Mexico

General Information

Summary

**Status:** ETS in force

**Jurisdictions:** Mexico

The Mexican ETS pilot started operating on 1 January 2020. Mandated by Provisional Article 2 of the July 2018 reform to the ‘General Law of Climate Change’ and implemented through its 2019 regulation, the pilot ETS will help test system design and will run for two years, plus one year of transition to the full operational ETS. It aims to enhance the quality of emissions data and build capacity in emissions trading for covered entities, ultimately improving the design of the operational period of the ETS, which will commence in 2023. The rules for the transitional phase in 2022 are yet to be announced. Together, the pilot phase (2020-2021) and the transition phase (2022) constitute the test program of the Mexican system.

The pilot covers direct CO2 emissions from entities in the energy and industry sectors generating at least 100,000 tCO2 per year. Around 300 entities are covered by the pilot, corresponding to ~37% of national emissions.

The Mexican pilot is designed to pose no economic impact on regulated entities during the pilot years; however, in case of noncompliance, entities lose the opportunity to bank unused allowances into the next compliance periods within the pilot. Moreover, noncompliant entities will receive fewer allowances during the operational period of the national ETS (two fewer allowances for each nondelivered allowance during the pilot).

Year in Review

After a process of public consultation, the Ministry of Environment and Natural Resources (SEMARNAT) published in October 2019 the implementing regulation of the Mexican pilot, which specified the system requirements such as scope, existence and use of reserves, allocation process, MRV process, compliance cycle, and existence of flexibility instruments (offsets and early action credits). The regulation also includes a mechanism of stakeholder engagement, the Consultative Committee, which is a consolidation of the stakeholder engagement process initiated between SEMARNAT and the private sector for the development of the ETS pilot rules.

In November 2019, SEMARNAT published the caps for 2020 and 2021, as well as allowance allocations for the different sectors.

Parallel to this process, SEMARNAT has been working on different infrastructure elements needed for the ETS: the system's registry, which is expected to be completed by the end of June of 2020, offset protocols, and the auction platform. SEMARNAT is considering having auctions during the pilot years, and expects to have the offsets registry ready within the next two years.

Overall GHG emissions (excluding LULUCF)

**Emissions:** 733.8 MtCO2e (2017)

Overall GHG emissions by sector

<table>
<thead>
<tr>
<th>Sector Name</th>
<th>MtCO2e</th>
</tr>
</thead>
<tbody>
<tr>
<td>Energy</td>
<td>522.4</td>
</tr>
</tbody>
</table>
### Overall GHG reduction target

<table>
<thead>
<tr>
<th>Year</th>
<th>GHG Reduction Target</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>BY 2020:</strong></td>
<td>30% below BAU GHG emissions baseline (aspirational, included in the ‘General Law of Climate Change’)</td>
</tr>
<tr>
<td><strong>BY 2030:</strong></td>
<td>22% below BAU GHG emissions baseline (NDC, included in the ‘General Law of Climate Change’)</td>
</tr>
<tr>
<td><strong>BY 2050:</strong></td>
<td>50% below 2000 GHG levels (aspirational, included in the ‘General Law of Climate Change’)</td>
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</tbody>
</table>

### Carbon Price

- **Current Allowance Price (per t/CO2e):** No information available yet.

### ETS Size

<table>
<thead>
<tr>
<th>Category</th>
<th>Details</th>
</tr>
</thead>
<tbody>
<tr>
<td>Emissions covered by the ETS</td>
<td>0.37</td>
</tr>
<tr>
<td>GHG covered</td>
<td>CO2</td>
</tr>
<tr>
<td>Sectors covered and thresholds</td>
<td>The pilot ETS will cover the energy and industrial sectors. The energy sector encompasses electricity generation, transmission, and distribution, as well as fossil fuel extraction, production, transport, and distribution. The industry sector includes automobiles, cement, lime, chemical industry, food and beverages, glass, iron and steel, metallurgical, mining, petrochemicals, and pulp and paper, as well as other industrial subsectors generating direct CO2 emissions from stationary sources at or above the threshold. The pilot ETS covers installations whose annual direct emissions from stationary sources amount to at least 100,000 tCO2.</td>
</tr>
<tr>
<td>Point of regulation</td>
<td>Downstream</td>
</tr>
<tr>
<td>Number of liable entities</td>
<td>~300. The broader mandatory National Emissions Register (RENE) requires mandatory reporting of direct and indirect GHG emissions for facilities with annual emissions at or above 25,000 tCO2e. Under RENE, emitters in the energy, industrial, transport, agricultural, waste, commercial, and services sectors are required to report the six GHGs identified by UNFCCC, as well as black carbon, CFCs, HCFCs, halogenated ethers, halocarbons, and their mixes. No information available yet.</td>
</tr>
</tbody>
</table>
| Cap                                   | **PILOT (2020-2021):**  
  - **Year 2020:** 271.3 MtCO2  
  - **Year 2021:** 273.1 MtCO2[1]  
  - Three reserves will be filled each year with allowances additional to the cap:  
    - auctions reserve (equivalent to 5% of the cap);  
    - new entrants reserve (equivalent to 10% of the cap, for new entrants as well as increases in production among existing regulated entities); and  
    - general reserve (equivalent to 5% of the cap, for ex post adjustment allocation for entities with higher emissions relative to their baselines).  
  - The reserves serve as safeguards to avoid any impact to competitiveness during the pilot phase, as required by the ‘2018 General Law on Climate Change’.  
  [1] The increase in the cap between 2020 and 2021 is due to an increase in the sectoral allocation for regulated entities categorized as “others.” |
## Phases & Allocation

