

ISSUE BRIEF **12.05.19**

Mexico's Independent Energy Regulatory Agencies: Institutions at Risk

Miriam Grunstein, Ph.D., Nonresident Scholar, Center for the United States and Mexico

INTRODUCTION

In any economic sector, regulatory commissions are considered essential to give private investors greater certainty and create a level playing field of opportunities, especially in industries where state monopolies exist. The legal frameworks of such regulatory commissions are also intended to decrease the impact of abrupt political shifts that can occur when administrations change. The elected terms of commissioners in energy regulatory agencies, for example, are often designed to outlive or straddle presidential terms in order to avoid undue political interference with market forces. Mexico is no exception to this pattern. The 2013 energy reform, which opened Mexico's hydrocarbon and electricity industries to private investors, addressed the autonomy and independence of the regulatory commissions. This was an important consideration due to the role these organizations play in the opening of the previously closed energy sector. Two regulatory commissions are central to this discussion: the National Hydrocarbons Commission (CNH) and the federal Energy Regulatory Commission (CRE).

The CNH is charged with tendering contracts for exploration and production to oil and gas companies, be they private or state-owned, domestic or foreign.¹ Thus, it is important to keep the CNH's work safe from political interference, which could influence how it awards these contracts.

As an example, for political reasons rather than technical ones, the president could decide to favor Pemex, Mexico's national oil company, to be the operator in certain areas over other, perhaps more competent or efficient, companies. The president could do this to revive resource nationalism in the general public discourse or enhance the political support of the oil workers union toward a certain government agenda or political party. However, the CNH was crafted to resist those political pressures. By law, its decisions must remain independent and consider the most capable oil and gas operators rather than only those with political support.²

A similar concern applied to the CRE, which was created in 1995 with limited power to regulate some midstream activities in the natural gas industry, and with even more limited power regarding electricity. The commission went through a significant overhaul in the 2013 reform, which gave it vast legal powers to regulate a wide variety of activities both in hydrocarbons and electricity. For example, the CRE sets the price cap for automotive fuels and regulates industrial and residential electricity rates, which was previously a power held by the Ministry of Finance. Yet as the CRE has become more powerful, it has also become more visible to the general public and therefore more open to scrutiny. After over 20 years of being largely invisible, the CRE began to be identified as responsible for decisions of significant



The legal frameworks of regulatory commissions are intended to decrease the impact of abrupt political shifts that can occur when administrations change.

social impact, such as establishing the prices of automotive fuels and electricity, following the 2013 energy reform.

REGULATORS: SMALL AGENCIES, BIG DECISIONS

In a market economy and a liberal democracy, regulatory commissions are an important part of the institutional scaffolding that protects markets and consumers. The commissions may be small in size, but they make important decisions that ensure market fairness and hold all market actors accountable. Gasoline prices in Mexico are an important example of their activities in this regard. Gasoline pricing initially brought the CRE to national attention, albeit not necessarily for the right reasons. During the Christmas season of 2016, when the price of gasoline increased significantly as a result of increased holiday demand, a spike in the price of oil, and the devaluation of the peso,³ social unrest flared and a public demand for greater accountability rose.⁴ Since the price of gasoline was still under government control, many people believed the government was responsible for the price hike.⁵ The Ministry of Finance responded that the price of gasoline had gone up as a result of the devaluation of the peso, increased imports, and high demand during the holiday season.⁶ José Antonio Meade, the minister of finance at the time, affirmed that the government had no control over the factors that caused the price hike, and that price controls and subsidies would have other significant costs. The money spent on subsidies would have to be taken away from education, housing, health, and other relevant programs. In sum, Meade made it clear that, although politically unpopular, the government decided to let prices rise as needed.⁷

