

“Energy Reform in Mexico: Pemex and its new role as a State-Owned Enterprise”

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1. Pemex's timeline in a nutshell.

FIRST STAGE. From 1938 to 1960 (Pemex as the administrator).

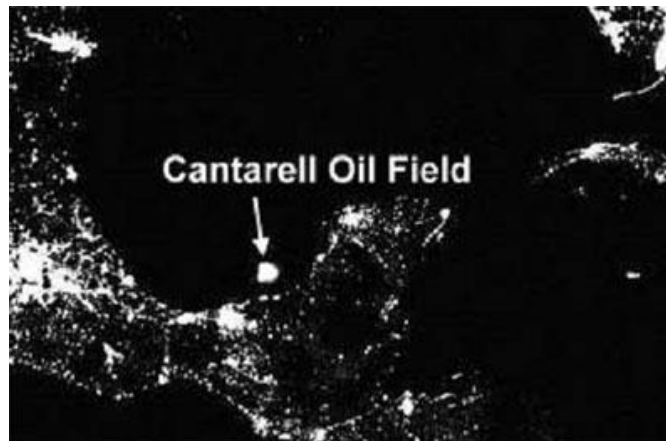
- Created by a Legislative decree on June, 1938 as a result of the **Mexican oil and gas expropriation** of March 18, 1938 (Mexican holiday).
- Originally, **not intended to exclude market participation**, but to serve as the **administrator of the recently expropriated resources** and infrastructure to help booster the social welfare and economic development.
- **Significant investment** in the period: upstream infrastructure, refining and transportation capacity.



1. Pemex's timeline in a nutshell.

SECOND STAGE. From 1960 to 1992 (Pemex as owner).

- Amendments to implementing legislation required **Pemex to act as a Monopoly** in Oil and Gas operations. Joint-Ventures and associations prohibited.
- Assumed the “*de facto*” responsibility of conducting the energy policy of the country and assuring its sustainability.
- This new role started the **decline in benefits** (production and internal capacity) but in **1976 Cantarell saved the show**.



Cantarell at night, with oil flares visible. Image courtesy of NASA.

1. Pemex's timeline in a nutshell.

THIRD STAGE. From 1992 to 2008 (“Status Quo”).

- Pemex's **contribution to government expenditure** reaches **30%** (and will be maintained there for upcoming years).
- Consensus that **change is needed** but no clarity on the extent.
- 1992, New **Pemex's Law** with **4 subsidiaries created** (E&P, Refining, Gas, Sec. Petrochemicals).
- Mexican giant **Cantarell** formally declared as a **declining field (Easy Oil gone)**.

1. Pemex's timeline in a nutshell.

FOURTH STAGE. From 2008 to 2013 (First effort).

