

On February 4, 2025, a bill containing the draft decree for the issuance of the new Power Sector Law (the "LSE") was presented to the Senate. If approved, as expected, the LSE will come into effect the day after its publication in the Official Gazette of the Federation, repealing and replacing the Electricity Industry Law (the "LIE"), which has been in force since August 2014.

The LSE bill aims to implement the reform to Articles 25, 27, and 28 of the Political Constitution of the United Mexican States, which took effect on November 1st, 2024, as well as the "National Power Sector Strategy" presented by the federal government at the beginning of that same month. From a structural standpoint, the LSE is based on the foundation, terms, and conditions of the LIE, adjusting them as necessary to achieve its objectives.

The LSE bill reflects the new constitutional model in which the Mexican State takes on a more active role, with a more relevant function and space, maintaining the planning and control of the National Electric System (the "SEN"), as well as exclusivity in the transmission and distribution of electricity, while allowing private entities to actively participate in various modalities of electricity generation and commercialization, as well as associated products. The LSE bill seeks the coordinated development of the energy sector, fostering collaboration between the State and private entities to achieve the desired goals, including providing the population with electricity at the lowest possible price.

The new LSE will create significant opportunities for the development, growth, and consolidation of the power sector, benefiting both the State and private entities, encompassing all participants (from builders and equipment suppliers to developers, generators, marketers, and other sector companies) especially considering the country's substantial energy needs.

EXECUTIVE SUMMARY

- **Strategic Activities Reserved for the State.** The bill confirms that the planning and control of the SEN, as well as the transmission and distribution of electricity, are strategic

areas reserved for the Mexican State. The control and planning of the SEN will be the responsibility of the Ministry of Energy (the "SENER"), with binding authority, following principles of reliability, continuity, and accessibility of the public electricity service, aiming, among other things, to promote electricity supply to the population at the lowest possible price, foster the energy transition, and expand and decarbonize the sector to meet SEN demand. The transmission and distribution of electricity, as well as the basic supply, will be exclusively assigned to the Federal Electricity Commission (the "CFE").

- **Prevalence of the Mexican State.** CFE, as a public entity of the State, will have prevalence in generating at least 54% of the electricity injected into the SEN during each calendar year.
- **Participation of Private Entities.** Subject to CFE's prevalence, electricity generation and commercialization will operate under a competitive regime in which both the Mexican State and private entities may participate, either individually or jointly with the State, in any of the following modalities:
 - ✓ **Distributed Generation.** Up to 0.7 MW of capacity, without requiring a permit.
 - ✓ **Self-supply.** Isolated or interconnected to the SEN, starting from 0.7 MW, with no capacity limit.
 - ✓ **Wholesale Electricity Market.** Starting from 0.7 MW, with no capacity limit.
 - ✓ **Mixed Development.**
 - Long-term contracts for sales to CFE, with no capacity limit.
 - Mixed investment, with at least 54% participation by CFE.
 - ✓ **Cogeneration.** No capacity requirement, subject to new rules that may reduce its operational efficiency.
- **Authorities and Entities in the Energy Sector.**
 - ✓ **National Energy Commission (the "CNE").** A new decentralized regulatory body replacing the Energy Regulatory Commission (the "CRE") and the National Hydrocarbons Commission (the "CNH").
 - ✓ **SENER.** Responsible for the country's energy policy, with broad powers, some of which overlap with those of the CNE, potentially creating uncertainty regarding government actions.
 - ✓ **CFE.** A public entity of the State, with a social function. It will be consolidated into a single entity that integrates all its subsidiaries and some affiliates, subject to operational separation rules, especially concerning its participation in the Wholesale Electricity Market (the "MEM").

- ✓ **National Center for Energy Control (the “CENACE”).** Maintains its status as a decentralized public entity responsible for the operation of the SEN.
- **Power Supply.** Power supply is a public interest service and can be provided in three different modalities:
 - ✓ **Basic Supply.** Exclusively provided by CFE for the benefit of non-qualified users, subject to a tariff regime.
 - ✓ **Qualified Supply.** Provided by CFE or private entities to users with higher requirements (more than 1 MW) of capacity (Qualified Users).
 - ✓ **Last-Resort Supply.** Offered by a permit holder to Qualified Users for a limited time to ensure service continuity
- **“Grandfathered” Regime.** The continuity of permits, contracts, and other administrative acts granted or executed under the Public Electricity Service Law (the “LSPEE”) and the LIE is recognized and respected.

