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Economic Package 2022 – Hydrocarbons and Petroleum Products

On October 26, the Mexican Congress approved the 2022 economic package, amending, adding and repealing several provisions of the Mexican Income Tax Law ("MITL"), the Value Added Tax Law ("VATL"), the Excise Tax Law ("LIEPS" per its acronym in Spanish) and the Federal Fiscal Code ("FFC"), submitted by the Federal Executive on September 8, 2021. Its publication in the Federal Official Gazette is still pending.

The 2022 economic package includes several amendments applicable to the hydrocarbons sector (the "Reform"), the most relevant are the following:

I. Volumetric Controls

Authorized Providers

The Reform aims to expedite the implementation of the volumetric controls project by **eliminating** the obligation to obtain an "authorization" to be a volumetric control service provider (equipment, software, verification services and reports).

The authorities will now be able to enforce the obligations related to the volumetric controls starting January 1, 2022, and taxpayers must ensure that they comply with the FFC, the Miscellaneous Tax Rules ("MTR"), as well as Annexes 30, 31 and 32 of such rules (which we understand will still contain the characteristics, periodicity, and requirements with which the taxpayers must comply regarding volumetric controls). Taxpayers will therefore be able to obtain these services/equipment from any qualified supplier, provided they comply with the aforementioned provisions.

Reforms to Article 28, Section I, Paragraph B of the FFC

The amendment to Article 28, Section I, Paragraph B of the FFC clarifies that certificates proving the proper functioning of the volumetric control equipment and software shall be deemed to be part of the taxpayers accounting.

Likewise, the Reform includes the obligation to specify the calorific value of natural gas by means of a report, in opposition to current regulation, which only contemplates the disclosure of the octane rating of gasoline.

Moreover, parameters regarding the obligation to carry out volumetric controls are added, namely:

i. Generate and keep the reports of each of the taxpayer's operations;
ii. The volume records must be obtained from measurement systems;
iii. The measurement location must be specified, and
iv. Volume records must be associated to tax invoices or custom's documents ("*pedimentos*").

Infringements and fines

The amendments to articles 81 and 82 of the FFC contemplate all the conducts that constitute volumetric control violations.

The reform also provides criminal penalties for taxpayers obliged to comply with volumetric control obligations which:

i. Do not keep volumetric controls, alter them, use them improperly or destroy them;
ii. Do not have the equipment and software to carry out volumetric controls or, do not keep them operating at all times, alter them, render them unusable or destroy them;
iii. Do not have the certificates proving the correct functioning of equipment and software to keep volumetric controls, or having them, alter or falsify them;
iv. Have any system or program installed whose purpose is to alter the volume registries or the information contained in the volumetric controls, or
v. Give tax effects to tax receipts issued by companies that simulate fuel acquisition operations.

Finally, the Reform includes the following three scenarios, in which it is understood that fuel of illicit origin is being sold (and thus subject to a penalty of 6 to 12 years of prison):

a) When there is a difference between the measured stock and the existing stock;
b) When it is detected that the taxpayer delivers more liters than contemplated in its invoices; and
c) When the taxpayer's invoicing is higher than its sale capacity.

II. Thin Capitalization

Current thin capitalization rules, contained in Section XXVII of Article 28 of the MITL, state that interest derived from debts contracted with related parties abroad will not be deductible when the amount of such debts exceeds three times the value of shareholders' equity.

However, the sixth paragraph of the aforementioned section XXVII establishes that debts incurred for the construction, operation or maintenance of productive infrastructure related to either strategic areas for the country or the generation of electric energy shall not be included among the debts that accrue interest for the purposes of thin capitalization computations.

The Reform provides that the abovementioned exception will only apply to the holder of the document issued by the competent authority, in accordance with the respective law, which contemplates that the taxpayer in question can carry out such activities on its own account.

