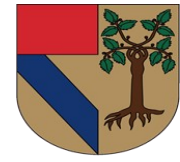




MEXICO UPDATE



UNIVERSIDAD
PANAMERICANA

Legal Consequences For The Mexican Energy Sector Due To COVID-19

Edmond Grieger

In an effort to diminish the effects of the pandemic generated by the SARS-CoV-2 virus, on March 31, 2020, the Mexican Ministry of Health issued a resolution ordering the suspension of all activities considered non-essential (the “**Activity Suspension Agreement**”).¹ Later, on April 21, 2020, the Activity Suspension Agreement was modified to establish that the suspension of non-essential activities last until May 30th, 2020.²

The Activity Suspension Agreement excluded the oil and electricity sectors, which meant that public entities such as the Ministry of Energy, the National Commission of Hydrocarbons (“**CNH**”), the Security, Energy and Environment Agency (“**ASEA**”), the National Energy Control Centre (“**CENACE**”) and the Energy Regulatory Commission (“**CRE**”) could continue with their activities. However, after the publication of the Activity Suspension Agreement, these governmental entities published resolutions declaring the suspension of legal and procedural terms until May 30, meaning that any request or writ submitted within said suspension would be considered filed until June 1, 2020.

Oil market and the impact on supply

Due to the COVID-19 pandemic and the price war between the Organization of the Petroleum Exporting Countries (“**OPEC**”) and Russia, oil prices have fallen more than 60% worldwide since the beginning of 2020. Therefore, on April 12, the OPEC+ alliance agreed to reduce oil output by 9.7 MMbd.

As a result, Mexican president Andres Manuel Lopez Obrador announced the temporary closure of oil wells until crude oil prices rose, and afterwards, he announced the rehabilitation of several oil wells and the construction of the *Dos Bocas* refinery. These actions, alongside the critical economic situation of *Petroleos Mexicanos*, have complicated the oil outlook in the country.

¹ *Agreement establishing extraordinary actions to address the health emergency by the SARS-CoV2 virus*. Published in the DOF, on March 31, 2020

² *Agreement that modifies the term that was established to attend the health emergency generated by the SARS-CoV2 virus*. Published in the DOF, on April 21, 2020

In the meantime, the Federal Electricity Commission (“**CFE**”) and other governmental entities in the energy sector, as well as affiliated entities like CF Energia, have continued to call for bidders for the supply of natural gas and liquefied petroleum gas, which is a good sign for the market.

Under the Regulations of the Hydrocarbons Law, fuel supply to end users could be legally suspended, as a result of the pandemic fortuitous cause or force majeure due to COVID-19. However, it is likely that supply will continue to be guaranteed according to the Activity Suspension Agreement, despite a likely significant reduction in the price of gasoline/diesel in the country.

In any case, under the fortuitous cause or force majeure due to the COVID-19 pandemic, individuals and companies may look to the CRE for remedies if they suffer damages arising from decreased sale or distribution of gasoline/diesel, lack of quality in these products or the impossibility of complying with contractual obligations as permit holders for commercialization, storage transportation or public supply of hydrocarbons.

Uncertainty for renewable energy sources

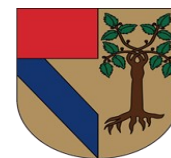
The Activity Suspension Agreement declared the electrical sector as an essential activity, therefore power supply should not be interrupted and the competent authorities shall take all the necessary measures to guarantee that the activities related to the generation, transmission and distribution of electricity continue on a regular basis.

However, on April 29, the CENACE published a highly questioned "Agreement to guarantee the efficiency, Quality, Reliability, Continuity and security of the

DISCLAIMER: The materials and information in this newsletter do not constitute legal advice. MEXICO UPDATE is a publication made available solely for informational purposes and should not be considered legal advice. The opinions and comments in MEXICO UPDATE are those of its contributors and do not necessarily reflect any opinion of the ABA, their respective firms or the editors.



MEXICO UPDATE



UNIVERSIDAD
PANAMERICANA

National Electric Grid, under the epidemic caused by the disease SARS-CoV2 virus” (“Electrical Continuity Agreement”). This agreement –although not mandatory since it has not been published in the Federal Official Gazette (“DOF”)–allows the CENACE to take measures to guarantee the continuity of the National Electric Grid during the COVID-19 pandemic and the decrease of electrical consumption.

Among other things, under this resolution, the CENACE can interrupt the pre-operational tests of the photovoltaic and wind power plants, which are in the process of initiating commercial operations, and can deny new requests to carry out these tests. In connection with this provision, CENACE alleged that the intermittence of these renewable sources compromises the continuity and reliability of the National Electric Grid. Several entities, including the Business Coordinating Council, have argued that the CENACE does not have an authority to issue such a resolution, because under article 132 of the Electricity Industry Law, the CRE is the competent authority to issue regulatory agreements and not the CENACE.

Additionally, the Electrical Continuity Agreement is ambiguous with regards to its duration, as it does not clearly specify when the measures will be lifted, thus leaving open the possibility for the CENACE to maintain such measures even after the COVID-19 pandemic is over.

The Federal Economic Competition Commission has recently advised on the risks of the Electrical Continuity Agreement,³ warning that it may indefinitely prevent new wind and photovoltaic power plants from participating in the market and may generate uncertainty about the possibility of dispatching for wind and photovoltaic plants that already operate in the market and that usually have lower production costs than conventional plants.

On May 12, the National Commission of Regulatory Improvement informed the Ministry of Energy that the Electrical Continuity Agreement must be subject to the regulatory improvement procedure as well as a Regulatory Impact Analysis, given that the regulatory proposal generates compliance costs for individuals.⁴

If the Electrical Continuity Agreement were to be published in the DOF in the form in which it was drafted, it would deter investment in renewable energy in Mexico. In addition, foreign investors and their affiliates, from States with which Mexico has signed a Bilateral Investment Treaty or a Free Trade Agreement with an Investment Chapter, might submit claims.

The Mexican Association of Solar Energy signaled that Mexico may lose 6,400 million USD of direct investment in the electrical sector in 2020. Therefore, these restrictive measures may result in not only an increase in the price of electricity, but also in reduced international investment and an even more dramatic collapse in the national economy.

DISCLAIMER: The materials and information in this newsletter do not constitute legal advice. MEXICO UPDATE is a publication made available solely for informational purposes and should not be considered legal advice. The opinions and comments in MEXICO UPDATE are those of its contributors and do not necessarily reflect any opinion of the ABA, their respective firms or the editors.

³ COFECE issues recommendations regarding the CENACE Agreement. Published by the COFECE, on May 7

⁴ Writ issued by CONAMER on May 12 forwarded to the Ministry of Energy