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Energy: Oil & Gas

Mexico – Law & Practice

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MEXICO

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Law and Practice

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Dentons has been for more than two decades at the forefront of the Mexican energy sector, and has been consistently recognised as the leading firm in this industry. Its practice covers the full range of the energy industry, from upstream, midstream and downstream oil and gas to electricity, including renewables. The practice enjoys the most recognised lawyers in energy regulatory matters, and a considerable hands-on expertise and a proven track record in the successful development of projects in Mexico, from LNG storage facilities, natural gas and liquids transportation pipelines, exploration and production projects, among others. Following the Mexican energy liberalisation of 2014, the firm is active in all aspects of the sector opening, including vast activity in the E&P rounds being awarded, Pemex farm-outs and development of midstream projects, among others.

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1. General Structure of Petroleum Ownership and Regulation

1.1 System of petroleum ownership

Like many other jurisdictions, Mexico has a state-ownership principle with respect to hydrocarbons. Under the Mexican Constitution, all domestic hydrocarbons belong to the nation, which then entrusts different operators with their exploitation. No rights or claims to the hydrocarbons are contemplated for states, municipalities, other political subdivisions or any other constituencies, such as indigenous groups. Given this principle, all matters related to the oil and gas industry (including at the midstream and downstream level) are handled at the federal level.

In 2014 Mexico underwent a sweeping reform of its energy industry that resulted in an overhaul of the sector, and a complete opening of the industry to private investment and competition. Prior to 2014, Mexico had a vertically-integrated monopoly in the oil and gas business. The national oil company, Petroleos Mexicanos (known as Pemex) was the single E&P operator. At this time there was a general lack of understanding as to the resources' ownership structure: people tended to believe that the oil and gas was owned by Pemex, whereas in fact Pemex was merely the operator.

After the reforms, the constitutional principle remained unchanged in the sense that the nation remained the owner of hydrocarbons. The only change was that the exploitation of the resources was opened up to a multiplicity of operators.

1.2 Regulatory bodies

The Hydrocarbons Law (enacted in 2014 to restructure the market with the reform) organises the regulation of the oil and gas sector in a bifurcated manner: upstream is regulated by the National Hydrocarbons Commission (*Comisión Nacional de Hidrocarburos* or "CNH") (see www.gob.mx/cnh), while the Energy Regulatory Commission (*Comisión Reguladora de Energía* or "CRE") (see www.gob.mx/cre), is entrusted with the regulation of midstream, including transportation, distribution, storage and marketing of both hydrocarbons and products. The Ministry of Energy (*Secretaría de Energía*) (see www.gob.mx/sener), which is mostly the policy maker and the coordinator with respect to energy planning, maintained regulatory powers on the side of refining (including permitting for new refineries and for the existing Pemex refineries) gas processing, and on the imports and exports side (both for hydrocarbons and products), primarily given its role in safeguarding national energy security.

In addition to such a structure, the 2014 reform opted for an additional bifurcation with respect to HSE, which is handled by a separate environmental agency created specifically for the oil and gas industry, as further described below.

1.3 National oil or gas company

While the 2014 reform opened the sector to private operators, it maintained Pemex (see www.pemex.com) as the largest and preponderant operator, on the upstream side, and as an additional player (with market preponderance as well), for the rest of activities. Given that the reform did not call for a divestiture of assets by Pemex, the NOC maintained the assets that it previously had as a legal monopoly, including all existing refineries, a network of logistics terminals and pipelines for products, and a strong presence in the natural gas sales market, among others. We note that the reform did call for the spin-off of the natural gas transportation network, but to another government instrument, the National Centre for Control of Natural Gas (so-called CENAGAS).

A new statute, the Pemex Law, was enacted to provide for the new Pemex structure, and to set its clear mandate: to create economic value in the industry. For that, Pemex's main purpose was to be a profitable exploration and production company, while midstream and other activities were set as optionalities. With respect to its E&P activity, with the 2014 energy reform Pemex was granted through the so-called "Round Zero" all the fields it was currently producing, and a portion (about 2/3) of those in which it was undergoing exploratory works prior to the reform. The rest of the reservoirs and fields in the country were released for administration by the CNH on behalf of the Mexican State.

