



Reform of the Mexican Energy Sector

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Commissioner
Energy Regulatory Commission
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*The opinions and facts are sole responsibility of the speaker

During 2013 and 2014, Mexico enacted much needed market reforms ...

Implementing Legislation introduces new elements in every aspect of the energy sector (9 new laws)

1. Hydrocarbons Act
2. Electricity Industry Act
3. Geothermal Energy Act
4. Productive Enterprises of the State Act
5. Energy Regulatory Commissions Act
6. HSE Agency Act
7. Mexican Petroleum Fund Act
8. Fiscal Decree
9. Budgetary Decree

Modifications of 12 Laws: the rest of the legal system is harmonized with the reform (Examples)

The reform of the Foreign Investment Act removes entry barriers to foreign companies

There is a new tax regime oriented to incentivize oil and gas investments

The reform of the Public Administration Act provides that the Regulatory Bodies will have Independent Status

... which have already been enforced in all levels of legal instruments ...

Energy Reform is the 1st “Structural” Reform to be approved in 70 years in this sector

... now that oil and gas energy markets have been liberalized, they are not longer isolated from competition and regulation

Constitutional Reform (December, 2013)
Articles 25, 27 & 28

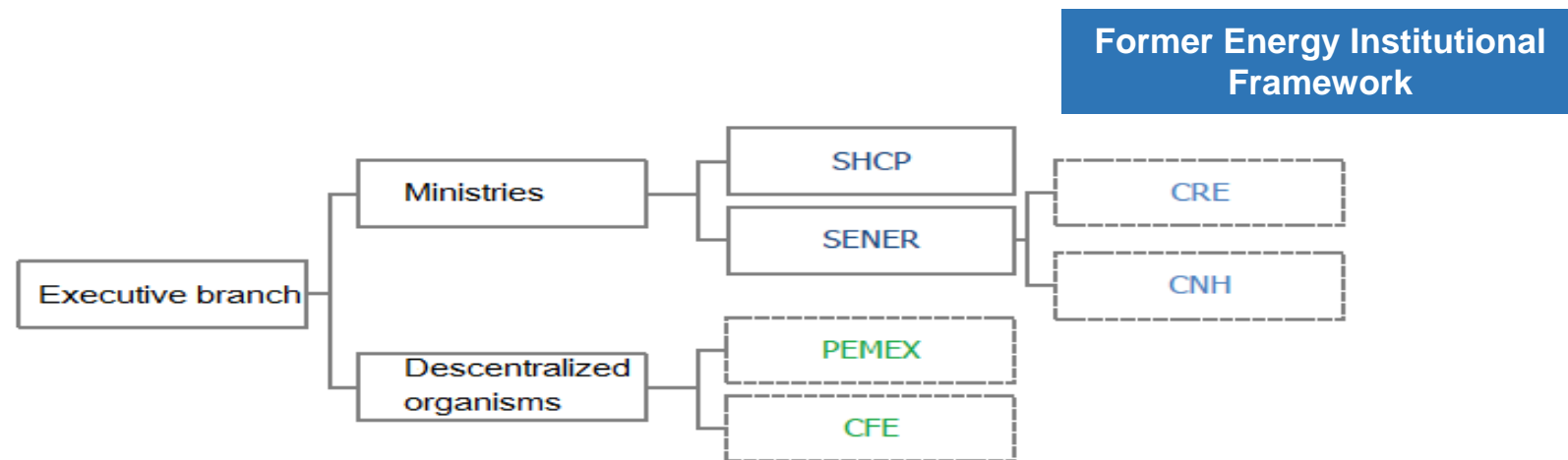
Federal laws (August, 2014)
12 new laws, 9 ammended

Executive regulations (October, 2014)

Administrative regulations
(ongoing)

Midstream and Downstream
Hydrocarbons activities are
liberalized (p.e. transportation,
distribution, refining, processing,
retail)

... and have imposed a new government structure to create a framework in line with market liberalization.