It should be noted that the Explanatory Statement (*Exposición de Motivos*) provides that the abovementioned exception is only applicable to E&P companies, since according to the Mexican Constitution, it is the Nation who carries out this activity by means of E&P contractors and productive companies of the State, such as Pemex, under contracts and assignments, respectively, and thus such amendment aims to clarify that the exception contained in the sixth paragraph does not apply to the oilfield services industry.

III. Tax invoice requirements

The amendment to article 27, section III, second paragraph of the MITL establishes that electronic tax invoices regarding the acquisition of fuel (maritime, air and land vehicle fuels) must include the fuel suppliers' current permit issued under the terms of the Hydrocarbons Law in order for such acquisition to be considered as a "deductible item". Such permit must not be suspended at the time of issuance of the tax receipt for the requirement to be met.

Therefore, we recommend taking the appropriate measures with the authorized certification providers of electronic invoices ("PACs") to ensure that such information is available at the time of issuing the tax invoices related to the sale/acquisition of fuels starting January 2022.

IV. VAT on temporary use or enjoyment of goods in national territory

Articles 21, 24 and 25 of the Value-Added Tax Law are amended in order to clarify that the temporary use or enjoyment of goods in Mexican territory has always been subject to the payment of value-added tax ("VAT"), regardless of the place of the material delivery.

The Explanatory Statement establishes that the previous text could be read in the sense that the use or enjoyment of goods was not subject to VAT in cases where the delivery of the leased goods had taken place outside of Mexico. Authorities may intend to apply this new criteria retroactively, which would violate several constitutional rights.

This amendment is relevant for companies in the hydrocarbons sector that carry out activities in Mexican territory and lease vessels or naval artifacts (such as drilling rigs) from abroad.

V. Excise Tax

The Reform adds a fifth paragraph to Section I, Subsection D), of Article 2 of the LIEPS to establish that, when tax/customs authorities determine that excise tax has been omitted regarding the import of automotive fuels, the applicable taxes will be levied based on the type of fuel, without prejudice to the administrative and criminal sanctions that may be applicable.

Moreover, an eighth paragraph is added to Article 5 of the LIEPS to establish that when tax authorities become aware of a payment omission of excise taxes applicable to automotive fuels, the corresponding taxes will be levied without applying the weekly excise tax incentive, since it is not reasonable to incentivize or support unlawful conducts.

As per the Reform's Explanatory Statement, such measures are intended to attack fuel contraband/smuggling, since tax authorities have identified that taxpayers import automotive fuels under an incorrect tariff classification in order to avoid the payment of the corresponding taxes.

VI. Contraband

Article 102 of the FFC establishes the scenarios considered as smuggling/contraband offenses. The last paragraph of such article states that a declaration of offense will not be submitted to the Ministry of Finance and Public Credit in the event that the tax or countervailing duties omissions do not exceed MXN$195,210 or 10% of the taxes triggered, whichever is higher.

The Reform repeals the aforementioned exception in the case of the excise tax applicable to automotive fuels in terms of Article 2, Section I, Subsection D) of the LIEPS.

Additionally, Article 103 of the FFC in force as of today establishes the scenarios under which a contraband offense is presumed to have been committed, including inaccurately declaring the tariff description or classification of good, consequently omitting the payment of taxes and countervailing duties, except if the customs agency has strictly complied with all the obligations imposed by customs and foreign trade regulations.

The Reform repeals the aforementioned exception in the case of excise tax applicable to the goods referred to automotive fuels.

Finally, the Reform amends Article 104 of the FFC to impose sanctions in the cases in which contraband is configured due to omissions of excise tax applicable to automotive fuels by definitively cancelling the respective taxpayer's import permit and the patent of the customs agent who carried out the customs clearance.

In case of requiring additional information, please contact Oscar López Velarde (olopezvelarde@ritch.com.mx) or Santiago Llano Zapatero (sllano@ritch.com.mx), Ritch Mueller's tax partners.