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LADB Staff

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Senate Could Consider Energy-reform Legislation By April

by LADB Staff
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The Mexican Senate could begin debate on comprehensive changes to the energy sector sometime in April, with the role of private capital at the center of discussions. All political parties agree on the need to provide the state-run oil company PEMEX with financial autonomy, but there are differences between the center-left coalition and the other parties in the Senate on the extent of private participation in the company. There are also differences among some members of the governing Partido Accion Nacional (PAN) on how the issue should be discussed in public. One proposal would have organized a debate between PAN Senate leader Santiago Creel and former presidential candidate Andres Manuel Lopez Obrador of the center-left Partido de la Revolucion Democratica (PRD), but this plan was shut down by PAN and congressional leaders, who said the issue was best debated within the Congress.

The urgency for Mexico to enact a comprehensive energy reform in 2008 is driven in large measure by the sharp drop in crude-oil reserves (SourceMex, March 07, 2007 and May 09, 2007). PEMEX has announced the discovery of new reserves in the Gulf of Mexico, but these are out of reach because of extraction costs and the company's lack of technical expertise (SourceMex, March 22, 2006 and June 21, 2006).

Major parties meet to consolidate, refine proposals

The three major parties the PAN, the PRD, and the Partido Revolucionario Institucional (PRI) have been working on proposals to overhaul Mexico's energy sector. All three agree that major changes to PEMEX's fiscal status, by which the company would be allowed to keep the majority of its profits, would go a long way toward boosting the amount of capital available for exploration and extraction, construction, and other activities. PEMEX now transfers a large share of its profits to the Mexican Treasury via a "corporate tax." In recent years, the Mexican Congress has reduced the amount of the tax paid by PEMEX (SourceMex, May 20, 2005 and September 19, 2007), but a comprehensive energy reform would allow the company to keep the lion's share of its profits.

PRI Sen. Francisco Labastida Ochoa, who chairs the Senate energy committee (Comision de Energeticos), said the intent of legislators is to give PEMEX a structure similar to that of a private company, which would allow PEMEX to grow and be competitive. The three parties also agree on the need for an independent energy regulator, which would ensure more transparent policies governing oil, gas, and electrical power. The congressional delegations of the three parties scheduled special meetings in late January to consolidate their positions on energy reform.

The PRD legislators met in Cabo San Lucas in Baja California Sur state, while their PAN counterparts were gathering in Cozumel in Quintana Roo state. The PRI was scheduled to meet in Mexico City. With the three parties still formulating their positions, it is very unlikely that energy legislation will reach the Senate floor in the next several weeks. And, any proposal that comes
before the full Senate must first be drafted in the energy committee (Comision de Energeticos). "This month and next we will most likely still be in the debating stage to try and put out a single initiative...that all parties can sign," said PAN Sen. Ruben Camarillo, a member of the Senate energy panel. "I hope we can all agree, I don't know whether it will be on 50%, 60%, or 70% of the points....But we will put down all the issues where we agree and put out one single initiative in the name of the energy committee," Camarillo told Reuters. Because of the compromises needed, the PAN senator predicted that legislation might not reach the floor for several weeks. "I estimate it should be during April [when we will finally discuss the issue] in the Senate," Camarillo said. Committee chair Labastida said that he hoped a bill could reach the Senate floor sometime before the end of March. Mexico's next legislative session runs from Feb. 1 to April 30, so any energy-reform measure would have to be approved during this period unless legislators call for a special session during the summer months.

The Chamber of Deputies is also planning to debate energy reform, but a timetable has not been released. It is likely that the lower house will take its cue from the Senate. PRD adamant against any "privatization" of PEMEX The PRD and its allies in the center-left coalition Frente Amplio Progresista, (FAP) argue that a change to the tax structure for PEMEX is the only major step required to reform the oil and gas sector. The FAP legislators argue that the rising price of oil should provide sufficient revenue to eliminate the need for any injection of foreign capital in PEMEX. "The price of a barrel of crude oil reached US$100 this year," said Sen. Rosalinda Lopez Hernandez. "And there are estimates that it could climb as high as US$150 per barrel next year." The PAN and the PRI are in general agreement with the PRD that the energy reform should not include any changes to Article 27 of the Mexican Constitution, which designates natural resources such as oil as the patrimony of all Mexicans. This, in effect, would eliminate any move toward a direct sale of any portion of PEMEX to private parties.

Still, there is disagreement on whether the involvement of private companies in activities of PEMEX through contracts constitutes privatization. "The efforts by the government of President Felipe Calderon and its supporters to turn over even partial ownership of our reserves to multinational energy companies is doomed to fail," PRD Sen. Carlos Navarrete said at the PRD's meeting in Cabo San Lucas, Navarrete said the multinational energy companies are not entitled to obtain profits from Mexico's oil resources nor should they participate in any other activities related to the oil industry. "Foreigners should not be involved in constructing refineries," said the PRD senator. Some senators suggested that the PRD might be willing to accept foreign partners in some deepwater activities, particularly drilling operations that involve oil in the vicinity of the border between US and Mexican territorial waters.

There is concern that Mexican oil will be sucked over to the US side by drilling there, unless Mexico moves fast to start production. "The proposal [for foreign partners in this endeavor] has a chance," said Fluvio Ruiz Alarcon, an energy adviser to the PRD legislative delegation. "The PRD has people who think it's absolutely necessary." One potential partner is the Brazilian state-run oil company Petrobras, which has extensive experience in deepwater drilling. Mexico and Brazil have already broached the idea of cooperating in oil projects (SourceMex, March 07, 2007 and August 08, 2007).