1.4 Principal petroleum law(s) and regulations

The legal framework governing Mexico's oil and gas sector is comprised mainly by the following statutes and regulations:

- Hydrocarbons Law (*Ley de Hidrocarburos*). This statute structures and organises the full sector, including upstream, midstream and downstream. With respect to upstream, it governs the procedures for granting of contracts/licences to operators, the terms of such contracts, principles and rules for the operators, among others. With respect to midstream and downstream it establishes the permit regime under which these activities can be performed, the terms and conditions of the same and the special rules that apply to each such activity;
- The Law of Co-ordinated Regulators for the Energy Sector (*Ley de Organos Reguladores Coordinados en Materia Energética*) sets forth the structure and jurisdiction of the CNH and CRE, establishes their powers, mandate and their co-ordination with SENER as policy maker;
- Pemex Law (*Ley de Petróleos Mexicanos*) governs the structure and mandate of Petróleos Mexicanos, as a "state productive enterprise" entrusted with creating value, and sets forth its corporate governance principles among which its Board of Directors is given latitude for a number of decisions which in the past limited the operation of Pemex as a commercial company;
- Hydrocarbons Revenues Law (*Ley de Ingresos sobre Hidrocarburos)* sets forth the taxes and fiscal regime in general for upstream activities, including royalty levels and other taxes, and the special fiscal regime applicable to Pemex;
- Regulations to the Hydrocarbons Law, which implement in detail the norms and rules for the granting of contracts and licences on the upstream side, rules for operators, the special regime that governs Pemex as the state operator, and detail terms regarding contents of the contracts and licences, among others; and
- Regulations to Title Third of the Hydrocarbons Law, which is the implementing regulation for the midstream side, under which the CRE grants permits for distribution, storage, transportation, marketing and retail of products.

In addition to the foregoing, note that the statutory framework provides both CRE and CNH broad rule-making powers for interpreting the laws and implementing further regulations, which they do in the form of General Provisions governing a number of issues, from rules for bids on the upstream side, to rules for open access on midstream assets.

2. Private Investment in Petroleum - Upstream

2.1 Forms of allowed private investment in upstream interests

A private operator may conduct the activities of exploration and extraction of hydrocarbons, i.e., explore, develop and produce, through an E&P contract granted by the CNH on behalf of the Mexican State. The CNH grants the contract to the private operator in the context of a competitive, international public bid, on the basis of maximisation of value for the state. The legal framework contemplates that the E&P contracts can be of several types: profit sharing, production sharing, licences, a combination of the above, or other modalities. The contract is given for a contractual area (an area delimited by geographic boundaries, geological formations or a combination of both), for a specific term and permits the operator to exploit the hydrocarbons in the area upon payment of consideration to the state. Whether the relevant block or area is exploited through a licence, a PSC or other, as well as the associated terms, is determined by the CNH with SENER (with the participation of the Ministry of Finance regarding base values for the setting of the government take).

2.2 Issuing upstream licences

Based on pre-defined areas of interest which are identified in a five-year national strategy by SENER, with the input of

CNH (and also based on statements of interest in specific areas by private parties), the CNH launches a round or series of bids to award upstream contracts/licences for each specific area. All awards of contracts are subject to international bids conducted under strictly public and open processes, on the basis of the party offering the best economic conditions to the state. In order to participate in a bid for a given contractual area, the CNH publishes the technical and financial criteria that must be satisfied by the bidder. These include, with respect to technical capabilities, the experience in operation of fields of a certain nature, whether at the level of the company or of its key personnel. From the financial standpoint the bid rules also require a certain minimum net worth for bidders to participate. These requirements can typically be satisfied by a single bidder or on an aggregate basis by the members of a consortium, subject to special rules and restrictions.

Bidders are generally required to post a bid guaranty, in the form of a bond or letter of credit, and a corporate guaranty from the parent company to be in place during the life of the contract.

