

## Mexico | Bill for constitutional energy reform

**On September 30, 2021, was filed a presidential initiative to reform the constitution regarding electricity and natural resources; it is of relevance to highlight its most important aspects.**

The President of the Republic submitted to in the Chamber of Deputies the "Initiative to amend articles 25, 27 and 28 of the Political Constitution of the United Mexican States on energy and natural resources" (the "**Initiative**"), which contains 9 transitional provisions.

In order for the Initiative to be approved, it must have the favorable vote of two-thirds of the legislators present in plenary sessions of each of the Chambers, the Chamber of Deputies, and the Senate, and also be approved by a majority of the legislatures of the 32 States of the Mexican Republic.

Its most relevant aspects, are the following:

1. According to the Initiative, its purpose is to strengthen the Federal Electricity Commission (the "**FEC**"), through its vertical and horizontal integration in order for it to operate autonomously as a single governmental body, while eliminating the great majority of its affiliates and subsidiaries. The State, through the FEC, shall be responsible for the National Electronic System, which shall also oversee preserving energy security and sufficiency and the continuous supply of electricity to the entire population.
2. It sets the electricity production percentages of the public and private sectors. The FEC shall generate at least 54% of the electricity required in the country, while the private sector is only allowed to generate 46%. The latter shall have to do so under the terms and conditions that the FEC determines unilaterally.
3. The reform provides for the abolition of the Energy Regulatory Commission and the National Hydrocarbons Commission, transferring each and every of their attributions and authority to the Ministry of Energy. Likewise, it aims to eliminate the subsidiary companies of the FEC, concentrating in the latter all of their activities.
4. With the reform, the only way electricity can be acquired will be through the FEC, which in turn, will be able to obtain it from the private sector. In addition, the FEC will enter into long-term bilateral financial hedging contracts or the contractual instruments determined by itself, creating an exceptional public procurement regime.



5. In this sense, the reform proposal establishes that all activities related to the electricity sector: generation, conduction, transformation, distribution, and supply, will remain as strategic areas reserved exclusively for the Nation.
6. The National Energy Control Center will rejoin the FEC. The FEC will now determine the rates of the transmission and distribution networks and for end-users. Therefore, the FEC will monopolize the economic dispatch of all generation units, observing the reliability, continuity, and stability criteria.
7. The "self-sufficiency" scheme of electrical energy will not be acknowledged. The generation of electric power under the "self-sufficiency" and "independent energy producer" schemes shall be considered within the maximum limit of 46% of participation of the private sector in the generation of electricity.
8. The reform establishes that from the moment it becomes effective, the electricity generation permits granted, the electricity purchase contracts with the private sector, and all the permit applications pending resolution will be canceled.
9. Clean energy certificates (known by their initials in Spanish as CELs) will be eliminated.
10. All references to productive companies of the State dedicated to the exploration and extraction of hydrocarbons will be eliminated.
11. The Initiative provides for the non-granting of more concessions on lithium or strategic minerals due to their importance within the energy transition process.
12. If approved, the legislative branch will have 180 days to issue the laws regulating this reform proposal.

In reality, the alleged strengthening of the FEC amounts to the creation of a risky state monopoly contrary to the national Common Good, which avoids the excesses of both individualism and statism. On the other side, eliminating the autonomous agencies in this sector, undermines pluralism and goes against the need to govern with technical and non-political criteria in an area so sensitive to the country's economy. In light of the above, it is fair to affirm that a reform aiming to modernize and be progressive would require having the national Common Good as fundamental guideline.

The Initiative, by providing the cancellation of permits and contracts unilaterally, may cause several non-compliance lawsuits, for large amounts against the Mexican State, and it could also possibly violate the USMCA. The idea of limiting the private parties as proposed by the Initiative, will incur in the assumptions of chapter 22 of the USMCA regarding State-owned Companies and Designated Monopolies, in its article 22.4 Non-Discriminatory Treatment and Commercial Considerations, since the control of the State of certain sectors, particularly concerning energy, will give preferential treatment to those that were not created under the Treaty.



Something similar will happen with the proposed reserve for the exploitation of lithium, given that it was not one of the previously established and agreed monopolistic activities of the USMCA; in fact, this activity will be against economic competition among the proposing State and the rest of the Parties, that will be limited by such proposal, which is prohibited in the same provision, in its section two, subsection (d), regarding designated monopolies.

Likewise, the provisions of the Initiative violate the international treaties regarding environmental protection (such as the International Covenant on Economic, Social and Cultural Rights; the Protocol of San Salvador or the United Nations Climate Change Conference, to name some of the most relevant), and affect the principle of the progressive nature of the human rights since, in the case of the Mexican energy market, in the last decade a costly transition towards non-polluting energies and technologies had started (an example of this was the incorporation of the CELs, which the Initiative aims to eliminate).

The Initiative may represent risks for the Mexican State, since it may discourage investors, both national and foreign, and may cause their withdrawal from the Mexican energy market, and promote the submission of lawsuits and claims, due to their violated rights, through the national and international legal instruments, as applicable.

It should be noted that the reform proposal, if approved, will undoubtedly have serious repercussions globally, causing the set-up of several investment arbitrations, in which the Mexican State would be sued. This would be the case of those companies and individuals that have acquired infrastructure to generate energy and sell it to the FEC or self-generate their power and that, at the time the Initiative is approved, will undoubtedly lose those rights.<sup>1</sup>

The elimination of the clean energy certificates represents a severe setback in environmental matters. Moreover, the Initiative's content goes against the currently prevailing ecological policies in the world to face climate change that threatens the survival of all and it is also against the progressive and increasingly frequent incorporation of ESG criteria, particularly for those listed in the stock market.

It is fundamental to analyze further the rights of all kinds that would be violated with the approval of the reform and the consequences that it would bring for the State and for the Mexican Nation and its citizens.

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<sup>1</sup> It is relevant to mention that the Mexican Bar Association (Barra Mexicana, Colegio de Abogados, A.C.), has requested the legislators not to approve the current reform in its terms, since the former considers necessary to create forums to debate the technical and legal feasibility of the Initiative.

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