

Electricity sector reform proposal – More faculties to public utility CFE

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- On Friday, President Andrés Manuel López-Obrador unveiled the initiative for a constitutional reform of Mexico’s electricity sector
- The reform aims to strengthen and provide a greater role to public utility CFE, establishing by law that the company should produce at least 54% of all electricity consumption nationwide
- Other relevant changes include:
 - (1) CFE would be integrated both vertically and horizontally, maintaining only one subsidiary and three affiliates;
 - (2) The *National Center for Energy Control* (Centro Nacional de Control de Energía, or Cenace in Spanish) would be a branch of CFE in charge of coordinating production between the company and private producers; and
 - (3) Regulatory entities CNH and CRE would disappear, with CFE responsible of granting permits and licenses to the private sector
- The designation of “State-owned Productive Company” is eliminated and replaced by “State Organism”. Moreover, it establishes that activities designated as strategic for the state –such as electricity– cannot be catalogued as monopolies
- The initiative also contemplates the cancellation of all permits granted for production and contracts for the purchase and sale of electricity with the private sector, including some modalities such as “Own-supply societies” (“sociedades de autoabastecimiento”, in Spanish)
- Lastly, lithium and other strategic minerals would be exclusively extracted by the state
- To achieve these goals, constitutional amendments are proposed to Articles 25, 27, and 28. Therefore, they require a supermajority (2/3) in both the Lower House and the Senate, as well as most state legislatures (at least 17 out of 32)

Initiative to reform the electricity sector. On Friday, President Andrés Manuel López-Obrador unveiled the initiative for a constitutional reform of Mexico’s electricity sector. This proposal aims to support previously approved changes to the sector (by Congress, back in March), which have not been implemented due to ongoing legal challenges. Broadly speaking, the reform aims to strengthen and provide a greater role to public utility CFE in the electricity sector through several initiatives. To achieve these goals, constitutional amendments are proposed to three Articles of the Constitution: 25, 27, and 28.

Changes in the company’s designation and in autonomous entities. One of the first issues addressed is converting public utility *Federal Electricity Commission* (Comisión Federal de Electricidad, or CFE, in Spanish) into a “State Organism”, instead of its current designation as a “State-owned Productive Company”. Moreover, it establishes electricity as a strategic activity in charge of the State. In this respect, the reform states that: “...*Activities exclusive to the State in strategic areas would not constitute a monopoly...*”.

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Hence, the latter would give the company more control of the sector (see below) as this would allow it to operate legally as a monopoly. CFE would be integrated both vertically and horizontally, maintaining only one subsidiary (*CFE Telecomunicaciones e Internet para Todos*) and three affiliates (CFEnergía, CFE International and CFE Capital). The *National Center for Energy Control* (CENACE, by its acronym in Spanish) would be a branch of CFE. Currently, this is a decentralized organism in charge of controlling the operation of the wholesale electricity market, as well as to guarantee an impartial access to the transmission and distribution grid. The reform also contemplates the disappearance of two regulatory entities, the *National Hydrocarbons Commission* (Comisión Nacional de Hidrocarburos, or CNH in Spanish) and *Energy Regulatory Commission* (Comisión Reguladora de Energía, or CRE). Specifically, the CRE is responsible for the regulation of the electricity system, grants licenses for generation, and establishes transmission and distribution tariffs. The initiative proposes to return these tasks to the Energy Ministry.

CFE would produce at least 54% of the country’s electricity. The Executive branch argues that the company currently produces only 38% of the country’s electricity (see table below), with private-sector participation affecting profits. In addition, it says there are several practices favoring the generation and purchase of electricity to the private sector at uncompetitive prices. In this sense, CFE would have at least a 54% market share of the country’s electricity consumption, with the rest (46%) for the private sector. This percentage would be managed through the controlled acquisition of electricity by CENACE (now in charge of CFE) based on competition principles and production costs.

Mexico’s electricity generation

% of total	
Producer	Percentage
Total	100
<i>Private sector</i>	62
Independent energy producers	31
Own-supply societies	12
Power plants built after the 2013 Energy Reform	15
Long-term auctions	4
<i>CFE</i>	38

Source: Reform proposal

Limits to the private sector. Although private-sector players would still participate, the proposal: (1) Establishes a limit of 46% of national consumption for them; and (2) says their production would be restricted by the plans and control of CFE. This implies that connections to the transmission grid would also be limited by the company’s decisions. For this to happen, all existing permits for electricity production and contracts for the purchase and sale of electricity would be cancelled, along with the diverse schemes for private generation. This suggests that permits would need to be obtained again. Production would not be recognized if it is from: (1) Own-supply permits stemming from modifications not compliant with the *Ley del Servicio Público de Energía Eléctrica*; and (2) surpluses from independent energy producers. On the contrary, those that would continue to be recognized include: (1) Independent producer power plants (without surpluses); (2) long-term auctions; (3) power plants built after the 2013 Energy Reform; and (4) electricity generated by authentic own-supply schemes.

CFE would oversee the energy transition. Under its new role, the company would be required to establish the country's energy transition to address climate change. Therefore, they would have its own strategy as well the faculty to grant permits for the plans of private producers. In this respect, the proposal criticizes realized profits by the private sector through *Clean Energy Certificates* (Certificados de Energías Limpias, or CEL, by their acronym in Spanish). As a result, the reform also includes the elimination of these certificates.

Lithium would be a strategic asset, so no concessions would be provided in this sector. Lithium is considered as a strategic area for the state's energy transition given that it is an essential component to produce new technologies. These include batteries for mobile phones and electric cars. As a result, its status would be similar to crude oil, so concessions for the exploitation of this mineral would not be granted. Nevertheless, they recognize some concessions are already in place, so they will be allowed if already in the exploration or exploitation phases. In this backdrop, the United States Geological Service (USGS) estimates that Mexico has the 10th biggest lithium reserves in the world, with around 1.7 million tons.

Given the need of constitutional changes, challenges for its approval could be in store. The initiative needs constitutional changes to Articles 25, 27, and 28. For these to be approved, they require a supermajority (2/3) in both the Lower House and the Senate, as well as more than 50% of state legislatures (at least 17 out of 32). Incumbent-party Morena and its most recent allies (PT and PVEM) currently have 277 seats in the Lower House (~55%). Therefore, they would need at least 57 more legislators from outside parties. In the Senate, if we add up 4 more senators from the PES party, the tally is 78 seats (~61%), or eight less than needed. Morena and its allies already have control of the required state legislatures, so this does not seem to be major challenge. According to comments by president López-Obrador, this is one of three constitutional reforms that will be pursued during the rest of his administration. The other ones include the incorporation of the National Guard to the Army and an electoral reform.

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