Companies holding an E&P contract are required to be incorporated in Mexico, and thus with local presence from the tax and legal perspective, with a permanent domicile in Mexico (although, as further described below, no restrictions on foreign ownership exist).

2.3 Typical fiscal terms under upstream licences

Pursuant to the Hydrocarbons Revenues Law, under a license contract scheme, the State shall receive:

- A bonus upon the execution of the contract determined by each contract (this is optional to be determined on a case-by-case basis by the State);
- A contractual fee during the exploratory phase (based on surface area);
- The royalties applicable for the type of product pursuant to the aforementioned law; and
- A consideration or additional royalty payable based on the market value of the hydrocarbons. These items shall be paid in cash for each period established in the contract.

Under profit and production sharing contracts, the State shall receive:

- A contractual fee during the exploration phase;
- Royalties applicable for the type of product; and
- A consideration determined by the application of a percentage on the operational profit.

The above-mentioned monies shall be paid to the Mexican Petroleum Fund (Fondo Mexicano del Petróleo) for their management and distribution under applicable statute.

2.4 Income or profits tax regime applicable to upstream operations

Private operators shall be subject to the applicable corporate income tax incurred under the Income Tax Law (*Ley del Impuesto Sobre la Renta*), currently at 30%.

Furthermore, for purposes of income tax deductions pursuant to the Hydrocarbons Income Law, contractors shall be able to apply the following percentages on amortisation related to upstream activities:

- 100% amortisation of original investments related to exploration, improved secondary recovery, and maintenance;
- 25% of original investments in development and production of crude oil and natural gas; and
- 10% of the original investments in storage and transportation facilities related to the E&P activities.

2.5 Special rights for national oil or gas companies

Pemex was given a right, through the so-called Round Zero, to keep all its production fields and a relevant portion of its then-ongoing exploration projects. Pemex maintains the operation of these fields through "allocations" or state licences, which are subject to a more stringent fiscal regime for Pemex than that imposed on others. If Pemex so decides, it has the right to "migrate" such areas into the new regime and convert them into E&P contracts (production sharing or licences). For that purpose, Pemex can secure a joint venture partner for the relevant block. As a particularity, the process to elect the partner for Pemex is not handled by Pemex itself, but for transparency reasons, this is left for the CNH, which manages a competitive bid to determine the partner on the basis of the maximum value of the royalty and of the investment committed by the partner in the "farmout" venture. Given the amounts that Pemex has invested in such areas, the investor is required to "carry" the investment required for Pemex.

Other than the above, we note that the legal framework does not demand a certain minority participation by Pemex in other blocks that the CNH may offer, or Pemex becoming the operator of the block, although the law contemplates the possibility of demanding such mandatory participation in cases of transboundary fields, if so determined by the regulator.

2.6 Local content requirements applicable to upstream operations

E&P activities are required to reach a 35% national content by 2025 (deep water and ultra deep water E&P activities are excluded from this provision). However, the mechanism to measure the national content depends on the type of the exploration or production areas, as well as the fields. Such mechanism to reach the above-mentioned goal is established

by the Ministry of Economy, whereby the following factors shall be considered:

- Origin of the assets and services contracted;
- National and qualified workforce;
- Training of the national workforce;
- Investment of local and regional physical facilities; and
- Transfer of technology.

Furthermore, Mexican labour laws require that private entities employ at least 90% Mexican nationals. However, this provision does not apply to directors or senior management. Furthermore, the law permits corporations to hire 10% of specialised employees on a temporary basis, mainly aiming for employees to train and transfer their knowledge to the Mexican employees.

2.7 Requirements of licence holder to proceed to development and production

In the event of a discovery in the initial exploration period the licensees and/or contractors shall submit an appraisal plan to the CNH for approval. After the end of the appraisal period, the contractor shall inform the CNH whether it considers the discovery to be a commercial discovery; in such event the contractor shall submit a development plan to the CNH for approval.

As a general rule, since the licensee or contractor carries the risk of commercial profitability of the areas subject to development and production, operators can define the means for development and production. Nevertheless, CNH has the authority to render observations to such development plans to ensure consistency with the corresponding contract and the Hydrocarbons Law. The licensees or contractors shall make the corresponding adjustments and operating solutions to the development plans in order to comply with the aforementioned observations.

