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Testimony for

Texas Senate Committee on Natural Resources Subcommittee Studying Impacts of Mexico's Energy Reforms on Texas

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Honorable Committee Members,

It is a pleasure to be here this morning and let me start by introducing myself. My name is Alfredo Ramos, I'm an Energy Partner with the law firm of Gardere, Wynne, Sewell LLP and I have significant Latin America oil & gas operator experience -- primarily in the countries of Mexico and Colombia. I previously held the position of Latin America Operations Legal Director for Lewis Energy Group LP, a Texas based oil & gas operator that maintains operations and offices in Mexico and Colombia. During my tenure at Lewis Energy, I traveled monthly to Latin America to perform my duties and I administered and managed Lewis' Latin America Exploration and Production contracts ("E&P Contracts"), Joint Operating Agreements and other related oil & gas agreements. In conducting my role, I acquired unique experience and knowledge that gives me a great understanding of the operational nature of Latin America oil & gas agreements between companies and Latin American governmental agencies. Additionally, while at Lewis Energy, I collaborated extensively with the administrative and operations teams in Mexico and Colombia to facilitate the movement of oil field equipment, investment funds, technology and personnel between Texas and Mexico or Colombia.

To better understand the scope of Mexico's recent energy reforms, it is demonstrative to look at the impact that significant energy reforms have had on other Latin American countries. Of particular comparison is Colombia's significant energy reform of 2003, which resulted in the creation of an oil & gas industry structure that was used by Mexico's legislators as one of the models for Mexico's December 2013 energy reforms.

The Colombia energy reform of 2003 has been extraordinary for its oil & gas sector. Over the last 10 years, Colombia has seen dramatic increases in oil & gas production and staggering improvements in the amount of foreign direct investment in its oil & gas sector. Since Colombia's 2003 reforms, Colombia has seen its crude output nearly double between 2005 and 2012, going from 525,000 barrels per day in 2005 to 969,000 barrels per day in 2012; the majority of which is a result of new technology used to increase recovery from old oil & gas wells.

Of similar importance, Colombia has experienced an over 1900% increase in foreign direct investment in the oil and gas industry, going from $278 million in 2003 to $5.39 billion in 2012, as reported by the Colombian central bank. These effects experienced in Colombia are truly exemplar and indicative of the transformation that Mexico's oil & gas sector will likely see as a result of Mexico's recent energy reforms.

Further, Colombia has experienced these significant oil & gas results with arguably less favorable terms that those set forth in Mexico's new contractual structure. Mexico's new energy reform structure is proving to be competitive with global oil & gas investment opportunities and, consequently, Mexico is likely to experience substantial investment from foreign sources. For example, a few of Mexico's internationally favorable contractual terms are: 1) sliding-scale royalties that provide international market price considerations to operators' investments, 2) reasonable local content requirements for E&P activities that begin at 25% in 2015 and will gradually increase to 35% by 2025, with potentially different local content requirements for deep water and ultra-deep water operations, and 3) the Mexican government's repeated commitment to anticorruption and transparency to its energy sector. With the proper implementation of the energy reforms, Mexico could surpass Colombia's 1900% increase in foreign direct investment considering its vast oil & gas reserves.

Having experienced, first hand, the impact that substantial energy reform can have on a country such as Colombia, it is truly exciting to see the development of Mexico's oil & gas potential, and opportunities for Texas' oil & gas companies, take shape. Prior to the passage of Mexico's historical energy reform, foreign companies were only able to participate in service contracts in

Mexico, and consequently, Mexico was not competitive with other E&P investment opportunities around the world and did not attract significant foreign investment in its oil & gas sector. However, under Mexico's new energy laws, Mexico has become competitive with other global E&P opportunities.

Today, under Mexico's new oil and gas structural framework, Mexico will allow for foreign investment in E&P operations through profit-sharing contracts, production-sharing contracts, licenses and service contracts, with the operators' ability to account for and book oil & gas reserves as expected income on their E&P blocks. Mexico's reforms also permit PEMEX to joint venture operations with foreign operators. Under this structure, it appears as if the largest foreign benefactor to Mexico's new hydrocarbons sector will arguably be multinational oil & gas operators that are awarded E&P Contracts or joint venture partners with PEMEX on oil & gas operations.

I. FOUR TYPES OF E&P CONTRACTS

The four different types of E&P contracts to be utilized under Mexico's new energy reforms are:

Profit-Sharing Contracts that will require that the operator pay the following to the Mexican government: 1) exploratory phase fees (monthly flat fees for non-producing areas on an E&P block – a concept similar to U.S. Oil & Gas Lease delay rental payments); 2) royalties that vary depending on the international market price of the particular type of hydrocarbon (crude oil, natural gas or condensate); and 3) the payment of a percentage of operating profits. All payments under profit-sharing contracts are to be made in cash.

Production-Sharing Contracts that will require that the operator pay 1) exploratory phase fees, 2) royalties, and 3) payments for a percentage of operating profits. Under Production-Sharing Contracts, the exploratory phase fees are to be paid in cash, and the royalties and share of operating profits are to be paid in-kind.

