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Environmental Impacts of Regional and International Energy Projects
Environmental Perspective in the US-Mexico Border

The Mexican Energy Legislation and its Impact on Cross Border Energy Projects

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I. Brief Overview of the Legal Framework of Energy Projects in Mexico

1.- Constitutional governmental monopoly of the energy industry under Mexican Law.

The Mexican Constitution dates back to 1917. It has since suffered hundreds of amendments spanning a very broad spectrum of topics and issues, not the least of which has been governmental control of the energy industries covering petroleum, gas, electricity, nuclear matters and associated endeavors.

From 1917 to the end of the thirties, the exploitation of energy related industries allowed for the intervention of the private sector and the participation of foreign investors who played very important and decisive roles in the development of Mexico's natural resources. This brought growth and prosperity to the industry but created social displeasure, which prompted the Mexican government to decree the expropriation of the petroleum industry**.** The result was the creation of its own electrical energy company and the advent of a new era of severe and practically absolute State control of all energy -related matters, which by the late 1950s brought an end to the participation of the private sector, and particularly of foreign investments, in the exploitation of electricity.

The core of these restrictions are currently found in articles 27 and 28 of the Mexican Federal Constitution, which create a monopoly of the Mexican State over the exploitation of natural energy resources, in most of their industrial and commercial forms.

The monopoly has taken the form of vertical integrations vested in the national petroleum entity, called *Petroleos Mexicanos (PEMEX),* and in the national electricity entities called the *Comision Federal de Electricidad* (*CFE)* and its sister company the *Compañia de Luz y Fuerza del Centro (CFC).* All of these entities are so-called "decentralized organizations" which are construed legally as government -controlled companies that have independent legal status and their own patrimony, subject of course to the direction of the Mexican Federal Government. They are therefore a part of the Mexican Federal Public Administration and, inter alia, governed by a series of secondary laws and regulations and budgetary allocations and constraints.

Because these entities are deemed to have been created in order to perform a public service, their management and resources have by necessity been governed by politics and governmental policy, as opposed to business policy and acumen. In addition, PEMEX's income has been subject to over -taxation**,** which contributes to an extremely important part of the Federal budget, thus depriving these entities of significant monetary resources required for future expansions, maintenance and growth in line with their inherent requirements and the needs of the population. Furthermore, CFE's and CFC's socially oriented purposes have led to decades of subsidies and a curtailment of the fixing of fees and services, in further detriment of their economic health and the ability to stay in tow with the times and need for their services.

The Mexican Government has not been insensitive to these problems, and it has for many years tried to reach a balance between the Constitutional principles of a State-run monopoly on energy resources and the need to inject the capital required to modernize the industry without increasing the burden thereof on the Federal budget. The government has consequently recognized in several efforts the need to allow the participation of the private sector in these endeavors, and even the convenience of allowing foreign investments in what has obviously become a globalized environment in which Mexico has to play a role, not only for its internal needs, but also to keep up with international standards that can no longer go unheeded.

To attend to these needs, as early as 1975 the Mexican Government enacted the Law Governing the Public Service of Electrical Energy (the "Electrical Energy Law") which, while preserving the monopoly on the generation, transportation, transformation, distribution and supply of electricity, also defined, regulated and encouraged private sector participation in five crucial areas**,** which included**:** (i) self supply and limited private production, as well as co-generation, (ii) the generation of electricity for sale to the CFE or independent power production known as IPP, (iii) the generation of electricity for export, (iv) the importation of electricity for the exclusive use of the individual consumers, and (v**)** the generation of electricity for emergency use in the absence of public supply. These early efforts were followed by sundry new laws and regulations which were designed to achieve the objective of a new balance between the constitutional norms and the effective needs of the times.

During the administration of President Ernesto Zedillo between 1994 and the year 2000**,** these efforts eventually led to a proposal to amend the Constitution to actually relax or repeal some of the restrictions applicable to private sector participation in electricity, without however going to the extreme of privatization. These efforts were rejected by Congress**,** and the Zedillo initiative was put aside.

