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Mexico, U.S. Reach Landmark Agreement on Deepwater Oil Exploration

By Carlos Navarro

In an unprecedented act of cooperation in the energy sector, the US and Mexican governments signed an agreement establishing a framework for US energy companies to work jointly with the state run oil company PEMEX to develop oil and gas resources in the deep waters of the Gulf of Mexico.

The agreement eases a dispute between Mexico and the US about ownership of reserves along a common boundary in the Gulf of Mexico, potentially opening more than 1 million acres to deepwater drilling. Mexico was extremely concerned that drilling by US companies could siphon off reserves on the Mexican side in what some described as the "efecto popote," or drinking-straw effect.

"With this, we are setting aside the old fear that honestly exists among many Mexicans that Mexico's oil could be extracted from the other side," President Felipe Calderón said in announcing the agreement at the meeting of foreign ministers of the Group of 20 (G20) industrial and developing countries in Los Cabos in Baja California Sur state on Feb. 20.

The Mexican president added that any common crude-oil reservoirs along the boundary would be exploited jointly and that Mexico would benefit from this arrangement.

Accord ends dispute on reserves ownership

Mexico and the US completed most of the negotiations on the Transboundary Agreement in 2011, but the pact was only formalized with the signatures of Mexican Foreign Relations Secretary Patricia Espinosa and US Secretary of State Hillary Rodham Clinton at the G20 meeting in Los Cabos.

One of the most important benefits of the agreement is an end to the current moratorium on oil exploration and production in the Western Gap portion of the Gulf of Mexico. The US Interior Department estimates that the area contains as much as 172 million barrels of oil and 300 billion cubic feet of natural gas, but these are relatively modest amounts when compared with the potential throughout the Gulf of Mexico.

"These reservoirs could hold considerable reserves that would benefit the United States and Mexico alike," Clinton told reporters in Los Cabos. The accord would also help facilitate joint exploration arrangements between PEMEX and US oil companies. And, in the absence of joint exploration agreements, each country has the right to exploit its share of hydrocarbons while protecting the other nation's interests.

The agreement also contains several clauses that allow the two countries to cooperate more closely in preventing and reacting to oil spills. These include creating joint inspection teams to ensure compliance with safety laws and environmental rules. Until now, neither was authorized to oversee the environmental and safety practices of the other, even though oil spills do not respect international borders. The clauses were included in the agreement partly in response to the massive oil spill at the Deep Water Horizon drilling rig in the Gulf of Mexico in April 2010.

"Each of the nations will maintain sovereignty and their own regulatory systems," Interior Secretary Ken Salazar told reporters at the G20 meeting. "But what this signifies, and what may be the most significant part of the agreement, is that we're moving forward jointly with Mexico to ensure we have a common set of safety protocols." Salazar and Mexican Energy Secretary Jordy Herrera Flores were on hand in Los Cabos for the signing of the agreement.

Experts believe the cooperation on safety will especially benefit PEMEX. "Mexico doesn't have the resources to combat a major oil spill, and the United States does," said energy expert Jorge Piñon, a research fellow at the University of Texas. "Coordination and sharing communications, training, personnel, equipment, and technology are essential for safe and productive drilling."

No fast track in Mexican Senate

But the agreement is far from a done deal, since the US and Mexican Senates must ratify the pact. There has been little comment from the US Senate, which is expected to easily ratify the accord. But Mexico's upper house has already made it clear that the agreement will not be given a fast track. Mexican senators have underscored the importance of examining the agreement closely to ensure that Mexico's sovereign rights are not violated.

"In principle, our delegation in the Senate agrees with the importance of signing an agreement of this type to better regulate the exploitation of wells," said Sen. Manlio Fabio Beltrones, coordinator of the opposition Partido Revolucionario Institucional (PRI) in the lower house. "But as long as we don't know the exact language in the agreement we cannot endorse it. We cannot be flexible in a matter that involves the Mexican Constitution."

The stance of PRI Senate members coincides with the position of presidential candidate Enrique Peña Nieto, who has said that private investment is needed in PEMEX to keep the company viable.

The center-left Partido de la Revolución Democrática (PRD), led by Sens. Carlos Navarrete and Pablo Gómez, also underscored the need to read the fine print in the agreement very closely but also promised not to become obstructionists if everything in the accord was in order. "If the accord is appropriate, the next step is to promote investments," said Navarrete.

Sen. Luis Alberto Villarreal, a member of the governing Partido Acción Nacional (PAN) and chair of the foreign affairs committee for North America (Comisión de Relaciones Exteriores para América del Norte) in the upper house, agreed with the importance of closely examining the terms of the agreement but pointed out that there would be less uncertainty about the agreement if Congress had approved a more comprehensive energy reform a couple of years ago.

Reforms approved in 2008 did allow limited private participation in the Mexican oil sector, giving PEMEX the green light to hire foreign companies for exploration and other activities by offering them multiple-services contracts.

Sen. Francisco Ramírez Acuña, PAN floor leader in the upper house, urged fellow senators to give President Calderón the benefit of the doubt. "Everyone was complaining that nothing was being done to resolve the problems related to the efecto popote, but now we have agreements," said Ramírez. "The agreement that the president announced was intended to ensure that territorial limits are respected and that our sovereignty is guaranteed."

In announcing the agreement, Calderón offered reassurances that it is in complete compliance with the Constitution. "This agreement was negotiated under the invariable principle of respecting the sovereign rights of each country to its natural resources," said the president. "Mexico's oil wealth belongs and will continue to belong to the Mexicans."

Financial benefits

Calderon stressed that the agreement should be viewed as a tool that would boost Mexico's energy security and increase revenues from PEMEX, which despite recent fiscal reforms still account for about a third of government income.

Lourdes Melgar, director of the Instituto para la Sostenibilidad of the Escuela de Graduados en Administración y Dirección de Empresas (EGADE), said the agreement could provide other financial benefits to the two countries. EGADE is associated with the Instituto Tecnológico de Monterrey (ITESM).

In an interview with the daily newspaper Reforma, Melgar said the international practice in situations where oil reserves straddle a common border is for the crude oil to be drilled on one side and the output to be distributed proportionally between the two countries. The scheme creates efficiencies that would reduce costs. If the two countries operated separately in this area, she said, they would each have their own platforms, oil transport facilities, and personnel.

Although the Senate has the ultimate authority to ratify all international treaties, the Chamber of Deputies will participate in public discussions regarding the Transboundary Agreement. PRD Deputy Armando Ríos Piter, who chairs the governing council in the lower house (Junta de Coordinación Política), said there are plans for PEMEX director Juan José Suárez Coppel and Energy Secretary Herrera Flores to testify before a joint session of the Congress. "We want a detailed explanation of the accord and assurances that the exploitation of the reserves is equitable," said Ríos Piter.

But Mexican legislators will also have to consider the reality that the country's proven reserves are rapidly dwindling, and the only hope lies in deep-water wells. For Mexico, the development of these wells will depend on attracting foreign investors, but this has to be done without violating the Mexican Constitution.