

# BERDEJA ABOGADOS, S.C.

PLANNING AHEAD:

KEY ISSUES FOR PRIVATE COMPANIES

PARTICIPATING IN MEXICAN ELECTRICITY FIRST BIDDING ROUND

## **Introduction**

On August 7, 2014, the Mexican Congress passed legislation implementing the energy reform, which legislation was signed into law by the President on August 11, 2014 and was published in the Official Daily of the Federation on such date. The new legislation came into effect on the day following the date of its official publication.

The new legislation empowers the Mexican Government, through bidding and other processes, to execute agreements with Mexican and foreign companies, so that such companies may undertake in Mexico the exploration and production of natural gas. The new legislation provides also that the Mexican Government may license Mexican and foreign companies to produce electricity, or to participate representing producers, as sales agents, in the electricity market. Producers will be permitted to sell electricity directly on the market.

Please refer to our memorandum dated July 29, 2014 for a review of the implementing legislation.

## **Scope of First Bidding Round**

Under the new legislation, bidding on agreements for electricity generation and production of natural gas will take place in several rounds which will group several projects over the next few years.

The Ministry of Energy announced on June 22, 2015 that the first bidding round of projects will include bidding to compete for 24 projects with a total estimated cost of US\$9,836 million, of which 8 shall consist of natural gas pipelines, 4 shall consist of electricity generation, 3 shall consist of power transmission and required substations, and 9 shall consist of electricity distribution and waste reduction. The purpose of such projects is to add 2,385 kilometers (roughly 1482 miles) of gas pipelines to the gas pipeline system, 1442 Megawatts of installed capacity to the electricity system and 3,084 kilometers (roughly 1916 miles) to Mexico's electricity transmission and distribution network.

# BERDEJA ABOGADOS, S.C.

## Representative Projects

Each project included in the first round will have its own set of requirements and relevant dates. Initial representative projects include the following:

- Natural gas underwater pipeline from South of Texas to Tuxpan, Mexico. Estimated cost US\$3,100 million. Length 800 kilometers. Estimated completion time: 30 months. Preliminary bidding basis issued July, 2015. Submission of proposals on November, 2015. Award to be rendered on December, 2015. Start of operations estimated for June, 2018.
- Natural gas pipeline from Nueces to Bronsville, Texas. Estimated cost US\$1,550 million. Length 250 kilometers. Estimated completion time: 30 months. Preliminary basis of Request for Proposal issued July, 2015. Submission of proposals on November, 2015. Award to be rendered on December, 2015. Start of operations estimated for June, 2018.
- Wind electricity generation Southeast I and II in Oaxaca, Mexico. Estimated cost US\$1,079 million. Two modules of 585 +/- 2% MW. Estimated completion time: 20 months. Preliminary basis under Financed Public Work scheme estimated for September, 2015. Submission of proposals on February, 2016. Award to be rendered on March 2016. Start of operations estimated for December, 2017.
- Electricity distribution and waste reduction Northwest Project. Estimated cost US\$35 million. Two modules of 400/115/34.5 kV 500 MVA. Estimated completion time: 18 months. Preliminary basis under Financed Public Work scheme issued on May, 2015. Submission of proposals on August, 2015. Award proposed to be rendered on September, 2015. Start of operations estimated for March, 2017.

## Regulatory Functions

An announcement made by the Ministry of Energy confirmed and further specified functions to be undertaken by regulators in the upcoming first bidding round.

The Ministry of Energy shall (i) issue bidding basis, (ii) draft agreement forms, with the previous opinion of other regulators as required, (iii) define minimum national content requirements to be included in such agreements, and (iv) establish the requirements of clean energy and clean emissions certificates.

The Energy Regulatory Commission shall (i) grant licenses for electricity production, (ii) regulate rates of producers, (iii) establish mechanisms for issuance and review of rules of operation in the market, (v) draft connection and retail agreements, issue clean energy and clean emissions certificates, and (vi) issue rules of operation to be observed between production and distribution companies.

## BERDEJA ABOGADOS, S.C.

The National Center for Energy Control is empowered to issue and oversee compliance with rules of operation of Mexico's electricity system, including rules applicable to production, transmission and distribution of electricity.

### Stages of Bidding Processes and Tentative Dates

A table showing a summary of tentative steps of initial bidding processes announced by the Ministry of Energy follows. Please note that each project shall have its own distinct dates.

Starting 2015	June	Ministry of Energy issues draft bidding basis.
Pending		Review and comments on draft bidding basis by interested parties.
Starting 2015	July	Ministry of Energy issues final bidding basis.
Starting 2015	July	Full information available to participants.
Starting 2015	July	Submission and review of bids.
Pending		Execution of agreements.

### Power Market Rules Released by Ministry of Energy (SENER)

The Ministry of Energy ("SENER"), released Power Market Rules on September 8, 2015 (the "Rules"). The Rules regulate (i) the functions of various participants in wholesale electricity markets, (ii) rates applicable to transmission, distribution, National Center for Energy Control ("CENACE") services, and other significant services required in the wholesale electricity market, (iii) disclosure and dissemination of market information, and (iv) disciplinary actions. The Rules are to be implemented in two stages.

In sum, Rules applicable to Stage One regulate day ahead and real time transactions. Fixed schedule import/export on day ahead transactions. Charges on real time transactions will be measured on the measuring data per hour. No virtual transactions are yet permitted. Financial transmission rights bids to be made on an annual basis.

Rules applicable to Stage Two contemplate virtual transactions. One hour ahead transactions. Import/export transactions on the day ahead and the hour ahead. The Rules provide that

# BERDEJA ABOGADOS, S.C.

financial transmission rights bids will be made on a monthly basis. The Rules will allow three year bids for financial transmission rights. Charges on the real time market will be based on each dispatch interval.

Proposed key dates are the following:

September 2015: start implementation, including market tests, of Stage One.

October 2015: bidding basis for Federal Electricity Commission (“CFE”) long term power supply contracts to be released.

December 31, 2015: start of operation of Stage One.

First Quarter 2016: CFE contracts to be released.

2018: start of operations of Stage Two (precise dates yet to be defined).

2018: clean energy certificates market to start operations.

SENER derives its expectation for managing operational and financial risks at the participants level from traditional operational responsibility rules and user protection goals. Potential participants should expect SENER and other regulators to use the Rules to inform its regulatory processes and examinations, and should consider whether their current practices are in line with those outlined in the Rules.

## **Preparatory Measures**

SENER and other relevant regulators are likely to publish regulations at a rapid pace in 2015 and early 2016 as both the implementation of the energy reform and the bidding processes of the electricity first round of projects continue. Given this increased activity, regulatory, operational and financial teams at interested private companies and other participants and their advisers will want to collaborate to review carefully existing regulations to ensure that adequate preparations to consider participation in such processes are made. This will require close coordination between the experts at interested private companies and other participants and their advisers.

\* \* \*

Please do not hesitate to contact us with any questions.

Berdeja Abogados, S.C.

September 29, 2015