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Violations to the T-MEC in the face of Mexico's Energy Policy.

By Ricardo Nerio.

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Last July, the government of the United States of America and subsequently the government of Canada requested to the administration of the Mexican president Andrés Manuel López Obrador, a request for Consultations under the Mexico - United States - Canada Free Trade Agreement (T-MEC), by which they intend to resolve the controversies that both countries are facing with Mexico's current energy policy. According to the allegations presented, it is claimed that Mexico has failed to comply with the energy-related provisions of the T-MEC, which could result in billions of dollars in penalties for the Mexican federal government, as well as severely impacting the country's exports.

In this context, Mexico is at risk of causing a deterioration in trade relations with its North American neighbors, and by following a nationalist stance, could even lead to the separation of the Mexican State from the trade agreement.

This article provides a summary of the key points of this controversy.

Disputed Issue

"...Mexico's Electricity Industry Law gives an advantage to the distribution of energy generated by state-owned companies, specifically to the Federal Electricity Commission (CFE) and the national oil company Petróleos Mexicanos (PEMEX)..."

According to the claims filed by the United States Trade Representative (USTR) and the Canadian Department of International Trade, it is alleged that Mexico's Electricity Industry Law gives an advantage to the distribution of energy generated by state-owned companies, specifically to the Federal Electricity Commission (CFE) and the national oil company Petróleos Mexicanos (PEMEX), over that generated by private competitors, which necessarily affects investor confidence and the integration of North American supply chains.

The main concern is because of the reform published last year to the Electricity Industry Law, which establishes a new electricity dispatch system that prioritizes the use of the electricity distribution networks to the Federal Electricity Commission -which has the greatest factual capacity to physically deliver energy -, starting with hydroelectric power, followed by its thermal power plants. This condition also benefits Petróleos de México, which could sell more fuel oil with high sulfur content to supply the CFE's thermal power plants[1].

This also means that traditional sources of electric power generation - especially coal and fuel oil used in thermoelectric plants - are favored over cleaner sources such as wind and solar energy, whose exploitation benefits the private sector with existing and new investment projects.

Furthermore, the U.S. government accuses the Mexican government of delaying, rejecting, or failing to act on private companies' applications for permits to operate in the energy business, as well as revoking or suspending existing ones.

Hence, the basis for the Consultations filed under Chapter 31 of the T-MEC relies on the following stated violations allegedly committed by Mexico in terms of the provisions of the treaty[2]:

- Chapter 2, NATIONAL TREATMENT AND MARKET ACCESS FOR GOODS, article 2.3 and 2.11, which

1.- https://imco.org.mx/reforma-electrica-la-cfe-contra-la-cfe/
2.- https://www.elfinanciero.com.mx/economia/2022/07/20/pasos-y-fechas-del-proceso-para-que-eu-y-mexico-resuelvan-controversia-energetica/

establishes: i) that each Party shall accord national treatment to the goods of another Party with no less favorable treatment than the most favorable that regional level of government accords to any like, directly competitive, or substitutable goods; and ii) that no Party shall adopt or maintain any prohibition or restriction on the importation/exportation

• Chapter 4, INVESTMENTS, article 14.4, which enacts that each Party shall accord to investors of another Party treatment no less favorable than that it accords, in like circumstances, to its own investors.

• Chapter 22, STATE-OWNED ENTERPRISES AND DESIGNATED MONOPOLIES, article 22.5, which establishes that each Party shall ensure that any administrative body that the Party establishes or maintains that regulates a state-owned enterprise exercises its regulatory discretion in an impartial manner with respect to enterprises that it regulates, including enterprises that are not state-owned enterprises.

• Chapter 29, PUBLICATION AND ADMINISTRATION, article 29.3 which ensures administrative proceedings for a consistent, impartial, and reasonable application all measures of general application with respect to any matter covered by the agreement[3].

Thus exposed, the unequal treatment and the centralization of the distribution of energy conducted by Mexican state-owned companies is imperative in the eyes of the international arena, due to the reforms proposed by Andrés Manuel López Obrador.

How has Mexico responded?