At the outset of the current Vicente Fox administration, members of different parties represented in the Federal Congress attempted to pass legislation which was also designed to open up the electricity sector without primary loss of State control, but again these efforts never met with fruition.

In 2002 the Vicente Fox Administration again tendered to Congress a legislative proposal to amend the Electrical Energy Law, seeking to:

- maintain the authority of the State as to the public service of the supply of electricity while at the same time recognizing the right of the consumer to seek alternate sources of electricity, either in the form of self-supply or through the acquisition thereof from third parties;

- give a more precise definition to the powers and functions of the Ministry of Energy and those of the Energy Regulatory Commission (the "ERC"), thus affording better legal certainty in respect of the rights and obligations of both the State as well as the consumer;

- properly regulate the transportation and interconnection of electricity to guarantee an equitable access to the means of transmission;

- define precisely what constitutes the public service of electricity and what does not, so as to objectively set the stage for State intervention or its abstaining therefrom;

- guarantee access to the consumer and to the producer of electricity, to the national transmission and distribution networks without any manner of discrimination;

- regulate rates for the rendering of conduction services; and

- regulate oversight and security, fines and other measures to be applied by the regulatory authorities.

This act has also not been passed by the legislature. In addition, during the course of all these attempts, the labor unions which work for the State-run energy companies have adamantly opposed any form of private sector participation which could be conducive to a significant change in the ownership or management of the State-run monopoly on energy, arguing that the monopoly is a historical victory of the Nation and cannot be tampered with. This attitude obviously has weighed heavily on the shoulders of the different legislatures that have had to analyze the proposed changes and continues to create a stalemate between those who argue for modernization and the need to avoid an inevitable crisis in the short term, and those who believe that any form of private sector contributions can undermine the superior values of the Nation.

Notwithstanding these setbacks, the private sector has acceded to the permitted forms of participation, which are described above, as independent power production ("IPP"), self-supply, cogeneration, limited scale production, export and import of electricity.

In the case of petroleum and gas, articles 27 and 28 of the Federal Constitution also shelter the natural resources of the country in the form of a monopoly of the State, which in the case of

exploration and production of crude oil and natural gas is reserved exclusively to the State, which performs such functions through PEMEX and four special purpose vehicles of PEMEX which are designed to attend to the different areas of activities ranging from exploration to commercialization, whereunder petroleum, gas, and primary petrochemicals all fall under the vertical monopoly of the State via PEMEX. Under this scenario, the ownership of subsoil hydrocarbons is vested in the State, no concessions are allowed for their exploration or exploitation and the workings of the petroleum industry reside exclusively in the State.

2.- The workings of the Ministry of Energy and its decentralized and deconcentrated entities and the norms and regulations governing the functions of the oil, gas and petroleum industries.

The Ministry of Energy has existed under other names for many years**,** but its present form dates back to 1994, as a result of amendments to the Organic Law Governing the Federal Public Administration**,** popularly known under the initials "SENER." It is vested with the powers to conduct the country's energy policy, as a result of which it acts as the coordinator of the energy sector with the power to exercise the rights of the Nation over non-renewable resources such as petroleum and other hydrocarbons, gas, primary petrochemicals, radioactive minerals, the use of nuclear combustibles for the generation of nuclear energy, as well as the optimal use of other material resources required for the generation, conduction, transformation, distribution and supply of electricity as a public service.

SENER performs its activities directly and through a variety of para-state entities which include so-called "deconcentrated agencies", which are contained within SENER but enjoy technical, financial and operational autonomy, and by so-called "decentralized organizations" which are independent legal entities with their own legal standing and patrimony. The Energy Regulatory Commission (the "ERC") is a prime example of a deconcentrated entity**,** PEMEX, CFE and CFC are the outstanding examples of decentralized organizations. All of these entities operate under the Mexican Federal Budget and are subject to the oversight of a variety of regulators and to the economic intervention of the Ministry of Finance and Public Credit (known as the "SHCP" for its initials in Spanish), primarily orbiting around the cost of fees and services.