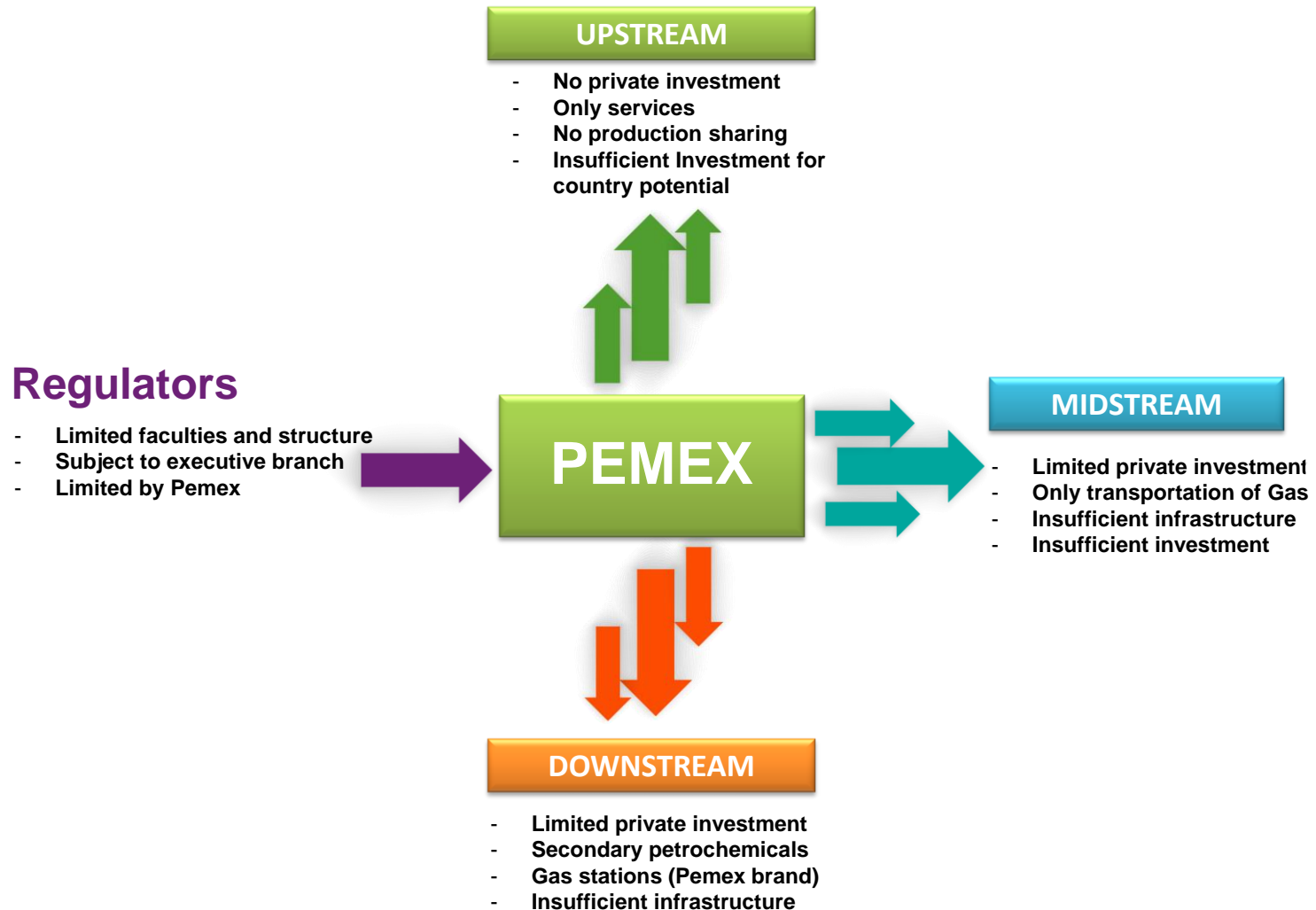
- **No consensus** for Constitutional amendment.
- **New Pemex's Law** enacted including **exceptional regimes**.
- **“Incentivized agreements (COPF's and CIEP's)”** executed. Closest to E&P operations in the country. Based on **fixed payment plus incentive**.
- **Operators not interested** in the scheme.

1. Pemex's timeline in a nutshell.

CURRENT STAGE. From 2013 to today (Integral Energy Reform).

- **Constitutional** amendment.
- Pemex should **take care** of ... Pemex.
- Government **reassumes ownership and control**.
- True **exceptional regimes**.
- Principle of **added value** and **best practices**.

