

# Navigating the First Deepwater Joint Venture with Pemex in Mexico

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While the story is not yet fully written on Mexico's energy reform, a key new chapter is about to begin.

Mexico's auction process, while hit hard by low oil prices, has had a positive transformation from the surprisingly unsuccessful first round, in which only two out of 14 exploration blocks were awarded to a very successful later round, in which 25 blocks were awarded. Ultimately, contracts for 19 blocks were signed. In many respects, these have formed an interesting sideshow, highlighting which midmarket players are interested in getting their feet wet and which private equity firms are backing Mexico management teams, rather than a process, revealing major trends.

However, that is about to change as next in line for the process is the deepwater 1.4 bid, which includes deepwater contractual areas. At roughly the same time, but under a separate process, the first farmout with Pemex is being offered, which will be auctioned to a bidder consortium. The deepwater contract areas have attracted significant attention, with 26 bidders commencing the pre-qualification process. It is expected that the Pemex farmout auction will generate a similar level of interest, although at the time of writing the pre-qualified bidders have not been revealed.

The guidelines for the farmout bid were published in late July and included the first-ever model of a Joint Operating Agreement issued by the Mexican Hydrocarbons Commission (CNH). The pre-qualification process is ongoing, with the publishing of the list of participants in early November and the auction in early December 2016.

The field chosen for this farmout was the Trion field, located near the U.S. border and strategically positioned near the contractual areas that also are open to bid in the 1.4 deepwater. Trion has a total surface of 1,285 square kilometers and estimated 3P (proved, probable and possible) reserves of 482.3 million barrels of oil equivalent, and it was one of the fields initially awarded to Pemex in 2014. The bid guidelines call for a minimum 45 percent nonoperator stake by Pemex, while the remaining percentage will be distributed in the bidding consortium (the only form of participation for this bid), with the designated operator receiving from 30 percent to 45 percent and lower percentages to the other consortium members. The minimum carry by the bidding consortium was set at \$464 million. The license agreement and the JOA for the Trion joint venture will have an initial term of 35 years with two possible extensions for 10 and five years, respectively.

The oil majors' constant search for new reserves makes the Pemex farmout an attractive prospect, as potentially does the opportunity to partner with Pemex itself. However, there are some questions that only time will be able to answer. Will the winners of the farmout bid be able to navigate the pitfalls and bring the needed technology and processes to bear? Will it give them a major leg up in Mexico? Will the license arrangement be more financially viable to bidders than the production sharing model?

In a period of low oil prices, coupled with external and internal push for modernization, this bid is even more critical for Pemex. This and future farmout projects are vital for Pemex's survival, and the progress will be closely followed by the Mexican government whose energy reform platform is largely a bet on its success. The farmout represents Pemex's best opportunity to see for itself (and its pockets) the benefits of the energy reform. Will the farmout allow Pemex to spread its E&P and financial risk to other companies in a manner that allows

it to invest in research and development and exploration and production and become a financially competitive international market player?

The challenges for both sides are significant, and the ultimate answers may take years to play out, but we are today at the crossroads of that journey. The next two to three months represent key first historic steps.

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