

COVID-19 | Latin America Energy, Mining and Infrastructure Podcast Series

Latin America Power amid COVID-19

May 4, 2020

COVID-19 has put Latin America in a challenging situation. The energy, mining and infrastructure sectors, which are facing new government regulations, amending private and public contracts, and reshaping their strategy and continuity plans due to this outbreak.

Now that we are dealing with this crisis, can we anticipate what would be the new normal in our sectors? We invite you to listen to our Latin America Energy, Mining and Infrastructure Podcast Series in which we aim to explain and facilitate discussions about what we are seeing in each sector and what trends we can anticipate for the steadiness of our businesses.

What is the current regulatory landscape in Latin America in the Power sector?

ARGENTINA



On March 19, 2020, the Argentine government set forth a mandatory isolation regime, which is still in force. The Isolation Regime prohibits the circulation of individuals on routes, roads and public spaces, but individuals involved "essential" activities are exempted from this regime. Power transport and distribution activities are considered essential, with a reduction of operations to maintain minimum standards and utilities have been maintained. In addition, as of April 7, activities related to private energy infrastructure are exempted.

BRAZIL



COVID-19 has impacted the power sector and created numerous uncertainties. After a period of relative frustration in the energy sector in 2019 due to the low demand from generation auctions, 2020 was seen with great expectation in relation to the recovery of the economy and, consequently, the growth of the power sector. Yet the scenario radically changed due to the COVID-19 pandemic. All generation and transmission auctions scheduled for 2020 have since been indefinitely postponed.

CHILE



- Energy generation has become a main trend in LatAm. Due to exponential economic growth in the last three decades, countries in the region have strengthened efforts to make their power sectors more appealing to investor and boost the depth and expansion of their electric networks.
- New renewables (solar & wind) have become more relevant, while hydro has decreased in prominence. Gas and coal still lead the race.
- Green hydrogen has begun to arouse interest among governments. In Chile, in particular, there is a task force in charge of addressing potential uses for green hydrogen-power

generation.

COLOMBIA



As it happens in other Latin American countries, the Colombian government has taken different measures to control and reduce the impact of the COVID-19 outbreak in different sectors of the economy, particularly the power sector. Such measures have taken the form of new regulations, and they are generally based on the fact that **all activities required to guarantee the operation, maintenance, storage and provision of power services are exempted from the mandatory lockdown measure, as such activities are considered essential**. This means that power generation, transmission, distribution and retail companies are operating in overall normal conditions, so long as they abide by specific behavioral rules.

The main measures implemented by the Colombian government regarding the power sector have to do with:

- The suspension of terms in disciplinary processes coursed before the Ministry of Mines and Energy
- The possibility for power retailers (*comercializadores*) to defer the payment of debts to the system administrator
- The adoption of temporary rules regarding the deferral of payments of power invoices by certain residential users
- The imposition of "general duties" on all agents conducting operations in the power sector, having to do with the development of safety protocols, the subjection to good practices published by the government (regarding personal care, work tools, transportation, accommodation, food supply, security, health services, etc.), among others.
- The suspension of the term to liquidate the contracts entered into by the Ministry of Mines and Energy with third parties.
- The establishment of compulsory sanitary measures.

As is expectable, energy demand has decreased significantly, the main consumption corresponding, at the moment, to residential users.

MEXICO



In March 30 and 31, 2020, the Mexican government issued executive orders declaring the sanitary emergency (not a sanitary contingency), due to the COVID-19 global pandemic. Through these orders, the government commenced a series of actions as an attempt to contain the spread of the virus, including restriction of all such activities not otherwise acknowledged to be "essential". After different amendments said executive orders, the restrictions have been extended up to June 1, 2020.

The government or law enforcement officials at the federal level have imposed no mandatory lockdown; some local governments had imposed restrictions on mobility, but no full lockdowns as in other jurisdictions; all lockdowns, operational restrictions or limitations, as well as social distancing, are still voluntary.

