
Impact of COVID-19 legislative changes: Hydrocarbon exploration and production contracts

Mexico City

March 2020



Due to the global outbreak of COVID-19, governments are taking measures to halt the increase of infections and deaths, to such an extent that the World Health Organization has characterized this health crisis as a pandemic. In the case of Mexico, on March 23, the General Health Council published in the Federal Official Gazette the resolution recognizing the epidemic caused by the SARS-CoV2 virus (COVID-19) in Mexico.

The purpose of this document is to give an overview of the potential impact of the health contingency measures on the hydrocarbons exploration and exploitation contracts (“E&P Contracts”) awarded in Mexico during the so called “petroleum rounds,” either under a license or as a sharing production.



This document covers (i) the measures taken to mitigate potential breaches of contractual obligations; and (ii) the procedures and measures that might be needed as a result of the health contention measures.

Overview

Like other jurisdictions, Mexican Law Recognizes situations in which the liability derived from the breach of an obligation cannot be attributed to a person because of an event beyond their control, that they could not foresee or that, even if foreseen, they could not prevent. This is usually known as an act of God or a force majeure event, and its main consequence is that the person bound by the contract is not contractually liable for the breach, under the principle that nobody is bound to do the impossible.

To prove the existence of an act of God, at least two conditions must be met: (i) the event is unsurmountable and absolute, i.e., those cases in which, although the applicable precautions were taken, the event cannot be avoided; and (ii) the obligation is general, i.e., no one can fulfil it in that situation.

Mexican civil law recognizes as a general principle that nobody is liable for an act of God, unless the liable person: (i) caused the event; (ii) expressly accepted that liability; or (iii) when required by law.

Acts of God in E&P Contacts

In the E&P Contracts entered into by the Mexican State with private companies through the National Hydrocarbon Commission (Comisión Nacional de Hidrocarburos, “CNH”), the parties’ exemption of liability is recognized in acts of God or cases of force majeure: under these clauses, none of the parties to an E&P Contract will be liable for the breach, suspension, or delay in the fulfillment of the obligations established, if they are the result of an act of God or a case of force majeure.

For purposes of the E&P Contracts, and consistent with the Hydrocarbons Law and Mexican civil law, acts of God or cases of force majeure are understood as acts or events that prevent the affected party from fulfilling its obligations provided that: (i) they are beyond its reasonable control; (ii) they are not the result of willful misconduct or gross negligence; and (iii) the act or event could not be prevented by taking diligent action. For illustration purposes, some instances of an act of God or a case of force majeure, such as restrictions due to quarantine and epidemics, are given without limitation.



Subject to the specific analysis of the obligations in question, the general, temporary, and emergency measures to face the health crisis would entail the materialization of an act of God in terms of the E&P Contracts and, in that case, the burden of proof would fall on the party that would enforce it, specifically, the contractor itself.

If necessary, contractors would be entitled to apply for an extension for their respective work programs, if they are unable to fulfill them because of these measures connected to the health crisis. To this end, a written request should be filed before the CHN within five calendar days from the date when they become aware that the act of God or case of force majeure has occurred, specifying the reasons for the extension. The CHN has, in turn, 30 days to reply such request. In addition to the extension to the work programs, the degree to which COVID-19 affects petroleum activities (as defined in the E&P Contracts), such as payment of considerations to the State, must be considered.

To apply for an extension to the exploration and evaluation periods in case of acts of God or force majeure, they must have had an impact on the respective oil activities for more than 30 days.

As for the exploration and development plans for extraction, it is important to consider that, if the act of God was previously recognized by the CNH, under the Guidelines Regulating Exploitation and Development Plans for the Extraction of Hydrocarbons, this could constitute a modification of the plans, provided that it is established that the scope, duration, or cost of the plan initially approved is affected.

Conclusions and recommendations

Given the general and temporary health emergency measures that may substantially affect fulfillment of the contractor's obligations under the E&P Contracts, the possibility of applying for a statement of act of God or force majeure in each specific case should be analyzed based on the specific nature of the obligations and the impact that it might have on the performance of the oil activities and, consequently, on the fulfillment of its contractual obligations as a direct result of this health crisis.

Contractors are therefore advised to take the following measures:

- Properly document any external event that might impact the normal performance of their petroleum activities and, in general, the fulfillment of their contractual obligations.
- Consider preemptive reporting of any situation connected to the contingency that might potentially affect fulfillment of the contractual obligations.



CUATRECASAS

- Obtain as much available documentary, technical and operating evidence as possible that might certify the existence of circumstances that prevent or might prevent the actual fulfillment of the contractual obligations, as well as document any mitigation measure taken regarding the health crisis.
- Given the current or imminent breach of obligations derived from the E&P Contract, prepare the supporting documents and immediately submit the notification to the CNH by the deadline established in the E&P Contract, taking care to avoid submitting after the deadline.
- Take into account that, under the terms of the General Administrative Provisions established in the Guidelines to Report Incidents and Accidents to the National Agency for Industrial Security and Protection of the Environment in the Hydrocarbon Sector, the Contractor may be required to report some of these events to the Agency.



For additional information, please contact Cuatrecasas.

Marco Antonio de la Peña

Partner

marco.delapena@cuatrecasas.com
Av. Paseo de la Reforma 483, piso 50.
06500, Ciudad de México.

Elías Gallardo Palma

Associate

elias.gallardo@cuatrecasas.com
Av. Paseo de la Reforma 483, piso 50.
06500, Ciudad de México.

Rafael Rodríguez Curiel

Associate

rafael.rodriguezcuriel@cuatrecasas.com
Av. Paseo de la Reforma 483, piso 50.
06500, Ciudad de México.

©2020 CUATRECASAS

All rights reserved.

This document is a compilation of legal information prepared by Cuatrecasas. The information and comments included should not be interpreted as legal advice on any matter.

Cuatrecasas owns the intellectual property rights over this document. Reproduction by any means, dissemination, transfer, or any other use of this document in whole or in part or in excerpted form without the express prior consent of Cuatrecasas is prohibited.

