Governance in the Mexican Petroleum Sector

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Contents

i. Country profile

ii. Key Concepts

iii. The Mexican Oil Sector – Historical Review

iv. Current Governance Arrangement

v. NOC – Ministry of Energy relationship

vi. Balance

vii. Working towards better governance
Country Information

- Form of Government: Federal Republic
- Population: 109 million inhabitants
- Territory: 1.9 million km²
- Official language: Spanish
- Currency: Mexican Peso
i. Country Profile (2)

Petroleum sector information*

- Production (liquid hydrocarbons):
  3.04 million BBLs/day
    • 2.7 million BBLs of crude oil
      • Heavy (maya): 60%

- Reserves:
  ▪ Proven: 14.2
  ▪ Probable: 14.5
  ▪ Possible: 14.7
  3Ps: 43.6 billion BBLsCOe

- Refining Capacity:
  ▪ 1.5 million BBLs/day
  ▪ 6 refineries (7th on the way)

- Crude oil exports:
  ▪ 1.3 million BBLs/day (90% maya)
  ▪ 43 billion USD p.a. (2008)

*Source: Pemex
ii. Key Concepts

- **What is Governance of the National Petroleum Sector?**
  Systems and set of arrangements by which the issues related to the oil sector are directed, organized, conducted and supervised.

- **What is the Governance Architecture?**
  Laws, norms and customs that establish the objectives, rights, responsibilities and the parameters for the interaction between all the stakeholders.

- **What is different about Governance in the public sector?**
  Public Sector organizations have to satisfy a different range of objectives than their counterparts in the private sector. They are also subject to a wider set of limitations and constraints.

- **What are the Governance Functions?**
  1. Policy-making
  2. Strategy-making
  3. Operational decision-making
  4. Monitoring & Regulation
ii. Key Concepts (2)

- **What are some key benchmarks of good governance?**
  A sound governance arrangement will provide effective accountability, reject opacity and foster value-creation.

  • **Accountability**
    Process whereby public agencies submit their decisions and actions to scrutiny.

  • **Transparency**
    Effective governance requires transparent and timely information of those involved in the petroleum sector. It serves not only the purpose of reducing corruption, but also to detect areas of opportunity.

  • **Value-creation**
    A well-run petroleum sector will have a positive impact in development plans.
ii. Key Concepts (3)

- **What is a Stakeholder?**
  Stakeholders are individuals, groups of people or organizations who have an interest in the set of activities related to the Mexican Oil Sector.

- **Which are some key stakeholders?**
  - Government
    - Ministry of Energy
    - National Oil Company
    - Regulators
    - Ministry of Finance
    - Congress
  - Non-Government
    - Civil Society
    - Business Groups
iii. The Mexican Oil Sector – Historical Review

- The Early Years
  - In 1938, expropriation of petroleum industry and creation of Pemex.
  - Scarcity of capital.
  - Seeking vertical integration.

- The Oil Sector Under ISI
  - Oil sector was key to Import Substitution Industrialization.
  - Supply of cheap & abundant fuel.
  - Inward-looking.
  - Oil-related revenue was used to finance subsidies.
- Looking abroad
  - Discovery of massive fields in the 70s.
  - Scope changed from inward to outward looking.

- The Boom years: hope unfulfilled
  - Oil sector grew large, but in a disorderly fashion.
  - Higher expectations about the duration of the boom.

- The 80s: Debt Service
  - Price dropped.
  - Oil related-revenue was mostly used to service debt.
iii. The Mexican Oil Sector – Historical Review (3)

- The 90s: limited reforms
  - Country underwent process of market-oriented reforms.
  - Limited transformation in the oil sector.
  - Organizational structure of Pemex was transformed.
iv. Governance arrangement

- The involvement of government institutions in the Mexican oil sector is not monolithic.

- The Government is the steward of national resources and it can exercise rights over the hydrocarbon endowment.

- Various public sector organizations are wholly or partly responsible for executing the key institutional functions described earlier.

- Through the Ministry of Energy, it is responsible for directing the course of the energy sector by defining policy imperatives.

- Through Pemex, it is responsible for exercising operational decision-making.