Licenses that will require that the operator pay 1) a signing bonus, 2) exploratory phase fees, 3) royalties, and 4) payments that consists of a percentage of the contract value of hydrocarbons produced. Under Licenses, the foreign operator may take and own the hydrocarbons in-kind at the wellhead.

Service Contracts for a fixed fee for services provided to the State that will require that all production be delivered to the State. The payments will be made from the sale of production derived from the respective Service Contracts.

II. OPERATOR QUALIFICATION AND BIDDING PROCESS IN MEXICO

To be an operator under Mexico's energy reforms, the foreign operator must be domiciled in and operate through a Mexican entity/subsidiary and it must also qualify as an oil & gas operator. The Ministry of Energy will select the areas for bidding and establish technical and financial qualifications, and the Ministry of Finance will establish the economic and fiscal terms to the E&P Contracts. The E&P bid rounds will be organized and conducted by the National Hydrocarbons Commission. Operator qualifications will be dependent on the company's legal, technical, financial and operational capabilities, and different requirements will be set for the different types of blocks up for bid. Upon an operator's qualification, the operator will enter into a competitive bidding process to compete for the awarding of an E&P contract.

Pursuant to Mexico's new Hydrocarbons Revenues Law, the variables to be evaluated for the awarding of E&P Contracts will be economic in nature and the contract will ultimately be awarded to the operator that will maximize Mexico's revenues.

III. Three Operational Phases Contained in E&P Contracts

Once an E&P Contract is awarded to an operator, the operator will be mandated to comply with certain contractual requirements during the life of the contract. Failure to comply with all of the obligations within each phase of the E&P contract could subject the operator to losing the block and/or all existing production on the block. These contractual requirements are contained in operational phases that will likely be: 1) the Exploration Phase; 2) the Evaluation Phase; and 3) the Production Phase.

Each of these phases will demand substantial operations, many of which require technologically advanced equipment and operational expertise -- which will likely come, in part, from Texas oil & gas companies that have the expertise and a geographical competitive advantage over others around the world.

Exploration Phase (Likely to be 4 – 6 years)

For this phase, the oil & gas operator will perform studies to determine the existence and location of hydrocarbons in the subsurface by conducting geophysical, geological and cartographic operations, likely through conducting subsurface seismic imaging. Also, in this phase, the operator will have to prepare a work program indicating its geophysical/geological findings and intended drilling obligations to comply with the E&P Contract.

Evaluation Phase (Likely to be 2 to 4 years)

During the Evaluation Phase, the operator will perform all the operations to explore and evaluate a discovery (including road and drill site construction, drilling operations, and completion operations), and the operator also will determine whether the well or wells drilled on the E&P Block are commercial or not commercial. In this phase, the operator will identify the hydrocarbon reservoirs and determine the viability of extracting the hydrocarbons from the block, while also analyzing the social, environmental, and economic impact of the oil & gas production on the area.

Production Phase (Likely 20+ years that may be extended during the economic life of the field)

During the Production Phase, the operator will drill development wells and develop the oil & gas fields, which includes the design, construction, installation and maintenance of equipment, pipe, transfer lines, transport systems and other oil & gas related transmission operations. As with the other phases, the operator will likely have to submit to the Mexican governmental agencies a work plan detailing the calculation of hydrocarbon reserves, a program for abandonment, the production work program, and the means of transportation for the hydrocarbons produced.

IV. Midstream

Additional business opportunities for Texas companies exist in the processing and logistics aspects of Mexico's reforms, since Mexico has a very limited hydrocarbon transmission infrastructure. Texas midstream companies have a significant competitive advantage over others due to their geographical proximity to Mexico, their working knowledge of the elaborate Texas pipeline infrastructure, and their ability to collaborate with Mexican companies to expand Texas pipeline systems and maximize hydrocarbon transmission throughout North America. Consequently, Texas midstream companies are likely to significantly benefit from Mexico's energy reforms and will likely be major players in the design, construction, installation and maintenance of Mexico's midstream infrastructure.

These midstream business opportunities in Mexico have already begun to unfold. In late July 2014, less than 2 months ago, Mexico's national power company, the Federal Electricity Commission, announced that it will offer $2.8 billion in natural gas and electricity infrastructure project contracts by the end of 2014. These projects include two combined-cycle power plants, two natural gas pipelines, as well as an electricity transmission project, all projects located near Mexico's northern border with the United States. Requests for Proposal for some of these projects have already been issued by Mexico's Federal Electricity Commission (some as recent as Wednesday) and midstream companies have already begun evaluating and preparing bids for these projects.

V. CONCLUSION:

To conclude, in the coming years vast business opportunities to participate in the historic opening of Mexico's energy industry will become available to Texas oil & gas operators, Texas service companies, and Texas' residents that are experienced in the oil & gas industry. I, as well as my Mexico City partners, assist energy companies in their pursuit of business opportunities in Mexico and we welcome discussions with energy companies looking to participate in Mexico's energy reform. I truly look forward to Texas' collaboration with Mexico on the development of North America's energy resources and, if there are any questions, I am happy to answer them for the Honorable Committee.