PEMEX of course is the most salient of the decentralized organizations in the sense that it represents Mexico as one of the world's most important producers of oil and associated products and that, furthermore, it is perhaps the number one contributor of income to the Mexican Treasury derived from the sale of its sundry products. In 1992 the Federal Administration decided to divide PEMEX into strategic areas to therefore better provide for the performance of its activities and the continuing modernization of its programs. As a result the following decentralized organizations of PEMEX were created, all of which have technical, industrial and commercial independence, and their own legal standing and patrimony**.** They pursue the following objectives:

- **PEMEX – Exploracion y Produccion ("PEP")** whose functions are to perform the exploration and exploitation of oil and natural gas, its transportation, storage and marketing;
- **PEMEX Refinacion ("PR")** which is charged with the industrial process in refining, preparation of petroliferous products and derivatives of petroleum which are susceptible

of serving as basic industrial raw materials, as well as the storage, transportation, distribution and marketing of the products and derivatives;

- ❖ **PEMEX – Gas y Petroquimica Basica ("PGPB"),** which is charged with the processing of natural gas, liquids derived from natural gas and artificial gas; also the storage, transportation, distribution and marketing of hydrocarbons, as well as the derivatives which are susceptible of serving as basic industrial raw materials; and
- ❖ **PEMEX – Petroquimica ("PP"),** which is in charge of industrial petrochemical processes whose products do not form a part of the primary petrochemical industry, as well as the storage, distribution and commercialization thereof.

The law which created these subsidiaries specifically states that the strategic activities which are for the account of PE, PR and PGPB can only be performed by the specific organizations.

It further states that PEMEX and its decentralized organizations, may pursuant to their purposes, enter into agreements with individuals or legal entities containing all manner of acts, agreements and contracts and may make and deliver negotiable instruments, while exclusively maintaining the ownership and control of the Mexican State over the hydrocarbons subject to the terms of the relevant law.

The ERC, which is a deconcentrated entity of SENER, was created by operation of a law dated in 1998 for purposes of promoting an efficient development of a number of activities**,** which include**:**

- the supply and sale of electricity to the consumers of a public service;
- the generation, exportation and importation of electrical energy which is performed by private citizens;
- the acquisition of electrical energy which is to be used for a public service;
- the services relative to the conduction, transformation and delivery of electricity among the entities who are charged with the rendering of a public service in electrical matters, and between these and the holders of permits for the generation, exportation and importation of electrical energy; the firsthand sale of natural and liquid gas;
- the transportation and storage of natural gas which is not indispensable or necessary to interconnect its exploitation or elaboration;
- the distribution of natural gas; and the transportation and distribution of liquid gas by means of pipelines.

- The ERC has very significant legal powers in all matters which are relevant to its area of expertise**.** These include**:**

- the determination of rates for the supply and sale of electricity**;**
- the approval of the methodology for the computation of consideration for conduction, transformation and electricity delivery services;
- the power to opine as to the convenience of having CFE perform projects or of having private sector participants to be called to bids for the supply of electrical energy and, as the case may, be the terms and conditions of these bids;
- the approval of the terms and conditions in the matter of the firsthand sale of natural gas and liquid gas;

- the approval of the terms and conditions for the rendering of transport, storage and distribution of natural gas;
- the approval of the terms and conditions applicable to the rendering of transport and liquid gas distribution services by means of pipelines;
- the granting and revocation of permits and authorization that pursuant to applicable law are required for the performance of the regulated activities;
- acting as a mediator or arbitrator in the solution of controversies related to the regulated activities; oversight powers and the right to demand information and the appearance of persons who perform regulated activities; and
- the imposition of administrative sanctions and all others which are conferred to it by secondary law under Article 27 of the Constitution and relevant statutes.

