

## **Takeaways and Implications of Mexico's New Energy Policies.**

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In the midst of major political and legal controversy, on May 15, 2020 the Mexican Ministry of Energy (*Secretaría de Energía* or *SENER*) published in the Federal Official Gazette the “Policy of Reliability, Safety, Continuity and Quality of the National Electric System” (*Política de Confiabilidad, Seguridad, Continuidad y Calidad en el Sistema Eléctrico Nacional*) (the “SENER Resolution”), a set of rules that SENER contends is needed to preserve the national grid’s reliability. The SENER Resolution expands on certain rules and guidelines that were broadly laid out by the Mexican National Center for the Control of Energy (*Centro Nacional de Control de Energía* or *CENACE*) on April 29, 2020 (the “CENACE Resolution”) in a similar but narrower resolution intended to ensure the efficiency and reliability of the national grid.

The industry and its players have considered that both the SENER Resolution and the CENACE Resolution impose undue burdens and severe limitations on new projects in the sector and particularly, to clean energy projects, such as solar and wind. Regardless of the very public pushback to both Resolutions, the Federal Government has defended the necessity of these new regulations, citing numerous reasons to justify them in the Resolutions as well as in public appearances from public officials, going from emergency reasons (COVID-19 pandemic and subsequent lower demand) to technical reasons (congestion and renewables’ intermittency), and political reasons (the shrinking role of the state-owned entity in the Mexican electricity generation portfolio). As the full list of ramifications of these Resolutions is still vague, the uncertainty in the Mexican electricity sector for all of its value chain will continue to grow, along with the potential legal implications of the measures taken by the Mexican authorities through these regulations. Below we briefly analyze some of these short-term impacts as the situation continues to develop.

### **I.- Main Takeaways from SENER and CENACE Resolutions.**

#### *a) CENACE Resolution.*

The CENACE Resolution was issued under the focal reasoning that the COVID-19 pandemic had brought down a decrease of electricity demand in the country and as such, priority should be given to reinforcing the reliability of the power grid, concluding that the intermittent nature of solar and wind energy power plants affected such reliability and the quality of the power grid.

As a consequence of the foregoing, CENACE resolved, among other matters, to: (i) provide that must-run power plants would be designated in certain regions of the national electric system; and (ii) temporarily suspend all pre-operative testing for intermittent solar and wind power plants and new projects of such sources. This Resolution is all but clear and leaves quite some room for interpretation on the criteria and mechanisms that will be employed by CENACE to enforce it, fostering the suspicions that the country’s independent system

operator would be acting discretionally in favor of the CFE, the state-owned electricity utility, and its conventional (non-intermittent) power plants.

*b) SENER Resolution.*

Following the industry's concern regarding the vagueness and potential legal implications surrounding the CENACE Resolution, SENER published the SENER Resolution, reinforcing the provisions of the CENACE Resolution and establishing new rules which in some cases clash with existing regulations. The SENER Resolution is also purportedly aimed to guarantee the reliability of the national electric system and of the electricity supply, by modifying some of the guiding principles of the Mexican electricity market, the operation of permitted activities and the role of the state-owned utility.

Through this Resolution, SENER introduced a number of provisions that have a tremendous impact in the operation of the electricity sector in Mexico, among them: (i) allowing CFE, which in terms of the Electric Industry Law ("LIE") is supposed to be another player in a free market, to have a prominent role in the design and definition of strategic infrastructure projects of the sector, and indirectly in the granting of new generation permits; (ii) imposing new requirements for the granting of electricity generation permits and setting stricter rules for the compliance with the terms and deadlines set forth in them and for their assignment, transfer and/or liens levied upon them; (iii) creating a new interconnection feasibility study that shall be carried out by CENACE and which shall preclude any power generation permit, and in which CENACE will be enabled to evaluate and potentially discriminate against new clean energy power plant projects based on location of the projects, grid congestion, scattering of clean energy power plants, weather, reliability and use of conventional power plants, among other broad concepts; (iv) creating new ancillary services (*servicios conexos*) to be provided by generators and aimed to ensure the reliability of the national grid and dispatch safety by functioning as backup capacity for intermittent clean energy generators; (v) disallowing the capacity (*potencia*) credit to intermittent clean energy power plants.

## **II.- Implications and Consequences of Resolutions.**

Listing and predicting the full array of implications and consequences that may arise from these Resolutions is an impossible task, as it is undeniable that there is an ongoing analysis of the technical, operational, financial and legal challenges that these new rules pose against existing projects and projects in the pipeline in Mexico. Below is a list of the most important legal implications that have already begun to come to surface in some fashion and which will continue to develop in the weeks to come if the Mexican Government does not reconsider its position and revokes or amends the Resolutions.