Keys:

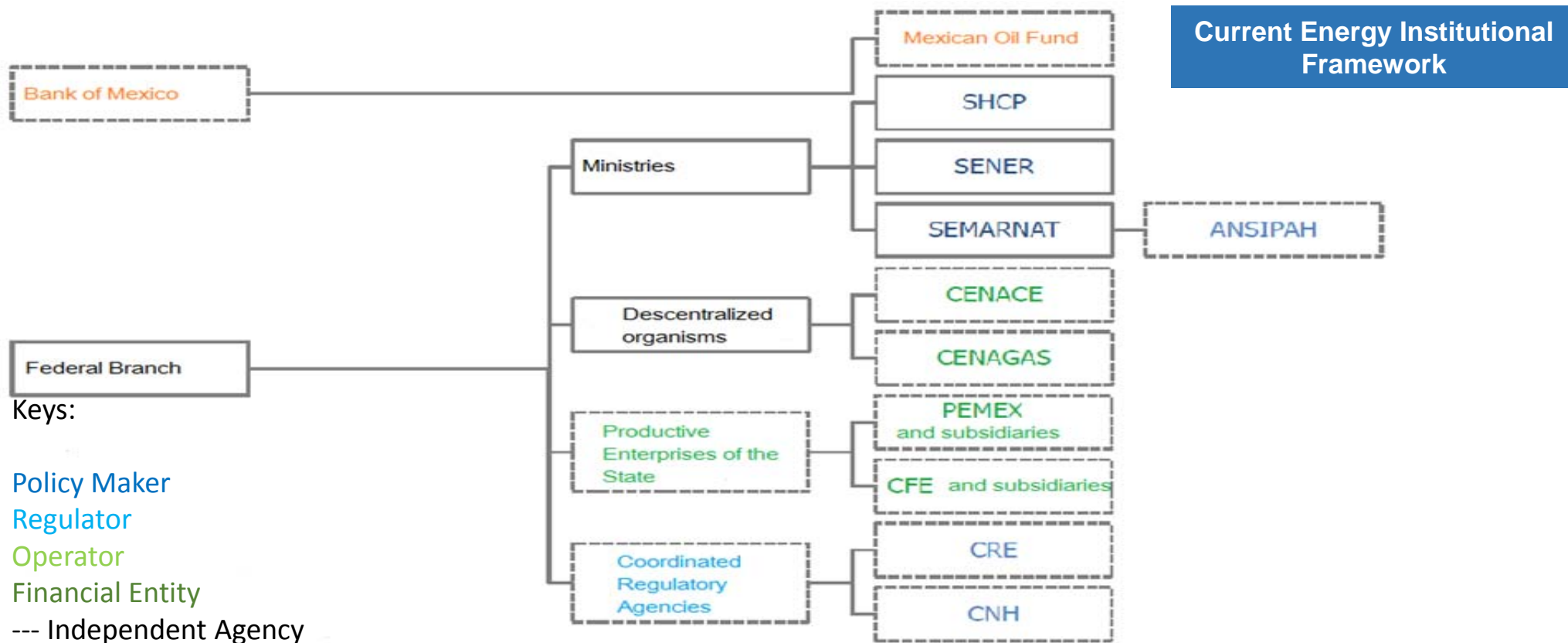
Policy Maker

Regulator

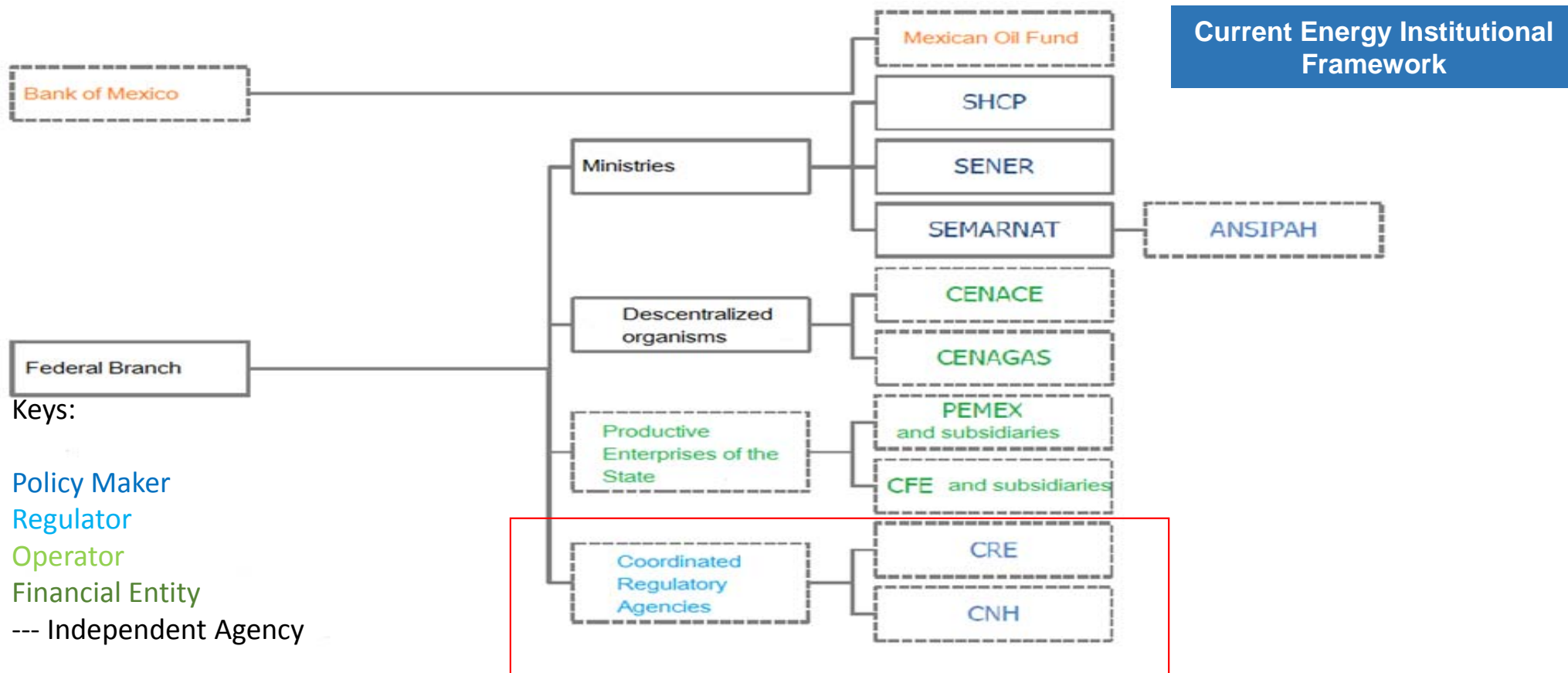
Operator

--- Independent Agency

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Upstream

INDEPENDENT REGULATORY AGENCIES HAVE BEEN CREATED

- Constitutional Powers and Authority
- Independence from central government
- Vested with financial independence
- Government board consists on 7 Commissioners appointed by the President and confirmed by the Senate.
- Staggered board with an appointment of 7 years for each Commissioner.
- Every act and decision is subject to the principle of maximum transparency.
- Subject to strict contact and transparency rules.



Electricity
+
midstream
and
Downstream

CRE is vested with relevant regulatory powers in the hydrocarbons downstream industry...



ECONOMIC REGULATION

- Granting of permits for comercialization, transport, storage, distribution and supply;
- Open acces to transport and distribution pipelines and storage facilities;
- Tariff and service regulation;
- Performance regulation;
- Distribution zones bidding processes;
- Own-usage determination;
- Transport and Storage system integration;
- Metering
- First-hand sale Price (Only for Pemex).



MARKET STRUCTURE

- Authorization and limits to vertical integration;
- Limits to crossed corporate participation;
- Limits to market concentration;
- Vertical divestment of activities;
- Rules of conduct between related companies;
- Opinion on planning and energy policy.