As such, initially all "new" construction works (i.e. works not essential for the proper maintenance and operation of existing infrastructure), and the construction industry as a whole, were ordered to shut down; however, government works - and particularly landmark projects as the Dos Bocas refinery, the new Santa Lucia airport, and the Maya Train, were expressly carved out from the restriction, hence, all works and duties related to government works and these

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projects specifically, could continue to the extent all sanitary prevention measures were strictly observed. It happened to all suppliers and vendors in the whole spectrum of the value-chain on these landmark projects (e.g. cement/concrete, glass, steel, etc.).

Construction companies - and employees - if not deployed to other government works or as labor for, or as government works' vendors, suppliers in a same value chain, have been put on standby. Many companies have filed or are assessing to file for force majeure coverage.

Utilities such as water, sewage, **power**, etc., are allowed to continue operations, but making sure their employees strictly comply with all sanitary measures.

PERU



- Due to the COVID-19 outbreak, the Peruvian government has issued a series of regulations establishing a mandatory lockdown. Such lockdown, however, does not apply to several activities identified as essential, such as the power industry. Thus, most generation, transmission and distribution companies are operating normally. Of course, their administrative staff are working remotely, but their operational staff are working on site with the corresponding health precautions.
- Despite the normal operation of the abovementioned companies, energy demand has decreased significantly, and so has the spot price. The week before the start of the lockdown, the maximum demand reached 7,274.49 MW and the average spot price was USD 7.9 / MWh. On the other hand, last week the maximum demand reached 5,087.30 MW and the average spot price was USD 2 / MWh.
- Additionally, the government has approved instalment payments for electricity bills. In this sense, receipts issued during the lockdown may be paid for up to 24 instalments. This benefit is only applicable to: (i) residential users with monthly consumption of up to 100 KWh; and (ii) rural residential users supplied with photovoltaic solar panels.

VENEZUELA



In Venezuela, the power industry is under state control.

How are companies facing the issues related to public and private contracts and the relationship with suppliers, in particular, in terms of force majeure and other contractual and legal considerations?

ARGENTINA



The entire value chain has been affected by the measures taken. The issues being faced depend mainly on the segment or situation of the industry under analysis. We have assisted clients in alleging force majeure to modify construction schedules of renewable projects.

In the power generation and power distribution segments, the situation is more complex. From an existing debt with CAMMESA (a company that manages the local power system) to generators, sanitary limitations due to COVID-19 have negatively impacted not only consumption but also collections. This has led AGEERA (power generators association) and ADEERA (power distributors association) to seek the Energy Secretariat's intervention and at least receive delayed payments. This was met with a power price freeze until June 2020. All these have put the sector in a situation of near-interruption of the payment chain, which might

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affect the normal power supply in the immediate future.

BRAZIL



The delay in the construction of projects awarded in energy auctions can result in heavy penalties before the regulator, based on the current and applicable laws and regulations, as well as in large exposures with respect to the commitments undertaken with other parties in the sector, whether in energy generation or transportation. It is important to verify the potential exclusion of liability for the delay, difficulty or impossibility of fulfilling any other obligation, taking into account that the pandemic could represent a force majeure event. It is essential there be no mismatch between the force majeure clauses/events provided for in the construction contracts and other contracts under which the developer undertook commitments linked to the operation of the asset. Otherwise, the mismatch may cause substantial exposure either by the developer or by the supplier/construction company.

- With respect to the energy free market, contracts negotiated between large consumers and energy generators or traders usually provide for force majeure clauses that exempt the party who fails to comply with certain obligations. However, due to the closure of several industries, we are already seeing companies notifying of force majeure events, which could lead to a "judicialization" wave in the sector.

CHILE



- PPPs are not a trend in Chilean power generation. Generation is carried out as a private business, with government just acting as orchestra director of the generation plants (the latter, due to the role of the National Energy Coordination, which is in charge of giving the green light to companies to start injecting energy into the network, based on pricing criteria).
- COVID-19 has not impacted energy generation or distribution to date. Force majeure due to corona-related effects has not been tested before courts yet.
- Likewise, there are substantial precedents before Chilean courts that events that could be construed as force majeure are not acceptable as a defense for companies in energy distribution. Hence, the chances of success of such a defense — in case an unforeseen event disrupts the service — is low.