**PEMEX has history of working with private companies**

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PEMEX has a recent history of working with private companies in exploration, extraction, equipment maintenance, gas distribution, and other activities. In many cases, the contracts are awarded to consortia involving Mexican companies and foreign partners (SourceMex, October 15, 1997, April 28, 1999 and October 19, 2003). In some cases, contracts are awarded directly to foreign companies. One US-based company, Halliburton, has 32 separate contracts with the state-run oil company to conduct perforation, maintenance, and other activities. "PEMEX argues that contracts were awarded to the US company because there were no Mexican companies that had the ability to provide this service," said the Mexico City daily newspaper La Jornada.

It is not clear what changes, if any, the Senate would make to the current practices of hiring foreign companies to conduct specialized activities for a limited period. It is also uncertain whether the PRD position would seek to limit such contracts in the future. The PRD's strong position against private participation in PEMEX stands in contrast to the PRI, where a majority of members are open to at least discussing creating some openings for the private sector to become involved in PEMEX.

The problem for the PRD and its FAP allies is that they don't have sufficient numbers to counteract the large plurality in Congress enjoyed by the PAN, the PRI, and allies like the Partido Verde Ecologista Mexicano (PVEM) and Partido Nueva Alianza (PANAL). The four parties hold 92 of the 128 Senate seats. Some PRD legislators have threatened to boycott Senate deliberations altogether and bring the discussion to the public. This strategy, say some analysts, could leave the PRI as the major power broker in the energy legislation. "With this plan, the PRD would be turning over negotiations with the PAN government to the PRI," said Leo Zuckermann, a columnist with the Mexico City daily newspaper Excelsior. A lack of PRD input could also give the PRI strong leverage to promote its legislative agenda. "The PRI could ask an extraordinarily high price in exchange for its votes in Congress," added Zuckermann.

**Creel-Lopez Obrador debate falls through**

A key member of the PAN, Sen. Santiago Creel Miranda, pushed to hold a public debate on energy reforms with ex-candidate Lopez Obrador, a vocal critic of the Calderon administration and a staunch opponent of opening PEMEX to private investment. Lopez Obrador immediately accepted Creel's proposal, but the plan fell through because of strong opposition from the PAN leadership. Creel, who had seen the debates as a way to clarify the PAN's position against offering ownership of PEMEX to any private sources, had gone as far as making initial contacts with the Lopez Obrador camp to discuss details of the possible debate before the plan was shot down by PAN leaders. "There won't be a face-to-face debate between Creel and Lopez Obrador," said newly elected PAN president German Martinez Cazeres, who said any debates would have to be conducted in the context of hearings and forums organized of the Senate energy committee.

The proposal also drew skepticism from PRI legislators. "If this debate were to take place, Creel would be representing his own personal interests and not those of the Senate," said Sen. Jorge Castro. It is uncertain how much interest a Creel-Lopez Obrador debate would have generated. A public-opinion poll by respected pollster Maria de la Heras showed considerable public apathy regarding the proposal. More than half of the 500 respondents to the poll, about 53%, said they had no interest whatsoever in the debate. In contrast, 19% said they would follow it closely. Still, the
PAN legislative delegation with officials from the Calderon government have acknowledged that the party's primary goal is to push for an energy-reform imitative that would attract an influx of foreign capital and expertise into PEMEX.

Among the proposals offered by the PAN is one to allow greater private investment in refineries, which would increase Mexico's capacity to process its own crude oil into gasoline. The increase in the global price of crude oil has been a double-edged sword for Mexico. While the country continues to enjoy high revenues from crude-oil exports, it also has had to pay large sums for imports of processed products, namely gasoline. In a report published late last year, the Banco de Mexico (central bank) said Mexico's gasoline imports for January-September 2007 amounted to US$7.19 billion, an amount almost eight times higher than during the same period in 2000.

PAN officials argue that strengthening PEMEX could help Mexico improve its financial position to counter the effects of the looming economic slowdown in the US. "Energy reform would be the main impetus to attract foreign investment into Mexico and promote economic growth," said deputy economy secretary Dionisio Perez-Jancome. The governing party has said, however, that elements of some of the proposals floated by the PRD and the PRI could be incorporated into a final package. "We are open to dialogue with all parties to approve those structural reforms that would benefit all Mexicans," said PAN president Martinez. Legislators propose to emulate Brazil's Petrobras. The PAN president said the Senate would consider the experiences of Cuba, Venezuela, Brazil, and the European Union (EU), which use their energy resources to create social wealth. Several legislators said a good example for Mexico to emulate was Petrobas, a company that embarked on a comprehensive restructuring effort over a 20-year period.

The company is now self-sufficient in energy production and is widely known as a global leader in energy technology. "Petrobras' strong performance during the past decade is the result not only of its capabilities in deepwater drilling, but also because it has eliminated dependence on foreign sources to supply fuel to Brazilians," said Labastida. The daily business newspaper El Economista noted strong contrasts between PEMEX and Petrobras in the way in which projects are financed. "Petrobras generates its own financial resources and has the capacity to decide how to use them," said the newspaper, which noted that the Brazilian company finances projects with 93% of its earnings and relies on financial markets for only 7%. "PEMEX, in contrast, finances the majority of its projects via bank loans, particularly from international institutions."

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