

Exploring new horizons:

How Louisiana businesses can prosper in an era of Mexican energy reform

BY EDWARD H. WARNER & DANIELA SUÁREZ DE LOS SANTOS

Energy reform in Mexico has ushered in a new era of partnerships, foreign direct investment, and future success stories for both Mexico and foreign businesses. Arguably, Louisiana businesses are in a great position to participate due to their incredible expertise in oil and gas. This article describes how Louisiana businesses can participate in the historic reform in Mexico while managing risk and a new legal landscape. Mexico's new energy legislation restructures the entire Mexican energy sector; however, the scope of this article is limited to oil and gas exploration and extraction.¹

The argument for mutually beneficial relationships between Mexico and Louisiana businesses

Companies in Louisiana now have the opportunity to build long-lasting relationships with a nearby neighbor that has an abundance of untapped resources. Mexico's new energy market welcomes the private sector (including U.S. companies) to participate and compete in projects for upstream, midstream and downstream activities.² Although at the time of the writing of this article the price of oil is low,³ creating these relationships now could produce long-term benefits for both Mexico and Louisiana's oil-and-gas industries.

Louisiana businesses certainly have the expertise that Mexico needs. Foremost, Louisiana is one of the U.S.'s top natural gas producers. It is also the country's top crude oil producer when production from its section of the federally administered Outer Continental Shelf (OCS) is included.⁴ Louisiana businesses have efficiently utilized new technology, such as hydraulic fracturing, and Mexican energy executives have already begun visiting Louisiana areas to "tap Louisiana oil and gas know-how."⁵

While Louisiana businesses have the expertise, there is a question as to whether many of the small and mid-sized companies will have the financial means to participate in the Mexican energy sector. However, it is likely that mature fields, oil and gas fields that were once in production but stopped because they required more investment, are great opportunities for small and mid-sized energy companies. The mature fields require a much smaller initial investment compared to offshore projects.⁶ There are also opportunities for Louisiana's many oil-and-



Photographed while in Mexico are authors Edward H. Warner and Daniela Suárez de los Santos.

gas service companies.

In sum, Mexican energy reform is an exciting development for Louisiana businesses that have the capacity and expertise to participate in new energy opportunities.

What background information must Louisiana businesses know in order to participate in the Mexican energy market?

Petroleos Mexicanos (Pemex) is fundamental to Mexico's oil-and-gas market. Pemex, Mexico's sole oil producer, had one of its biggest discoveries in years when it recently found four new oil-and-gas fields in shallow water in the Gulf of Mexico.⁷ Even so, this recent discovery comes at a time when Pemex's oil production has been undermined.⁸ Pemex previously produced approximately 5 million barrels of oil a day, whereas now it only produces about half of that amount.⁹

The recent energy reform legislation has opened the door for private investment and collaboration that could put the country back on track. In addition to amending the constitution, Mexico's congress also passed the Hydrocarbons Law and reformed the Foreign Investment Law.¹⁰ While other laws and reforms were also passed, the Hydrocarbons Law and the Foreign Investment Law are two prominent measures pertinent to U.S. oil-and-gas

exploration-and-production (E&P) companies. These laws directly impact foreign investment in oil-and-gas E&P.

The restructuring of Pemex is also significant. For nearly 75 years, Pemex controlled all petroleum production in the country. Under the new legislation, Pemex is a State Productive Enterprise or SPE. This means that Pemex will be able to enter into joint ventures with the private sector to explore and develop oil-and-gas-producing areas under various types of E&P contracts.¹¹

The new contracts have the potential to generate tremendous revenue for foreign companies operating in Mexico. Companies will be able to apply for various E&P contract models including license contracts, production-sharing contracts, profit-sharing contracts and service contracts. Generally, these contracts are awarded through public bidding processes, and foreign companies that partner with Pemex are likely to get more favorable consideration in the awarding of contracts.

In sum, Louisiana companies should consider collaboration with a Mexican company, particularly Pemex, to successfully enter the market.

What are the practical steps a Louisiana business must follow to enter the Mexican energy market?

As a preliminary matter, each Louisiana business entering the Mexico oil and gas market should be prepared for a process that will take at least nine months to a year.¹² The companies should be prepared to navigate various regulatory agencies.

