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Panel Discussion of the Business of Water in the Republic of Mexico

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John E. Rogers: The case of Cochabamba was mentioned earlier. Are any of you sufficiently familiar with that case to be able to tell us what went wrong and how you would have managed it more successfully?

Jacques Letondot: I have certain ideas about what could have gone wrong. Most probably, the problems began with a misconception of the contractual agreement. It was a concession agreement whereby the responsibility for the provision of water and wastewater services were given to Azurix, which is no longer in business, by the way. What Azurix had in mind, a misconception on their part, was that if they had a sufficiently strong contractual agreement with the municipal government, the municipal government would stick to what it had promised, and everything would go smoothly. In that contractual agreement, the parties had provided for a huge increase of the tariffs to eventually be in a position to improve the system. As it is written in the contract, Azurix had the right to increase the water price by X%. When a municipality does not improve the service first and then increase the tariff, the public can be expected to react strongly. They want to know why they should pay more for a service which is still lousy, water which is still discolored, and to which they can only have access for two hours a day. They wonder if they are simply lining the pockets of a foreign company. The flaw was in the perception of the contractual relationship between the municipal government and the party that holds the concession.

Stephanie Pincetl: I, too, have a question for Mr. Letondot. In the structure that you explained that a private company such as yours can provide, why would a nonprofit organization not be able to provide exactly the same kind of services with the same kind of structural arrangement with a municipality or another kind of level of government? The reason I ask this question stems from the rise in southern California of new governmental arrangements around natural preserves that are being promulgated by the Trust for Public Land and the Nature Conservancy. While they may have some ownership arrangements of land, they also contract to do land management and studies and those kinds of services that are somewhat similar to what you described. Have you seen any examples of that alternative method of service provision in somewhat the same contractual arrangement?

* Biographies of the panel members will follow the discussion.
1. John E. Rogers is an attorney with Strasburger & Price, S.C., in Mexico City.
2. Cochabamba, Bolivia.
3. Stephanie Pincetl is the coordinator of the Sustainable Cities program at the University of Southern California in Los Angeles.
4. Trust for Public Land (TPL) is “the only national nonprofit working exclusively to protect land for human enjoyment and well-being. TPL helps conserve land for recreation and spiritual nourishment and to improve the health and quality of life of American communities.” Their website is http://www.tpl.org/ (last visited 3/30/03).
5. The Nature Conservancy was founded to “preserve the plants, animals and natural communities that represent the diversity of life on Earth by protecting the lands and waters they need to survive.” Their website is http://nature.org (last visited 3/30/03).
LETONDOT: I agree that the provision of those services might be well done by non-governmental organizations (NGOs). The only problem with this is that NGOs might not be the most appropriate body to do it in a widespread way. It is true that for a specific project in a specific place it may work and may be very efficient. For example in El Alto, Columbia, which is a suburb of Bogotá, we are providing the water to the most disfavored population of the capital city of Colombia. We combined our capabilities, equipment, and capital with the workforce of El Alto. All of that has allowed our company to provide water to that part of the city at a lower cost than what they were paying previously to the water vendors from whom they were obliged to buy their water. In order to do that, we formed a partnership with the local church because it was the only organization that was capable of pulling the community together. It worked for that little part of Bogotá, which is almost 600,000 persons, so it can work for other places. I agree that it need not be a private company or corporation. A non-governmental organization may do it.

MIGUEL JÁUREGUI ROJAS: How do you envision obtaining project financing that is more creative than what they have already? The background, as I understand it, is for years we have obtained money from the World Bank and the Federation of Mexico, to train municipal presidents or local authorities of the municipalities to collect and handle money, to give and administer concessions, and to supervise the concessionaires. I do not see that we have improved in issuing municipal paper such as bonds and debentures. What is your idea about that?

RAUL RODRIGUEZ: If you do not solve the basic problems that underlie many of those issues, the financing of this will not improve. At least it will not improve drastically to the point that we actually close that gap between fiscal revenue resources that are available and the investment needs. As I mentioned, you need to close the gap, which is 70% of the total needed.

Let me mention a few specifics here. Going back to guarantees, in most cases in Mexico the assets of public utilities cannot be encumbered. Ultimately, you have to rely on the kind of lending that need does not solve the issue; it is simply a band-aid to the kind of financial challenge that this sector presents.

What we are doing is a bit closer to project finance because we do not have a sovereign guarantee, unlike the World Bank and the International Development Bank (IDB). But still, we are relying on the participaciones and other kinds of very limited sources of guarantee in order to finance and move these projects forward. Ultimately, we must develop the municipal financial market. That is the litmus test in terms of reaching a solution. Examples are everywhere, starting with the U.S. itself, where there are thirty years or more of successful finance market operation. In fact, what do you recall in terms of failures? Orange County? Was that truly a failure of a market structure and design, or something else? Other than that, the market has been pretty successful, well run, and very fruitful, particularly in terms of the vicious process that it takes in a particular community.