In the midst of popular discontent, another voice emerged to address this issue—the CRE. The CRE advocated for market-based pricing for fuels and fewer government controls. The chairman of the CRE announced a series of measures

to gradually liberalize fuel prices starting in January 2017. This announcement was relevant for a number of reasons. First, matters related to fuel prices had previously been dealt with by the Ministry of Finance, primarily due to the impact of fuel prices on constituents. Mexicans were used to fuel price controls and not used to dealing with pragmatic, market-based decisions on fuel pricing. When the former chairman of the CRE, Guillermo García Alcocer, delivered a press conference⁸ on the mechanisms by which prices would be liberalized, his speech was more technical than political. Also, the minister of finance, who traditionally controlled gasoline pricing policy and was the previously authorized spokesman regarding these matters, was allowed to take a lead role at the conference; the idea was that the conference should be seen as a moment of transition for Mexico's fuel price policy. This turned out to be a mixed blessing for the CRE. On the one hand, the days of being invisible were over. On the other hand, public perception was not favorable. The regulator was perceived to be a friend of private companies and a foe of the people.⁹ This first impression was not forgotten and became part of the political-electoral fight during the 2018 elections just a few years later.

By the time the Peña Nieto government left office in 2018, gasoline and diesel prices were being set by market forces. However, upon his election, the media asked President Andrés Manuel López Obrador what he thought of energy policy and regulators in general. He responded that regulators were the makers of neoliberal policies that protect the interests of private companies instead of serving the people.¹⁰ His words found support in the electorate, and based on his statements in daily press conference and other interviews,¹¹ it subsequently became clear that the new president would seek to undermine independent regulators. The question was how. Would he put significant political pressure on them? Would he go as far as amending the constitution and the law to diminish the independence of the

regulators? To understand this better, it is important to understand the institutional design of the regulators before the 2013 reform and how it has changed today.

ENERGY REGULATORY AGENCIES BEFORE AND AFTER THE 2013 REFORM

Up until the 2013 energy reform, the energy sector's regulatory commissions were part of the Department of Energy. Although there was not a clear relationship between the independent commissions and the secretary of energy, as they were legally autonomous, there were several aspects in the commissions' design that made them vulnerable to political pressures from the energy department and beyond. At first, commissioners were appointed by the president, with no Senate approval required. However, a constitutional amendment in 2011 established a more intricate appointment procedure, with greater checks and balances.¹² Following this amendment, the president could not propose a single candidate for a commissioner vacancy to the Senate and instead must submit three candidates with specific qualifications. Those candidates had to appear before the Senate for evaluation and approval.¹³ The candidate with the most Senate votes would fill the commissioner vacancy. Furthermore, removing a commissioner required clear, well-established legal reasons that had to be argued and proven.¹⁴ Several commissioners were appointed in this fashion, while none were removed.

When the 2013 energy reform was discussed, the 2011 change to the appointment procedures was deemed insufficient to ensure true regulatory independence. Besides Senate approval and clear legal reasons for removal, additional measures were taken to ensure the autonomy and independence of energy regulators. Here, it is important to be clear what autonomy and independence mean. Autonomy refers to how much these agencies are governed by their own rules and if they have specific legal powers

that allow them to act without external authorization. In turn, independence is a series of conditions that shield commissioners from external pressures, including those from interest groups, regulated companies, legislators, and even the government.¹⁵ Both the autonomy and independence of the energy regulators were to be protected in the new energy reform. Even so, the fact that the 2013 reform overhauled the energy model from a state-controlled to an open one still posed many new challenges for the regulators both in terms of their autonomy and independence. However, the new framework was good progress.

Despite these advances, it was still unclear if regulatory commissions would be able to enforce their legal powers without external pressure or interference, especially in an environment where they are often seen as suspicious and they faced formidable market actors such as Pemex. Indeed, this question was particularly relevant when it came to regulating Pemex, a previously protected monopoly, as a competitor in an open market. Before the reform, pressures from the government itself kept the regulatory commissions from enforcing market efficiency rules against Pemex.¹⁶ It was common for industrial groups doing business with Pemex, for example, to file for and obtain injunctions against measures that would end energy subsidies by the company. Each time the regulatory commissions tried to adjust tariff rates toward market benchmarks, industrialists would resist regulatory change, be it through political means or litigation.¹⁷ Industrial groups have even reached out to the secretary of energy for guidance rather than deal with the commissioners, who were considered technocratic and insensitive to the plight of Mexican industrialists. If the industrial groups claimed that they were entitled to low tariff rates because they were essential to the Mexican economy, the secretary of energy sided with the them, often against the recommendations of the commissioners, because of the political costs involved in ignoring industrial groups.