In the event of disagreement or deadlock over the development plans, in most contracts the contractor may pursue the dispute-settlement mechanism established under the contract, mediation procedures to be followed by the parties or, ultimately, arbitration. The licensees/contractors have the right to relinquish part of the block awarded, or even to terminate the relevant E&P contract early, subject to certain rules (e.g. complying with a minimum work program, abandonment rules, etc.).

2.8 Key terms of each type of upstream licence

Hydrocarbons in the subsoil shall be the property of the nation. However, upon extraction and payment of the corresponding royalties, in the case of a licence the licensee is entitled to take title to the hydrocarbons and dispose of them. In the case of production-sharing contracts, the contractor shall deliver the hydrocarbons produced and receive from the Mexican Petroleum Fund the share of production belonging to the contractor, i.e. after payment of the government share, and all royalties and fees. In addition, under PSCs, the contractor may be entitled to reimbursement of "recoverable expenses" provided that the expenditures have a reasonable basis according to industry standards and satisfy a number of specific requirements established under the E&P contract and the applicable laws and regulations. Note that the reimbursement is subject to a certain maximum of the revenues generated and recovery is contingent upon commercial production. Contracts and licences are awarded for 25-35 year terms, subject to extensions for five to ten year terms.

In all contracts, a so-called "adjustment mechanism" is included to calculate considerations of the State and the contractor. The intent of this mechanism is for the State to receive any windfall profits due to high oil and gas prices.

There is forced unitisation provision. The contractor is responsible for notifying the CNH and Ministry of Energy in the case of shared reservoirs or fields. Although the contractor(s) or entitlement holders (ie Pemex) propose the unitisation plan and agreement, ultimate approval of the plan rests with the government.

Each contract provides the exploration and production periods, as well as the minimum work programme thresholds for the contractors or licensees. Extensions and modifications are granted on a case-by-case basis subject to CNH approval as long as they are in accordance with the applicable contracts and statute. The liability and risk are, generally speaking, responsibility of the contractor or licensee. As discussed, contractors and licensees have the authority to withdraw from the contract areas at their discretion (nevertheless, the minimum work programmes shall be performed).

It is important to note that in the event of termination of the contracts, caused either by withdrawal or administrative/contractual termination by CNH as established under the contract, the materials and assets used in the hydrocarbon activities as well as the contractual areas shall be transferred to the state free of liens or encumbrances and without consideration to the contractor or licensee. As further discussed below, contractors are required to set aside funds in an abandonment trust for the abandonment phase.

2.9 Requirements for transfers of interest in upstream licences

Transfers of participating interest in a PSC or licence (ie a farm-in or farm-out), require the approval of the CNH, where the CNH will verify financial capabilities (if dealing with a non-operator, and technical operational capabilities in the case of an operator. Generally speaking, for a term of five years as of the effective date of the contract, the farmee

shall satisfy the same requirements included in the bidding guidelines originating the contract. Depending on the contract, there may be restrictions to replace the operator for a given term, and generally speaking, the operator may be required to have a minimum interest of the project (normally one third of the project).

The CNH issued a set of guidelines and requirements to be satisfied in order to request and receive an approval to transfer a participating interest under an E&P contract.

3. Private Investment in Petroleum - Downstream

3.1 Forms of allowed private investment

The Mexican market had an initial partial opening, allowing private participation in transportation, distribution, storage and marketing of natural gas, back in 1995. Since then, considerable gas transportation infrastructure has been developed by private players, mostly anchored by government offtakers, i.e. the power monopoly CFE, through long-term PPAs. Three LNG regasification terminals were also developed, similarly anchored. Despite this opening, the market for sales of natural gas continued to be vastly dominated by Pemex, who also controlled 90% of the pipeline system and offered customers a bundled service. With the 2014 reform, the rest of the midstream and downstream sector was fully liberalised, allowing private investment in transportation, distribution, storage, import, export, marketing and retail of all products, as well as refining and gas processing.

