
*The Ministry of Energy modifies the terms
for the strict legal separation of the Federal Electricity Commission*

On March 25 2019, the Federal Energy Ministry ("SENER") published in the Federal Official Gazette the Agreement that modifies the terms for the strict legal separation of the Federal Electricity Commission ("Agreement"), which aims to modify diverse guidelines and terms for the operation of the Subsidiary Productive Companies and Affiliate Companies of the Federal Commission of Electricity ("CFE").

In this regard, it is worth mentioning that the referred Terms for the strict legal separation of the CFE ("Terms"), were issued on January 11, 2016 as a result of the constitutional reform in energy matters with the objective of diversifying CFE's activities in different companies, which would allow CFE's participation in the electricity industry's activities under market conditions and with the purpose of promoting open access and the efficient operation of the electricity sector.

In this regard, within the main arguments that SENER used to issue the Agreement, is that the Terms did not achieve their purpose due to: (i) an increase of costs and lack of operational efficiency in CFE; (ii) failure to consider regional organization of generation assets; (iii) additional complexity in CFE's administrative processes, among others.

Therefore, the most relevant aspects of the Agreement are:

1. The Agreement modifies the minimum of four Subsidiary Productive Companies ("SPC") and Affiliate Companies ("AC") that CFE must have for generation activities and establishes only the requirement of having "the necessary SPC and AC ". CFE currently has six SPC responsible for energy generation activities, with what is established in the Agreement, we understand that the intention is to reduce the number of SPC.
2. Grants authority to SENER in order to directly reorganize CFE generation SPCs, authority that was previously the sole responsibility of CFE's Board of Directors.

3. Eliminates the possibility of CFE Transmisión and CFE Distribución to associate or to execute contracts with other SPCs, ACs and individuals in order to carry out joint participation schemes in the provision of the Electric Power Transmission and Distribution Services, however the possibility to execute other type of contracts remains open.

In this regard, it is worth noting that the foregoing would be inconsistent with the provisions of Article 27 of the Political Constitution of the United Mexican States, which establishes that contracts may be entered into with individuals in relation to public service transmission and distribution of electricity.

4. It allows for CFE companies to coordinate in order to implement technologies that reduce operating costs, allowing CFE to give preference to the application of technologies for the generation of electric energy through fossil or nuclear sources.

5. Establishes the obligation of the Board of Directors and committees, the CEO and the employees of CFE to "privilege the efficiency of the electric sector, that translates into lower prices for the end users", allowing CFE to establish power plants by fossil or nuclear sources under the argument of the sector efficiency and price reduction.

6. It limits the participation of the Board of Directors and committees, the General Director and the employees of CFE in strategies that coordinate the installation or operation of power plants that intentionally induce the increase of the marginal costs of energy in the medium and long term. From the above, it can be interpreted as a restriction for the participation of CFE, its SPC and AC in the Long and Medium Term Auctions.

7. CFE Distribución may directly carry out electricity commercialization activities through a Business Unit different from the rest of the Distribution activities and it may temporarily or permanently share employees with other CFE companies.

8. Revokes the prohibition that SPC and AC generation companies had in order to not share information related with the operation, planning, maintenance and commercial strategy of power plants to the other

SPCs and ACs that carry out generation or commercial activities, as well as to any other person or company that performs such activities. Allowing these economic agents to obtain an advantage over their competitors in the market.

9. Establishes that CFE must submit to SENER the new proposal for reassigning assets and generation contracts of the SPC and AV generation companies, within 60 calendar days after the publication of the Agreement. With this modification, the assignment of assets and contracts published on November 4, 2016 for the SPC and AV generation companies will be reversed.

Consequently, we consider that with the issuance of the Agreement, CFE seeks to reorganize its generation assets in order to generate more favorable market conditions for CFE in several activities within the power industry.

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Sincerely,

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Mexico City, April 1, 2019.