February 5, 2021

Constitutional Controversy 89/2020 (SENER's Policy)

At is has been extensively reported in domestic and international news outlets, on February 3, 2020, the Second Chamber of Mexico's Supreme Court of Justice (*Suprema Corte de Justicia de la Nación*) ("**SCJN**" or "**Court**") ruled on Constitutional Controversy (*Controversia Constitucional*) 89/2020 brought before the SCJN by Mexico's antitrust regulator: the Federal Commission on Economic Competition (*Comisión Federal de Competencia Económica*) ("**COFECE**").

The issue before the Court was the validity of the Order issuing the Policy on Reliability, Safety, Continuity and Quality in the National Electric System (*Acuerdo por el que se emite la Política de Confiabilidad, Seguridad, Continuidad y Calidad en el Sistema Eléctrico Nacional*), published in the Federal Register (*Diario Oficial de la Federación*) by the Ministry of Energy (*Secretaría de Energía*) ("**SENER**") on May 15, 2020 (the "**Policy**") on grounds that the Policy, among others: (**i**) prevented COFECE from exercising its constitutionally mandated duties to ensure free and competitive markets in the generation and supply of electricity markets; and (**ii**) established barriers to the entrance of new agents to the electricity generation and supply markets to the ultimate detriment of Mexican consumers.

In a 357-page opinion, Justice (*Ministro*) Luis María Aguilar Morales proposed to the Court the invalidation of certain key provisions of the Policy, while confirming the validity of other provisions claimed unconstitutional by COFECE. The opinion was approved through a majority vote with a single dissenting opinion.

In summary, the Court confirmed (recognized) the validity of provisions 1.2.4, 3.8.5, 4.17, 8.10 and 10.8 of the Policy.

Provision 1.2.4 establishes that one of the objectives of the Policy is the strengthening of Comisión Federal de Electricidad ("**CFE**"), while 3.8.5 provides that CFE may, in its capacity as transmission and distribution company, propose plans for the expansion and modernization of the national transmission grid and elements of the general distribution grid. In turn, provisions 4.17, 8.10 and 10.8 of the Policy deal with Related Services (*Servicios Conexos*) of intermittent power facilities for which generators using these technologies may be liable for.

On the other hand, the Court held that provisions 3.8.4, 5.4, 5.23, 5.7, 5.12, 5.12.1-12, 5.13, 5.15 (in the part referring to the interconnection feasibility study issued by CENACE), 7.1, 8.4 and 10.2 of the Policy are invalid.

The provisions held invalid include: (**i**) the requirement of an interconnection opinion from the National Center for Energy Control (*Centro Nacional de Control de Energía*) ("**CENACE**") to apply for a generation permit from the Energy Regulatory Commission (*Comisión Reguladora de Energía*); (**ii**) priority in the dispatch of generation facilities (*i.e.*, SENER's proposed hard rule on safety over efficiency);[1] (**iii**) CFE's role (in its capacity as a State productive enterprise and not merely in one or more of the phases of the electricity industry) in the designation of strategic projects and priority in the interconnection of these strategic projects; (**iv**) the ability to reject interconnection studies for clean (intermittent) facilities; and (**v**) CENACE's ability to discard efficient plants on the account of safety and reliability of the National Electric System.

While the ruling itself is great news for the renewables industry in Mexico as it generally confirms the rationale behind the injunctive relief obtained by generation companies from multiple lower federal courts during 2020, the analysis and arguments used by the SCJN in the opinion includes interesting points that will surely play an important role should Congress pass the bill of amendments to the Electricity Industry Law (*Ley de la Industria Eléctrica*) ("**LIE**") recently sent by President López Obrador on a preferential basis.

Key (Legal) Takeaways from the Ruling.

In addition to the actual ruling of the Court with respect to the Policy (summarized above), what follows are key points and considerations of the analysis made by the SCJN to arrive at the determination to invalidate or recognize the validity of certain provision of this Policy.

1. The Court dismisses the fact that the Policy did not undergo a full regulatory impact analysis on the account that: (**i**) the National Commission for Regulatory Improvement (*Comisión Nacional de Mejora Regulatoria*) granted SENER's request for exemption and further confirmed the inapplicability of the regulatory improvement procedure to SENER;[2] and (**ii**) the Policy does not constitute an

[1] *See*: paragraph 645 of the opinion.

