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# PRI Commits to Open Energy Sector to Private Investment

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In a somewhat controversial decision, the former governing Partido Revolucionario Institucional (PRI) endorsed the concept of opening Mexico's energy sector to private investment but also reiterated its position that the state should retain control of the petroleum and electrical-power industries. The PRI decision was announced March 3 at the party's annual national assembly in Puebla state. The party has historically had mixed positions regarding the energy sectors.

The energy policies of former Presidents Carlos Salinas de Gortari and Ernesto Zedillo, both members of the PRI, included some opening of the petroleum and electricity sectors to private capital (see SourceMex, 1994-03-30, 1996-02-14 and 1999-02-03). Salinas' and Zedillo's policies, however, represented a major shift from the party's longstanding defense of energy resources as the patrimony of all Mexicans, a policy in place since former President Lazaro Cardenas nationalized the oil industry in 1938.

While Salinas and Zedillo managed to push through some reforms that allowed some private investment in the state-run oil company PEMEX and the Comision Federal de Electricidad (CFE), the PRI had never openly embraced the moves as a position of the party. Party looking ahead to 2006 election

PRI leaders acknowledged that the recent move to commit to some opening of the energy sector is intended to better position the party ahead of the upcoming presidential and congressional elections. "A party cannot be a viable contender for the 2006 elections without an economic proposal that incorporates modernization of the national energy sector," party congressional leaders Deputies Emilio Chuayffet and Manlio Fabio Beltrones said after the Puebla meeting.

The PRI statement was careful to emphasize that the state would continue to have ownership and full control of the energy sector. The PRI purposely offered a vague commitment on the energy sector to allow further debate. Party leaders said any proposal to open up the energy sector would be submitted to the party's rank and file for approval. "Any plan we draft has to have full legitimacy," said the PRI.

Beltrones said he has urged the party's energy committee to begin work on a proposal that could eventually be brought for a vote to the Chamber of Deputies and the Senate. He pointed out that PRI members have drafted some of the plans that have been discussed in the Congress. "There are already several initiatives from PRI members that have been brought to the energy committee (Comision de Energia) in the Chamber of Deputies," said Beltrones. He mentioned proposals presented by Deputies Salvador Rocha Diaz, Jorge Chavez Presa, and Guillermo Hopkins, Sen. Alejandro Gutierrez, and ex-Deputy Natividad Gonzalez Paras. "All of these PRI initiatives are worth considering under our new commitment to modernize PEMEX and the CFE," said Beltrones.

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Some members of the party criticized the PRI's new stance on the energy sector. Sen. Manuel Bartlett Diaz, a staunch opponent of private participation in Mexico's energy sector, said the measure is another ploy by PRI president Roberto Madrazo Pintado to position himself ahead of the 2006 election. Madrazo is considered by many the front-runner to gain the PRI nomination, although there is strong opposition within the party (see SourceMex, 2005-02-16). "[Madrazo] is a hypocrite," said Sen. Bartlett. "He has made promises to open the energy sector to business organizations knowing that the majority of PRI members reject privatization."

Other PRI members are not as concerned about the entry of private capital into PEMEX and the CFE as they are about foreign participation in the state-run enterprises. A coalition of PRI deputies, which describes itself as the "popular sector," has offered a proposal to capitalize the company by allowing the sale of PEMEX stock exclusively to Mexican citizens. PRI leaders attempted to soften potential criticism by publicly rejecting the energy policies advocated by Zedillo and continued by President Vicente Fox. "We support neither the privatizing policies put forth by Ernesto Zedillo nor the ones employed by the government of Vicente Fox," said Beltrones.

Fox has complicated this effort by suggesting that his policies differ little from those presented by the PRI. "I offer an emphatic 'No' to any move to turn the energy sector over to private interests," Fox told reporters. He insisted, however, that Mexico must be open to joint ventures between the government and private companies to help capitalize the energy sector. Fox and Zedillo have both pushed initiatives that allow private companies to only "sell" their services to a state-run agency, which would retain control over petroleum, gas, electricity, and other energy resources. State control ensures compliance with Article 27 of the Mexican Constitution, which designates all energy resources as the patrimony of all Mexicans, according to the Zedillo and Fox policies.