6. Miguel Jáuregui Rojas is a founder and member of the firm of Jáuregui, Navarrete, Nader, y Rojas in Mexico City.

7. Debentures are defined as unsecured debt backed only by the integrity of the borrower, not by collateral, and documented by an agreement called an indenture. One example is an unsecured bond.
I would daresay that in the Mexican case, as in general in the developing world, the development of the municipal financial market has many more obstacles on the political side than on the technical/financial side.

**Molly Macintosh:** I have a question about private water markets for Mr. Stokes. What is there in the overarching framework in that area of Las Cruces, Juarez, and El Paso for a farmer whose land has been reduced down to 20 acres? What is going to prevent him in the future, as demand increases, from selling his water right across the border? Assume first that there is no return flow, but then in the second hypothetical, if there were some way to bring the return flow back to New Mexico, is there anything that would prevent that?

**Len Stokes:** The courts have yet to decide whether it would be preventable or not. New Mexico has introduced some statutes that are designed not to prevent export, necessarily, but to assure that New Mexico has enough water for the needs of New Mexicans in the foreseeable future, which has been defined as 40 years. That is where the New Mexico export statute is pinned, and I expect a test relatively soon. Our neighbors to the south are indicating that such a test will take place. I think eventually it will. I represent the City of Las Cruces and my job is to do the best I can for them, and if that is to work in this market before the price gets through the ceiling, then I will try to keep the price from going through the ceiling. The courts will ultimately decide if we can protect that for very long.

**Macintosh:** There is going to be obviously huge demand in the future and some very thirsty people in the area, and I wonder, Mr. Ramos and Mr. Hernandez, would there be anything under Mexican law that would prevent a Mexican community or a rancher from purchasing water from across the border? From what you have said, I assume it would be impossible to sell in this direction.

**Carlos Ramos Miranda:** I do not see anything that would prevent it, but it becomes a matter of how to deliver the water. During delivery, if the water touches some type of national surface, that water would become national property. There would need to be some type of concession from that point. It really depends on how the water is channeled.

**Student:** With regard to water transfers within Mexico, is that a possibility? Is there a Mexican counterpart to what the United States has done and if so, how does that happen?

**Hernandez:** Yes, there is the possibility, especially with the creation of the water rights registry. Water rights may now be transferred provided they are in the same area. One of the things that struck me was when you mentioned consumptive use is that it is the key word used in the law. One can freely transfer water rights, provided the consumptive use is the same. If the water will be used for a different purpose or different consumptive use, then a permit is required from the National

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8. Molly MacIntosh is an attorney with Bauman & Dow, P.C., in Albuquerque, New Mexico.
Water Commission. But one can transfer water rights. Now, say you own a concession under which you operate a well, to maintain an industrial facility. Say you own a maquiladora and you are shutting it down because you are transferring to China. Then you sell your water rights to an interested entity, the first well is shut down, and the second well is drilled, or if it is already drilled then it is put into operation because you transferred your water rights.

STUDENT: Then it can be sold and the compensation goes to the previous owner, is that correct?

HERNANDEZ: Yes, you determine the price. It is supply and demand. In your off-limits zones, the water rights can become very expensive because no new wells are permitted to be drilled.

MIRANDA: The law allows for the use of water. Once the concessionaire has used the water, before it is finally disposed, it can continue to be exploited by third parties. So there is also a possibility to create some other type of markets and business opportunities for water, while enhancing the most efficient water use.

DAVID BROOKSHIRE: Mr. Letondot you spoke of the real economic price. Actually, this is a contentious issue that communities, governments, states, and individuals face. The University of New Mexico has done some work that shows the price of water is 80% below its scarcity value. From your firm’s point of view and from a private enterprise point of view, it would be helpful if you could clarify what the real economic price is, because I suspect the real economic price would be different from the perspective of the non-governmental organization (NGO) that Stephanie Pincetl spoke of. Could you clarify what your firm thinks of as the real economic price? Is it simply recovery of cost and no scarcity value?

LETONDOT: It is very simple. It is all the costs associated with the production, distribution, and transportation of the water plus a certain amount of margin that is the normal expected return. It is not more than that.

BROOKSHIRE: So, the classical term cost does not include environmental cost?

LETONDOT: Well, if the municipal government includes an environmental cost, then it would be included in the price. In many countries you have, whenever you use a well, obstruction rights and therefore you have to include that in the price of the water, which is to be borne by the consumer. But it is more than the cost.

