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CLIENT ALERT

AMLO sends a bill overhauling Mexico's power industry

Yesterday, September 30, 2021, President López Obrador submitted to the Mexican Congress a bill to amend the Mexican Constitution on Energy Matters (the “**Bill**”).¹ The Bill has been anticipated by the President following the lack of success of statutory and regulatory reform over the last couple of years. In essence, the Bill seeks to undo the changes introduced by the 2013 reform known as the “Energy Reform” and to some extent even previous reforms that first opened this sector to private investment: especially in the power sector.

In what is unarguably AMLO's most ambitious legal reform since he took office in 2018, AMLO's proposed amendment to the Political Constitution of the United Mexican States (“**Mexican Constitution**”) seeks to completely overhaul the current legal framework² of the electricity industry (and perhaps others) by:

- (i) transforming the generation, transportation, transformation, distribution and supply of electricity into an activity reserved to the Mexican State. This means that these activities are the responsibility of the Mexican State and therefore it chooses who participates in the industry;
- (ii) effectively making the Comisión Federal de Electricidad (“**CFE**”) a policy maker, power dispatcher (*i.e.*, National Electric System's operator), and regulator of the Mexican electricity industry at the same time;
- (iii) making CFE responsible for Mexico's “*Energy Transition*”, granting CFE broad powers and discretion to use Mexico's natural resources and property for such end;
 - a. given the role of natural gas as a traditional “transitional fuel” it is unclear whether CFE or Pemex will have additional or special rights regarding its

¹ The full name of the bill is: Bill with draft decree amending Articles 25, 27 and 28 of the Political Constitution of the United Mexican States on Energy Matters.

² The Bill restricts activities that were originally open to private investment since the early 1990s.





exploration, production and marketing. The Bill grants CFE broad powers over all natural resources and property in order to implement and carry out the Energy Transition.

- (iv) establishing a statutory cap of 46% on the private industry's participation in the electricity generation market;
 - a. This statutory cap would prevent private participation beyond this ceiling. In other words, CFE would be required by law to produce all electricity outside this 46%.
- (v) **disappearing (abolishing) the Energy Regulatory Commission and the National Hydrocarbons Commission.** In principle, all of the authorities, duties, powers and responsibilities currently handled by these regulatory bodies will be transferred to the Ministry of Energy;
 - a. The Energy Regulatory Commission (“**CRE**”) and the National Hydrocarbons Commission (“**CNH**”) exercise regulatory powers in the oil and gas industry as well. Moreover, in the case of the CNH, it acts as the representative of the Mexican State in all 100+ contracts entered into for the exploration and production of hydrocarbons with local and international companies (including Pemex). In the case of the CRE, it issues and regulates permits for storage, transportation, commercialization, distribution and retail sales on a plethora of products, including hydrocarbons (crude oil and natural gas), refined products and petrochemicals.
- (vi) changing the legal nature of CFE and Petróleos Mexicanos (“**Pemex**”) to public instrumentalities (*organismos del Estado*) instead of State productive enterprises (their current Constitutional legal status);
 - a. Among effects/impacts on procurement activities, corporate governance, ability to joint venture, among others, this may have an impact on the treatment and legal nature of any obligations (debt) assumed by Pemex and CFE.
- (vii) cancelling any existing generation permits and power purchase agreements executed with private parties;





- a. While the text of the Bill is limited to “generation permits” it is unclear whether other permits that may now be exclusively carried out by CFE will be revoked or terminated by operation of law.
- (viii) reincorporating Mexico’s only independent system operator (CENACE) to the CFE;
 - a. as part of the 2013, CENACE was spun-off CFE’s structure in order to create an independent system operator for the National Electric System. Now that CFE reassumes that role, CENACE goes back to CFE.
- (ix) mandating that all power produced by private parties be sold to the CFE at competitive costs; and
- (x) effectively nationalizing lithium deposits by disallowing concessions to explore for and produce lithium by private parties, considering the mineral “strategic” under the Mexican Constitution. Current concessions with actual exploration and discoveries of lithium (as verified by the Ministry of Economy) are excluded from this “nationalization”.
 - a. It is likely that the CFE will be responsible for directly conducting all activities related to lithium in Mexico.

The Bill is a Constitutional amendment only and, *if passed by Congress*, it proposes that the Mexican Congress will have 180 days to make changes to secondary legislation. This secondary legislation will have big task on determining or establishing, among many other issues:

- (i) the “transition” process of CENACE merging with CFE;
- (ii) treatment of distributed generation activities (small on-site producers who have the ability to supply electricity to the grid) and other activities that are not considered “generation” under current laws and regulations;
- (iii) termination of power purchase agreements executed with private parties;
- (iv) potential payment of compensations to affected parties;
- (v) new/amended organizational statutes of CFE and Pemex;





- (vi) amendments to the federal statutes dealing with the organization of the Federal Public Administration so that the Ministry of Energy may exercise all duties currently entrusted to the CNH and CRE; and
- (vii) amendments to the Mining Law (*Ley Minera*).

This is the first time since December 2013 that Articles 25, 27 and 28 of the Mexican Constitution are amended regarding natural resources and energy.

In addition to the foregoing changes, the transitory provisions of the Bill provide:

- That CFE will once again be a vertically integrated public instrumentality, without prejudice of maintaining certain existing affiliates and subsidiaries.
- Independent power producers will be allowed to continue selling power to the CFE but only for the capacity originally included in permits (not taking into account any excess generation).
- “Authentic” self-supply permits (in other words, permits who have not supplied power to third parties)³, Long Term Auctions and other generation facilities built since the 2013 reform may continue to produce electricity but for the exclusive sale to the CFE.
- CFE will acquire electricity produced by the private industry based on lowest production costs.
- Transmission and distribution rates will be set by the CFE.
- Clean Energy Certificates are abolished.

In order to pass a Constitutional reform such as the Bill, it will require a two-thirds majority of both houses of Congress and the majority of the local legislatures of the 32 Mexican states. At this point, it is unclear whether the Bill will gather the necessary support.

³ Please consider that the Government has argued that even the sales/supply of power to shareholders or members of these self-supply companies is in breach of both the former and current applicable law.



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ABOGADOS

We can expect strong opposition by the right-wing parties such as the PRI, PAN and others. However, smaller parties could make the difference in ultimately giving AMLO the necessary votes.

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This document does not constitute legal advice..

