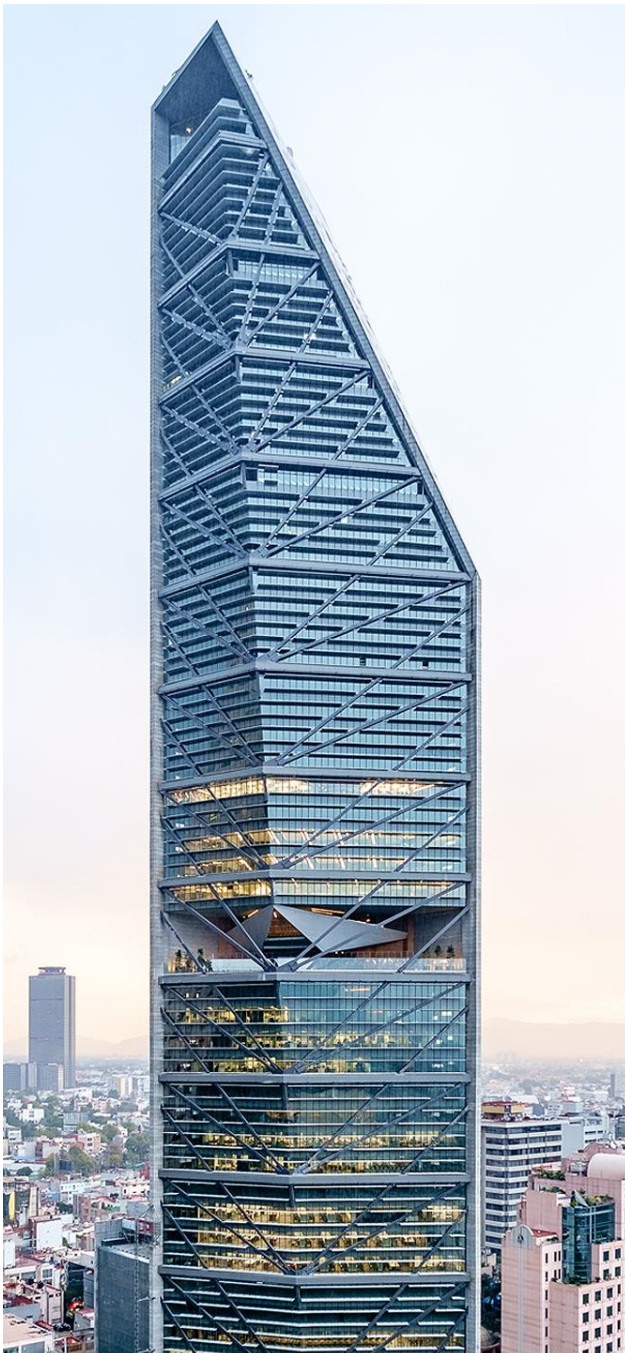

Bill of reform to the Hydrocarbons Law

Mexico City - Energy

March 2021



President López Obrador has introduced Bill of Reform to amend the Hydrocarbons Law (*Ley de Hidrocarburos*) (the "**Bill**" and the "**Law**", respectively) to the House of Representatives in order to strengthen the role of *Petróleos Mexicanos*' ("**Pemex**") as a key and predominant agent within the hydrocarbons sector.

In general terms, the Bill affects the permit and sanction regime currently set forth in the Law and grants greater powers to the Ministry of Energy (the "**SENER**" per its acronym in Spanish) and the Energy Regulatory Commission (the "**CRE**" per its acronym in Spanish) to grant, review and revoke the different permits contemplated in the Law, under new criteria.

The Bill's entry into force is subject to discussion and approval by the Mexican Congress and, if applicable, its subsequent publication in the Official Gazette of the Federation (the "**DOF**").

This document elaborates on the relevant implications of the Bill and its impact on the hydrocarbons industry in Mexico.



Background

On March 26, 2021, the House of Representatives published in the Parliamentary Gazette (*Gaceta Parlamentaria*) the Bill to reform the Hydrocarbons Law, introduced by President Andres Manuel Lopez Obrador. This Bill reiterates previous attempts by the Federal Government to modify the hydrocarbons' legal framework with the admitted purpose of strengthening the state-owned Pemex, formerly a governmental body organized as a decentralized organization (or public utility) and then transformed into a State Productive Enterprise along with the 2013 Energy Reform.

One of the main goals of the Energy Reform was to abandon the vertically integrated monopoly within the hydrocarbons sector to foster an environment of economic competition in the activities of the oil industry. However, the Bill is contrary to the Energy Reform's spirit as it affords Pemex (indirectly and through the participation of SENER and CRE) a privileged position within the market.

It is worth mentioning that the Bill has not been introduced on a preferential basis, thus its discussion and voting will be adjusted to the ordinary sessions established in the Political Constitution of the United Mexican States (the "**Constitution**"). We are currently in the second ordinary period, which ends no later than April 30. Therefore, it is possible that the Bill will be *fast-tracked* to be voted and approved by the Mexican Congress shortly.