9. David Brookshire is a Professor of Economics at the University of New Mexico in Albuquerque, New Mexico.

10. Scarcity value is an economic term attached to water and wastewater use signifying the marginal productivity or utility of water as a scarce resource. Demand for water, potential uses of water, and profits that can be derived from water all figure into its scarcity value.
Biographical Summaries

Moderator:

Lic. Abdon Hernandez is Group Vice President and General Counsel of Industrias Penoles, S.A. de C.V. Lic. Hernández was a founding member of the Asociación Nacional de Abogados de Empresa, A.C. (ANADE) and President from 1982 to 1984. He is President of the Legislative Commission of the Mining Industry Chamber of Commerce since 1987. He is a Member of the Board of Directors of the United States-Mexico Law Institute and the American Bar Association Section of Business Law and International Law and Practice. He was the President of the Legislative Analysis Commission of the Consejo Coordinador Empresarial from 1985 to 1989. He has published articles on Business, Corporate and trade law matters. He has the B.A. degree from Bard College, New York, the MBA from the Universidad de las Americas, Mexico City, the Advanced Management Diploma from Pennsylvania State University, and the licenciado en derecho from the Universidad Nacional Autónoma de México in 1963.

Commentators:

Jacques Letondot holds an MBA of Economy from the French University of Paris II, Pantheon/Sorbonne. After four years as a civil servant in the French Ministry of Finance, Jacques Letondot has spent his entire professional career in the group now known under the name of Suez, a multinational industrial group active in the fields of water and waste water, industrial and municipal waste, electricity, gas and communication services. He has held managerial position in various subsidiaries of the group i.e. ETPM an offshore oil development company (Chief Financial Officer), GTM a civil Construction Company with a focus on concession operations (Deputy General Manager) and ONDEO Services the Suez subsidiary in charge of the water and waste water operations throughout the world. Appointed in 1994 Managing Director for Greater China and Director of Lyonnaise Asia Water, an Investment Fund seeking participations in water operations in Asia, he has contributed significantly to the expansion of the activities of the group wit more than 12 joint venture contracts signed with various municipal governments in China. He was also President of the French Chamber of Commerce in Hong Kong from 1998 to 2001. In 2001 Jacques Letondot was appointed Managing Director for Central Europe and Central Asia of Ondeo Services responsible for the existing activities and their development in those countries. Following the creation of the Suez Environment division in 2002 he was nominated Managing Director, based in Mexico, to follow its activities in Mexico, Central America, and the Caribbean. Mr. Letondot has been a French Foreign Trade Advisor since 1998.

Lic. Carlos Ramos Miranda has recently been appointed as Co-Chair of the Mexican Law Committee of the American Bar Association. He has published papers and law review articles, among them: “Doing Business in Mexico through a Joint Venture Agreement” (1995); “Foreign Investments in Mexico” (2001) and “Concentrations under the Federal Antitrust Law” (2001). As a member of Barrera, Siqueiros y Torres Landa for over 10 years, Lic. Ramos Miranda has developed his expertise in
corporate, foreign investments, insurance, project finance, procurement and water law. He was a foreign intern in the law firm of Dickstein, Shapiro, Morin & Oshinsky, Washington, D.C., from 1995-1996. He has also been a professor of Corporate Law at Universidad Anahuac and currently teaches Corporate Law at the Instituto Tecnológico Autónomo de Mexico. Lic. Ramos Miranda graduated from the Instituto Tecnológico Autónomo de México Law School in 1994. He later obtained, his LL.M. degree, at the Georgetown University School of Law, in 1995, and in 1996 he obtained a diploma on Executive International Finance, from the Georgetown University School of Business.

Len Stokes consults in the areas of water, wastewater, and environmental issues. He has managed the design, permitting, and construction of four major solid waste landfills in southern New Mexico. He has also served as project manager on three wastewater treatment plants in the State. For the past six years, Len has focused primarily on water supply and water rights issues. Mr. Stokes serves as consultant, facilitator, project manager, and as a legislative lobbyist for his clients on those issues. At the current time his clients include the City of Las Cruces, the City of Alamogordo, the Lea County Water Users Association, and the Village of Ruidoso. Mr. Stokes attended New Mexico Military Institute and New Mexico State University.

Raul Rodriguez is currently the Managing Director and the CEO of the North American Development Bank. Mr. Rodriguez has been Executive Director of the Mexican Foreign Trade Bank; Mexico's Trade Commissioner in Canada; Secretary of Economic Development for the Mexican border State of Tamaulipas; and Professor and Research Fellow at ITESM. He has also participated as a speaker and lecturer in more than 30 countries on business, financial and managerial topics. Mr. Rodriguez holds a degree in Engineering from the Monterrey Institute of Technology and Advanced Studies (ITESM) and a Master's degree in Public Administration from Harvard University.