II. Legal issues in the case of cross border Energy Projects

1.- The Problem of national sovereignty and the conflict of law.

It is very evident that the system of law of Mexico and that of the United States vary in many important ways. Mexico practices the civil law system, embedded in a tradition which dates back to the rule of law under the Spanish and French, while of course the United States is a common law system heavily influenced by the English.

Constitutionally**,** however**,** the two countries are not that far apart. The Mexican Magna Carta was crafted much in the way of that of the United States Constitution**,** and our bill of rights is very similar to that of the U.S.'s**.** Our Constitution has, however, had several different versions over the centuries**,** and the present Constitution is in many ways the product of a violent and socially oriented revolution**.** This revolution inspired in the fathers of the 1917 Federal Constitution an appreciation for an exclusionary form of tenancy in agrarian and basic natural resources which almost a century later still limits the ownership and exploitation of everything from land for farming and ranching to mining, crude oil, gas and primary petrochemicals. These constitutional principles in modern times are difficult to cope with in a globalized world economy, where efficiency, technology, and economies of scale must be achieved in order to nurture and expand Mexico's use of its natural resources. In addition, the States of the Mexican union have never had true autonomy in these matters and the federal statutes are for the most part applicable law.

In the early 1970s these constraints came to the forefront when the federal authorities recognized that the State did not have the resources necessary to confront the emerging and growing needs of the population. Solutions were sought to legally soften vertical integrations and to permit the private sector, and even foreign investors, to contribute to the promotion and development of certain sectors of the economy which very clearly were demanding the infusion of investment and technology which were no longer available in the public sector. The problem then and the problem now, is how to achieve these endeavors without actually changing the entrenched nationalistic policy of the Magna Carta.

The Salinas Administration, which was in power from 1988 through 1994, removed obstructions to international trade which helped set the stage for the attempts of his successors to free the bonds of energy in Mexico**.** One of the most successful steps was the North

American Free Trade Agreement (NAFTA), which opened the Mexican borders to imports, investments and more abundant trade among the United States, Canada and Mexico. Strategic areas such as energy did not however receive the same benefits as commercial trade. That said, Articles VI and X brought Mexico closer to a more significant intercourse with its neighbors in previously precluded areas.

NAFTA is an international treaty that was approved by the Mexican Congress and became law. Under the resolutions of the Mexican Supreme Court, international conventions fall between the supremacy of the Constitution and the application of secondary laws, so NAFTA prompted the issuance of a variety of complementary legislation which supports and enhances the convention and allows the private sector to invoke novel and previously restricted ways of doing business within and without the country. Furthermore, NAFTA is protected by a system of federal injunction procedure, called the "Amparo," which allows a private person of any nationality to challenge acts of authority which fall outside of the Constitutional norms, including acts which undermine or dishonor the contents of an international convention which for all purposes is federal law.

In the 1980s efforts were made to regulate energy in a more realistic manner, which provided for continued State control of the Constitutional monopoly but only when that control was really relevant to the rendering of a public service as opposed to merely providing leeway for the private sector when the interests of the public at large were not at stake. Thus the Zedillo Administration attempted to amend the Constitution. When that failed in the face of stiff Congressional opposition guided by a desire to continue embracing national sovereignty, the Fox Administration attempted to introduce reforms which could loosen the framework without cutting into the heart of the paradox. That too failed as discussed above.