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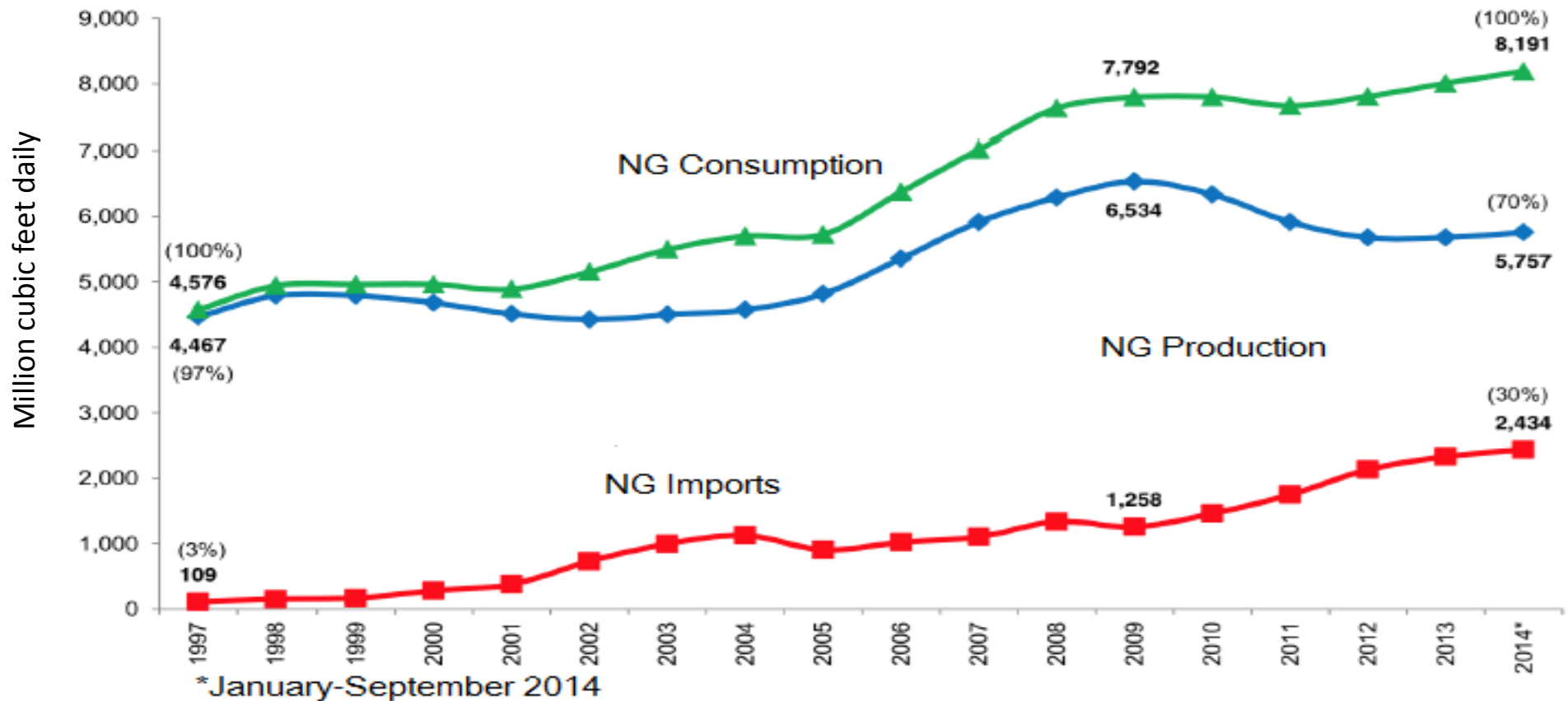
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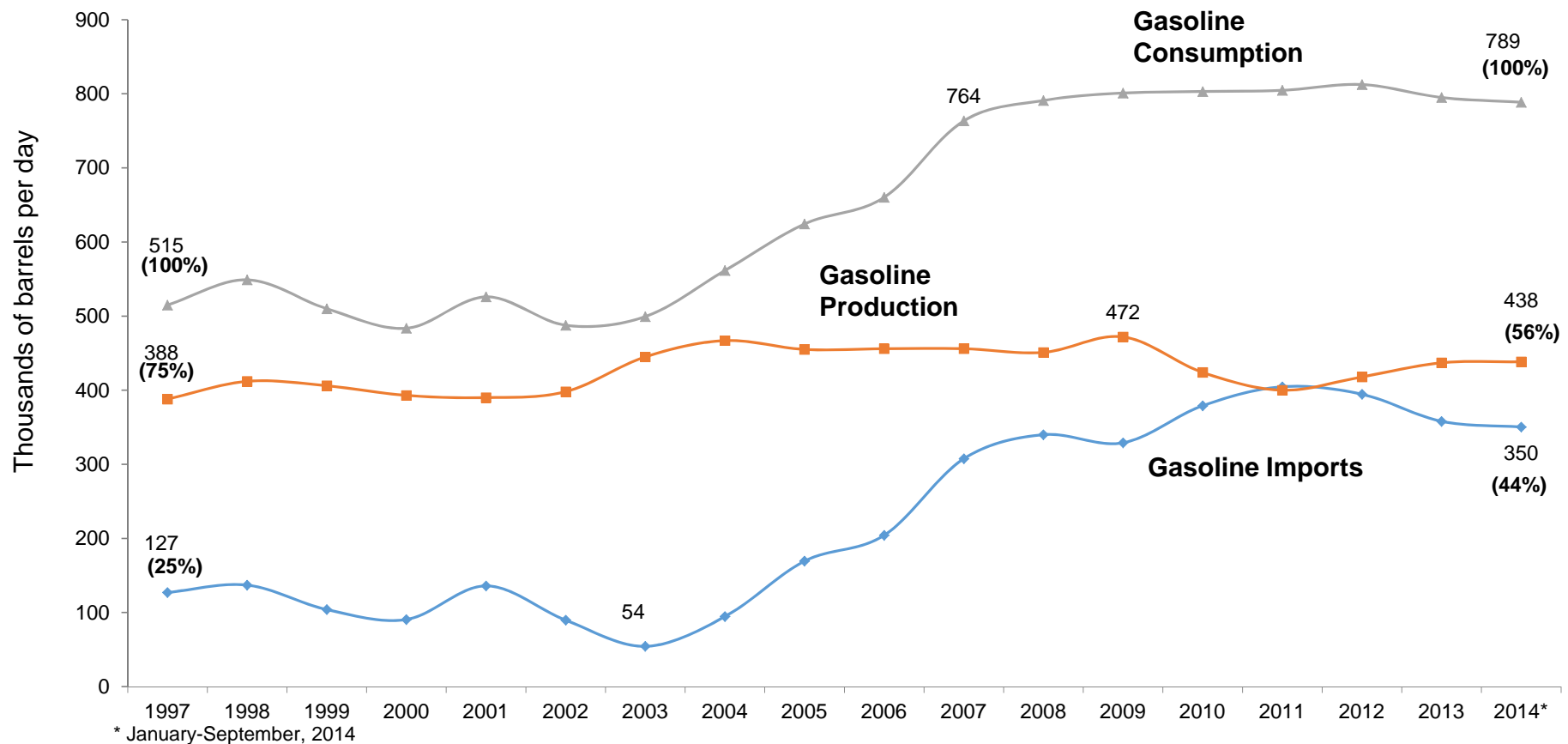