First, companies start the bidding process by paying a fee to gain access to the “Data Rooms” and become pre-qualified. The Data Rooms will contain geological information pertinent to the E&P site. The National Hydrocarbons Commission (Comisión Nacional de Hidrocarburos or CNH) will publish a list of the technical, operational, financial and legal documentation necessary for the prequalification process.¹³

Second, after presentation of prequalification documents and bid submissions by interested companies, CNH will award contracts and announce the winners. CNH is charged with executing E&P contracts, and the model of the contract will depend on the conditions of the E&P site offered.

Finally, it is important to note that CNH may only execute E&P contracts with Mexican-incorporated commercial entities. Thus, prior to, or upon selection as a winning bidder, a Louisiana business must form or acquire a Mexican business entity. Some of the requirements for registering a new company may take up to nine months for completion.¹⁴

In sum, Louisiana businesses should be prepared for a relatively long and arduous process in order to participate in the Mexican energy sector. Foreign companies should be aware of CNH, one of the key regulators in Mexico.

Other major regulators include the Ministry of Energy (Secretaría de Energía or SENER), Ministry of Finance (Secretaría de Hacienda y Crédito Público or Hacienda), and the Energy Regulatory Commission (la Comisión Reguladora de Energía or CRE).

What are the additional ways Mexico has made its oil-and-gas market more attractive?

Many experts with an eye on the Mexican energy market raise the issue of transparency. Mexico, in addition to opening its market to foreign investment, has implemented important measures to ensure that the energy reform progression is a transparent process. Essentially, with the goal of increasing interest in the market and making it more attractive, Mexico has established eight principal transparency and anticorruption mechanisms that comply with well-known international norms.

First, all of the bidding rounds to assign license contracts, profit-sharing/production-sharing contracts, and service contracts will be made public. The bidding process guidelines will also be available to the public.¹⁵

Second, each contract that is awarded will constitute a legal act (instrumento jurídico) under Mexican law. The contracts will contain transparency clauses so that they can be viewed by the public.¹⁶

Third, all natural gas and oil E&P companies have public-disclosure requirements. Each company must make public all costs incurred and any payments received in the process of oil-and-natural-gas E&P.¹⁷

Fourth, the Mexican government will also have public-disclosure requirements. The government must make public any natural gas or oil that it extracts in connection with an oil contract under the new legislation. The government must also disclose how the natural resources will be used.¹⁸

Fifth, the regulatory agencies that implement and monitor the oil reform progression will be subject to strict transparency rules and auditing/accountability measures. Salient measures to hold regulatory bodies accountable include responsibilities such as establishing a code of ethics for each agency and the removal of agency commissioners for cause.¹⁹

Sixth, Pemex must make public disclosures modeling the requirements of companies listed in the Mexican Stock Exchange. The terms of such disclosures must also comply with the strictest international standards.²⁰

Seventh, the Mexican government has established a system of checks and balances between four government agencies: SENER, Hacienda, CNH, and the Mexican Petroleum Fund. The system ensures transparency and accountability in the design, administration, and bidding of the hydrocarbon E&P contracts, and prevents any contract assignment from being a discretionary decision of any one government authority.²¹

Finally, Mexico recently passed the constitutional


reform establishing the new anticorruption law (El Sistema Nacional Anticorrupción or SNA). The new system will create a coordinated effort among various levels of the government to prevent, detect and sanction administrative liability for corruption.²²

In sum, Mexico has introduced numerous transparency mechanisms that aim to minimize legal risk.

Conclusion

There is a strong argument for Louisiana businesses to begin entering the Mexican market. Louisiana businesses that have the required financial capital and expertise are likely to be contenders in the bidding rounds. However, companies should set expectations for a long and arduous process.

Nevertheless, partnering with Mexican companies, particularly Pemex, is likely to ease the process of entering the market and result in more favorable consideration for contract awards.

The question remains which will be the first Louisiana-based company to explore new horizons in this era of international partnerships?²³ 

¹ Given the recentness of this legislation and on-going efforts by the Mexican government, the information in this article is subject to change and/or modification.

² *Key elements of the Energy Reform*, Mexican Embassy in the United States, <http://embassyofmexico.org/web/KeyElementsoftheEnergyReform.pdf.pdf>.