- Monitoring & Regulation is exercised through various agencies.
iv. Governance arrangement (2)

- How are governance functions distributed in the current governance arrangement?
  - Policy-making
    - Ministry of Energy
  - Strategy-making
    - Ministry of Energy / Pemex Governing Body
  - Operational decision-making
    - PEMEX
  - Monitoring & Regulation
    - Ministry of Energy
    - Ministry of Public Function
    - Congress
    - Ministry of finance
- The Mexican public administration structure is divided in two sectors:
  - Centralized: mainly comprised of Ministries.
  - Decentralized: State-owned enterprises, credit institutions, public trust funds, etc.

- State-owned enterprises (SOEs) are organized under a Sector Ministry Model.
  - SOEs are gathered according to affinity of economic activity and placed under the responsibility of a Sectoral Head.
  - Pemex, the National Oil Company, is coordinated by the Ministry of Energy.
- Pemex was created in June 1938 by a presidential decree that defines it as a technical, industrial and commercial decentralized entity with its own patrimony and legal personality.

  - It’s mission is to maximize the economic value of hydrocarbons and its by products in order to contribute to sustainable development in Mexico

  - Pemex holds the monopoly of exploration, production, refining, etc.

  - Pemex is run by a CEO with oversight from the Board of Directors

  - Organizational Structure
    • Exploration and Production
    • Refining
    • Gas & Basic Petrochemicals
    • Petrochemicals
v. NOC – Ministry of Energy Relationship (3)

The Ministry of Energy was created in 1994 when it replaced The Ministry for Mining and Parastatal Industry.

- The Ministry of Energy is in charge of conducting national energy policy in order to guarantee a competitive, sufficient, high quality, economically and environmentally viable energy supply.

- Organizational Structure
  - Undersecretariat of Hydrocarbons
  - Undersecretariat of Electricity
  - Undersecretariat of Planning & Technological Development

- Additionally, as sectoral head it supervises the following:
  - Centralized
    - Comission for the Efficient use of Energy
    - Comission for Nuclear safety
  - Decentralized
    - Pemex
    - Federal Electricity Commission
    - Central Light & Power
    - Mexican Petroleum Institute
    - Electrical Studies Institute
    - Nuclear Studies Institute
The relationship between the NOC and the Ministry of Energy tends to be conflictual.

They are involved in a principal-agent dynamic

- Principals (Ministry of Energy) and Agents (Pemex) objectives may divert, at least partly.

- Pemex has often overpowered the Ministry.

- National Vs Commercial mission

- Pursuit of non-entrepreneurial objectives hinders performance.

- Pure entrepreneurial direction in pursuit of commercial gain may affect the overall development plan.
What factors determine the relationship between Pemex and the Ministry of Energy?

- Size
- Asymmetry of information
- Diffuse boundaries
- Enablement
- Fiscal issues
vi. Balance

- Ineffective governance in the Mexican oil sector produced:
  
  ▪ Questionable accountability.

  ▪ Poor Transparency.

  ▪ Poor operational results
    • Production peaked in 2004 and is going down.
    • Reserves are declining steadily.
    • Limited refining capacity (40% of domestic consumption of gasoline comes from imports).
vii. Working towards better governance

- In an effort to try to solve these maladies, in 2008 the Mexican Congress passed a series of acts that Reform the Energy Sector

  ▪ Expanding capacity in the Ministry of Energy
    • Determines oil production platform and oil reserves policy.
    • Provides new tools for long-term energy planning.
    • Promotes better enablement.

  ▪ Creation of the National Hydrocarbons Commission
    • Promotes optimal use of oil-wealth.
    • Regulates and supervises exploratory and extractive activities.
    • Regulates transport and storage of hydrocarbons related to exploration and extraction projects.
    • Will assist the Ministry in establishing oil production platform and reserves policy.
vii. Working towards better governance (2)

- New Organic Law for Pemex
  - New and explicit mandate: to add value.
  - Liberty to modify its organizational structure.
  - Budgetary freedom when it comes to core-business investment projects and greater flexibility in other budgetary issues.
  - Decision-power over debt acquisition (with Ministry of Finance oversight).
  - Performance-based compensation for employees.
  - Board re-composition: addition of five professional (independent) directors.
  - CEO has the faculty to appoint second level officials.
vii. Working towards better governance (3)

- Transparency & Accountability
  - Internal Auditing Committee for performance evaluation.
  - Internal Control Organ will only deal with normative compliance.
“Good governance and sustainable development are indivisible”

Kofi Annan
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