In this scenario it is obvious that conflicts of law will arise and that cross border energy projects will by definition have to deal with the same issues. For that purpose, concerted tripartite efforts have occurred which attempt to put the issues on the table and to analyze the differences in applicable law as well as the start of potential solutions. An example of this is the North American Energy Working Group (NAEWG) which was born in 2001 under the auspices of the Canadian Minister of Natural Resources, SENER and the U.S Department of Energy to enhance North American energy cooperation. NAEWG has done careful, albeit not official, studies of the legal environment of each of its members and has memorialized the results in the 2005 "Guide to Federal Regulation of sales of imported electricity in Canada, Mexico and the United States." The Guide indicates that "The goals of the NAEWG are to foster communication among the governments and energy sector of the three countries on energy-related matters of common interest, and to enhance North American energy trade and interconnection with the goal of sustainable development for the benefit of all." The Guide recommends that it should be used in conjunction with the North America-Regulation of International Electricity, a "companion guide to federal regulation of the construction and operation of cross-border power lines and the permitting requirements to allow exports and imports of electricity in Canada, Mexico and the United States that was issued by NAEWG in December 2002." These publications, while not official, are nevertheless very valuable in understanding comparative law among the three countries and have served the purpose of informing the Mexican legislators as to the issues and the problems raised therein, which hopefully will forge common grounds when discussing them during the course of their periodic meetings among their other

international peers. This forum also permeates down to the different levels of local and federal government agencies which have to deal with permits and projects, thus providing them with crisp information and a clearer vision of the comparative cross border legal barriers which have to be attended to in order to move ahead in the energy related industries.

As an example of their importance, on July 18th, 2006, the Mexican Secretary of Energy, reported to the Mexican media that the Mexican Secretary of Energy, the United Status Secretary of Energy and the Canadian Minister of Natural Resources signed an agreement to improve their energy efficiency programs and foster cooperation in the matter of investigation and development of clean technologies. The report stated that the three countries had signed a commitment letter sent to their respective heads of State that included facilitating the marketing of technology for the supply of clean energy and contemplated negotiations to sign a trilateral agreement to serve as a framework for cooperation in science and technology within the energy sector. The agreement is a part of the agenda of the March 31 meeting in Cancun, Mexico within the workings of the Alliance for the Security and Prosperity of North America.

The Secretaries of the participating countries, focused principally on the role that is played by acts of cooperation, took advantage of the work previously undertaken by NAEWG in regulatory matters.

Another laudable example of international cooperation is the Border 2012 U.S. Mexico Environmental Program which is predicated on the 1983 Agreement on Cooperation for the Protection and Improvement of the Environment in the Border Area (La Paz Agreement). The La Paz Agreement "empowers the federal environmental authorities in the United States and Mexico to undertake cooperative initiatives and is implemented through multi-year binational programs."

2.- Multiple jurisdiction permits-extraterritorial reach of energy regulations.

The issue of multiple jurisdiction permits and the extraterritorial reach of energy regulations presents a very important subject that is open to debate. Clearly the energy regulations of the three North American countries present different requirements and standards, and even though there do exist efforts to bring them into sync for the benefit of all concerned, the culture and history of each participant create legal issues which in many instances have not been overcome, and in the case of Mexico, are conditioned by the Constitutional order and its secondary law regime. Efficiency and environmental concerns are present in every country. The extent, however, of how they are addressed varies, and in some cases **is** even further complicated by the local legislation of the States of the Union of the United States and the Canadian dominions.

The regulations of energy law in Mexico are deemed to be of public interest and they cannot legally be subordinated to foreign laws or requirements. However, it is reasonable to assume that if the foreign standards in a cross border project are more demanding than those in place in Mexico, upgrading those standards with the cooperation of the relevant cross border authorities should not be an obstacle. Downgrading the Mexican standards would obviously be unacceptable. The regulatory authorities of all three countries are, as described above, already trying to apply cooperation in many areas of energy related enterprises and working within the framework of the Mexican Constitution. Cooperation will, in our opinion, eventually lead to

harmonizing these standards and perhaps even enacting legislation to customize their application.

Energy is not the sole example of this dilemma. The banking sector in Mexico is today greatly controlled by foreign players, not only from North America but also from the European community, and Mexico has issued norms and regulations in order to allow foreign regulators to make home country demands on Mexican banks and other financial institutions which, while not diminishing the authority of the Mexican regulators, provide means to accommodate extraterritorial rules and regulations. Cooperation is key in these efforts and respect for Mexican law and institutions has prompted the cooperation of the Mexican financial authorities and in some instances has led to the adoption of foreign source regulations which strengthen the local markets.