A. Purpose and Objectives of the LSE

According to the bill, the LSE’s objectives include:

- ✓ Ensuring the efficiency, quality, continuity, accessibility, security, reliability, and sustainability of the SEN and the power sector;
- ✓ Defining the conditions under which private entities can participate in power generation and commercialization, subject to CFE’s prevalence in these activities;
- ✓ Providing power supply to the population at the lowest possible price, without profit motives in basic supply;
- ✓ Promoting the sustainable development of the power sector with social, economic, and environmental responsibility;
- ✓ Encouraging the use of clean energy sources and the energy transition; and
- ✓ Reducing pollutant emissions, favoring the decarbonization of the power sector, and meeting international commitments in these areas.

B. CFE’s Prevalence Over Private Entities

According to the constitutional mandate in force, private entities may participate in power generation and commercialization, provided that their participation does not have “prevalence” over that of CFE.



The LSE bill defines “prevalence” as CFE’s preferential right to inject at least 54% of the total electricity injected into the SEN each calendar year. This concept is justified by CFE’s responsibility to ensure the reliability, security, continuity, and accessibility of public electricity service and to provide electricity to the population at the lowest possible price.

The proposed definition raises several considerations:

- Inconsistency with the Constitutional Mandate. Regardless of the preferential 54% quota assigned to CFE, the concept of “prevalence” proposed in the LSE bill is not entirely consistent with the intent of the constitutional reform that gave rise to it. As previously mentioned, the amended Article 27 of the Constitution defines “prevalence” in a negative sense for private entities, stating that they shall not have prevalence over CFE. However, despite a few references throughout the LSE that reflect the intent of the constitutional reform, the LSE bill reinterprets the concept of “prevalence” positively for CFE, meaning that CFE will have prevalence over private entities. Thus, CFE’s “prevalence”, understood as a minimum of 54% of the total energy injected into the SEN annually, effectively means that CFE’s right to participate in electricity generation and commercialization has no upper limit and could, in theory, be equal to or exceed 54%, up to 100%, depending on SENER’s determination in its exercise of planning and control over the SEN. This rule differs from the intent of the constitutional amendment, which uses the concept of “prevalence” to recognize a right for private entities to participate in power generation and commercialization. In our opinion, a proper interpretation of the constitutional concept of “prevalence” should begin with recognizing the right of private entities to participate up to a maximum of 46%, considering the 54% quota proposed for CFE under the LSE bill. This shift in perspective could result in significant limitations for private entities.
- Dispatch Privilege for CFE. From a practical standpoint, the concept of CFE’s prevalence, as defined in the LSE bill, could implicitly lead to preferential dispatch of CFE-owned power plants over those owned by private entities. Otherwise, it would appear difficult for CFE to meet the annual 54% minimum injection into the SEN, especially considering that, as stated by the federal government in its presentation of the “Plan México”, CFE’s electricity generation in 2024 was below the 54% threshold it now seeks to achieve. This situation gives rise to various concerns and speculations. For example, if by the final months of a calendar year, CFE’s energy injection into the SEN were to fall below the required 54%, CENACE could be forced to dispatch CFE-owned power plants with absolute priority over private plants, regardless of technology or cost. This scenario would violate



principles established in the very same LSE bill, shaping the sector's operation based on ideological principles rather than actual energy needs and failing to meet the population's supply demands. Moreover, it could even contradict the Constitution and the LSE's stated purpose of providing electricity to the population "at the lowest possible price". A preferential dispatch mechanism favoring CFE power plants would not only contravene the new legal framework but also prevent the realization of the objectives underlying the constitutional reform that led to the LSE (namely, to improve electricity service for the population by making it more universal, more efficient, and lower in cost).

That being said, the LSE bill includes multiple provisions that contradict the application of preferential dispatch in favor of CFE, among which stand out the obligation of CENACE, as the SEN operator, to consider security, reliability, and economic efficiency criteria in the assignment and dispatch of power plants as well as the execution of said assignment and dispatch regardless of the ownership or representation of power plants in the MEM. Another relevant provision of the LSE bill obliges CENACE to operate the MEM based on an economic load dispatch, which implies the scheduling of generation resources minimizing their variable production costs.

Given these factors, there is a real risk that the concept of "prevalence" may be misinterpreted, potentially creating obstacles and restrictions on the development of the power sector and hindering the achievement of the objectives envisioned under the new constitutional and legal framework. Ideally, the legislative review process should identify and correct these inconsistencies.