General Aspects of the Bill

Following the common parliamentary practices in Mexico, the text of the Bill begins with the explanation of motives (*exposición de motivos*), which reveals the legislative intent. This is particularly relevant because, according to the explanation of motives, the main purposes sought with the Bill are: (i) pursue the fulfillment of the Policy of Minimum Storage of Petroleum Products (*Política de Almacenamiento Mínimo de Petrolíferos*);¹ (ii) increase the regulation on revocation of permits; (iii) combating the fuel theft (illegal bunkering); and (iv) introduce the suspension of permits in the event of a national security issue.

Therefore, the Bill proposes to amend the Law as follows:

¹ *Política Pública de Almacenamiento Mínimo de Petrolíferos*, published in the DOF on December 12, 2017 (https://www.dof.gob.mx/nota_detalle.php?codigo=5507473&fecha=12/12/2017), as amended by means of Decree published in the DOF on December 6, 2019 (https://www.dof.gob.mx/nota_detalle.php?codigo=5581171&fecha=06/12/2019).



CUATRECASAS

- (i) Engaging or having the storage capacity required by SENER, likely referring to the Minimum Storage Policy of Petroleum Products, will be now a criteria to obtain a permit;
- (ii) It also provides for the revocation of those permits that, as of the date of entry into force of the Decree, fails to comply with the *storage* requirement determined by SENER.
- (iii) It amends the effect of the public administration's silence when processing permits from the legal fiction of affirmative decision (currently in force) to a negative decision.
- (iv) It increases the events of permit revocation, by incorporating the recidivism in the following cases:
 - a. non-compliance with the provisions applicable to the quantity, quality and measurement of hydrocarbons and petroleum products; and
 - b. the modification of the technical conditions of systems, pipelines, facilities or equipment without the corresponding authorization.
- (v) It grants CRE and SENER, in accordance with their respective attributions, the authority to temporarily suspend the permits in the event of a national security issue, an energy security issue or danger to the national economy, at their discretion. However, the Bill does not establish the criteria under which those authorities shall determine whether such circumstances are met, nor the procedure under which the permit suspension would be enforced, pursuant to the rule of law principle.
- (vi) Furthermore, the Bill sets forth that, in the event of a permit suspension, the authority will be in charge of the administration and operation of the permit holder to ensure the continuity of the relevant activities, in order to guarantee the interests of the end users and consumers, being able to use the personnel that operated the facility or hire new personnel. Furthermore, the Bill provides that the suspension will long as much as the authority determines, albeit the permit holder may request the termination of the suspension, provided that the causes giving raise to it had disappear (except in events of illegal commercialization, transportation or alteration of the fuel components).
- (vii) In line with paragraph (vi) above, it eliminates the possibility of the State engaging experienced third parties to operate those facilities that, for the



purpose of safeguarding the interests of the Nation, have been temporarily occupied or intervened by the authority.

Legal Remarks

The Bill raises a number of constitutional issues that, if passed by the Congress, may give rise to many constitutional remedies (such as *amparo* claims and unconstitutional actions) or even investment arbitrations pursuant to the different International Trade Agreements and the Investment Protection Agreements to which Mexico is a party.

In general terms, the amendments introduced by the Bill potentially affect all kind of permits, indistinctly. This means that, in principle and without prejudice of certain provisions applicable to specific activities or products (for instance, fuels or petroleum products), SENER and CRE will be able to revoke, suspend or intervene, among others, the following permits:

- Export and commercialization of hydrocarbons (potentially affecting the upstream sector);
- Liquefaction, transportation and storage of natural gas, oil or petroleum products (potentially affecting the midstream sector and the facilities associated therewith); and
- Import, commercialization, distribution and retail of petroleum products (potentially affecting the downstream sector and the facilities associated therewith).

Thus, the proposed amendments will not only affect the investments and projects that were developed from the 2013 Energy Reform, but will also hinder future investments due to the uncertainty that the Bill, if approved in its terms, would generate for the private sector, especially in the *midstream* and *downstream* sectors of the industry. While the Bill, in principle, does not seem to affect the activities of hydrocarbons Exploration and Production *per se*, it is important to note that, given the broad authority granted to the CRE and SENER, the Bill may potentially impact the sale of crude oil and natural gas, as such activity requires a commercialization or export permit and indirectly affect the development of Hydrocarbon Exploration and Extraction activities.

Finally, the purported revocation of permits set forth in the Bill violates the constitutional principles of rule of law, due process, and non-retroactivity of the law.



For further information related with this document, please contact our Energy and Natural Resources team in Mexico

Contact:

Marco Antonio de la Peña | marco.delapena@cuatrecasas.com

©2021 CUATRECASAS

All rights reserved.

This document is a compilation of legal information prepared by Cuatrecasas. The information or comments are included in it. The intellectual property rights over this document are owned by Cuatrecasas. Reproduction by any means, distribution, assignment and other use of this document without the prior authorization of Cuatrecasas is prohibited.