³ Campbell Roberston, *Louisiana Squeezed as Oil Prices Drop*, The New York Times (Jan. 31, 2015) http://www.nytimes.com/2015/02/01/us/louisiana-squeezed-as-oil-prices-drop.html?_r=0.

⁴ *Industry Sectors*, Louisiana Mid-Continent Oil and Gas Association, <http://www.lmoga.com/industry-sectors/> (last visited July 9, 2015).

⁵ Billy Gunn, *Mexican energy officials looking to tap Acadiana's expertise*, The Advocate (Sept. 9, 2014) <http://theadvocate.com/home/10180649-123/mexican-energy-officials-looking-to>.

⁶ Sergio Chapa, *Mexico's 'Mature Fields' Bids an Opportunity for Smaller Companies*, San Antonio Business Journal (July 12, 2015), 2015 WLNR 13939829.

⁷ Adam Williams, *Pemex Reports Its Largest Oil Find in 5 Years in Gulf of Mexico*, Bloomberg Business (June 10, 2015) <http://www.bloomberg.com/news/articles/2015-06-11/pemex-reports-its-largest-oil-find-in-5-years-in-gulf-of-mexico>.

⁸ John Burnett, *Excitement Over Mexico's Shale Fizzles As Reality Sets In*, NPR (March 16, 2015) <http://www.npr.org/sections/parallels/2015/03/16/393334733/excitement-over-mexicos-shale-play-fizzles-as-reality-sets-in>.

⁹ Gunn, *supra* note 5.

¹⁰ The Hydrocarbons Law, Cámara De Diputados Del H. Congreso De la Unión (Aug. 11, 2014) http://www.diputados.gob.mx/LeyesBiblio/pdf/LHidro_110814.pdf; The Foreign Investment Law, Cámara de Diputados del H. Congreso de la Unión (Aug. 11, 2014) http://www.diputados.gob.mx/LeyesBiblio/pdf/44_110814.pdf.



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¹¹ Guillermo Zúñiga, *Energy Reform in Mexico: Overview, Challenges & Opportunities* [PowerPoint slides], EUCI (July 21, 2015) <http://www.euci.com/preconference/jul21energy-reform.pdf>.

¹² Interview with Claudio Rodriguez, Partner, Ramírez, Gutiérrez-Azpe, Rodríguez-Rivero y Hurtado, S.C., Mexico City, México (July 2, 2015); Interview with Miguel Cinta, General Manager, ABS Group, Mexico City, México (July 2, 2015).

¹³ Comisión Nacional de Hidrocarburos (CNH), *Prequalification Criteria R01-L01/2014*, (2014) [http://ronda1.gob.mx/English/pdf/PDF-L-01/R01L01 Prequalification Criteria.pdf](http://ronda1.gob.mx/English/pdf/PDF-L-01/R01L01%20Prequalification%20Criteria.pdf).

¹⁴ University of Texas at San Antonio, et al., *Economic Impact and Legal Analysis of the Shale Oil and Gas Activities in Mexico*, ISBN 9709882791 (May 2015) <http://www.iedtexas.org.php53-6.dfw1-2.websitetestlink.com/wp-content/uploads/2015/05/MXShale-web.pdf>.

¹⁵ Gabriel Heller Green, *Reforma Energética: Ronda 1*, Secretaría de Energía, Director General de Relación con Inversionistas y Promoción http://sener.gob.mx/webSener/rondauno/_doc/Reforma%20Energetica%20Ronda%201.pdf

¹⁶ The Hydrocarbons Law, Article 19, Section IX, Cámara De Diputados Del H. Congreso De la Unión (Aug. 11, 2014) http://www.diputados.gob.mx/LeyesBiblio/pdf/LHidro_110814.pdf.

¹⁷ Green, *supra* note 15.

¹⁸ *supra* note xvi at Capítulo II De la Transparencia y el Combate a la Corrupción.

¹⁹ *Id.* at Artículos 26-30.

²⁰ *Id.* at Capítulo V De la Regulación y Obligaciones.

²¹ *Id.*

²² México Diario Oficial De la Federación (DOF). (May 27, 2015) http://www.dof.gob.mx/nota_detalle.php?codigo=5394003&fecha=27/05/2015.

²³ Conducting proper due diligence for all companies is vitally important to any potential partnership.



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