

Mexican Law Amendment Could Stifle Mining Activity

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On May 8, Mexico enacted an amendment to its mining law, national waters law, general law for ecologic equilibrium and environmental protection, and general law for the integral management of residue.

Affecting both new and existing concessions, Mexico's amendment endorses a series of drastic changes to the Mexican legal regime applicable to all mining concessions and reduces the duration of mining concessions and replaces the current grant system with a public bidding process.

Additionally, it restricts the extraction of minerals solely to those expressly described in the concession, imposes previous authorization requests for assignments, and imposes a series of new social and environmental obligations before a concession may be granted.

While some of the proposed changes may have laudable goals, the changes will, in practice, result in substantially more costly and, in some instances impracticable, burdens on all mining activity in Mexico.

Rapid Legislative Process and Lack of Dialogue

Mexican President Andrés Manuel López Obrador, better known as AMLO, submitted a proposal to amend the mining law and the national waters law on March 28, secured approval by the Mexican House of Representatives on April 20, and obtained approval by the Mexican Senate on April 28.

The process was unusually fast for Mexican standards, and excluded from any meaningful debate both members of the mining industry and AMLO's opposition.

While the populist nature of the amendment is not a surprise for AMLO's administration, the depth of the enacted changes is surprising and should have a chilling effect on the entire Mexican mining industry.

Main Changes Applicable to Mining Concessions



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The amendment endorses a series of drastic changes to the current mining legal regime in Mexico, including the following.

Reduction of the Duration of Mining Concessions

The duration of mining concessions would be reduced from 50 years renewable for another 50 years to 30 years renewable for another 25 years.

The reduction cuts nearly in half the maximum concession duration, which will adversely affect long-term operations and long-term investments.

Restrictions on Mineral Extraction

Concessions now must expressly state the specific minerals to be extracted under the concession with sanctions ranging from hefty fines to five to 10 years in prison for the extraction of unauthorized minerals.

This is particularly problematic because it is rarely possible to extract solely one mineral from a deposit. The failure to properly identify all minerals and secure concessions for all minerals may have dire consequences for anyone engaged in mining activities in Mexico.

Public Bidding Process

The first-come-first-served grant system is replaced by a public bidding process, eradicating any incentive for miners to identify — typically at great expense — new mining sites.

Miners now will have to participate in a public bid for new concessions to be granted, regardless of the substantial investments required to discover new projects. This new rule eliminates any first-mover advantage that miners had in being the first to discover a new mining site.

The natural consequence of this shift will be that miners and investors likely will no longer spend funds to identify new projects, which cost will fall on the Mexican government.

Exclusive Exploration Rights

The Mexican government now has exclusive exploration rights, through the Mexican Geological Service or other federal entities.

This is problematic because it is now the state that decides when and where to explore, and this could lead to exploration coming to a halt because the Mexican Geological Service does not have the resources or the same incentives that mining companies have to undertake exploration.

Additionally, in the event a private party obtains information regarding the availability of minerals for which no concession has been granted, either in an existing site or in a new site, the Mexican Geological Service may elect to enter into a collaboration agreement with such private party, for a nonrenewable period of five years, in which the private party must prove that there are economically explorable minerals in the site.

Then, if the Mexican Geological Service concludes that exploration is economically feasible, it shall

propose to the Ministry of Economy to carry out a public bid, in which the collaborating private party may win, provided its offer is at least 90% of the highest bid and the remaining legal requirements are met.

Additional Environmental Obligations

The amendment also creates additional environmental obligations for concessions, and establishes the prohibition of mining activities in areas without water or in natural protected areas.

This is a significant shift from the previous policy requirements, which authorized mining projects — and quite frequently did so — in natural protected areas, provided that sufficient assurances were furnished to the satisfaction of the Secretariat of Environment and Natural Resources.

Now, the amendment makes those projects illegal, even if satisfactory to the Secretariat of Environment and Natural Resources.