During the Consultation period - as a dispute resolution mechanism through which a settlement is sought to prevent having to establish a Panel of specialists - President López Obrador has been in contact with the U.S. administration to obtain information regarding the exact reasons why it is considered that Mexico is in violation of the trade agreement, so that the public administration can immediately address the issue, which Canada has also raised.

"…López Obrador has stated that he will not give in and that even though trade relations with the United States are very important, nothing is above the independence and sovereignty of the State…"

Considering this, the President of Mexico has been highly confident of his good relationship with President Joe Biden and even assured that "bilateral trade in goods between the United States and Mexico has reached 384 billion dollars this year, surpassing pre-pandemic levels to reach an all-time record"; thus, assuring the good trade relationship between both countries[4].

However, in other communiqués, after being questioned about the various amparo claims filed by foreign companies for the current violations in the energy sector, López Obrador has stated that he will not give in and that even though trade relations with the United States are very important, nothing is above the independence and sovereignty of the State[5]; all at the same time that the Mexican public administration assures that there has been progress with the Consultations.

3.- Agreement between the United States of America, the United Mexican States, and Canada 7/1/20 Text, as retrieved from https://ustr.gov/trade-agreements/free-trade-agreements/united-states-mexico-canada-agreement/agreement-between
4.- https://www.elfinanciero.com.mx/nacional/2022/09/02/amlo-confirma-que-joe-biden-respondio-a-su-carta-sobre-consultas-al-t-mec-estoy-satisfecho/
5.-https://buenasnoticiasmexico.mx/2022/09/08/los-temas-de-amlo-en-la-mananera-del-08-de-septiembre/

In this context, Mexico has tried to justify its actions under Chapter 8 of the T-MEC in support of the argument of sovereignty, to exempt itself from any limitation in energy matters; a chapter which establishes the RECOGNITION OF THE UNITED MEXICAN STATES' DIRECT, INALIENABLE, AND IMPRESCRIPTIBLE OWNERSHIP OF HYDROCARBONS.

The greatest risk for Mexico.

In concrete terms, Mexico is still in the middle of an already extended Consultation period, but if the dispute is not resolved through this phase provided for in the aforementioned Chapter 31 of the T-MEC, it moves to a second phase with the establishment of a Commission to reach a mutually satisfactory solution; finally, as the last phase, if the matter is not yet resolved, it would move to the establishment of a Panel composed of specialists to render a final report.

"…it is undoubtedly essential to reform the Electricity Industry Law to finally put the CFE on a competitive level and eliminate any mechanism that prioritizes its processes with PEMEX."

If Mexico is found to be in non-compliance, the United States and Canada would have the right to claim multi-million-dollar compensation or impose tariffs on key Mexican products, which could represent retaliation and huge economic losses for the country. With tariffs, the prices of the products exported by the country would rise and Mexico would exit the North American market since similar products from other countries could be cheaper and, therefore, more attractive to the population.

Among the actions that Mexico would be obliged to consider during this phase to obtain a mutually satisfactory solution, it is undoubtedly essential to reform the Electricity Industry Law to finally put the CFE on a competitive level and eliminate any mechanism that prioritizes its processes with PEMEX. Likewise, it is essential to eliminate the impediments, delays, denials, and revocations of permits that private companies have; barriers that the Mexican government has placed to give preference to state-owned companies, when instead of seeing these companies as rivals they could and should be conceived as complementary.

The importance of trade relations with North America is an issue that should not and cannot be set against the sovereignty of the Mexican State in this controversy; being able to export and sell products to one of the most important markets in the world and build alliances with our northern neighbors is something that undoubtedly marks the path towards the country's prosperous future. Chapter 8 of the T-MEC regarding hydrocarbons has nothing to do with the violations present in the Electricity Industry Law.

In any case, the provisions contained in the T-MEC are possibly not being assessed in an accurate manner, since, in accordance with the Mexican Constitution, the treaty is on an equal hierarchical level as the Constitution and its provisions on the field of energy do not contravene the domestic legal order in any way.