... which is likely to gain more economic importance due to increasing demand of natural gas and other fuels ...



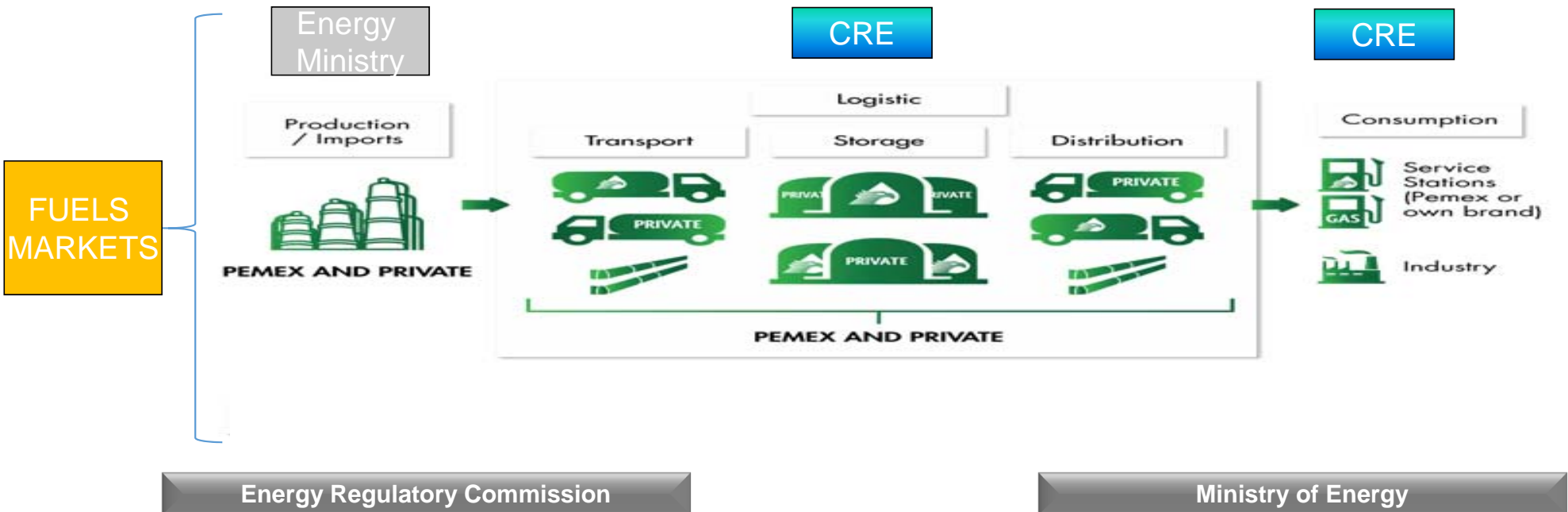
Source: Pemex, annual average 1997-2014.

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... so the economic environment must be adequate for the entry of new competitors and capacity development.



Issues permits for:

- Sales, transportation, storage, distribution and retail of oil, LP gas, other kind of fuels and petrochemicals.