While currently Pemex continues to own the six existing refineries in Mexico, the system already allows for private refineries to be built, with the simple issuance of a permit from the Ministry of Energy. No bid process is required for such permit to be issued.

All midstream infrastructure may be built through the issuance of a permit from the CRE as well. Permits are issued upon evidence of project feasibility, including technical capabilities of the operator, consistency of the financial model (in most cases including the approval of a regulated rate), and approval of regulated terms of service and general terms of service. The permits issued by the CRE do not grant any type of exclusivity for the infrastructure to be built, and to that extent their issuance does not entail a bidding or other competitive process.

3.2 Rights and terms of access to any downstream operation run by a national monopoly

In general terms, all midstream infrastructure permitted by the CRE is subject to an open access principle, thus allowing any interested third party to book available capacity or participate in a project expansion. Services are to be provided under a regulated rate, which is approved by the CRE based on the capital and operating expenditures of the project, a reasonable rate of return and operating efficiencies, taking into consideration market benchmarks. The regulated rate is reviewed periodically by the CRE. Any expansions should be done through the launch of an open season to accommodate the potential needs of third parties.

Shippers are entitled to receive not unduly discriminatory treatment, including the granting of any special conditions given to other shippers under similar circumstances. A shipper that is not receiving due treatment, including rates, can resort to the CRE.

As a general rule, storage of liquids enjoys a lighter regulation with no rate regulation.

3.3 Issuing downstream licences

A permit for transportation, distribution or storage of gas or products is granted by the CRE upon approval of the conditions of the project. As discussed above, the permitting process does not entail any type of bid. It is possible that certain exceptional strategic projects on the natural gas side, to be launched by the National Center for Control of Gas (CENAGAS) may be awarded through a competitive bid.

The permitting process before the CRE is generally done online. Permits are issued to Mexican persons only; to apply for a permit, the application shall include, among other requirements, the payment of governmental fees, corporate documentation (ie including a description of the corporate structure), description of the project, business plan and other specific requirements according to the activity.

3.4 Typical fiscal terms under downstream licences

Midstream and downstream projects are not subject to a special fiscal regime, in terms of payment of a special contribution or a government take. The facilities are subject to regular corporate income taxation of the permit holder. Given that permit holders are generally speaking special purpose companies, they maintain a specific project financial model. For purposes of rate-making proceedings, the CRE would take into consideration the impact of federal income tax in the model and in the projected ROI, to ensure that in an efficient operation scenario the developer of the infrastructure can obtain an appropriate return.

3.5 Income or profits tax regime applicable to downstream operations

Regular corporate income tax applies to downstream projects. In structuring the project and its financial model, the sponsors need to consider other local taxes, which mainly refer to property tax on the site or right of way, and statutory profit sharing for the employees in terms of labour laws.

3.6 Special rights for national oil or gas companies

Due to the largely predominant position that Pemex had in the midstream and downstream sectors prior to the 2014 opening, the CRE has implemented "asymmetric rules" to reduce Pemex's share in the market and allow other competitors to come in. These asymmetric rules include regulated terms and conditions of sale, capped prices and other regulation applicable to Pemex only (capped prices are no longer applicable to natural gas sales). With respect to natural gas, the rules entail that Pemex is required to divest a material proportion of its portfolio of customers, to keep only a 30% of the market share in four years. As part of the reform, the natural gas pipelines formerly owned by Pemex were spun-off into a separate entity – CENAGAS – as an independent operator, to ensure access to any interested gas marketer. CENAGAS is undergoing an open season to allocate capacity in the system to shippers and to users directly.

3.7 Local content requirements applicable to downstream operations

Neither the Hydrocarbons Law nor the CRE as regulator require a local content programme for a permit-holder or developer of infrastructure. However, the Ministry of Economy is entitled, at any point, to issue rules encompassing the oil and gas industry as a whole (ie including downstream activities).