The fact that the 2013 reform overhauled the energy model from a state-controlled to an open one still posed many new challenges for the regulators both in terms of their autonomy and independence.

These considerations led the 2013 energy reform to include greater protections for the regulatory agencies and their commissioners. In addition to keeping the previously mentioned congressional approvals, the reform included some institutional changes to strengthen both the autonomy and independence of regulatory commissions. For one, agencies would be positioned outside the department of energy, and they could request and administer their own budget. They could also retain any of the duties paid by companies for their services, including permits, authorizations, or licenses. This was intended to secure a sufficient and independent income for the commissions.¹⁸

REGULATORY AGENCIES AND THE ENERGY REFORM

During the Enrique Peña Nieto administration (2012–2018), regulatory affairs were conducted smoothly, and regulatory agencies showed no signs of conflict with any political, social, or economic interest group. The CNH conducted two complete rounds of exploration and production contracts. As a result, 145 contracts were awarded to companies from all over the globe, including Pemex, which in fact won the most contracts, including both solo and collaborative contracts.¹⁹ The degree of professionalism and transparency of the CNH's procedures won recognition in the international community. In just five years, the CNH has come to be regarded as a highly professional and efficient regulator in the global oil and gas industry.²⁰

The CRE, on the other hand, had different challenges when compared to the CNH. While the latter has legal power to regulate matters exclusively related to hydrocarbon exploration and production, the CRE's scope of work encompasses a wide spectrum of activities related to both the hydrocarbon and electricity industries. In the former, it regulates downstream and midstream activities, such as the transport, storage, and distribution of hydrocarbons, refined products, and petrochemicals.²¹ In

the electricity industry, the CRE has taken the challenging tasks of determining how to calculate the tariff rates for the residential and industrial sectors,²² drafting model contracts, and approving generation permits.

Both agencies went through a steep and complex learning curve, and each one faced its own particular challenges. From the outset, the CNH had to create a market of exploration and production transactions in a country that had an energy monopoly for nearly 80 years. The exclusivity of Pemex had been neutralized in the law with the energy reform, but not in the discourse of important political figures like López Obrador, who became president in 2018. The CRE, on the other hand, was handed the challenging task of launching the electricity and fuel markets, as well as determining the pricing frameworks, which are sensitive to the reactions of consumers. In this sense, the CNH was expected to raise production and the CRE was supposed to regulate the markets to lower prices.

Thus far in 2019, neither of these expectations has been met. Since 2004, Mexico's hydrocarbon production has continued to decline with only a slight recovery in 2019.²³ This has been largely because the oil wells for which the new contracts were tendered hold relatively small potential and are still in the development stage.²⁴ There are promising projects located in the deep waters of the Gulf of Mexico that have just begun exploratory drilling. Expected production from these fields may come in eight to 10 years from the time of this writing, contingent on exploratory success.²⁵ This is largely why Mexican oil comes from Pemex, which has been in worsening financial and operational conditions.²⁶ For these reasons, production has continued to decline, and López Obrador has argued that the energy reform is simply not able to reverse this trajectory. While the numbers seem to support his claim, the problem may actually be in the way the reform was implemented and not in the reform model itself. If the Peña Nieto government had tendered larger and more profitable oil and gas fields, it is possible that Mexico could be experiencing more exploratory success, if not greater production.

López Obrador has, however, blamed

The CNH was expected to raise production and the CRE was supposed to regulate the markets to lower prices. Thus far in 2019, neither of these expectations has been met.

the reform model itself for falling short of the expectations created by the Peña Nieto government.²⁷ In his discourse, López Obrador blames the reform for Mexico's shrinking hydrocarbon richness. To this effect, he has warned that his government would stop all exploration and production tenders and that he would undertake a revision of all projects in three years, which is the deadline he gave companies to produce results, regardless of the timeline established in their original contracts. López Obrador's rationale for suspending all tenders until production increases has no basis on industry experience, which indicates that if Mexico needs more reserves and oil, it needs more operators and stronger regulators. Instead of cancelling tenders, the government should take the opposite route. It should tender more contracts over larger areas to more capable companies.

