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Tax benefits to promote hydrocarbon production

In addition to the tax benefits granted to assignees in the hydrocarbon sector in August 2017, on May 24 the Federal Official Gazette (“DOF”) published a decree by which new incentives are assigned in order to encourage the hydrocarbon production (“Decree”).

By means of the Decree, assignees may apply broader limits of deduction for costs, expenses and investments, higher than those provided for in the Hydrocarbon Income Law (“HIL”), as long as the assignments are different from those that already benefit from the tax incentive granted in August 2017.

I. BACKGROUND

1. The HIL provides that assignees must pay the Profit-Sharing Duty each year by applying a rate of 65% to the amount resulting from subtracting deductions to the value of the extracted hydrocarbons.

2. The HIL lays out the following as deductibles:

a) 100% of the original investment for exploration, secondary recovery and non-capital maintenance.

b) 25% of the original investment for development and extraction of oil or natural gas deposits.

c) 10% of the original investment for storage and transport infrastructure.

d) Costs and expenses for the extraction of oil or natural gas deposits, exploration, transportation and delivery of hydrocarbons.

e) Extraction tax effectively paid.

3. Similarly, the HIL provides that such deductions may not exceed the following amounts:

a) For hydrocarbons other than non-associated natural gas and condensates, extracted onshore, 12.500% of the annual value of hydrocarbons or USD$8.30 per barrel of crude oil extracted during the period, whichever is higher.

b) For hydrocarbons other than non-associated natural gas and condensates extracted in shallow waters, 12.500% of the annual value of hydrocarbons or USD$6.10 per barrel of crude oil extracted during the period, whichever is higher.

4. The second article of the decree by which the HIL was issued, provided for a transitional regime which set forth the application of rates other than those laid down by the HIL, both for the estimation of the Profit-Sharing Duty and for deductions in case of hydrocarbons different from non-associated natural gas and condensates, extracted onshore and shallow waters, as follows:

Fiscal Year	Rate for the estimation of the Profit-Sharing Duty
2015	70.00%
2016	68.75%
2017	67.50%
2018	66.25%

Fiscal Year	Percentage for the estimation of deductions
2015	10.600%
2016	11.075%
2017	11.550%
2017	12.025%

5. On August 18, 2017, a decree was published in the FOG in which an incentive was granted regarding the percentage for the deduction limit in the estimation of the Profit-Sharing Duty relative to costs, expenses and investments. Such incentive was applicable instead of the one provided by the HIL, as long as it did not exceed the following amounts:

a) 40% of the annual value of hydrocarbons other than non-associated natural gas and condensates, extracted onshore.

b) 35% of the annual value of hydrocarbons other than non-associated natural gas and condensates, extracted in shallow waters.

II. 2019 INCENTIVE

The new tax incentive for assignees in the hydrocarbon sector, published in the FOG on March 24 ("2019 Incentive") provides for the application of deduction limits greater than those set forth in the HIL for costs, expenses and investments in the estimation of the Profit-Sharing Duty, as follows:

a) 40% of the annual value of hydrocarbons other than non-associated natural gas and condensates extracted onshore.

b) 35% of the annual value of hydrocarbons other than non-associated natural gas and condensates extracted in shallow waters.

The above percentages may be applied instead of those established by the HIL, provided that these amounts are not exceeded.

For provisional payments of the Profit-Sharing Duty, the same percentages will be applied to the value of hydrocarbons extracted from the beginning of the year until the last day of the month in which the payment is due.

The 2019 Incentive, effective as of May 25, is applicable only to assignments different from those that already benefit from the stimulus provided for in August 2017, which remains in effect. Likewise, it will be exclusive for areas of assignment in which the deductible cost, expense or investment was generated, and therefore may not be extended to other areas.

To attain the 2019 Incentive, assignees should submit an application for validation during the first trimester of each fiscal year and receive favorable resolution from the authority. For 2019, the application may be processed within three months of its entry into force.

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