2. Pemex and the Oil and Gas Industry: Prior to the Reform.



2. Pemex and the Oil & Gas Industry: Post Reform.

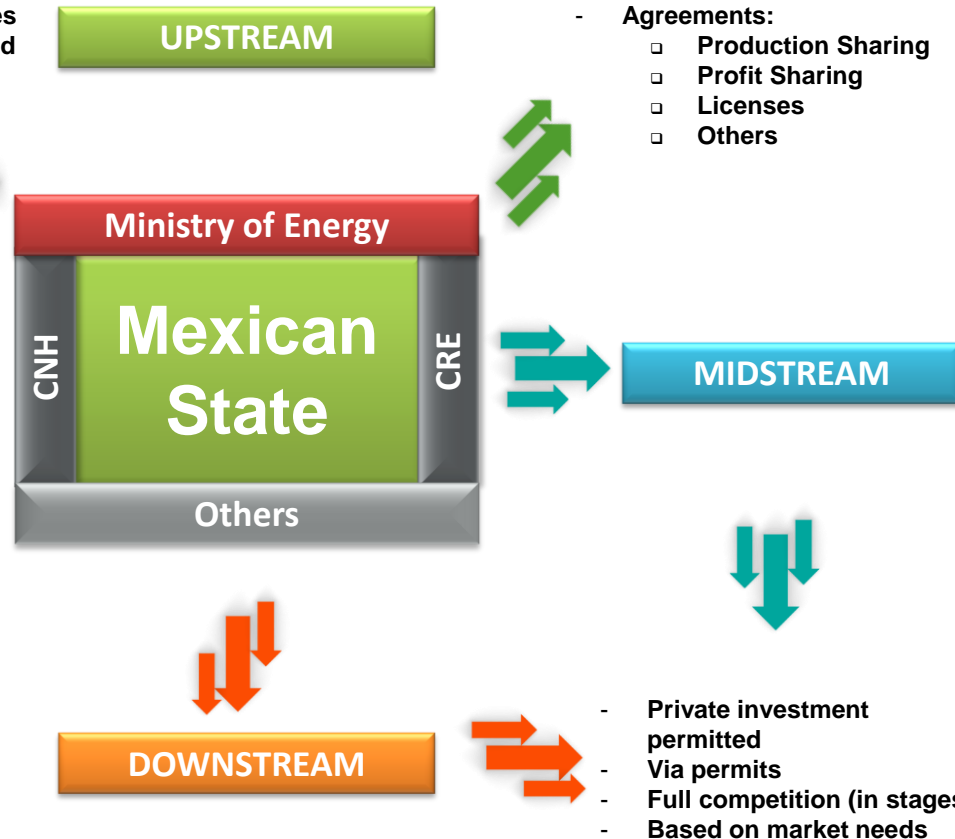
Assignments

- No private investment
- Round "0" is the basis
- Only to Governmental Companies
- Only services contracts permitted
- May be transformed into E&P



Regulators

- Strong faculties
- Autonomy to make decisions
- Act in benefit of Industry



E&P Agreements

- Private investment permitted
- Via Public Tender
- Agreements:
 - Production Sharing
 - Profit Sharing
 - Licenses
 - Others

Figure 2

3. What are State-Owned Enterprises?

- **New legal entities** not previously considered in Mexican law.
- Ownership **must remain** with the government (Constitutional provision).
- Operational scheme **based on best practices**.
- Part of the executive branch but **focused on productivity and value**.
- **Exclusivity** in receiving **assignments** (Round “0”).
- True **exceptional regimes**.
- Commercial activities **as private parties**.

4. The concept of “*competition*” for Pemex.

- Pemex has **never faced competition** inside of Mexico.
- Focused on **profitability** as a company.
- **Upstream:** present **offers for new fields**; can **lose assignments**.
- **Upstream/Downstream/Midstream:** May refuse and abandon projects.
- **Efficiency** is a must (procurement, financial, human resources).
- In a nutshell, **treated as an enterprise**.

5. New corporate structure and special regimes.

- **How to face competition?** New corporate structure/Special regimes

New corporate **structure**:

- ✓ **Prior to the Reform (Pemex and 4 subsidiaries):**

- ❖ E&P.
- ❖ Refining.
- ❖ Gas and Basic Petrochemicals.
- ❖ Secondary Petrochemicals.

- ✓ **Post Reform (Pemex, 2 subsidiaries and 5 affiliates):**

SUBSIDIARIES

- ❖ E&P (Subsidiary).
- ❖ Industrial Processing (Midstream & Downstream).

AFFILIATES

- ❖ Drilling.
- ❖ Logistics.
- ❖ Cogeneration and Services.
- ❖ Fertilizers.
- ❖ Ethylene.