Establishes:

- Tariffs for regulated activities.
- Regulation to guarantee open access on non discriminatory conditions.
- Regulation regarding horizontal/vertical integration to avoid abuse of market dominance.
- Asymmetric regulation for Pemex to avoid abuse of its dominant position

SENER

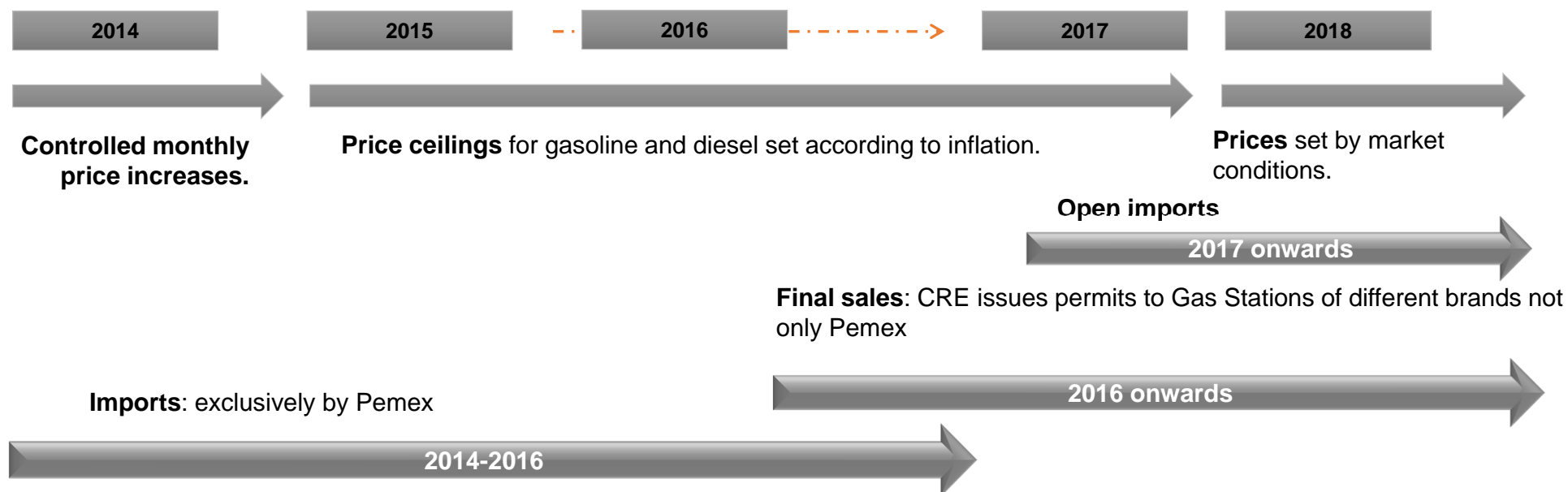
Issues permits for:

- Oil refining
- Natural gas processing
- Oil and other hydrocarbons imports/exports

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Gradual Liberalization of Gasoline and Diesel Markets

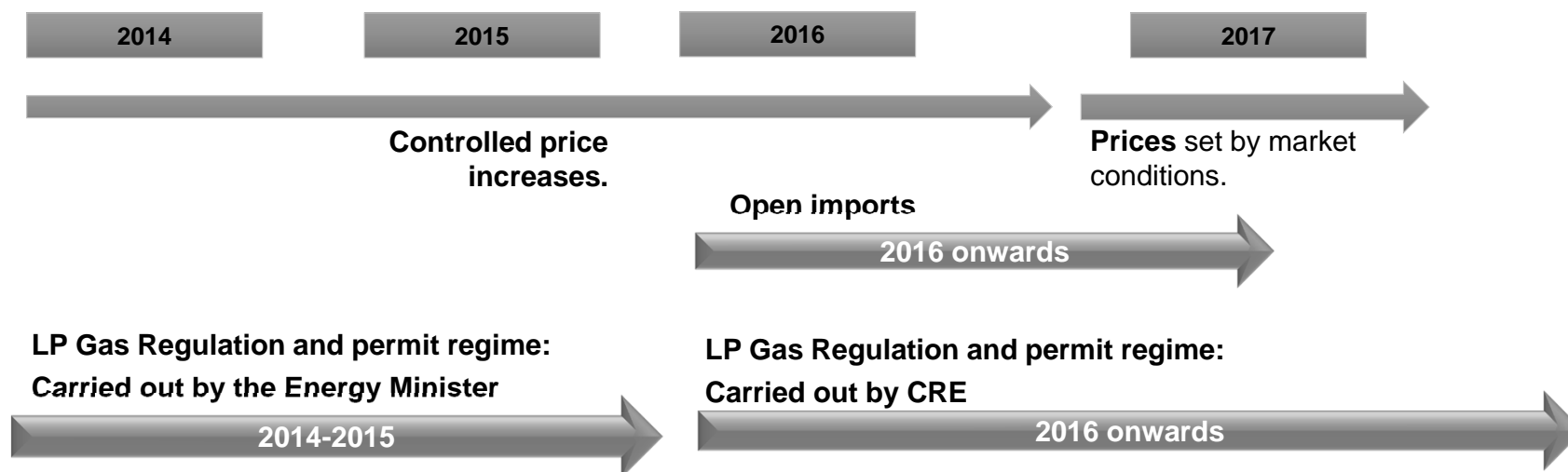
- Gasoline and diesel **prices will be liberalized in 2018** (ceiling prices are in force since 2015)
- **Open importation** will enter into force **on 2017**.
- **From 2016, gas stations** will be able to **carry any brand (Pemex or any other)**. As of September, 2015, CRE has granted the first over 1100 gas station permits.