COLOMBIA



Despite the fact that the entire value chain has been affected as a result of the COVID-19 outbreak and the subsequent decisions made by Colombian government, most contracts whose purpose relates to the provision of goods and services directly related to the power sector (including construction of generation or transmission infrastructure) have not been required to be suspended on the grounds of force majeure. The reason for this is that, setting aside commercial considerations that could lead to valid force majeure claims, from a regulatory standpoint these kinds of contracts could in principle continue to be performed.

What we anticipate will be impacted the most is the schedule for construction and commencement of operations of new generation (and possibly transmission) assets, considering that, in these projects, the value chain consists of more variables. However, we also anticipate greater collaboration from the relevant authorities and network operators to extend any imperative deadlines.

From an economic standpoint, it must be pointed out that a major cause for concern is, naturally, the risk of delays in payments, in general. To alleviate the burden of retailers that have to pay the system administrator (XM) the whole tariff collected from end-users, including all

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components (generation, transmission and distribution), the regulator (CREG) issued a resolution allowing a payment deferral. However, this only alleviates one end of the whole chain.

Since the Colombian government is not a major power offtaker in Colombia, unlike in Peru (where PPAs are private), payment of remunerations under private PPAs are not guaranteed, and thus, the risk of payment default is more likely.

MEXICO



While force majeure is a principle acknowledged by Mexican law, its "protection" or coverage is nevertheless particularly limited by contract and jurisdiction; court's criteria has been issued and can be enforced, but it is still an issue to be analyzed on a case by case basis. Immediate remedy under force majeure is to suspend compliance with obligations and such compliance be deferred for a period of time equal or similar to the period the parties suffered the relevant force majeure.

PERU



- Companies in the sector are concerned about a rise in payment delays or even a possible break in the payment chain. For example, several free users are facing liquidity problems and, therefore, are triggering the force majeure / hardship clauses under their PPAs. They are also negotiating with their suppliers to postpone monthly payments or pay them in instalments.
- On the other hand, transactions in the spot market could be affected by a break in payment continuity, since distribution companies will collect less from the users that benefited from the payment by instalment of their receipts.
- Companies that entered into agreements with the Peruvian government (PPAs with the Peruvian government or concession agreements for cold reserve power plants) are in a better position. Under these agreements, remuneration is usually guaranteed; thus, the risk of payment default is less likely.

VENEZUELA



No special measures have been taken. General rules on force majeure can apply to contract non-performance.

Will the Energy transition to Renewables/alternative energy sources be the new normal?

ARGENTINA



It is difficult to say at this stage. In the case of Argentina, in addition to COVID-19 limitations there are tight exchange control regulations and other macroeconomic situations that have affected the viability of projects and reception of investments. However, there are still many renewable projects under construction due to past successful bidding programmes (RenovAr) that are expected to go online, thus suffering delays due to the pandemic.

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BRAZIL



Thanks to the prominence of hydro energy in Brazil, renewables make up the majority of the country's energy matrix. In previous years, Brazil has been increasing its wind generation portfolio (emerging as the world's 8th largest wind power producer) and consistently expanded its solar generation capacity, with very low prices in public auctions. Renewable corporate PPAs are becoming more popular, as the government is slowly opening the market to any consumer (not only the large ones) to freely negotiate and contract energy agreements. Renewables are still subsidized, although the government is considering ending the subsidies to the extent the renewable market is well developed. Distributed generation is also on the rise and contributed to the solar power sector's development. Offshore wind farms are under studies and may soon become a trend.

CHILE



- Chile is in the midst of a transition to renewables / alternative energy. Government is working with companies to suspend coal and gas plants, to the extent possible.
 - The goal in Chile is to reach 60% renewables by 2035 and 70% by 2050.
 - Hence, when it comes to development of new projects, renewables will be the new normal, but when talking about raw generation, coal and gas will remain key players for at least the next 10 years.
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COLOMBIA



Colombia has traditionally been highly dependent on hydroelectric generation, and thus, its generation matrix is considered fairly clean in general terms. However, since 2016 the government has enacted several different norms and regulations to effectively boost the development of non-hydro renewable generation projects to diversify the matrix and make it cleaner, reducing the dependence on coal and gas generation especially during times of El Niño.