3.8 Other key terms of each type of downstream licence

Generally speaking, service providers are required to provide services on a firm and interruptible basis. Hence, shippers are entitled to reserve capacity on pipelines or terminals on a long-term basis, provided that it is effectively utilised. Capacity may be assigned to third parties in a secondary market.

Transportation companies are required to bear the risk of loss on the products while being transported, and are required to carry proper insurance for risks relating both to the product and operational casualties. Permit holders are required to ensure continuity of services to their customers, and therefore have to abide by special rules in order to terminate service.

3.9 Condemnation/eminent domain rights

Private investors do not have condemnation/eminent domain rights. In securing rights of way, transportation companies are required to follow a very strict process of acquisition of rights. The process is designed to provide certainty to the developers, but requires compliance with a number of steps, including formal appraisals, information to owners on the project specifics, validation of the contracts by a federal court, and the possibility of conciliation in cases of failure to reach agreement.

3.10 Rules for third party access to infrastructure

As noted above, generally speaking all facilities for transportation and storage of crude oil, gas and products are subject to an open access principle. The sizing of a project prior to its development requires in most cases the launching of a mandatory open season, in terms approved by the CRE and supervised by the regulator. Where facilities are financed through long-term contracts with an anchor shipper, such anchor shipper has the ability to secure long-term capacity on a 100% or such other capacity requirement it needs. With respect to storage of products, the open season may not be mandatory, and a more strict regulation may only be applied in specifically contemplated circumstances where the CRE determines such stronger intervention is warranted.

3.11 Restrictions on product sales into the local market

The local market is now fully opened as a result of the market liberalisation, and any party is entitled to sell products in the local market, obtaining a marketing permit from the CRE. By the end of the year, retail prices of both gasoline and diesel will be determined at free market prices in the entire territory.

3.12 Requirements for transfers of interest in downstream licences

A permit holder is entitled to transfer its permit to a third party, and therefore the project, with the approval of the CRE. The regulator reviews the qualifications of the assignee in terms of operational capabilities and financial wherewithal, and approves the amendment to the permit to include the assignee as its holder.

4. Foreign Investment

4.1 Foreign investment rules applicable to investments in petroleum

But for isolated exceptions in jet fuel supply within airports and bunker supply, there are no restrictions from the foreign investment law perspective to invest in the energy sector in Mexico. Foreign investors conducting a project in Mexico may enjoy the benefits of the investment protection treaties that Mexico has with their respective countries of origin. Mexico has the broadest array of bilateral investment protection treaties worldwide, including with most major economies. These generally cover investor-state arbitration, protection against expropriation, including creeping or de facto expropriation.

Resolution of disputes under the E&P contracts is subject to international commercial arbitration.

5. Environmental, Health and Safety (EHS)

5.1 Principal environmental laws, and environmental regulator(s)

As part of the 2014 energy reform, the Mexican Congress created a specialised agency to deal with environmental and health and safety matters in the oil and gas industry: the Agency for Environment, Health and Safety for the Hydrocarbons Industry (Agencia de Seguridad Industrial y Protección al Ambiente del Sector Hidrocarburos), known by its acronym as ASEA. The ASEA is entrusted with overseeing compliance and with the issuance of environmental permits for oil and gas projects, as well as official technical specifications of mandatory applicability in the industry.

As to legal framework, the main statutory bodies are the following:

- General Law of Ecological Equilibrium and Environment Protection (Ley General de Equilibrio Ecológico y Protección al Ambiente) ("LGEEPA"). The LGEEPA is the main law on environmental protection in Mexico, and provides for the federal jurisdiction on all environmental matters pertaining to the energy industry. The principal provisions for the hydrocarbons sector are those regarding the applicable procedure and requirements for the Environmental Impact Evaluation; water protection, including those regulations on industrial water discharges, water concessions and prevention of sea pollution; the prevention and control of air pollution and the regulation of highly risky activities. The LGEEPA also protects the rights to environmental information and participation, which allow for the society to obtain any information regarding water, air, soil, flora, fauna and environmental resources as well as notice of any activities that could possibly damage them, and to participate in decision making which could potentially affect the environment;
- Federal Law on Environmental Liability (Ley Federal de Responsabilidad Ambiental) ("LFRA"). The LFRA regulates the operation of an environmental liability system, including the determination of shared liabilities and joint obligors, the form of reparation and compensation for environment damages, among others;
- National Agency of Industrial Safety and Environmental Protection for the Hydrocarbons Sector Law (Ley de la Agencia Nacional de Seguridad Industrial y Protección al Ambiente en el Sector Hidrocarburos) ("LASEA"), which is the statute governing the operation of the ASEA;
- General Law on the Prevention and Integral Management of Waste (Ley General para la Prevención y Gestión Integral de los Residuos) ("LGPGIR"); and
- National Water Law (Ley de Aguas Nacionales) ("LAN"). This statute governs the handling, use, management and exploitation of water and water bodies, and their preservation.