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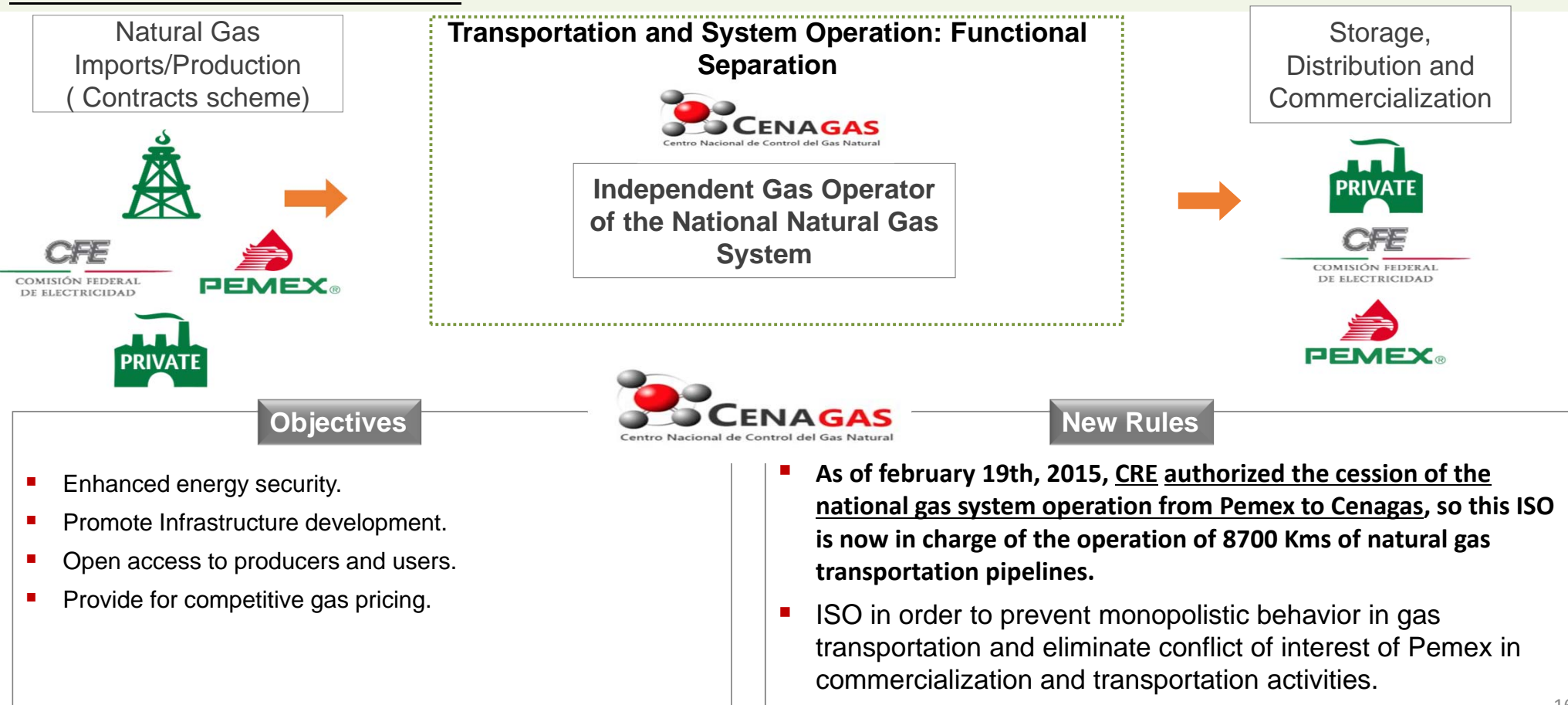
Gradual Liberalization of LP Gas Markets

- **2016:** Regulation and **permit granting transferred from SENER to CRE,**
- **2016: SENER starts issuing import permits** to private companies
- **2017:** Prices determined by the market.