## *Proposal elicits different reactions from PRD, PAN*

The center-left Partido de la Revolucion Democratica (PRD) has joined with Bartlett and other PRI dissenters in criticizing the party's commitment to open the energy sector. Mexico City Mayor Andres Manuel Lopez Obrador, a leading candidate to represent the PRD in the 2006 presidential election, said the proposal is an indication that the PRI differs little from the governing Partido Accion Nacional (PAN). "The PRIAN the PRI and the PAN already have an agreement in place to privatize the petroleum and electrical sectors," said Lopez Obrador.

The opposition to an opening of the energy sector is not unanimous within the center-left party. A handful of PRD members contends that Mexico should consider limited private investment in PEMEX to allow the oil company to regain financial viability. "We have to explain why it is indispensable," Sen. Demetrio Sodi de la Tijera said recently.

Another indication that the issue could become a major issue in the 2006 presidential campaign is the participation of Interior Secretary Santiago Creel in the debate. Creel, considered the most likely candidate to win the PAN presidential nomination, called on the PRI to put its commitment into action. He suggested that the PRI and PAN immediately begin negotiations on a proposal. "If the PRI has decided to open the energy sector, now is the time for it to assume its responsibility and offer a proposal for reform," said Creel.

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PRI members immediately jumped on Creel, accusing the interior secretary of anticipating a policy that had yet to be finalized. Calling Creel a "clumsy political operator," PRI technical secretary David Penchyna Grub accused the secretary of trying to use the energy issue as an opportunity to gain public favor in advance of the 2006 elections. Creel is considered the favorite for the PAN's nomination.

Other key members of the PAN, however, see little chance for any cooperation between the two parties in the near term. "There's no point in trying to make a pact because they [the PRI] simply don't want to talk," said Energy Secretary Fernando Elizondo. Fox's initiatives encounter difficulties One of the important energy initiatives implemented by Zedillo, but originally proposed by Salinas, was to allow private companies to construct electrical-power plants to meet their own energy needs and to sell surplus production to other companies (see SourceMex, 1999-04-24).

The Fox administration attempted to expand on Zedillo's plan by proposing that private companies be allowed to sell electricity to the CFE. The courts shut down this proposal in 2002 (see SourceMex, 2002-05-01). Fox's most important energy initiative has been to open up exploration and extraction of gas in the Burgos Basin in northeast Mexico to private companies under the Contratos de Servicios Multiples (CSM) program (see SourceMex, 2003-02-19 and 2003-07-23).

The Fox administration has had mixed success in this endeavor, initially attracting strong interest from private companies, usually partnerships between Mexican and foreign companies (see SourceMex, 2003-10-29 and 2004-01-28). The administration has, however, had difficulties of late convincing companies to participate in the CSM program.

The government found no takers when it opened bids for exploration of the Ricos parcel in the Burgos Basin earlier this year. A few weeks later, only one bidder stepped forward in the opening of the Monclova parcel. The bidder, comprising US and Mexican interests, was given the contract. Critics say poor profitability and a lack of technical information have kept participation low in the CSM program. "PEMEX has failed to provide sufficient geological information on some of the sectors that are about to be opened," said Juan Carlos Collado, an attorney who has represented some of the private companies that have participated in the program.

The concerns presented by Collado and others have led PEMEX to develop a new proposal to make the program more attractive to foreign investors. One element of the proposal would have PEMEX assume a much larger share of the exploration risks. Other recent initiatives to open up PEMEX activities to private investors have met apathy. The oil company, for example, has received little interest from private companies in a proposed concession to drill for oil in the deep waters of the Gulf of Mexico. Exxon Mobil Corp., Conoco, BP Plc, and other international oil producers have said they do not plan to participate in the project because the proposal is not profitable enough. The contracts "do not recognize the high cost and high risk of [operating in] deep water," said Tim Cejka, president of Exxon Mobil's exploration unit, based in Irving, Texas.

