

## New Regulations Bolster CFE, Put Independent Renewable Power Projects in Limbo

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Over the last three weeks, the Mexican government adopted measures to suspend preoperational tests for solar and wind plants and allow the power market operator (“CENACE”) permanent authority to prioritize the dispatch of power plants based on reliability concerns rather than cost. The acting agencies (CENACE and the Ministry of Energy) justified their regulatory changes in the name of establishing grid security as a response to the changing market dynamics wrought by the COVID-19 crisis and related fluctuations in demand. The measures are expected to have a significant impact on wind and solar projects.

### CENACE’s Interconnection and Testing Order

On April 29, 2020, CENACE issued a Resolution to Guarantee the Efficiency, Quality, Reliability, Continuity and Safety of the National Electric System (the “Interconnection and Testing Order”). The Interconnection and Testing Order invokes broad authority to mitigate the adverse effects of the COVID-19 pandemic on the operation of the National Electric System (“SEN”). Citing concerns over the adverse effects of intermittent power generation by solar and wind plants on the SEN, the Interconnection and Testing Order mandates, effective May 3, 2020, and until further notice, the suspension of any preoperational testing of wind and solar power plants – a required step for commercial operation of a power project in Mexico – in effect precluding recently completed projects from starting commercial operations for an indefinite period.

As a result, in the week after the Interconnection and Testing Order went into effect,

the share of solar and wind power generation to the SEN [reportedly suffered](#) a near 30% drop – while power generation costs grew 13% – a clear sign of significant market interruption. Subsequently, CENACE’s Director General [confirmed](#) that CENACE had suspended preoperational tests for 17 power plants with a total capacity of 2,326 MW – seven wind farms and 10 solar plants – without mentioning the names of those power generators.

## The Ministry of Energy’s Dispatch Policy

Only a few weeks later, on May 15, the Ministry of Energy (“SENER”) published its Policy for the Reliability, Safety, Continuity and Quality of the National Electric System (the “Dispatch Policy”). As part of a wide-ranging set of measures aimed at guaranteeing the reliability of the SEN, the Dispatch Policy grants CENACE permanent authority to prioritize the dispatching of electricity from certain power plants over others based on reliability considerations, rather than cost. As a result, in managing the grid, CENACE may give preference to the state-owned utility’s (“CFE”) on-demand fuel oil and natural gas-fired plants over more cost-efficient, but intermittent, privately owned solar and wind power generators. The Dispatch Policy also grants CENACE the power to reject requests for interconnection studies for new plants.

Another controversial feature of the Dispatch Policy is the imposition of early termination obligations in new or renewed generation permits and interconnection contracts. The early terminations would be triggered by a failure of a generator to make “interconnection improvements” required by a CENACE interconnection feasibility study. The phrasing is ambiguous and could require generators to make unspecified additional investments or changes to a project at a late stage without the costs having been included in the original project budgets.

More generally, the Dispatch Policy expands CFE’s influence in the process for making authorizations for the interconnection of new power plants and in the planning of the expansion of the SEN – including prioritizing for the Ministry of Energy “strategic infrastructure projects required to foster a public and universal electricity supply service.” This new role for CFE – essentially reestablishing the market influence CFE enjoyed prior to the 2013 reforms in the energy sector – may allow CENACE to prioritize conventional energy sources, including those operated by CFE and fueled by the state-owned oil and gas company, Petróleos Mexicanos (“PEMEX”).

## Public Response

The Interconnection and Testing Order and Ministry of Energy Dispatch Policy have set off a volley of interagency and public responses. COFECE, Mexico's antitrust regulator, submitted [a formal opinion](#) to the Ministry of Energy, the CRE and CENACE asserting that the Interconnection and Testing Order breached antitrust laws and recommending its modification to ensure that the measures are temporary, justified on technical grounds and not discriminatory.

The National Commission for Regulatory Improvement ("CONAMER") [tried to halt](#) the publication of the Dispatch Policy by recommending a preemptory regulatory impact analysis – just as CONAMER did last February to stop CRE from issuing rules preventing transfer or amendment of certain power-generation permits that would have prejudiced renewable projects. Nonetheless, the Ministry of Energy [fast-tracked the publication](#) of the Dispatch Policy, citing concerns over intermittent solar and wind production. CONAMER's head [announced his resignation](#) via Twitter shortly after the publication of the Dispatch Policy.

Early this week, a major Mexican business association [promised legal actions](#) against the new measures. As of May 20, seven companies had [obtained temporary injunctions](#) against the Interconnection and Testing Order. In response to the legal challenges, CENACE has [reportedly exempted](#) 23 power plants from the application of the Interconnection and Testing Order and authorized the continuation of those preoperational tests that were ongoing at the time of entry into force of the Interconnection and Testing Order. Internationally, diplomats from Canada and the EU have publicly criticized the measures and [demanded meetings](#) with Mexican officials in defense of investors from their jurisdictions whose projects may be negatively impacted.

## Looking Ahead

Private solar and wind power projects now account for most of the new capacity on the Mexican grid – approximately [10.74 GW of capacity](#) added to the national grid in 2019 was from solar and wind projects. According to the Mexican Solar Energy Association ("ASOLMEX"), there are [63 solar plants](#) in operation in Mexico, 24 of which were installed in 2019, while the contribution of wind power generation to the national grid [grew 34%](#) in the same period. According to the Mexican Wind Power Association ("AMDEE"), 44 renewable energy projects are scheduled to start commercial operations between this and next year, representing [investments of \\$6.4 billion](#).

As the new measures force clean power projects to delay the commencement of their operations or reduce production, clean power producers [may suffer significant revenue shortfalls](#) and experience difficulties fulfilling their commitments under power purchase agreements. Projects in construction and development could find it more difficult to obtain financing. Additionally, the new measures may have negative repercussions on the public sector, as CFE is a purchaser under many of power purchase agreements with renewable energy projects, and Mexican development banks have provided billions of dollars alongside commercial lenders [to fund](#) many of those wind and solar projects.

The effect of the Interconnection and Testing Order may depend on the length of time during which preoperational tests are suspended. The effects of the Dispatch Policy, meanwhile, could vary considerably depending on how forcefully CENACE acts with respect to its new powers, as well as opposition from other Mexican private and public actors.

*This post was co-authored with Hernando Becerra, Oscar Moreno and Diana Pineda of Gonzalez Calvillo.*

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