5.2 Environmental obligations for a major petroleum project

The conduction of a petroleum project requires a number of environmental approvals, but the following are critical:

- Environmental Impact Authorisation (Autorización de Impacto Ambiental) ("EIA") which, based on the environmental impact assessment presented by the sponsor and analysed by the ASEA, contemplates mitigation measures and performance conditions;
- Social Impact Study (Estudio de Impacto Social) ("EIS"). Pursuant to the Hydrocarbons Law, the Ministry of Energy shall carry out in advance the necessary free and informed consultation procedures to safeguard the interests of the indigenous communities and people located where an upstream project will be developed, in co-ordination with the Ministry of the Interior and other competent authorities. Further, private parties developing a midstream or downstream project are required to conduct a social impact study and obtain the corresponding authorisation;
- Environmental Risk Study (Estudio de Riesgo Ambiental) ("ERA"). When the regulated parties develop activities in the hydrocarbons sector considered to be highly risky. The ERA must be presented to the ASEA for its authorisation. The ERA should be considered as a technical element for making risk-based decisions, establishing prevention and mitigation measures, and to protect the environment, the security of the facilities, and the security of the people; and
- Change of Forest Land. The change of the land use on forest land (Cambio de Uso de Suelo Forestal) ("CUSF") authorisation issued by the ASEA is necessary if the facilities of the regulated party are planned to be constructed on land where different types of vegetation are located.

5.3 EHS requirements applicable to offshore development

Offshore activities are regulated by the so-called General Administrative Provisions on Guidelines for Industrial Safety, Operational Safety and Environmental Protection, applicable to Hydrocarbons Recognition and Superficial Exploration, Exploration and Extraction (Disposiciones administrativas de carácter general que establecen los lineamientos en materia de Seguridad Industrial, Seguridad Operativa y protección al medio ambiente para realizar las actividades de Reconocimiento y Exploración Superficial, Exploración y Extracción de Hidrocarburos) (the "Upstream HSE Guidelines"). These set forth specific obligations that will specifically apply, respectively, for recognition and superficial exploration activities and exploration and extraction activities. In addition to the general obligation mentioned above, regulated parties shall file before ASEA several notices, including those regarding Commencement of Operations Notice;

Change of Operations Notice; Dismantling and Abandonment Authorisation Application. Also, they must verify the mechanical integrity of their facilities during design, construction, operation, maintenance, operational closure, dismantling and abandonment; prepare and keep documentation on several technical and operational specifications such as the drilling fluids management and the system to mitigate risks from the recollection and mobilisation of hydrocarbons and document certain events and circumstances such as sighting of species, location of Data Acquisition sites, among other operational specifications and measures.

Operators are required to maintain proper insurance coverage. The ASEA has issued the General Administrative Provisions on Guidelines that establish the rules for insurance policies for exploration and extraction of hydrocarbons and the treatment, refining and processing of crude oil and natural gas (Disposiciones administrativas de carácter general que establecen las reglas para el requerimiento mínimo de seguros a los Regulados que lleven a cabo obras o actividades de exploración y extracción de hidrocarburos, tratamiento y refinación de petróleo y procesamiento de gas natural).

