

MAYER • BROWN

Preparing Mexico's Legal Framework for Energy Markets

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UPSIDE DOWN

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How to introduce energy markets?

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- ❖ The starting point for the creation of markets is the introduction of the legal figure of a private oil mineral interest into all links of the energy value chain.

Energy Markets in Mexico

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- ❖ Mexico's Energy Ministry (SENER) annually publishes series on the outlook for the “market” of diverse energy products: natural gas, LPG, electricity—even crude oil

**Prospectiva del Mercado
de Gas Licuado de Petróleo
2010-2025**

**PROSPECTIVA DE PETROLÍFEROS
2007-2016**

**Prospectiva del Mercado
de Petróleo Crudo
2010-2025**

But none of this is real

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- ❖ Energy markets today do not exist in Mexico
- ❖ What exists is a state-run logistics system in which the consumer is charged a government-set fee for the right to utilize state-owned, energy property
- ❖ The system represents an enormous opportunity cost for the economy in general and Mexico's NOC in particular.

Mexico's constitution has needed a good editor

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ARTÍCULO 27

1ª Reforma DOF 10-01-1934
2ª Reforma DOF 06-12-1937
3ª Reforma DOF 09-11-1940
4ª Reforma DOF 21-04-1945
5ª Reforma DOF 12-02-1947
6ª Reforma DOF 02-12-1948
7ª Reforma DOF 20-01-1960
8ª Reforma DOF 29-12-1960
Fe de erratas DOF 07-01-1961
9ª Reforma DOF 08-10-1974
10ª Reforma DOF 06-02-1975

ARTÍCULO 28

1ª Reforma DOF 17-11-1982
2ª Reforma DOF 03-02-1983
3ª Reforma DOF 27-06-1990
4ª Reforma DOF 20-08-1993
Fe de erratas DOF 23-08-1993
5ª Reforma DOF 02-03-1995

History Lesson

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- ❖ From 1884-1917 the legal figure of a private oil mineral interest gave subsoil mineral rights to the owner of the surface property.
- ❖ From 1917-1958 the legal figure of a private oil mineral interest was embedded in terms and conditions to be established by the state.
- ❖ On Nov. 29, 1958, the Petroleum Law (in Article 6) eliminated the legal figure of a private oil mineral interest.

Constitutional Article 27

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- ❖ Article 27 in the original text changed the legal figure of a private mineral interest from absolute to conditional.
- ❖ There were no commercial restrictions.

En los casos a que se refieren los dos párrafos anteriores, el dominio de la Nación es inalienable e imprescriptible, y sólo podrán hacerse concesiones por el Gobierno Federal a los particulares o sociedades civiles o comerciales constituidas conforme a las leyes mexicanas, con la condición de que se establezcan trabajos regulares para la explotación de los elementos de que se trata, y se cumplan con los requisitos que prevengan las leyes.

Constitutional Article 28

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- ❖ The original text of Art. 28 does not mention petroleum at all.
- ❖ The notion of “*Petroquímica Básica*” is not based on chemistry, but on a policy distinction that creates a category of “strategic product,” which has no constitutional basis.

Art. 28.—En los Estados Unidos Mexicanos no habrá monopolios ni estancos de ninguna clase; ni exención de impuestos; ni prohibiciones a título de protección a la industria; exceptuándose únicamente los relativos a la acuñación de moneda, a los correos, telégrafos y radiotelegrafía, a la emisión de billetes por medio de un solo Banco que controlará el Gobierno Federal, y a los privilegios que por determinado tiempo se concedan a los autores y artistas

Constitutional Article 134

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- ❖ The Government Procurement Clause has been strengthened since 1917, but not enough.
- ❖ In addition to PRICE, QUALITY, FINANCING, TIMELINESS, the text should be amended to include reference to the BUSINESS MODEL that provides the best overall positive externalities.
- ❖ A new clause is needed to consolidate all constitutional references to PETROLEUM.

Article 6 of the Petroleum Law

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- ❖ The 1958 revised text of Article 6 of the Petroleum Law lacks a constitutional foundation.
- ❖ TO BE REVISED: *The commercial exploitation of hydrocarbons will be carried out in accordance with the precepts and principles set forth in Constitutional Article 128, as well as by the terms and conditions established by pertinent dispositions.*

Doctrine of First-Hand Sales

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- ❖ The doctrine of “first-hand sales” (VPM) was introduced, as a mere clause, in the Petroleum Law of 1958.
- ❖ We find no constitutional basis for this doctrine.
- ❖ This doctrine, along with the elimination of the legal figure of a private oil mineral interest, has caused immense value destruction in the energy sector.

Doctrine of “Basic Petrochemical”

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- ❖ The doctrine of “basic petrochemical” was introduced, as a mere clause, in the Petroleum Law of 1958.
- ❖ We find no constitutional basis for this doctrine.

Other needed changes to the legal framework for a market dynamic

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❖ CNH Establishment Act of 2008

- Revise the mandate: *The Commission is responsible for providing public oversight of the assessment and exploitation of the national petroleum patrimony.*
- *Leases for exploration shall be issued by its authority.*
- *Leases confer a temporary oil mineral interest to a lease-holder that is contingent on the fulfillment of the terms and conditions in each case.*

Summary: What has to change in the Mexican legal framework?

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- ❖ Eliminate constitutional distinction between “strategic and priority” areas of the economy
- ❖ Eliminate the doctrine of “First-Hand Sales”
- ❖ Eliminate the doctrine of “Basic Petrochemical”
- ❖ Eliminate commercial clauses in Constitutional Article 27
- ❖ Eliminate the commercial restrictions of Article 6 of the Petroleum Law
- ❖ Strengthen Constitutional Article 134, adding a clause regarding petroleum
- ❖ Give market orientation to legal mandates of CRE, CNH, Pemex and CFE.

Anticipated results with the creation of a conditional, private oil mineral interest

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Benefits

❖ Upstream

- Economic incentives for joint ventures with Pemex
- Economic incentives for major IOC participation
- Development of DW, conventional and non-conventional fields

❖ Midstream

- Economic incentives for wellhead-to-market pipelines
- Economic incentives for gas and product storage

❖ Downstream (with elimination of doctrine of First-Hand Sales)

- Economic incentives for investments in refining, storage and distribution



Por su atención, muchas gracias

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