Multinational organizations such as the International Finance Corporation, which members include the countries of North America, are in fact already imposing standards on energy related projects financed by the organization, that surpass those found in Mexican law and the Mexican borrowers are encouraged to meet these standards if they wish to access the relevant loans and credits, even under the penalty of having to increase their project costs. These issues may also crop up when Mexican borrowers tap the resources of Mexican banks to finance a local project, to the extent that the local bank is foreign owned and is required to apply the relevant rules of its parent company on the extension of credit to energy related projects.

In addition, Mexico is reported to be a net importer of gas from the United States, and gas of course is the driving power source of many of Mexico's energy projects. In connecting the Mexican pipelines to sources in the United States**,** Mexico faces the need to follow the standards applicable to its suppliers**,** As a result**,** it needs to reevaluate its standards to permit cross border imports of this power source. In the electricity field, the export of electrical power generated in Mexico, particularly from the border regions, has to be adjusted to meet the regulatory requirements of its neighboring entities; otherwise its efforts will be blocked by foreign laws and regulators. Once again, mutual understanding of these needs and cooperation on an international scale are key to the continuity of Mexico's growth in the energy markets.

III. Extraterritoriality of Energy Projects

1.- Bidding processes.

In general**,** the acquisition, leasing or receipt of services by the agencies of the Mexican Federal Government are acts governed by the 2000 Law Governing Acquisitions, Leases and Services of the Public Sector (the "Procurement Law"). Chapter X of NAFTA addresses the matter of international bidding processes among participants of the three signatory countries and the individual energy laws contain procedures for bidding the awarding of permits and authorizations in order for the private sector to be able to perform the permitted activities encapsulated in such laws (i.e. articles 28, 38 et al. of the 1995 Regulations of Natural Gas provide the conditions under which permits can be granted in a first public bid for the distribution of gas).

Under the Procurement Law, such acquisitions, leases or services are further governed by the 2000 Public Works and Related Services Law (the "Public Works Law"). The Procurement Law and the Public Works Law have resulted in regulations, both of which were published in 2001.

The Procurement Law regulates the planning, programming, contracting, expenditure and control of the acquisition and leasing of movable assets, as well as the rendering of services of any kind, by the Mexican Federal Government and its agencies. The Public Works Law regulates the planning, contracting, execution and control of public works and related services, which comprises the construction, installation, remodeling and maintenance of immovable assets or real-estate, as well as turn key projects, exploration, detection and perforations required to exploit petroleum and gas resources, among others.

The acquisition of goods and services, as well as the contracting of public works and related services, must be performed by the Mexican Federal Government:

- through a public bid process, which may be (i) national, if the participants are required to be Mexican nationals and the goods and services are required to be produced in Mexico with a national content of not less than 50%, or (ii) international if the participants are allowed to be either Mexican nationals or foreigners and the goods are allowed to be either of national or foreign origin; or

- by invitation with not less than three participants, in those cases specifically provided therefor in the Procurement Law or in the Public Works Law; or

- by a direct award, in those cases specifically provided for in the Procurement Law or in the Public Works Law.

Each of the Procurement Law and the Public Works Law also contain their own specific rules applicable to public bidding processes to be followed by the Mexican Federal Government as the case may be. All acquisitions of movable assets and services as well as the contracting of public works by the Mexican Federal Government must be performed by the applicable referred procedures which are very similar in both laws, commencing with the publication of a public bid call made by the relevant governmental entity and the preparation of the relevant bidding guidelines which the participants may purchase. Said bidding guidelines must follow the procedure and rules of, and must contain the basic information provided by, the Procurement Law or the Public Works Law, as the case may be.