5.4 Requirements for decommissioning

As a first obligation, the management system of the regulated parties must include the decommission phase, which shall be implemented and evaluated by a specific area of the company. Other obligations are imposed for the different times of the decommission phase, including activities prior, during and after the phase:

- Prior to the decommission phase, the regulated parties have to apply for an authorisation before the ASEA, which has to be for each well and/or for each of the facilities;
- During the decommission phase, al activities carried out must be done in compliance with the corresponding Environmental Impact Permit; and
- After the decommission phase, an expert opinion issued by an authorised third party must be presented to the ASEA, in order to demonstrate the compliance of the authorised program issued after the Notice of Change of Operations.

The Upstream HSE Guidelines establish obligations and requirements for abandonment activities, such as the obtainment of an authorisation prior to performing any abandonment activity.

5.5 Climate change laws

Mexico has adopted the major international treaties on climate change, and has also adopted a General Law on Climate Change (Ley General de Cambio Climático) ("LGCC"). The LGCC regulates greenhouse gas emissions to achieve the stabilisation of their concentration in the atmosphere at a level that prevents anthropogenic interferences in the climate system. It regulates the hydrocarbons sector, granting power and authority to the federal government to establish mechanisms that promote the prevention of gas emissions in the extraction, transportation, processing and use of hydrocarbons. Specific regulations in the environmental laws implement a federal registry of pollutants and releases and a transfer register, and regulations on atmosphere pollution require oil and gas industry players to install controlling equipment, adopt reduction mechanisms and maintain pollution inventories, among other obligations.

6. Miscellaneous

6.1 Unconventional upstream interests

Unconventional resources are developed under the same scheme as conventional resources (i.e. through licence agreements or PSCs granted by the CNH), with the exception of coal-bed methane gas which is associated with coal production and is exploited through a mechanism associated with the relevant mining concession.

Also, a separate set of HSE guidelines for unconventional resources was issued by ASEA in the last few months. These are applicable to exploration and extraction of onshore unconventional resources. The federal water regulator (CONAGUA) is also expected to issue a set of guidelines related to conservation of national waters in unconventional E&P activities.

6.2 Liquefied natural gas (LNG) projects

From the regulatory perspective, LNG terminals are treated as gas storage terminals. The three existing LNG regasification terminals were built in Mexico prior to the energy reform. The new framework does contemplate a specific additional permit for liquefaction, but is to a great extent ancillary to the storage permit. Imports and exports of LNG are treated as those of natural gas and do not enjoy any special treatment. Neither do they have any special restriction.

6.3 Unique or interesting aspects of the petroleum industry

Unlike most oil and gas jurisdictions that also have one or more national oil company(ies), Mexico's production-sharing contract model, or any other E&P contract for that matter, does not require the participation of the NOC in oil and gas projects. Generally speaking, Pemex, the NOC, is treated like any other private party when participating in the E&P contract scheme. Another key difference is Pemex's ability to transform its entitlements to E&P contracts while farming out the project to OICs. The selection of Pemex's farmees (partners) is subject to the scrutiny of the upstream regulator; this achieves a level of transparency never before seen in upstream transactions with IOCs.

6.4 Material changes in oil and gas law or regulation
ASEA, the oil and gas HSE regulator has issued regulation related to onshore unconventional E&P activities. It is expected that this will allow the Ministry of Energy and CNH to launch the bidding rounds for unconventional resources in northeast Mexico before the end of the year.

Guidelines and specific requirements to complete an assignment of a participating interest under an E&P contract, whether through a farm-out agreement or otherwise, were issued by the CNH in the first quarter of this year.

Federal courts have issued the first opinions and criteria related to the Hydrocarbons Law and the law creating the oil and gas regulators: CRE and CNH. In a couple of cases, specific provisions of these federal statutes and rules issued by the regulators have been challenged on constitutional grounds. Federal courts have upheld the constitutionality of the aforementioned statutes and regulation. As more aggressive regulation, or deregulation occurs, it is expected that more challenges will arise.

Finally, in June 2017, the CRE removed Pemex's so-called "first-hand sales" regulation on sales of natural gas. This means that all domestic sales of natural gas by Pemex or its affiliates are no longer subject to maximum price formulas or caps.

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