C. Participation of Private Entities in Power Generation and Commercialization

According to the LSE bill, power generation may be carried out by both the Mexican State and private entities, either independently or in partnership with the State through mixed investment schemes. Electricity generation may take place under any of the following modalities:

- Distribute Generation. A generation modality through power plants with a capacity of less than 0.7 MW, interconnected to distribution circuits with a high concentration of load centers.

In this modality, electricity and associated products must primarily be used for self-consumption. However, the electricity and associated products generated

under this scheme may also be sold to qualified service suppliers, last-resort suppliers (for later sale to qualified users), and CFE, as a basic service supplier. In the latter case, sales must be made under terms and conditions approved by the CNE through standardized contract models and methodologies for calculating, determining, and updating compensation. To this end, power plants operating under the Distributed Generation modality may access the MEM and connect to the General Distribution Networks (the "RGD") when technically feasible, according to the technical specifications issued for this purpose. These specifications may include simplified procedures for typical cases and conditions that facilitate the sale of energy and associated products. Electricity generation under the Distributed Generation modality does not require a generation permit from the CNE. Furthermore, SENER has the duty to promote credit schemes and other financing mechanisms for power plants operating under this modality using clean energy.

It is noteworthy that the LSE bill does not define the concept of "self-use", distinguishing it from the analogous concept used in the LIE, which referred to "meeting one's own needs". The LSE bill retains this concept under the Self-Supply modality, which is explained below. As was done under the LIE, it is likely that the CNE will issue general provisions defining these terms. Ideally, these provisions should allow some flexibility for generators operating under this modality.

- Self-Supply. A generation modality through power plants with a capacity of 0.7 MW or more, with no upper limit, where electricity must be used to meet the self-consumption needs at the site of the holder of the corresponding generation permit. According to the LSE bill, self-supply should preferably be carried out using renewable energy sources.

The LSE bill considers two distinct types of Self-Supply:

- ✓ Isolated: when the power plant responsible for electricity generation is not interconnected to the National Transmission Network (the "RNT") or the RGD and uses its entire production exclusively for self-consumption on-site within a private network.
- ✓ Interconnected: when the power plant responsible for electricity generation is interconnected to the RNT or the RGD. Generators operating under the Interconnected Self-Supply modality may inject excess electricity into the SEN without receiving compensation or sell it exclusively to CFE, which will have the discretion to acquire it under terms and conditions approved by the CNE. It is important to note that if the plant operating under this



modality generates electricity intermittently, it must have backup as a condition for its interconnection to the RNT or RGD, either through its own storage system or by acquiring backup from CFE.

Under the LSE bill, interconnected self-supply from power plants with a capacity between 0.7 MW and 20 MW will benefit from a simplified process for obtaining a generation permit, according to guidelines to be issued by the CNE.

The condition in the LSE bill requiring that the production of power plants under the Self-Supply modality be used exclusively for self-consumption (except for excess electricity in the Interconnected Self-Supply modality) will limit the use of this generation modality. Ideally, the legislative review process should identify and correct these limitations. If not, the CNE might expand the definitions of “self-use” or “self-consumption”, as it did when regulating the concept of “meeting one’s own needs” under the LIE, to allow the production of electricity to meet the needs of companies belonging to the same economic group as the permit holder or even to tenant companies in industrial parks.

Self-Supply load centers that do not meet their electricity needs through their power plant may connect to the RNT or RGD to purchase electricity and associated products as a Basic Supply User, Qualified Supply User, or Qualified Market Participant Use.

- Generation for the Wholesale Electricity Market. A generation modality through power plants with a capacity of 0.7 MW or more, with no upper limit, for the commercialization of electricity and associated products through any of the mechanisms provided in the MEM
- Mixed Development or Mixed Investment. A generation modality through power plants developed by private entities jointly with the Mexican State under two main schemes:
 - ✓ Long-Term Production: development of power plants by private companies under long-term contracts with CFE, which terms and conditions will be subject to regulations established in the LSE’s implementing regulations and other general provisions issued by SENER, subject to the following main conditions:



- The power plants must be included in the "Power Sector Development Plan" (PDSE) managed by SENER;
 - The Mexican State, directly or through CFE, will not be required to contribute capital for the development of the respective project;
 - All electricity and associated products generated by these power plants must be sold exclusively to CFE, which will be obligated to purchase them as per the respective contract;
 - The power plants must be represented in the MEM by CFE;
 - The transfer of assets comprising the power plants will be optional and at no cost to CFE upon the expiration of the respective contract; and
 - The power plants may not obtain another permit, operate under another modality, or commercialize any excess capacity with entities other than CFE.
- ✓ Mixed Investment. Development of power plants through co-investment between private entities and CFE, subject to the following main conditions:
- CFE's participation in the respective project, whether direct or indirect, must be at least 54%; and
 - Electricity and associated products generated by the power plant may be acquired by CFE or commercialized with third parties.