As for energy matters, López Obrador has shown himself to be a nationalist president who distrusts private investment and economic processes on a competitive level, opting to centralize the operation of energy markets in the technologically obsolete and polluting operations of the CFE and PEMEX. This policy is part of the President's transformation of the country under the mantle of populism. He will try to maintain for as long as possible the legality of the disputed regulation and uphold a stance of pride in the sovereignty of the country vis-à-vis the United States and Canada, all while the investors and final consumers are directly affected, as always....

Mexico will invest $48 billion dollars with U.S. support to reduce up to 35% polluting emissions by 2030.

Due to Mexico's climate commitment to reduce the country's carbon emissions by up to 35 percent, Foreign Minister Marcelo Ebrad announced at the climate conference that Mexico, with the support of the United States, will invest 48 billion dollars to double the generation of solar, wind, hydroelectric and geothermal energy. Measures have already been taken by Mexico's state-owned oil company, which has already begun to replace its energy sources. *www.aristeguinoticias.com/1311/mexico/mexico-invertira-48-mil-mdd-con-apoyo-de-eu-para-reducir-hasta-35-emisiones-contaminantes-en-2030/* November 13, 2022.

Second-largest solar power plant in Mexico opens in Campeche.

A new solar park with the capacity to generate enough electricity to meet the annual needs of over 300,000 households has begun operations in Campeche. The solar park, La Pimienta, officially opened last Thursday, November 17, 2022, and has also celebrated a 15-year contract with the Federal Electricity Commission (CFE) in efforts to support the power needs of the Yucatán Peninsula. La Pimienta is composed of more than a million solar panels, spread across 651 hectares, generating approximately 789 Gigawatt hours annually. This project looks to supply clean energy to the Yucatán Peninsula in efforts to avoid the emission of more than 1.7 million tons of CO2. *www.mexiconewsdaily.com/news/solar-power-plant-mexico-campeche/* November 21, 2022.

Telecommunications company to invest in US-Mexico 'digital highway' in Gulf of Mexico.

Gold Data will invest $150 million to develop a "digital highway" in the gulf of Mexico to link its digital infrastructure in Miami with its data centers in Mexico City, Cancún, and Querétaro. This will be done through a 1,889 kilometer submarine cable, composed of ten pairs of fiber, and the capacity of 250 terabytes per second. These cables are used for international internet connections, this being the first cable to be in Mexico in over 20 years. This plans to revolutionize connectivity in Mexico, and reduce latency by up to 35%, which is a key factor for businesses and content providers seeking reliable, low latency, high quality connectivity, according to the company. *www.mexiconewsdaily.com/news/telecommunications-company-to-invest-in-us-mexico-digital-highway-in-gulf-of-mexico/* November 24, 2022.

Migrants and authorities clash in Chihuahua over eviction.

Migrants and authorities from all three levels of government clashed in Ciudad Juárez, Chihuahua, after the municipal police, accompanied by the National Guard, evicted a makeshift camp where mainly Venezuelan nationals were living. The refugees living in this spot were told by municipal authorities that they should leave the place and be transferred to a shelter where their basic needs would be met and would not suffer the inclement weather. However, the migrants did not agree with the disposition considering they are awaiting to be granted entry to the United States. *www.politica.expansion.mx/estados/2022/11/28/migrantes-autoridades-enfrentan-chihuahua-desalojo* November 28, 2022.

CCE endorses 20% minimum wage increase.

The Business Coordinating Council (CCE) announced that it supports the 20% increase in the minimum wage proposed by the President, although the private sector had suggested a lower increase. The National Commission of Minimum Wages (CONSAMI) is currently debating the increase for next year in the midst of the highest general inflation in two decades. Prior to Lopez Obrador's presidency, minimum wage was 88.36 pesos daily (4.40 USD), however, the minimum wage currently sits at 172.87 pesos (8.6 USD) Although the Employers' Confederation of the Mexican Republic (COPARMEX) had asked for a 15% increase, the president of the CCE pointed out that the unions were asking for a higher increase, so they are looking to reach an average. *www.forbes.com.mx/cce-avala-aumento-del-20-del-salario-minimo/* November 28, 2022.

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