In this sense, we do hope that the transition to non-hydro renewable sources of power will be the new normal, also considering that the Colombian government, through the Ministry of Mines and Energy, has made public its goals to significantly increase the installed capacity of renewable sources for 2022. Hopefully, the current pandemic situation will not hinder the development, construction and commissioning of new projects of this sort.

Furthermore, there is currently a regulatory project on course that will allow for consumers (residential, commercial and industrial) to inject, to the grid, energy generated through solar panels installed at their homes or premises (i.e., distributed generation).

MEXICO



It is unclear how the electricity market in Mexico will react in the short and medium terms. The key factors to be monitored are: (i) the reduction of the oil prices will do more competitive fossil fuels sources in the electricity dispatch; (ii) the new vision of Mexican authorities on how the energy sector must be addressed and the strategic role of State monopolies (such as PEMEX and CFE), and (iii) the power requirements that the productive sectors in Mexico (i.e. manufacture, automotive, chemical, etc.) will demand at cheapest cost in the short and medium terms by using the National network or from distributed sources.

PERU



- No. Since the demand shrank due to the lockdown, it has been covered mainly by hydro and thermal (natural gas) generation.
 - Once the lockdown is over, it is expected that the activities will gradually resume, which will increase the electricity demand proportionally. However, in this context, companies in the
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sector will focus their efforts on regaining their financial position rather than investing in new projects.

- Therefore, the measures to be adopted by the government to reactivate the economy should include the promotion of renewable energy.

VENEZUELA



Energy transition is not to be seen in the near future.

Fossils and hydroelectricity will remain the top sources.

What are the continuity plans amid service interruptions? How are companies in Power dealing with COVID-19?

ARGENTINA



For now, there have not been any specific measures to alleviate the delicate situation of the power industry in Argentina. All the contractual disruptions related to COVID-19 sanitary measures have been discussed in the context of force majeure. Some alternatives can be implemented, such as the readjustment or renegotiation of certain terms of an agreement to avoid a potential termination or a total interruption of compliance and protection of the value chain of the projects.

BRAZIL



The Brazilian Power Regulator has taken several measures to ensure the continuity of the energy distribution service during the COVID-19 pandemic period. The measures will be valid for 90 days and may be extended. The main measures are temporary suspension of face-to-face service to the public by distribution utility companies; prohibition of suspension of the energy supply to urban, rural and essential services consumer units in case of lack of payment; and prioritization and preservation of the energy supply to the essential services activities by concessionaires.

- Due to these measures for avoiding service interruption, the distribution public utilities is certain to be the most affected player in the power sector. The government has already approved financial support for distribution public utilities.

CHILE



- Energy generation, transmission and distribution is considered an essential business, so workers in such industries have safe-conduct permits to continue operating during the lockdowns and curfews that have been decreed.
- Government agreed with energy distribution companies to suspend service interruptions due to non-payment of service bills (for both commerce and residential purposes). This may impact revenues for Q2 and Q3 2020. It is highly likely that the government will cover such costs.

COLOMBIA



Both incumbents and new investors in the Colombian power sector are focusing their efforts on maintaining their current assets and operations in somewhat normal conditions, and are revising their respective business plans so as to suspend or postpone new investments.

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MEXICO



On May 1, 2020, pursuant the executive order declaring sanitary emergency and by arguing a lack of reliability into the power system as per such sanitary emergency, the Mexican operator, CENACE (National Energy Control Center) indefinitely suspended preoperative test process for new renewable projects and limited the production of the existing one which are operating. Because of this, it is unclear the reaction of the private investment in renewable energy and how those project will be defended against this administrative provision.

PERU



- As mentioned, the government has considered the power sector as an essential activity and, consequently, it has been operating normally. Likewise, there have been no service interruptions, except for some minor events.
 - An important topic that generation and distribution companies should consider is their commercial relationships with their clients. Several free users belong to the mining, retail and industry sectors, which are seriously affected by the lockdown. In those cases, beyond the parties analyzing whether the force majeure / hardship clauses should be applied, the parties should negotiate and agree to reschedule payments in order to protect their long-term commercial relationships.
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VENEZUELA



Power generation and distribution are exempted from the general quarantine imposed by the government. Thus, to some extent, service interruptions have not hit this industry as hard as the rest.

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