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Regulatory framework for verification of local content in the hydrocarbon industry

According to the Hydrocarbons Law, exploration and extraction activities carried out on national territory through contracts and assignments must attain, on average, a minimum of 35% of local content.

This means that at least 35% of the goods and services, labor force, training, investment in infrastructure and technology employed to carry out such activities must be of domestic origin.

Assignees and contractors should comply individually and progressively with the minimum percentage of local content that the Ministry of Energy determines for the assignment or contract, which will also include a program for its fulfillment. In turn, the Ministry of Economy will verify that the percentage is met in each case.

In order to regulate the verification of local content, on January 23 the Ministry of Economy published in the Federal Official Gazette, the Agreement establishing the provisions for verification of compliance with local content obligations of assignees and contractors regarding Exploration and Extraction activities in the national territory ("Provisions").

The most important aspects of the Provisions are the following:

I. General

- a) Provisions will be implemented by the Unit for Local Content and the Promotion of Production Chains and Investment in the Energy Sector ("Unit"), through the General Management of Local Content in the Energy Sector of the Ministry of Economy (GMLC), which shall verify that the information submitted by assignees and contractors is correct, complete and truthful, and demonstrate that they fulfilled their obligations regarding local content.
- b) Verification shall be carried out no later than 5 years after the submission of the local content report, in accordance with the appropriate legislation.
- c) For verification purposes, the GMLC will only consider the information provided properly and in time by assignees and contractors, as contained in their respective files.

RITCH

M U E L L E R

- d) In the absence of proper and timely documentary support of the information, or where such information cannot be verified, local content shall be deemed to be zero and will be deducted from that reported by the assignee or contractor.
- e) The GMLC may carry out three types of verification procedures:
 - » Measurement of reported local content percentage verification
 - » Cabinet verifications
 - » Verification visits

II. Measurement of reported local content percentage verification

- a) Such verification shall be carried out for all local content reports submitted by assignees and contractors.
- b) The GMLC will corroborate that the report does not include concepts that should be excluded, or it excludes concepts to be included. It will also confirm that local content amounts coincide with those reported by their direct providers.
- c) Where appropriate, the GMLC shall request clarification, correction or completion of the information.

III. Cabinet verification

- a) The Unit may require all information on local content from assignees, contractors, direct or indirect suppliers, authorities and anyone who may provide it.
- b) Cabinet verification shall be carried out on the selection of assignees and contractors chosen under the methodology determined by the Unit.

IV. Verification visits

- a) The GMLC may carry out verification visits any time and whenever it deems appropriate.
- b) During the visit, the GMLC will be able to verify assets, facilities, documents, people and all items related to the local content reported by assignees, contractors, and providers.

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M U E L L E R

V. Requests for information

- a) Apart from the data to verify compliance with local content obligations, the GMLC may require assignees and contractors to clarify, complete or correct any information previously rendered.
- b) Legal timeframe to answer requests of information may not be of less than 5 business days or longer than 20 business days.
- c) Such deadlines may be extended on a single occasion.

VI. Resolution

- a) The decision of the GMLC will determine whether the assignee or contractor fulfilled its local content obligations.
- b) Prior to the resolution, the GMLC will issue an opinion with the results of the verification. Assignees and contractors may submit their arguments within 10 business days after being notified of such an opinion.
- c) Resolutions must be issued no later than 18 months after the cabinet verification or the verification visit.
- d) In the event that the assignee or contractor is found to have breached its local content obligations, the GMLC shall inform its resolution to the National Hydrocarbons Commission within 5 days of its issuance.

The Provisions, which entered into force on January 24, also provide the following:

1. The methodology for selecting the assignees and contractors to be verified by the cabinet must be defined by April 22. In the meantime, oldest to earliest reports will be selected.
2. The requirements of the Local Content Report Form under the modality of A) Assignment and B) Contract (Form SE-FO-23-001), published in the Federal Official Gazette on May 26, 2017, are eliminated. Such requirements are as follows:

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- a) Registration before the Ministry of Finance and Public Credit by which the Federal Taxpayer Registry is issued.
- b) Official identification of the legal representative in both original and photocopy.

For information regarding this subject, please do not hesitate to contact us at 9178 7000 or through the following e-mail: contacto@ritch.com.mx