*a) Diplomatic Tension and International Treaties' Protection.*

Two weeks after the CENACE Resolution was issued and ill-received by the vast majority of local and international participants of the Mexican electricity market, the publication of the SENER Resolution came as the last straw in the perceived crusade by Mexico's current Federal administration against renewable energy projects, foreign investors and disregard against the free-market rules of the electricity sector. In response to the CENACE Resolution, the Canadian Government and the European Union published letters sent to SENER hours prior to the publication of the SENER Resolution, voicing their concern with respect to the perceived restrictions laid out by CENACE to clean energy projects which could affect companies from Canada and from the European Union, respectively. Mexico's President issued political remarks with respect to such letters and SENER has vowed to answer accordingly.

In spite of any answer which may come from SENER or CENACE, affected foreign companies and their investors could look for the protection provided by the applicable bilateral international treaties, as well as multilateral international treaties such as the North American Free Trade Agreement (NAFTA), the United States Mexico Canada Agreement (USMCA), the Comprehensive and Progressive Agreement for Trans-Pacific Partnership (CPTPP), and the investor-state dispute settlement chapters contained therein.

*b) Amparo lawsuits and local challenges.*

A staple of Mexico's legal framework and judicial system, the *amparo* constitutional protection lawsuit, can be filed by any affected party to challenge the implementation of the Resolutions. As of this moment, multiple *amparo* lawsuits have been publicly filed against the CENACE Resolution and federal courts have granted provisional suspension of the implementation of such Resolution in favor of at least twenty-three plaintiffs, as of the moment of publication of this article.

It is widely expected that the SENER Resolution will be challenged in federal courts through *amparo* lawsuits which will try to have the effects of such Resolution permanently suspended and revoked. Now, as the SENER Resolution encompasses a larger audience with the provisions it introduced, plaintiffs of these *amparo* lawsuits could include electricity generators, basic suppliers, qualified suppliers, electricity marketers, self-suppliers, and distributed generation users, among others, who, in turn, could dispute the constitutionality of the Resolution based on potential violations to constitutional rights and existing regulations. As previously stated, the Resolution at best overlaps and at worst directly contradicts the LIE and its regulations, including the open-access rule, the role and distribution of authorities among CENACE, SENER and the Energy Regulatory Commission (*Comisión Reguladora de Energía* or *CRE*). These new rules would also contradict and hinder the compliance with energy transition laws and climate change laws. Likewise, the process for its publication also contradicts public consultation laws, among other arguments that could be structured to challenge the constitutionality of the Resolution.

*c) Antitrust Matters.*

Both Resolutions indirectly (CENACE) or directly (SENER) provide for a prominent role of CFE in several activities, in clear detriment of the free competition principle of the Mexican electricity market. Having the CFE, already the dominant player of the market, influence the decision on which projects may be interconnected or not to the national grid, presents a hard antitrust challenge to both Resolutions.

Prior to the publication of the SENER Resolution, the Mexican Federal Competition Commission (*Comisión Federal de Competencia Económica* or *COFECE*) issued a non-binding opinion in which it argued that the CENACE Resolution violated the free competition rule and dispatch rules set forth by the LIE, even though it was not entirely clear that CFE would be directly benefited by CENACE. The SENER Resolution is even more straightforward in the role it envisions that CFE should have, which, in line with the COFECE's previous opinions, would result in a clear and direct violation of free completion, economic dispatch and open-access rules.

*d) Force Majeure.*

Force majeure provisions have recently come to the spotlight as a result of the COVID-19 pandemic (for our review of such concept in Mexico, please [read our article here](#)), and for this particular scenario, a case-by-case analysis should be carried out to identify the potential impacts that both Resolutions will have on existing agreements, such as the power purchase agreements or PPAs entered into by electricity generators, suppliers

and consumers, as well as the financing and security agreements entered in connection with generation projects and in particular, clean energy projects.

These Resolutions, which depending on the language of the applicable provisions, could become force majeure events that could significantly impact the viability of the projects or their current status. Cash flow of new and existing projects could be impacted if the Resolutions and the new dispatch rule prevail, the interconnection feasibility study for new projects would present an additional hurdle that could derail the project, and the inexistence of capacity credit for clean energy intermittent projects would diminish their value considerably.

*e) Changes to Operation of the Market and to the Electricity Sector.*

Both Resolutions have a tremendous impact in the electricity market in Mexico, and while the CENACE Resolution is supposedly intended to have a provisional effect while the COVID-19 pandemic situation persists, the SENER Resolution was issued with the intention to overhaul the operation of the market in the particular instances amended by such regulation.

Every step of the implementation of these Resolutions should be paid special attention by all market participants. Mexican Courts and possibly COFECE may further shape these Resolutions, but unless the Federal Government backtracks completely from these regulations, these changes will be in some way introduced in the legislation and shall be complied by the participants.

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