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COFECE issues recommendations to Mexican Congress on the initiative to reform the Law of the Electric Industry

On February 12, 2021, the Board of Commissioners of the Mexican Federal Economic Competition Commission (*Comisión Federal de Competencia Económica*, “COFECE”) issued an opinion on free concurrence and economic competition, with non-binding effects and identified as OPN-001-2021, addressed to the Mexican Congress (*Congreso de la Unión*, the “Congress”) (the “Opinion”), whereby it recommends not to approve the initiative presented by the Federal Executive to Congress which seeks to reform the Law of the Electric Industry (the “Initiative”), since it would severely damage competition in the generation and commercialization of electricity.

COFECE determined that the Initiative, if approved in its terms, would have such adverse effects, since:

- (a) It would eliminate the economic dispatch of electricity (which implies first taking the electricity offered at the lowest price), modifying the order of priority for its dispatch, favoring the Federal Electricity Commission (*Comisión Federal de Electricidad*, “CFE”).**

The economic dispatch of electricity guarantees that the energy with the lowest price is dispatched first. The Initiative eliminates this rule and establishes that electricity must be dispatched in the following order of priority: (i) firstly, dispatching hydroelectric plants, which are mostly owned by CFE; (ii) secondly, dispatching other CFE power plants; (iii) thirdly, wind and solar power plants; and (iv) fourthly, privately-owned combined-cycle power plants. COFECE stated in its Opinion that the proposed modification in the order of dispatching as established in the Initiative would artificially benefit CFE, since it would guarantee the sale of its electric energy without necessarily being the one with the lowest price, and would harm other generators, consumers and the environment.

In the Opinion, COFECE recommends maintaining in the Law of the Electric Industry (*Ley de la Industria Eléctrica*, “LIE”) the obligation to guarantee economic dispatch since it is an essential tool aimed at preserving a competitive environment that motivates the most efficient generation of electricity and, therefore, consumer access to it at the best possible prices.

- (b) It would undermine the principle of open access to the National Transmission Network and the General Distribution Networks, affecting competition in the generation and commercialization of electricity.**

COFECE recognizes in its Opinion that the National Transmission Network (*Red Nacional de Transmisión*, “RNT”) and the General Distribution Networks (*Redes Generales de Distribución*, “RGD”) constitute fundamental inputs to compete in the generation and commercialization of electricity, since both generators and suppliers need access to the RNT and the RGD to be able to deliver electricity from power plants to final users. As stated by COFECE in its Opinion, the Initiative, if approved in its terms, would grant the National Energy Control Center (*Centro Nacional de Control de Energía*, “CENACE”) broad discretion to deny access to the RNT and the RGD for

“technical reasons”, without providing the specific criteria to deny such access and without regard to the fact that the current legislation already regulates the terms and conditions that apply to all connections and interconnections. Such discretion could deny access to the RNT and RGD to certain power plants in situations where it should not be denied for technical reasons.

Therefore, COFECE recommends in the Opinion to maintain the obligation to guarantee open and not unduly discriminatory access to the RNT and the RGD on the terms and conditions currently established in the LIE.

(c) It would allow CFE Basic Services Supplier to acquire electricity without resorting to competitive mechanisms that guarantee better prices.

The LIE establishes that CFE Basic Services Supplier (*CFE Suministrador de Servicios Básicos*, “CFE SSB”) may enter into legacy supply contracts (*contratos legados de suministro*) to acquire electricity from legacy power plants (*centrales legadas*), which are power plants owned by CFE that were already in operation at the time the LIE entered into force or that were projected in the 2014 Federal Expenditure Budget. Legacy contracts were designed as a transitional contractual mechanism, intended to promote an orderly transition to a competitive electric market in such a way that, upon expiration of such contracts, CFE SSB could only acquire electricity through competitive auction mechanisms.

The Initiative proposes to classify as legacy power plants any CFE power plant, even new ones, and to eliminate the obligation of CFE SSB to participate in auctions to buy electricity, allowing CFE SSB to acquire electricity through non-competitive means.

In this regard, COFECE recommends not to modify the legacy contract regime, maintaining its transitional nature, and above all maintaining in the LIE the obligation for basic suppliers to comply with their electricity coverage commitments through competitive methods, which would require reinstating the electricity auctions organized by CENACE.

(d) It would allow the Commission for Energy Regulation (*Comisión Reguladora de Energía*, “CRE”) to deny the granting of permits without cause, which would create legal uncertainty for participants to compete in the electricity market.

The Initiative would grant broad discretion to the CRE for the granting of permits, which would generate legal uncertainty, affect market entry conditions and reduce incentives for new investments in electricity generation projects.

Therefore, COFECE recommends in the Opinion to avoid tying the granting of permits to unclear criteria and to ensure the timely resolution of all applications for new permits and for amendments to existing permits.

(e) It would disrupt the Clean Energy Certificates (“CELS”) market by increasing the CEL supply and eliminating the effectiveness of this mechanism to promote the development of additional clean energy generation capacity in the country.

The purpose of the CELs is to promote the development of new electricity generation projects through clean energy sources and to increase the generation capacity through these sources, in

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order to incentivize the development of additional clean generation capacity to reach Mexico's clean energy commitments.

The Initiative provides that all power plants that generate electricity through clean energy sources should be entitled to receive CELs, even those in operation before the LIE came into force. This would eliminate all together the functionality of the CELs as instruments to motivate new investments in clean energy generation, as the number of available CELs would increase considerably if the Initiative is approved in its terms, but it would not necessarily mean that Mexico would be generating more clean energy.

Therefore, COFECE recommends in its Opinion not to modify the criteria for the granting of CELs so as to ensure that the CELs remain as a mechanism to promote the development of clean energy projects and enable Mexico to meet its clean energy commitments.

The Opinion is especially relevant to highlight COFECE's position that the Initiative, if approved in its terms, would contravene the constitutional framework that governs the national electricity industry at present, which is based on principles of free competition and free concurrence. COFECE's analysis of the Initiative demonstrates, once again, the importance of having a technical authority in Mexico, as an autonomous constitutional body, protector and promoter of competition in the markets, for the benefit of society.

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