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The New Natural Gas Model



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New Natural Gas Infrastructure Development



The new market structure will be enforced through new regulations prepared by CRE...

Developing regulations

- Following the issuance of new federal laws, CRE must develop **154 new regulations** by December 31st, 2015.
 - ✓ 45 regulations related to hydrocarbons, fuels and petrochemicals;
 - ✓ 109 related to the electricity industry;
- Such regulations will enforce –at an administrative level- the mandates found in the implementing legislation.

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Developing regulations

- Some of the subjects to be covered through new regulations related to hydrocarbons, fuels and petrochemicals:
 - ✓ Transport and storage in regulated systems;
 - ✓ Open Season procedures;
 - ✓ Regulated tariffs and prices
 - ✓ Requirements to be filed when applying for a permit
 - ✓ Transactions registry
 - ✓ First-hand sales / asymmetric regulation for Pemex (transitorily)

... in a way that investments in new capacity will be aligned with the public interest and avoid market dominance situations.

- All projects (strategic or not) carried out by Pemex and CFE are to be awarded through bidding processes.
- CRE is in charge of the approval of the bidding rules for those projects, taking into account several key aspects, such as:
 - ✓ Effective Open-access obligations;
 - ✓ Enough capacity to match present and potential demand (Open Season);
 - ✓ Adequate redundancy when needed to provide certainty;
 - ✓ Supply security;
 - ✓ Overall consistency with new legal framework and competitive conditions.

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Main principles to be developed in new regulations:

- Open access
 - Permit holders have to grant non-discriminatory open access to their systems;
 - Open access will be granted as long as it is technically feasible. Economic feasibility will be determined by the applicant
 - Through open access regulation, CRE will address certain important market issues, such as:
 - Limits to participation in the capital stock
 - Maximum participation that economic agents can hold in the market;
 - Percentage of reserve capacity in transport and storage facilities



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Main principles to be developed in new regulations:

- **Open Season Procedures**

- Under the new legal framework, an Open Season is a procedure regulated by CRE, in order to provide a leveled plain-field and transparency in the allocation or acquisition of available capacity to any interested parties.
- An Open Season instructed by the CRE also provides valuable information of potential demand that can give support investment to increase capacity during the planning stage of a new project.
- When?
 - ✓ When a new project is developed;
 - ✓ In case of an expansion/extension of an existing system;
 - ✓ When there is unused capacity that needs to be reallocated.



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Main principles to be developed in new regulations:

- Controls on Vertical Integration
 - In order to limit undertakings' market power, CRE will issue regulations on vertical integration (with support from the antitrust authority);
 - Regulations will seek the strict legal, functional, operational and accounting separation between regulated activities;
 - Crossed corporate participation between regulated activities will be subject to CRE's approval, and only be accepted when:
 - Clear legal and corporate mechanisms are provided
 - Activities are carried out in independent systems
 - Prior favorable opinion of the Federal Competition Commission

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Main principles to be developed in new regulations:

- Transparency and maximum publicity
 - Regulations must go through a public consultation process, held by COFEMER;
 - Regulations mandate the publication of permits and authorizations through electronic means;
 - CRE officers are subject to a Code of Conduct, which regulates:
 - Rules for public hearings with regulated parties;
 - Rules to participate in academic/diffusion events, as well as in forums and public events
 - The prohibition to accept gifts, tickets for traveling and other valuable From regulated enterprises.



Conclusions

- ◆ The Energy Reform in Mexico has deeply changed the economic structure of energy markets and has complied with a very strict and demanding timetable.
- ◆ The Energy Reform has opened up practically every aspect of the hydrocarbons industry following the best international practices.
- ◆ The institutional framework of the Mexican government has changed in order to cope with the challenge of regulating the new markets.
- ◆ One of the main goals is to attract private investment in a context driven by market competition and liberalization, in which every participant will have a leveled plain field.



Thank you very much

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