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Amendments to the terms for legal separation of the Federal Electricity Commission

On March 25, the Ministry of Energy (SENER) published in the Federal Official Gazette (FOG) the Resolution Amending the Terms for the strict legal separation of the Federal Electricity Commission (the "Resolution"), which were originally published on January 11, 2016.

The amendments, as mentioned in the considerations of the Resolution, are due to the negative results in the application of these Terms (TESL), including:

- Cost increase and efficiency reduction in the operative and administrative management of the six subsidiary productive companies (SPCs) and the one affiliate company (AC) created by the Federal Electricity Commission (CFE) during its reorganization process.
- Inadequate distribution of assets in five of the SPCs, for they focused in that the power plants assigned to each of them did not have regional preponderance, a fact that prevented them to achieve joint economic results.
- Inefficient operation due to long distances and loss of specialization in regional technical sub-managements, as well as administrative complications and unnecessary expenses resulting from personnel and spare parts transfers between SPCs.
- Reduction in the availability of CFE generation plants from 86.65% in 2015 to 76.89% in 2018.
- Decrease in net thermal efficiency from 33.90% to 33.45% between 2015 and 2018, which increases the variable cost of the kilowatt.
- No profitability nor better costs in the generation of energy in four of the SPCs.
- Increase in fuel acquisition costs.
- Failure to promote free competition.

• AMENDMENTS

The Resolution, as noted, seeks to make power generation plants more efficient, reduce their operating costs and guarantee lower prices for end users through various amendments, among which the following are noteworthy:

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1. The number of power generation companies is modified from the former four SPCs or AC provided in the TESL, to any number of SPCs of AC that proves to be necessary, along with their respective Business Units.
2. Business Units are included in the portfolio of power plants and contracts for power generation companies.
3. CFE will be responsible for both the creation and the reorganization of power generation companies.
4. Public services of power transmission and power distribution will be carried out through SPCs created for such purpose, in accordance with article 27 of the Constitution.

For both services, amendments eliminate the possibility for SPCs to associate or sign contracts with other SPCs, AC and individuals to carry out, among other activities, the financing, installation, maintenance, management, operation and expansion of infrastructure.

5. CFE companies executing independent activities may coordinate between them or with other companies in the design, development and implementation of technologies for reducing operating costs, provided they will not endanger the electric system.
6. In exercise of its powers, the CFE will guarantee the effectiveness of the strict legal separation and shall privilege the efficiency of the electrical sector so it translates into lower prices for the end user and therefore:

a) CFE will refrain from strategies that negatively impact the wholesale electricity market, i.e., intentionally inducing the increase of marginal energy costs in the medium and short term. Originally, the TESL exclusively prohibited 'anti-competitive strategies'.

b) Regarding investments of CFE companies, evaluation for each project will consider not only its effect over the investing company itself but also its benefits for CFE as a whole and its possible contribution in lowering prices for end users.

Previously, in accordance with the TESL, project evaluation considered only the investing company, without taking into account any possible effects on other CFE companies.

7. As to business relations between CFE companies, the Resolution provides that they may be able to share employees on a permanent or temporary basis.
8. The Resolution repeals the prohibition for CFE companies to share information related to their operation, planning, maintenance and commercial strategies to other CFE companies or any other that carries out power generation or commercialization activities.

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- **ADDITIONAL PROVISIONS**

- Under the Resolution, in force as of March 26, any regulations and provisions opposing it are repealed.
- No later than May 23, CFE must submit to SENER its proposal regarding the reallocation of assets and power generation contracts to the SPCs and AC whose contribution to efficiency proves to be more feasible.
- Once such proposal is published in the FOG, the National Energy Control Center should reallocate all assets and contracts registered in the Market Information System within the next 30 calendar days, in accordance with the new structure.
- During the two years following reallocation, all transfer of goods, rights and obligations necessary for the reorganization will not require any formalization through public deeds. In this way, agreements of the Board of Directors will serve as property or transfer of ownership titles for all legal purposes, including recordation in the public registry.

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