The LSE bill does not specify the structures that co-investments between private entities and CFE must take to operate under the Mixed Investment modality, nor does it regulate the manner in which CFE must participate in each project. This could be a positive aspect, as it may allow private entities and CFE to implement creative structures for projects they seek to develop.

- Cogeneration. A generation modality in which electricity production:
 - ✓ Occurs jointly with steam or another type of secondary thermal energy, or both;
 - ✓ Uses thermal energy not utilized in the industrial processes of the permit holder for direct or indirect electricity production; or
 - ✓ Uses fuels produced in the permit holder's industrial processes for direct or indirect electricity generation.



In this generation modality, the capacity covered by the corresponding permit will be limited exclusively to the power that can be obtained using the thermal energy not utilized in the associated industrial processes.

Power plants operating under this modality will have a limited mandatory dispatch subject to:

- ✓ The capacity and electricity production required to meet the steam needs of indirect processes;
- ✓ The power plant's capacity must not exceed the thermal needs of the indirect process; and
- ✓ Electricity may only be consumed at the facility associated with the cogeneration process (any surplus must comply with economic dispatch rules).

D. "Grandfathered" Generation Modalities Prior to the LSE

Despite recurring threats from the federal government against electricity generation projects under the self-supply, cogeneration, and independent power production modalities that originated in 1992 following a reform to the LSPEE (then in force), the LSE bill, in its transitory articles, reaffirms the principle of non-retroactivity of the law. It establishes that permits, contracts, and other administrative instruments or acts granted under the LSPEE and the LIE will continue to be in effect until their expiration and will be governed under the terms in which they were granted and the legal provisions in force at the time of their formalization. Furthermore, the transitory articles of the LSE bill allow permit holders under the LSPEE or LIE to request the migration of these permits to the figures provided in the LSE. For these purposes, SENER will be responsible for issuing guidelines to regulate the migration process through an expedited procedure, as well as implementing a single-window system to facilitate processing. This system may include administrative simplifications, extensions for meeting technical requirements, or exemptions from certain procedures and requirements contained in applicable regulations.

E. Power Sector Development Plan

The LSE bill assigns SENER the responsibility of drafting and issuing the PDSE, which must establish medium- and long-term planning for the SEN, as well as programs for the installation and retirement of power plants and the expansion and modernization of the RNT and the RGD. The LSE stipulates that these programs must be binding.

Binding planning requires SENER to consider several principles, including:

- Ensuring the reliability, continuity, and accessibility of the public electricity service;
- Preserving Mexico's energy sovereignty and security while ensuring electricity supply to the population at the lowest possible price;
- Promoting the energy transition and electrification;
- Encouraging the expansion and decarbonization of the sector;
- Guaranteeing CFE's prevalence within an MEM operating framework based on economic dispatch, subject only to reliability and security restrictions; and
- Incentivizing the installation of sufficient infrastructure to meet SEN demand.

The expansion and modernization of the RNT and RGD will be carried out under binding programs authorized by SENER, subject to CNE's opinion. CFE will be responsible for executing the projects included in these programs, following instructions from SENER. Expansion and modernization programs related to the MEM will be authorized by SENER based on proposals from CENACE or CFE, in its capacity as a transmission or distribution entity, with CNE's prior opinion.

The PDSE will have a significant impact on the following schemes:

- Permits: The granting of permits by the CNE for regulated activities must take into account the binding planning criteria set forth in the PDSE.
- Distributed Generation: The PDSE must consider the expansion and modernization of the RGD required to interconnect power plants operating under the Distributed Generation modality.
- Mixed Development or Mixed Investment Schemes: The generation of electricity under the mixed development or mixed investment modality must be contemplated and subject to the binding planning programs outlined in the PDSE.
- Clean Energy Certificates (CELS): The requirements for acquiring CELs, established as a proportion of total electricity consumption at load centers, must align with the binding planning in the PDSE.