[2] See: *Id.* at paragraph 11.

administrative act of general application but rather it determines the guidelines to be follows by other authorities in the subject matter.

Since the latter has been a focal point for certain companies who filed Constitutional actions (*juicios de amparo*) against the Policy, this determination from the Court may have ramifications for lower federal courts;

2. It is concluded that the Policy did not require what the Court calls a "reinforced argumentation" (*motivación reforzada*) because the Policy: (**i**) establishes policy lines (*i.e.*, principles, guidelines and provisions) that will impact the regulation of the electricity sector and with respect of which the Executive Federal Branch (*Ejecutivo Federal*), through SENER, has a "*relatively broad margin to establish such lines*";[3] and (**ii**) deals with an economic field and not human rights directly.[4] In its response to COFECE's claim, the Federal Executive Branch insisted that the Policy was not required to include this type of reinforced argumentation.

3. The Court examines and reviews the legislative history of both the 2013 Energy Reform and the 2013 Constitutional reform on competition matters that brought about COFECE's current legal nature and Constitutional duties. This point is particularly important because, while the Energy Reform opened the electricity sector to private investment, neither the amendments to Articles 25, 27 and 28 of the Constitution (defined below) nor the transitory provisions of the Energy Reform expressly mention that the services of generation and commercialization of electricity will be subject to free competition. For that matter, the Energy Reform does not contain the word "competition" in it.[5]

Despite the above, the Court reaffirms that to the extent an economic activity is not within the "strategic activities" carveout included in the Constitution and the Federal Law on Economic Competition (*Ley Federal de Competencia Económica*)[6] - generation and commercialization/supply of electricity activities are clearly outside

[3] *See*: *Id.* at paragraph 153.

[4] *See*: *Id.* at paragraph 168.

[5] *See*: the first paragraph of Article 4 of the LIE, which the Executive Branch is proposing to delete in the bill of amendments to the LIE sent to the Mexican Congress on January 29, 2021.

[6] *See*: Article 6 of the Federal Law on Economic Competition.

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of these "strategic activities" reserved to the Mexican State-, such economic activity will be subject to the full jurisdiction of COFECE and therefore free markets and competition rules shall apply;

4. In furtherance of point 3 above, the Court undertakes a detailed analysis of COFECE's standing and powers under the Political Constitution of the United Mexican States (*Constitución Política de los Estados Unidos Mexicanos*) (the "**Constitution**") with respect to its authority across all markets of the Mexican economy;

5. The Court reaffirms that the Constitutional reform of 2013 (*i.e.*, the so-called Energy Reform) establishes core principles with respect to the electricity industry, including but not limited to: (**i**) free and competitive conditions in the generation and commercialization sectors (*see* point 3 above); and (**ii**) the sustainability principle adopted by the Mexican State to transition away from a fossil fuel-based generation matrix;

6. In the case of free markets and competition, the Court concludes that a "*consumer human right*" is a Constitutional right against the "abuse of producers, industrials, merchants or businessmen of services, that prevent free competition in the market",[7] which means that competition and free market conditions are just as important as other Constitutional considerations such as SENER's discretion (which is not unrestricted and is required to comply with other Constitutional principles and laws) to dictate the energy policy of the country.

   Given that SENER's mandate to establish the country's "energy policy" is an undefined concept of the Energy Reform, the fact that the SCJN confirms that such discretion has its limits (*i.e.*, SENER has discretion to issue the Policy pursuant to the "*applicable legal framework, respecting the constitutional principles, particularly the objectives of the energy reform*")[8] is a positive development for other areas regulated by SENER or where SENER exercises influence, including but not limited to the minimum storage of refined products, import and export of hydrocarbons and refined products, among others; and

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[7] *See*: paragraphs 433 and 491 of the opinion.

[8] *See*: *Id.* at paragraph 515

7. The Court confirms that: (**i**) the sustainability principle of Article 25 of the Constitution establishes an obligation on SENER and the Mexican State to pursue the satisfaction of the goals established in the federal statutes dealing with climate change and energy transition;[9] and (**ii**) the human right to a healthy environment has a relationship with the Policy and therefore the Policy shall be consistent with this Constitutional right of the Mexican population.

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If you have any questions or comments on the matter, please contact us.
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[9] *See*: *Id.* at paragraph 315.