Political pressure has also certainly been used against these regulatory bodies. With regard to the CRE, López Obrador has claimed that it has served "neoliberal" interests, is technocratic, and has no social purpose—all major problems in his view.²⁸ This is the kind of discourse that puts the regulatory institutions at risk, through political pressure and the threat of future changes in the law. Political pressure also accounts for the resignation of various commissioners from the CNH.²⁹ At the same time, a former chairman of CRE, Guillermo García Alcocer, declared publicly that he was under pressure to resign but that he would not.³⁰ The president, in his daily press conference, responded that García Alcocer was under investigation by the government due to conflicts of interest.³¹ This prompted the resignations of three commissioners, Marcelino Madrigal, Montserrat Ramiro, and Guillermo Zúñiga.³² For months, the CRE did not have the manpower to deliberate and vote on issues under its purview, and no permits or rules were discussed or issued either.³³

García Alcocer stayed and new commissioners were appointed following a controversial selection process in which all nominees failed senatorial review twice

because the Senate committee felt that they lacked technical expertise.³⁴ However, the Law of Coordinated Regulatory Agencies establishes that after two rejections from a Senate committee, the president may appoint the persons he wishes without further consultation with the Senate.³⁵ Thus, López Obrador was able to appoint four commissioners without Senate approval, and the CRE restarted its operations, now staffed with López Obrador's loyalists.³⁶ These appointments directly threaten the independence of the commission. Not surprisingly, a few days after the new commissioners took office, García Alcocer announced his resignation and explained that López Obrador's vision of a state-controlled industry of the new commissioners was incompatible with his own.³⁷

ENERGY REGULATION NO MORE?

The fate of Mexico's energy regulators is uncertain at this point. The CNH's commissioners do meet, make decisions, and grant approvals. They also hold seminars and information sessions to engage the public. Under the new commissioners, there is no apparent tension between the commission and the current government, but the work of the CNH is no longer as effective as it was with the previous government. When the Peña Nieto government was in office, for example, tenders for exploration and production contracts made by the CNH were a critical part of the energy reform. But no such contracts are discussed today and all tenders are now cancelled,³⁸ making the work of the commission largely irrelevant.

The status of the CRE is different, as it is being run by López Obrador's appointees. For this reason, the relationship with the administration runs more smoothly. However, the efforts by the CRE to decrease the dominance of state monopolies over the energy market have halted. The current state of affairs for both the CNH and CRE raises the question of whether Mexico may be facing the end of independent energy regulation. What is certain is that these are institutions at risk, and potential investors

The current state of affairs for both the CNH and CRE raises the question of whether Mexico may be facing the end of independent energy regulation.

in Mexico's energy sector may shy away as the guarantors of a competitive market are now substantially weakened.