5. New corporate structure and special regimes.

- **How to face competition?** New corporate structure/Special regimes

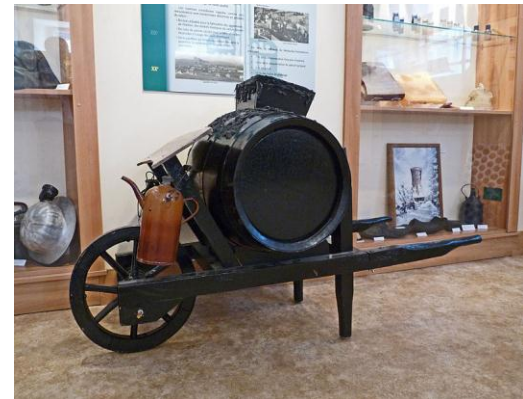
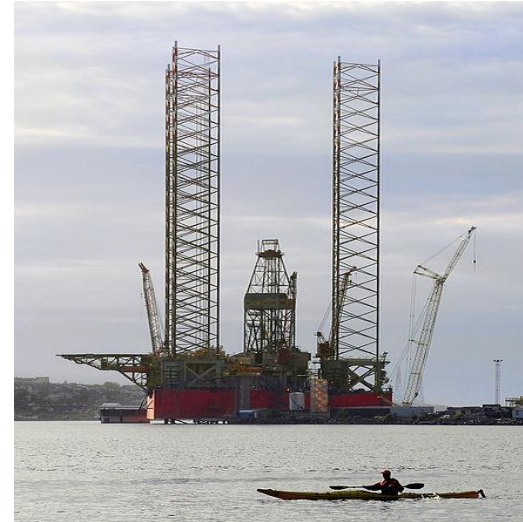
Special regimes:

- **Human resources:**
 - ✓ Protect and **retain talent**.
 - ✓ Constitutional provision that **no public servant can make more** than the President.
 - ✓ **No lay-offs** expected.
- **Procurement:**
 - ✓ Special **flexible regime**.
 - ✓ New **centralized system**.
 - ✓ **Category** management.
 - ✓ Can procurement **make the difference?**
- **Others:**
 - ✓ Assets and liabilities.
 - ✓ Budget.
 - ✓ Debt.

6. Pemex and “upstream”: Opportunities in Mexico.

UPSTREAM

- **Upstream** remains as the only “*strategic*” activities in the Constitution, **subject to substantive control**.
- **Assignments** (entitlements):
 - ✓ Only awarded to **State-Owned Enterprises**.
 - ✓ **No right to free association** (JV, PSA’s and others).
 - ✓ **Services** contracts permitted.
- **E&P Agreements**:
 - ✓ **Free to associate** but subject to compete.
 - ✓ Joint ventures permitted.
 - ✓ **Restrictions** imposed by **SENER** or **CNH**.



6. Pemex and “upstream”: Elsewhere?

UPSTREAM

- **No restrictions:**
 - ✓ Decided by the **Board of Directors** as part of strategy.
 - ✓ Pemex **can and will** invest abroad.
 - ✓ May also **act as operator** (Vaca Muerta).

7. Pemex and “midstream-downstream”: Opportunities in Mexico. Elsewhere?

MIDSTREAM

- **General Rule:** No restrictions/Free market.
- **No longer considered “Strategic”.**
 - ✓ This allows for **private participation**.
 - ✓ **Regulated free market conditions**.
- **Procedure.**
 - ✓ Preparation of **projects**.
 - ✓ **Permits** issued by the regulator.

DOWNSTREAM



8. What is the strategy?

- **Solid basis and diversify.**
- **Solid basis:**
 - ✓ Resources acquired from **Round “0”** (Assignments).
 - ✓ **20.5 Bboe** in 2P reserves.
 - ✓ **2.5 Mboe** per day for **next 20 years**.
 - ✓ **JV’s** through **services agreements**.
- **Diversify:**
 - ✓ **All Rounds: NO!** (shallow waters).
 - ✓ **Strategic Rounds: YES!** (deep water and shale).
 - ✓ Investment and operation **abroad: YES!**
 - ✓ **JV’s** in Mexico for **Upstream: YES!**
 - ✓ **Midstream** and **downstream: YES!** (efficiency agreements, operation agreements and others).

9. Questions?

Fernando Cano-Lasa is a Mexican licensed attorney currently working for Squire Patton Boggs as Of Counsel based on the firm's Houston office. Prior to joining Squire Patton Boggs, Fernando worked for Pemex and its subsidiary and affiliated entities for more than 12 years in such roles as in-house counsel for the Chief Legal Office and Vice President of Legal and Strategy of Pemex Procurement International, Inc. Fernando holds the equivalent of a J.D. degree for the Universidad Panamericana in Mexico City and a Master of Laws degree from the University of Houston, Law Center. Fernando has appeared as a speaker on several panels dealing with the Energy Reform in Mexico, including those organized by the University of Houston Law Center, the Association of International Petroleum Negotiators (AIPN) and the International Law Section of the Houston Bar Association. Fernando's practice is focused on advising international clients on Mexico and Latin America energy and infrastructure projects and all types of corporate transactions in the region.