After one or more clarification meetings between the participants and the relevant governmental entity, the participants in the bid process must submit to the entity their bid proposals, which are divided into a "technical proposal" containing all technical specifications requested in the bidding guidelines, and an "economic proposal" containing specificity in respect of each applicable item (in the case of unit prices), or a specific total amount (in case of lump sum contracts). After review of the proposals based on the criteria established in the applicable law, the entity will issue its award to the winning participant for it to thereafter execute the relevant contract with the interested entity.

Pursuant to the Procurement Law and the Public Works Law, the winning participant in a public bid must guarantee (i) any advance payment received from the host entity, and (ii) the performance of the relevant contract, the form and amount of which guarantees shall be established by the governing bodies of the host entity.

In addition, both laws provide that the winning participant must be liable for any defect of the assets and works subject to the contract, according to applicable law and to that established in the relevant contract. Furthermore, the relevant resulting Public Works Contract will provide that the wining participant must guarantee the work to be performed for a period of twelve (12) months, through a bond, letter of credit or a guarantee trust, for an amount equivalent to ten percent (10%) of the total value of such works.

Prior to the actual bid, the rules for bidding may require from the participant the surrender of a bond or similar guarantee to secure performance of the participant in the event the participant receives the winning award, thereby helping to ensure that the participant will in fact enter into the relevant procurement or service agreement.

In practice, the referred guarantees have been met in some instances by international participants with displeasure, alleging that such guarantees are excessive in form and amount considering other international bidding processes, and because they drive up the cost of the relevant project.

Energy projects are governed by the Electrical Energy Law and its Regulations, which provide for a specific public bid process to be followed by the participants in a bid for an energy project for the Mexican Federal Government to acquire energy. The bid process is similar to the bid process established in the Procurement Law and in the Public Works Law.

During the current Fox Administration, PEMEX has promoted the use of so-called "Multiple Purpose Agreements" which PEMEX has publicly defined as "a tool meant to reduce the importation of natural gas and to take advantage of the natural resources of Mexico to transform Mexico into a self-sufficient State, by means of an agreement signed by PEMEX with companies which hold a proven record of success, economic solvency and technical experience and that can offer the lowest prices for their services during a term of 10 to 20 years." The underlying difference between this manner of agreement and the traditional public contract is, in the view of PEMEX, that it currently manages more than 10,000 individual agreements per annum which commits hundreds of experts to abandon their strategic activities in order to prepare, execute and manage all such agreements while Multiple Service Agreements include sundry services to be performed by one company alone during a term of 10 to 20 years. On the surface, the Multiple Service Agreements seem to make sense, but in some important quarters they have been called unconstitutional and even a form of subterfuge to defeat secondary laws, insofar as some of their clauses seem to abandon restricted activities and to deliver them to the private contractor. Most of the discussion has been around the so-called "Burgos" projects in northern Mexico, where these manner of agreements have been applied**.** In the end, the Multiple Service Agreements continue to be bogged down in debates and challenges which thwart their effectiveness.

2.- Examples of approved private sector Energy Projects.

SENER has reported a variety of authorized energy projects with cross border and national characteristics which have been published by SENER in its 2005 yearly report on the activities of the Ministry of Energy called "Natural Gas Prospective 2005-2014" (the "SENER Gas Report") and in SENER's 2005-2014 "Electricity Sector Prospective 2005-2014" (the "SENER Electricity Report"). The salient items are as follows:

- 152 permits have been issued for the transportation and distribution of natural gas, which represent investment commitments close to **$**2.7 billion dollars. The vast majority of these permits are operational today. At least 6 of these permits are in use in the Mexico-U.S. border areas.

- Since 1996 the ERC has performed around 17 public bids for the distribution of natural gas, many of them in the border areas. As a result, together with the regularization of existing distributors, the ERC issued 21 distribution permits that will reportedly benefit around 12% of the Mexican population.