ENDNOTES

1. This important charge is specified in Article 35 of the Law of Coordinated Regulatory Agencies, <http://www.cre.gob.mx/documento/lorcme.pdf>.
2. Its independence is explained in Article 36, Section III, of the Law of Coordinated Regulatory Agencies.
3. Miriam Grunstein, *The Winter of our Discontent* (Houston, TX: Rice University's Baker Institute for Public Policy, 2017), <https://www.bakerinstitute.org/research/winter-our-discontent/>.
4. Fernando Mejía Barquera, "Gasolinazo': ¿incapacidad o estrategia informativa?" *Milenio*, January 12, 2017, <https://www.milenio.com/opinion/fernando-mejia-barquera/cambio-de-frecuencia/gasolinazo-incapacidad-o-estrategia-informativa>.
5. Carmen Luna, "La Reforma Energética: ¿Culpable del gasolinazo?" *Expansión*, January 3, 2017, <https://expansion.mx/economia/2017/01/02/hechos-y-dichos-en-torno-al-aumento-de-la-gasolina>.
6. Grunstein, *The Winter*, 3.
7. Jesusa Cervantes, "El gasolinazo tiene nombre: Meade, y su apellido es PRI: PAN," *Proceso*, January 4, 2018, <https://www.proceso.com.mx/517277/el-gasolinazo-tiene-nombre-meade-y-su-apellido-es-pri-pan>.
8. "A partir del 30 de noviembre habrá libre comercio en los mercados de gasolinas y diésel en todo el país," CRE Press Release, November 30, 2017, <https://www.gob.mx/cre/prensa/a-partir-del-30-de-noviembre-habra-libre-comercio-en-los-mercados-de-gasolinas-y-diesel-en-todo-el-pais?idiom=es>.
9. Alejandro Faya, "Neoliberalismo y Reguladores," *Reforma*, March 20, 2019, https://www.reforma.com/aplicacioneslibre/preacceso/articulo/default.aspx?id=153048&flow_type=paywall&urlredirect=https://www.reforma.com/aplicaciones/editoriales/editorial.aspx?id=153048&flow_type=paywall.
10. Mariana León, "AMLO acusa a los reguladores; son contrapeso, reviran," *El Financiero*, February 12, 2019, <https://www.elfinanciero.com.mx/economia/lopez-obrador-acusa-a-organismos-autonomos-de-simulacion-y-saqueo-a-mexico>.
11. Mexico's president gives daily press conferences that can all be watched on his YouTube channel: <https://www.youtube.com/channel/UCxEgOKul-n-WOJaNcisHySg>.
12. Based on Article 28, Paragraph 21, of the Constitution, and Article 6 of the Law of Coordinated Regulatory Agencies.
13. A more detailed explanation of this process can be found in Alejandro Faya, *Fortalecer A Los Reguladores Cambiando Las Reglas Del Juego En México* (Mexico City: CIDAC, 2010), 24–42.
14. Such causes are set forth in Article 9 of the Law of Coordinated Regulatory Agencies.
15. Article 16 of the Law of Coordinated Regulatory Agencies establishes a code of conduct to avoid regulatory agency capture.
16. *Ibid.*
17. Lilia Gonzales, "Industriales mantendrán amparos contra CRE por alza de gas," *El Economista*, August 28, 2016, <https://www.economista.com.mx/empresas/Industriales-mantendran-amparos-contr-CRE-por-alza-de-gas-20160828-0093.html>.
18. Article 22, Section 6, of the Law of Coordinated Regulatory Agencies.
19. Encuentro Nacional de Energía, "Pemex, la Empresa con más contratos en las rondas mexicanas," April 4, 2018, <https://encuentroenergia.mx/hidrocarburos/pemex-la-empresa-con-mas-contratos-en-las-rondas-mexicanas/>.
20. The Natural Resources Governance Institute rated the CNH's practices as consistent with international standards. See Natural Resource Governance Institute,

Mejores practicas internacionales para la transparencia en la administración de contratos (New York: Natural Resources Governance Institute, 2016), https://www.gob.mx/cms/uploads/attachment/file/183435/NRGI_REPORTE_TRANSPARENCIA_CNH-V_ESPA_OL_Dic_2016_.pdf.

21. The scope of the CRE is established in Article 41 of the Law of Coordinated Regulatory Agencies. Section 1 of this article refers to the CRE's legal powers over hydrocarbons.

22. Section 3 of the Law of Coordinated Regulatory Agencies describes matters concerning electric power.

23. The "Servicio de Información Energética" (Energy Information Service) of the Department of Energy reveals that while production was as low as 1,641,514 barrels per day in January of 2019, it rose to 1,692,132 barrels per day in May of the same year. This is considering since production was 3.4 million barrels per day in 2004. See "Sistema de Información Energética: Petróleos Mexicanos," Secretaría de Energía, accessed August 2019, <http://sie.energia.gob.mx/bdiController.do?action=cuadro&cvequa=PMXBIC02>.

24. Fabio Barbosa, "Situación de las reservas y el potencial petrolero de México," *Economía UNAM* 3, no.7 (January–April 2006): 79–102, http://www.scielo.org.mx/scielo.php?script=sci_arttext&pid=S1665-952X2006000100005.

25. According to CNH Commissioner Alma América Porres, there are 52.6 million barrels of oil per day in the deep waters of the Gulf of Mexico. However, these oil reserves are still "prospective resources," which means that they still need to be confirmed through exploration. Alma América Porres, "Potencial de los hidrocarburos en México," Comisión Nacional de Hidrocarburos, 2017, https://www.gob.mx/cms/uploads/attachment/file/433141/Pl_tica_7_Potencial_de_Hidrocarburos_en_M_xico.PDF.

