On December 12, Mexico’s Congress passed legislation aimed at a major overhaul of the nation’s energy sector. Despite opposition protests and much political theater, the bill easily passed the Senate and Chamber of Deputies before being approved by a majority of state legislatures.

There is no lack of commentary or analysis on the content of the legislation, but there are three broad areas that perhaps have not received the attention in the last few days that they merit, and deserve highlighting as the process winds toward implementation.

**It’s not just about oil**

For a variety of obvious reasons, oil and the changes at Pemex have dominated the headlines swirling around the unveiling of the 295 pages of legislation. True, electricity is nowhere near as polemic or political as oil in Mexico, but in terms of the impact on Mexico’s competitiveness and fostering sustained economic growth and development, it is arguably just as critical. And, what the energy reform outlines for the future of Mexico’s electric sector is perhaps just as monumental and could be as transformational as that for oil and natural gas.

As with the changes at the national oil company, Pemex, the state power monopoly, CFE will also be forced to transition from its current monopoly status to that of a state-owned enterprise a “productive public company” and a new reality, particularly when it comes to planning and control.

The reform legislation sets forth a path to the creation of an independent system operator (CENACE) from that which is controlled by CFE today. The goal is to incentivize private participation in power generation to keep up with demand growth and to redress Mexico’s uncompetitive electric tariffs, particularly for the industrial sector. But the reform also maintains the role for the state and CFE in transmission and distribution, thereby demanding massive investment in infrastructure as well as more transparent and feasible interconnection policies with CFE to create the market envisioned and to bring online the power generation that the other changes intend to unleash.

Patience is indeed a virtue and overhauling Mexico’s electric sector should be thought of in terms of years and maybe even decades. But, in sum, the changes set forth for the power sector in Mexico are a big deal too.

**The Peruvian model**

For years, Mexico’s energy reform debate in terms of what international oil model to draw from oscillated between that of Norway, Brazil and Colombia. All three again figured throughout the legislation set forth and approved by the Senate; the stipulation of a sovereign oil fund and how it would be managed was a clear nod to Norway. But the recent question marks surrounding Brazil’s efforts to revamp its petroleum law, principally with regards to the pre-salt, were not missed by the drafters of Mexico’s energy reforms.

Enter Peru. Indeed, the section in the legislation focused on how the Peruvian model works was at once intriguing but more importantly illustrative. The flexibility in the...
model for oil and gas licenses in the Andean nation received considerable attention and will continue to do so as follow-on legislation in Mexico takes shape.

Peru is not a major oil producer, but has realized several international bid rounds and has contracts in place with many major international firms. From state ownership of hydrocarbons in situ to the contract terms and tax and royalty scheme, the Peruvian model is, as the legislation notes, worth reviewing as Mexico moves forward with a new upstream reality.

The homage to the Peru model surely undergirds the cautious optimism that is circulating among the international investment community and especially international oil companies this week.

The devil is in the details – or in the secondary legislation

The events of the last few days are immense and certainly historical markers for Mexico. The legislative package set forth, in all of its 295 page glory, was clearly a product of exhaustive analysis and underscores the capabilities of Mexico’s technocrats and functionaries. But, what it does not change is the importance of the follow-on legislation that will fill in the ample gaps that remain on Mexico’s path to transformational energy reform. The legislation’s flexibility is at once a huge positive but also a signpost that the hard work is only beginning with the Constitutional amendments.

There are a range of areas where the Mexican Congress has been charged with developing follow-on laws and regulations, many of them in a stipulated time period (which are, in large measure, quite aggressive).

These may be the most critical: Round Zero. What Pemex chooses to keep in its portfolio and what the round looks like will go a long way to determining the opportunities for private companies down the road. Defining the interface between SENER, CNH and Pemex and the licensing and bidding process for upstream investment. Moreover, clear delineation of the composition of the “new” CNH is vital. It will require strong, politically capable authorities as evidenced by Brazil and Colombia’s examples when they launched new upstream regulators in 1997 and 2003, respectively.

Cautious optimism is circulating among the international investment community

Breaking decades-old monopolistic behaviors at Pemex and CFE will take more than just the current assertions in the legislation. The rules of the road and outline for the transition of Pemex and CFE from state monopolies to profit seeking state owned enterprises and particularly vis-à-vis the unions at each are of critical importance and will also require political savvy across the senior levels of both.

Borrowing from former US Secretary of State Dean Acheson, it is amazing to witness what is transpiring and those involved can rightfully claim to be present at the creation of a new energy chapter for Mexico.