory limitations to acquire rural property in Colombia according to the Colombian agrarian legislation.

4. Notarial Aspects:

As it was mentioned before, the transfer of real estate in Colombia must be done with the formality of a public deed held before a Public Notary. Similarly, when fiduciary contracts involving transfer of real estate are constituted, the formality of a public deed must be complied, even though the transfer of fiduciary rights over them can be made by means of a private document. The public deed content is public which means that anyone can access the information of



a real estate transaction.

The process to prepare a public deed begins when the interested party approaching any Public Notary office in the country, since there is freedom of choice except when dealing with transactions in which the state participates as a party, because there it would apply a distribution system to select among notaries. Once the request is made, the officials of the public notary will inquire which legal transaction is going to be held and request the documents required for each specific deal; in the case of the sale and purchase agreements, the required documents are: (i) No liens' certificate (*certificado de tradición y libertad*) of the properties involved in the transaction; (ii) Documents of existence and legal representation of the parties; (iii) Proof of payment of property taxes of the last five years; (iv) No debts certificate issued by the applicable tax authorities in relation to the properties; and, (v) No debts certificate issued by the administration when the properties are subject to the condominium regime.

The deed process takes approximately 5 business days, and the notary fees are regulated by decree for the entire national territory. Afterwards, the public deed must be registered at the Registration Office to which the property is linked.

5. Registration Aspects:

Public deeds in Colombia must be registered to considering transferred the property, because without registration there is no transfer of ownership rights. The registration offices are divided into registry circles that are distributed according to the location of the real estate properties. The purpose of the registration is to give

knowledge to everyone about the transactions and legal acts that have been done or that may affect the property.

The registration process takes about 15 business days and its fees to register are set by the authorities at the national level, however, registration taxes must be paid as well, and they are set by each municipality government, so they may vary among municipalities. To register a deed, the first copy of the document issued by the Public Notary must be taken to the Registration Office of the circle to which the property belongs with the proof of payment of the applicable registration fees and registration taxes. Once the Registration Office receives the documents, it proceeds with the registration after checking that everything was made accomplishing the applicable laws, if not, the Registration Office can make return notes indicating the motifs of such return and/or those aspects that must be corrected before presenting them again for registration.

6. Costs related to Real Estate Property:

a. *Property tax (Impuesto Predial):*

It is a tax that municipalities charge annually to real estate properties. In general, the tax authorities set the tax amount to be paid, however, sometimes there is a form of self-assessment in which the owners declare the value of the real estate to set the property tax to be paid, and the tax authority may present or not an objection to such value.

b. *Valuation contribution (Contribución por Valorización):*

It is a tribute that eventually the municipalities charge when they are



going to carry out publicworks that may increase the value of a property. For the State, it is a financing mechanism, and it is usually used to finance the construction of city infrastructure, among others, roads, bridges and public spaces.

c. *Added value tax (Participación en Plusvalía):*

It is a tax charged when by means a public action the municipality generates the possibility that in a property the construction index raised, the destination of the land changed to a more profitable one or, the land is incorporated from urban-to-urban expansion. This tax is set onlyonce by each municipality, and the law defines when its payment become enforceable to theproperty owner.

d. *Administration Fees:*

The administration fees are the amount charged to each private property under a building ora group of buildings subject to the condominium regime. Such amount is intended to cover administration costs such as surveillance, cleaning, equipment maintenance or replacement, public utilities of the building, among others.

7. Brokerage:

The real estate brokerage contract has as object to put potential buyers and sellers in contact to enter a sale and purchase transaction over real estate. Brokerage is a partially regulated activity in Colombia; however, a license is not required to operate as a real estate broker.

Commission rates are freely agreed by the

parties but generally the commission is equivalentto 3% of the sale price of the property when located in urban areas and 5% when located in rural ones.

It is not necessary to have a real estate agent, it is simply an additional activity. However, real estate agents serving under this kind of transactions may help to find the best property and to save time to complete it.