26. Anthony Harrup, "Fitch Cuts Mexico's Pemex Rating by Two Notches," *The Wall Street Journal*, January 29, 2019, <https://www.wsj.com/articles/fitch-cuts-mexicos-pemex-rating-by-two-notches-11548817302>.

27. See Gabriela Jiménez "Rondas petroleras se suspenderán hasta el año 2021: Rocío Nahle," *El Sol de México*, November, 20, 2019, <https://www.elsoldemexico.com.mx/finanzas/rondas-petroleras-se-suspenderan-hasta-el-ano-2021-rocio-nahle-2687663.html>.

28. Marco A. Mares, "AMLO: Fin del modelo neoliberal," *El Economista*, December 3, 2018, <https://www.eleconomista.com.mx/opinion/AMLO-fin-del-modelo-neoliberal-20181203-0016.html>.

29. Iván E. Saldaña, "Renuncia otro integrante de la Comisión Nacional de Hidrocarburos," *Excelsior*, February 26, 2019, <https://www.excelsior.com.mx/nacional/renuncia-otro-integrante-de-la-comision-nacional-de-hidrocarburos/1298657>.

30. "No renunciaré: titular de la CRE," *El Heraldo de México*, February 19, 2019, <https://heraldodemexico.com.mx/mer-k-2/no-renunciare-titular-de-la-cre/>.

31. Ibid.

32. Arturo Solís, "Una renuncia más en la CRE: Ahora dimite la comisionada Montserrat Ramiro," *Forbes* January 29, 2019, <https://www.forbes.com.mx/una-renuncia-mas-en-la-cre-ahora-dimite-la-comisionada-montserrat-ramiro/>.

33. Julio Reyna Quiroz, "Cuarta renuncia de comisionados deja a la CRE sin quórum para sesionar," *La Jornada*, January 30, 2019, <https://www.jornada.com.mx/2019/01/30/economia/021n2eco>.

34. Rolando Ramos, "Senado rechaza las ternas para comisionados de la CRE," *El Economista*, March 22, 2019, <https://www.eleconomista.com.mx/empresas/Senado-rechaza-las-ternas-para-comisionados-de-la-CRE-20190321-0144.html>.

35. Article 6, paragraph III, of said law establishes this presidential right.

36. Jannet López Ponce, "AMLO designa a integrantes de la CRE," *Milenio*, April 4, 2019, <https://www.milenio.com/politica/amlo-designa-a-integrantes-de-la-cre>.

37. Staff, "Renuncia Guillermo García Alcocer, presidente de la CRE, por diferencias con nuevos comisionados," *El Financiero*, June 3, 2019, <https://www.elfinanciero.com.mx/economia/renuncia-guillermo-garcia-alcocer-presidente-de-la-cre>.

38. Rocío Méndez, "Solicita CCE se reactiven las rondas petroleras recién canceladas," *MVS Noticias*, June 18, 2019, <https://mvsnoticias.com/noticias/economia/solicita-cce-se-reactiven-las-rondas-petroleras-recien-canceladas/>.

AUTHOR

Miriam Grunstein, Ph.D., is a nonresident scholar at the [Center for the United States and Mexico](#), the chief energy counsel at Brilliant Energy Consulting, and a part-time professor and researcher at the Universidad ORT Mexico. Her consulting and research focus on energy law, public regulation, administrative law, and international transactions.

center for the
united states
and **Mexico**

Rice University's Baker Institute for Public Policy

See more issue briefs at:

www.bakerinstitute.org/issue-briefs

This publication was written by a researcher (or researchers) who participated in a Baker Institute project. Wherever feasible, this research is reviewed by outside experts before it is released. However, the views expressed herein are those of the individual author(s), and do not necessarily represent the views of Rice University's Baker Institute for Public Policy.

© 2019 Rice University's Baker Institute for Public Policy

This material may be quoted or reproduced without prior permission, provided appropriate credit is given to the author and Rice University's Baker Institute for Public Policy.

Cite as:

Grunstein, Miriam. 2019. *Mexico's Independent Energy Regulatory Agencies: Institutions at Risk*. Issue brief no. 12.05.19. Rice University's Baker Institute for Public Policy, Houston, Texas.

<https://doi.org/10.25613/AYRA-EM24>