

# Amendment to the Hydrocarbons Law is enacted

Energy – May 4<sup>th</sup>, 2021

On May 4, 2021, the "Decree whereby several provisions of the Hydrocarbons Law are amended and supplemented" (the "Amendment") was published in the Official Gazette of the Federation, resulting from a bill introduced by Mexico's President.

According to the explanatory statements (*exposición de motivos*) provided in the bill, the Amendment is needed due to an alleged damage caused to the energy sector in the "neoliberal period", as a result of the approval of the Energy Reform. It mentions as well that, although there is no doubt about the leading role that the state-owned oil company *Petróleos Mexicanos* should play, elements of corruption within such company have had repercussions on the country's energy efficiency. Therefore, the Amendment aims at strengthening State-owned companies, including *Petróleos Mexicanos*, through several amendments to the HL.

The Amendment was approved by the Mexican Congress in practically the same terms as the those provided in the bill that was introduced by the President.

Following is a summary of the various amendments and additions to the Hydrocarbons Law ("HL") that are established in the Amendment:

1. Accreditation of storage capacity as a requirement to obtain permits.- For the granting of the permits referred to in the HL, the applicant must now demonstrate that it has the storage capacity determined by the Ministry of Energy ("SENER").

For context, on December 12, 2017, SENER published in the Federal Official Gazette the Public Policy on Minimum Storage of Petroleum Products, which establishes the obligation for marketers and distributors of petroleum products (i.e., gasoline, diesel and jet fuel) to have minimum inventories of the product.

2. "Deemed denial" in the procedures for the assignment of permits.- A "deemed denial" is introduced in the proceedings for the assignment of permits granted by SENER and the Energy Regulatory Commission ("CRE").

Previously, the HL provided that, if SENER or CRE, as applicable, do not rule on the applications for the assignment of permits within the statutory deadline, such applications are deemed approved. Because of the Amendment, such applications would now be deemed to be denied.

3. Introduction of new causes for revocation of permits.- The following causes are added as grounds for revocation of permits:
- a. The performance of activities of transportation, storage, distribution or retail of hydrocarbons, petroleum products and petrochemicals, when it is proven that such products have been unlawfully acquired, or illegally imported, and
  - b. Repetitive violations in (i) non-compliance with the quantity, quality and measurement provisions of hydrocarbons and petroleum products, and (ii) modifying the technical conditions of equipment under a permit without the corresponding authorization.

In addition, the transitory articles of the Amendment provide that, as of the date of its coming into force, the competent government agencies shall revoke permits when their holders have failed to comply with the provisions of the HL. Likewise, it is specifically provided that when permit-holders fail to comply with SENER's storage requirements, the corresponding permits shall be revoked.

4. New permit suspension concept.- The concept of "permit suspension" is introduced, which implies that SENER and CRE, within the scope of their authority, may suspend, temporarily or permanently, the permits granted under the HL whenever an "imminent danger to national security, the energy security or the national economy" is expected.

In the event that a suspension is declared, the corresponding authority may take-over the administration and operation of the permit-holder to ensure the continuity of operations.

The permit holder may request the authority to terminate the suspension by demonstrating that the causes for the suspension have disappeared, provided further that such causes do not refer to a violation of the law.

Additionally, it is established that, in the event of (i) a permit suspension, (ii) a temporary occupation of the facilities necessary for the provision of the service, or (iii) an intervention of the activities under a permit, the authority may only engage State-owned companies to continue with the operations of the facilities under the permit (under the current terms of the HL, private companies may also be engaged for this purpose).

The Amendment provides that any and all provisions that are opposed to the Amendment are repealed by its enactment. In addition, it is provided that all permit-holders whose rights may be adversely affected by the Amendment may request compensation for the corresponding damages, in terms of the applicable regulations; however, it is not clarified to which regulations the Amendment refers.

Additionally, the Amendment establishes that upon the entry into force of the Amendment, the competent authority will proceed to terminate the legal effects of the permits that have expired in terms of Article 55 of the HL.

On April 9, 2021, the Federal Economic Competition Commission (“COFECE”) issued an opinion on the bill to amend the HL, stating that if the bill was approved, free competition in the hydrocarbons sector would be negatively affected, mostly due to the distortion of the conditions of entry, which depend to a great extent on the permit regime established in the HL, the implementation of the “deemed denial” in applications for the assignment of permits, and the requirement of demonstrating certain storage capacity in order to obtain permits, which could result in a restriction of supply.

Finally, COFECE determined that the amendments considered in the bill would affect the grant and use of permits throughout the hydrocarbon, petroleum, and petrochemical value chain, creating legal uncertainty to the entry of new participants, as well as to participants already operating in the markets, also enabling the artificial restriction of the supply of these products and services. COFECE deemed that this could result in the increase of prices of goods and services offered throughout the value chain of these markets, with the negative impact on the purchasing power of consumers and the increase of costs and loss of competitiveness of companies. Based on the above, COFECE recommended Congress not to approve the bill in the proposed terms.

The Amendment may entail several violations of general principles of law, as well as several fundamental rights protected by the Mexican Constitution, including in competition matters that were identified by COFECE.

Thus, any person that suffers an adverse effect resulting from the Amendment may combat it through a constitutional remedy (*amparo*) before a Federal District Court. This, whether the affected party is directly affected, as could be a hydrocarbons marketer, or indirectly or abstractly affected, as could be the case with end-users.

Depending on the special circumstances of each case, *amparo* lawsuits would have to be filed within 30 business days of the enactment of the Amendment, or within the 15 business days following the formal notice of the first act of authority that is based on the Amendment’s provisions. As part of the *amparo* proceedings, companies may request injunctive relief from the Federal District Court.

Likewise, Mexico’s counterparties in USMCA, the Trans-Pacific Partnership and the various investment protection treaties executed by Mexico may bring formal claims against the Mexican Government, based on the protections provided by such treaties (no undue discriminatory treatment and no expropriation without compensation, among others). Investors from countries signatories to the above-mentioned treaties may also commence investment protection arbitrations under such treaties.

Amendment to Thirteen Transitory Provision of the HL

It should be noted that the Amendment does not include the modification of the Transitory Article Thirteen of the HL that was proposed by the President's party, MORENA, in the House of Representatives. This amendment seeks to remove asymmetric regulations imposed on PEMEX in the hydrocarbons market. The amendment of Transitory Article Thirteen was approved by the Mexican Congress on April 29, 2021; however, it is yet to be enacted through publication in the Official Gazette of the Federation, as a requirement to become effective.

Do not hesitate to contact us for any question or comment in connection with the above.

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