- In 2004**,** the ERC granted two new permits for open access transportation of gas**.** One permit will allow the connection of the Altamira Tamaulipas liquefied natural gas terminal with the electric plant at Tamazunchale San Luis Potosi The second will expand the open access transport service in the Yucatan Peninsula and will allow interconnection with the gas line of Energia Mayakan.

- Between 2004 and 2005, the ERC granted 19 gas transport permits for self-supply which represent an estimated investment of **$**13.8 million dollars**.** One of the permits is linked to the generation of electrical energy**,** and the remainder are intended to satisfy the needs of industrial consumers.

- As of June 2005 the ERC had granted 5 permits for the storage of liquefied natural gas, all of them located in or around the border between Mexico and the United States.

- 330 permits have been issued for the generation of electrical energy, 87% of which are currently active.

- For purposes of continuous self production, 59 permits are currently in effect and 90% of those permits are linked to co-generation.

- In the case of independent energy producers, there are currently 21 permits in effect, 15 of which are active and the remainder are in a state of construction.

- In the case of self-supply, 17 new permits were issued in 2004 for a total of 184 current permits.

- Co-generation has not changed, with two new permits issued in 2004.

- In the case of exportation, the current permits are 5, 4 of which are in operation.

- Imports registered new demands**,** and 19 permits were issued by 2003 with two additional permits issued in 2004. Reports have it that 40 companies in Baja California have proclaimed an interest in importing electricity in order to increase their competitiveness and a total of 17 Baja California companies have received permits therefore, but only 3 have commenced their imports.

3.- Experiences derived from liquefied natural gas (LNG) projects between Latin-American suppliers and Mexican LNG liquefaction facilities.

The SENER Gas Report states that ERC has issued 5 permits for the storage of liquefied natural gas, one of which will not be used as a result of urbanization or land use related problems. The others are active for use in Altamira, Tamaulipas, Ensenada, Baja California and in the *Islas Coronado* in a place which is offshore of Baja California.

In reviewing the issues and problems related to these storage efforts**,** we have detected the following areas of analysis and concern:

a) Origin of the LNG. If the LNG originates in a given Latin American country (the "First Supplier"), the sponsors will have to deal with the energy and other laws of the country of origin in order to understand how to resolve such complex matters as extraction and hydrocarbon issues, general regulatory and permitting issues, general environmental law issues, contract law, corporate structure, sale of gas issues, taxes, export permits, liquefaction, construction and use of pipelines, potential bankruptcy scenarios, funding and security issues and the policy of the government of the First Supplier as to the exploitation and subsequent sale of its gas resources abroad.

b) Transportation of the LNG through a third country. If the LNG is to be transported by pipelines or otherwise through a third country in order to be shipped from there to Mexico, by use of a convenient port of export, that will create a second supplier (the "Second Supplier") and the sponsors will have to deal with energy and other laws of the Second Supplier to resolve most of those matters relative to the First Supplier, as applicable, as well as new issues related to the construction of the incoming pipelines, port facilities, storage, liquefaction and export of the LNG to Mexico. In addition, certain political conditions may require the analysis and resolution of adverse policies of the government of the Second Supplier of running LNG through its geographical corridors.

c) Importation of the LNG to Mexico. In Mexico (the "Third Supplier") the sponsors will have to address and resolve issues pertaining to general regulatory and permitting issues, contract law, the sale of LNG, degasification, pipeline transportation, general environmental law issues, permits pertaining to storage and use of land, corporate structure, taxes, export issues, potential bankruptcy scenarios, funding and security issues. Consideration must also be given to what portion of the LNG, if any, will stay in Mexico to supply local needs subject to the requirements of Mexican energy law.

d) Exportation of the LNG to the United States. Once the LNG is stored in Mexico and ready for export, the sponsors will have to analyze and resolve the applicable

requirements of the local and federal laws of the United States in the matter of importation of the LNG with all of what that may mean from an environmental and regulatory point of view.

All of the above topics are too broad to address in a presentation of this nature, but the guidelines are there and due diligence in each of the participating countries must be comprehensive and creative.