Additionally, this prohibition raises significant concerns for existing mining projects that are located in natural protected areas and whether the Mexican government will allow those projects to continue or whether it will revoke those concessions.

Governmental Approval for the Assignment of Concessions

Assignments will now have to be authorized by the Ministry of Economy.

Arrangement Obligations

The amendment also establishes an obligation to enter into an arrangement with local communities, Indigenous communities or Afro-Mexican communities for the superficial use of land and to pay those communities a minimum of 5% of the tax result declared pursuant to the income tax law.

In addition, the amendment further expands upon the existing requirement that concessions — and assignments of concessions — undergo a process of consultation with indigenous populations and transfers the cost of that process to the party applying for the concession or its assignment.

Additional Environmental Obligations

Additional environmental obligations include the provision of a guarantee issued through a trustworthy instrument — such as insurance, deposit, trust, letter of credit — for all prevention, mitigation and compensation measures resulting from the social impact of the mining activity. These also include a requirement that mining projects must recycle at least 60% of the water used in mining operations.

The amendment is unclear on whether these new obligations apply solely to new concessions or whether they may also apply retroactively to existing concessions.

Additional Circumstances for Concession Termination

New circumstances by which the Mexican government may terminate a concession include the failure to initiate works within one year of the concession date, not having the requisite quantities of water available for the project and any of the causes under Article 55, which include suspending production for

any period of time once commenced absent a court order or reasons of force majeure.

It is particularly unreasonable for the Mexican government to have the ability to terminate a concession due to a failure to commence the works within one year of the granting of the concession or a suspension of production for any period of time.

Notably, the amendment ignores the need for scheduled maintenance suspensions or other suspensions that may be advisable but do not meet the very high threshold of force majeure.

The amendment is unclear whether these new circumstances apply solely to new concessions or whether they may also apply retroactively to existing concessions.

Prohibition of Water Rights Transfer

The amendment also establishes a prohibition of water rights transfer for use in mining projects and new causes for termination of water rights.

The amended National Waters Law provides that water rights may be terminated for public interest reasons or because of any type of economic, social, environmental or other imbalance, but the law does not define any of these terms.

As such, because water availability is a requirement under the amendment, the Mexican government now can terminate mining concessions by revoking investors' water rights, in accordance with the new standards under the amended National Waters Law.

Particular Concerns for Existing Concessions

Even though the amendment should primarily apply to new concessions, some provisions of the amendment may — and likely will — affect existing concessions. Some of the main impacts include:

- A reduction in duration, per Article 15;
- A prohibition of assignments without previous authorization, per Article 23;
- A prohibition of extraction in natural protected areas without exceptions, per Article 14, which, as discussed above, raises significant concerns as to whether the Mexican government will revoke existing concessions granted in these areas, which is certainly a risk under the new legal regime applicable to mining concessions in Mexico;
- Potentially requiring the provision of a guarantee for the prevention, mitigation and compensation measures, per article 27;
- Additional causes for cancellation of an existing license, including failure to initiate the works within one year of the concession date, per Article 42, Subsection VI, and suspension of the production for any period of time once commenced, per Article 55, Subsection XIX; and,
- Restrictions on water use, per Article 27, combined with the Mexican government's new authority to terminate water rights pursuant to Article 29 Bis 4 of the National Waters Law, puts at risk all concessions of being targeted by AMLO's administration.

These are some general concerns for existing mining concessions. However, mining companies should engage in a case-specific assessment because it is not clear whether certain provisions of the amendment apply retroactively to existing concessions.

While many of the amendment's objectives are laudable — such as ensuring the availability of drinking water for the population and ensuring that mining projects comply with environmental regulations — the process through which the Mexican government enacted the amendment may result in costly and unwanted consequences.

The amendment constitutes a blank check for Mexican authorities to selectively pick and choose which miners will be permitted to continue and which miners will be subject to particular scrutiny, which may include the cancellation of their concessions, fines and potentially prison sentences.

This latest populist act from a populist government may be a recipe for disaster for both domestic and foreign investors in Mexico.

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