Some oil-company executives said they would consider participating in the project if PEMEX would agree to invest between US$100 million and US$150 million, thus demonstrating its willingness to assume a larger economic risk in the project. A similar situation exists in the electrical-power

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sector, where companies like Electricite de France (EDF) are seeking a greater commitment from the government to modernize the sector. "Mexico has a very internal and nationalistic vision on energy," said Cintia Angulo, an EDF representative in Mexico. "Other more flexible and innovative options must be explored."

## *Congress debates overhaul of PEMEX tax structure*

Politicians from all parties agree that if Mexico continues to place strict limits on private investment in the petroleum industry, the legislative and executive branches are obligated to enact major reforms to the PEMEX tax structure. The Mexican government continues to rely heavily on PEMEX revenues to fund the federal treasury, leaving little money to the company to invest in exploration, infrastructure, and general operations. Under current practice, the government takes the majority of oil-export revenues through a hefty "tax" on PEMEX.

The company's operations are then funded through a federal budget. In recent testimony before Congress, PEMEX director Luis Ramirez Corzo warned that the company faces the danger of "collapse" if its tax status is not changed. Among other things, Ramirez said PEMEX's limited budget is preventing the company from replacing and upgrading aging pipelines and other infrastructure.

Aging infrastructure, especially leaky pipelines, has created major hazards for the environment in Veracruz, Campeche, and Tabasco states. This year alone, PEMEX needs 8.4 billion pesos (US$749 million) beyond what was allocated for repair and upgrade of 36,000 km of pipeline, Ramirez Corzo told legislators. More than half the pipelines in the southeastern states of Veracruz, Campeche, and Tabasco were installed in the 1970s, and most are now in the process of deterioration.

Leaks in PEMEX pipelines have occurred frequently in the three states in recent years, but the situation made major headlines in late December when a massive spill caused significant contamination to the Coatzacoalcos River in Veracruz state (see SourceMex, 2005-01-05). "The signs of danger are especially apparent in the pipelines that carry refined product, particularly liquefied petroleum gas (LPG) and basic petrochemicals," Ramirez Corzo told Congress. The Congress intends to push through reforms to the PEMEX tax structure, but has been unable to enact major changes because no alternative has been developed to replace lost revenue from crude-oil exports.

The Chamber of Deputies started the ball rolling late last year, approving a limited tax-reform plan for the oil company and sending it to the Senate. The full Senate has yet to take up the proposal, sending it instead for further study to the energy, finance and legislative-affairs committees. PAN Sen. Jorge Nordhausen Gonzalez, who chairs the Senate's energy committee (Comision de Energeticos) is among those who have come out in support of the legislation approved by the lower house.

Other senators are not as keen on the plan and are putting forth alternative plans. A coalition of PRD and PRI senators, for example, has developed a scheme that would involve a more comprehensive structural reform of PEMEX. Under the proposal, Congress and the executive would have equal say in establishing petroleum policy, including setting the limits on extraction and exports of oil. [Note: Peso-dollar conversions in this article are based on the Interbank rate in effect on March 16, reported at 11.22 pesos per US$1.00] (Sources: The New York Times, 03/03/05; Agencia

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de noticias Proceso, 02/28/05, 03/02/05, 03/07/05, 03/10/05; Spanish news service EFE, 03/03/05, 03/07/05; Notimex, 03/08/05; El Financiero, 01/10/05, 02/11/05, 02/14/05, 02/22/05, 02/23/05, 03/07/05, 03/09/05; The Herald-Mexico City, 02/22/05, 02/25/05, 03/07-09/05; El Universal, 02/01/05, 02/25/05, 03/08-11/05, 03/14/05; La Jornada, 12/20/04, 01/05/05, 01/27/05, 02/01/05, 02/14/05, 02/23/05, 02/25/05, 03/07-11/05, 03/14/05, 03/15/05; La Cronica de Hoy, 01/31/05, 02/01/05, 02/03/05, 02/23/05, 03/08-11/05, 03/14/05, 03/16/05; La Crisis, 03/08-11/05, 03/16/05)

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