As a government-controlled planning instrument, the PDSE's binding nature will impose restrictions that may interfere with the installation, expansion, and operation of electrical infrastructure, limiting market flexibility. While the LSE bill seeks to ensure SEN's accessibility, quality, and reliability, government bureaucracy may lead to administrative inefficiencies, resulting in delays in project development and restrictions on innovation. As a practical consequence, private entities will have to adjust to government programs



contained in the PDSE, effectively reducing their capacity to develop independent projects.

F. Federal Electricity Commission (“CFE”)

Since the LIE became effective in August 2014, CFE’s generation, transmission, distribution, and commercialization activities were legally, functionally, operationally, and financially separated, leading to the creation of various CFE subsidiary and affiliate companies operating under a separation regime.

The LSE bill, in its Eleventh Transitory Article, repeals the terms regulating CFE’s separation, which were issued by SENER and published in the Official Gazette of the Federation on January 11, 2016. The repeal proposed by the bill will take effect on the date the new law regulating CFE (State Public Entity Law, Federal Electricity Commission) comes into force. Meanwhile, only the provisions referring to CFE’s affiliate companies will temporarily remain in effect until SENER issues new regulations to replace them.

In line with this, the Eighth Transitory Article of the LSE bill implies that CFE’s subsidiary companies will be reincorporated into CFE, stating that all contracts entered into with CFE and its subsidiaries must be transferred to CFE as a state public entity. These contracts will continue to be governed by their respective terms and by the provisions of the LIE or LSPEE, as applicable. Despite this reincorporation, CFE will be required to maintain operational separation in terms of nominations and bids for the MEM, in accordance with applicable regulations, particularly regarding the MEM’s settlement system, billing, invoicing, account statements, collections, and financial balancing.

G. National Energy Commission.

Currently, the CRE serves as the regulatory body in the electricity sector, working alongside the CNH on non-electric energy matters. CRE was originally created in 1992 as a centralized federal agency with technical, operational, and managerial autonomy, aimed at promoting the efficient development of the electricity industry.

During President López Obrador’s administration, CRE’s independence was severely undermined, and it ceased functioning as an autonomous and independent body, instead acting under the control of the federal government and CFE. Following this trend, a constitutional reform on organizational simplification took effect on December 21, 2024, mandating the dissolution of various autonomous agencies, including CRE and CNH, which are expected to cease to exist before April 2025.



The LSE bill proposes replacing CRE and CNH with a single commission named the “National Energy Commission” (the “CNE”), which will be a decentralized body under SENER with technical specialization and independence. Alongside the LSE bill, Congress is expected to receive other legislative proposals, including a new “National Energy Commission Law”.

Under the LSE bill, CNE’s powers will be nearly identical to those previously assigned to CRE under the LIE, adjusted as necessary to comply with the LSE. These powers include, among others:

- Granting permits for regulated activities, except for electricity import and export, which will be under SENER’s authority;
- Issuing and enforcing tariff regulations applicable to transmission, distribution, CFE’s basic supply operations, CENACE’s operation, and final rates for basic supply;
- Establishing administrative provisions for calculating and determining compensations required by the LSE and approving the contract models applicable under its provisions;
- Issuing, reviewing, adjusting, and updating the MEM rules and overseeing CENACE’s decisions to ensure efficient operation and regulatory compliance;
- Issuing Clean Energy Certificates (CELS) and establishing regulations for validating ownership;
- Defining efficiency criteria for clean energy classification; and
- Authorizing general technical specifications proposed by CENACE for interconnecting new power plants and connecting new load centers, as well as approving fees for related technical studies.

Unlike CNE’s powers, SENER’s powers under the LSE bill have been significantly expanded compared to the LIE, with overlapping responsibilities between CNE and SENER creating potential regulatory uncertainty.

This duplication of functions will create confusion among industry participants, reducing legal certainty in key procedures such as planning, project development, permit issuance, and other regulatory matters.

Ideally, the legislative review process should identify and correct these inconsistencies.



H. National Center for Energy Control

Towards the end of President López Obrador's administration, various government officials expressed interest in dissolving CENACE, aligning with the broader plan to eliminate autonomous agencies under the constitutional reform on organizational simplification. The proposal was not to eliminate CENACE entirely but rather to merge it back into CFE, stripping it of its autonomy.

Despite these discussions, the LSE bill recognizes CENACE's continued existence and role, maintaining its function as the entity responsible for operating and controlling the MEM.

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