### Trading period
- Pilot phase (2020-2021); and
- transition phase to the operational period of the ETS (2022).

The schedule of implementation as contained in Annex I to the ETS pilot regulation contains compliance and allocation dates for the compliance cycle of 2020 and 2021. Emissions for 2022 will be covered by the operational period of the ETS.

SEMARNAT is expected to publish the regulation of the operational period of the ETS in 2022.

### Allocation

The pilot will use free allocation with the following specifications.

**Initial Allocation:** Entities will receive free allowances based on historical emissions. New entrants will receive free allowances based on their reported emissions in the year in which they first crossed the 100,000 tCO2 threshold.

**Ex-Post Adjustment:** An adjustment allocation will be carried out from the general reserve for those participants whose verified emissions in that year are higher than the free allocation received. The regulation does not specify how adjustments will be made in the event that demand for additional allowances exceeds reserves.

When an installation closes permanently, the installation may have to surrender the allowances that it has for the compliance period of the year before its closure. Additionally, it may need to return the free allowances received for the compliance period in which it closes. Whether the installation has to only surrender allowances, only return allowances, or both depends on the date of the year in which it closes. These allowances are then cancelled by SEMARNAT.

With regards to auctions, starting from the second year of the pilot and depending on market behavior, SEMARNAT may auction allowances from the auction reserve.

## Flexibility

### Banking and borrowing
If participants are in compliance with their surrender obligations, then their remaining allowances may be banked for use in subsequent compliance periods within the pilot. Allowances issued in the pilot will be valid only for the pilot, although SEMARNAT is tasked to also assess the viability of allowing a share of pilot allowances to be banked into the national ETS. Although the possibility of borrowing is not explicitly stated, surrender of allowances for a given compliance period is done after allocation of allowances for the subsequent compliance period takes place.

### Offsets and credits

**QUALITATIVE LIMITS:** Two types of flexibility instruments are foreseen, both of which will generate “offsets credits” eligible for use under the pilot.
- Offsets: SEMARNAT will establish a domestic program for the generation of credits that can be surrendered for compliance in the national ETS. Eligible mitigation projects or activities are domestic projects that have been validated and verified under internationally or domestically recognized protocols (as yet unspecified). Emission reductions related to all GHGs will be eligible, though the pilot ETS regulates only CO2.
- Early action: For those projects or mitigation activities operating under recognized protocols that receive offsets before the pilot comes into force, SEMARNAT may issue offsets credits if a certificate of cancellation is presented. These projects will be allowed to continue generating offsets during the pilot.

**QUANTITATIVE LIMITS:** Participants will be able to meet up to 10% of their compliance obligations with offset or early action credits.

### Market Stability Provisions
No information available yet.
Compliance

Compliance Period

From 1 January to 31 December

Reporting Frequency: Annual self-reporting based on electronic templates prepared by SEMARNAT.

Verification: Verification by independent accredited verifiers is required by 30 June each year.

Framework: A monitoring plan is required from all regulated entities, but noncompliance has no effects on free allocation or ex post adjustments. Report of verified annual 
CO2 emissions is made both to the RENE (on top of other obligations that regulated entities have to report to the RENE) and to the ETS registry.

Enforcement

The system is designed to pose no economic impact on regulated entities; however, in case of noncompliance, entities lose the opportunity to bank unused allowances for the next compliance periods within the pilot. Moreover, noncompliant entities will receive fewer allowances during the operational period of the national ETS (two fewer allowances for each nondelivered allowance during the pilot).

Linking

Links with other Systems

The ‘General Law on Climate Change’ foresees possible linkages between the Mexican ETS and ETSs in other countries. Various cooperation activities have taken place in recent years. Mexico signed a Memorandum of Understanding with California in 2014 and with Québec in 2015 that includes cooperation on ETS. In August 2016, Mexico, Québec, and Ontario issued a joint declaration on carbon markets collaboration. Additionally, in December 2017, Mexico—together with four countries and seven subnational governments—issued the Paris Declaration on Carbon Pricing in the Americas for carbon pricing implementation, which creates a platform for cooperation among countries in the region.

Other Information

Institutions involved

SEMARNAT;
National Institute for Ecology and Climate Change (INECC)

Evaluation / ETS review

SEMARNAT will annually review the pilot, publishing reports on topics such as price behavior and emissions reductions achieved. An evaluation of the pilot, supported by the INECC and by the Consultative Committee, will also be conducted to determine if adjustments to the ETS design are necessary before the start of the operational period of the program. This evaluation process may involve consultations with civil society and academia. Regulations for the operational period of the Mexican ETS are to be published in 2022.

Revenue

No information available yet.

Implementing Legislation

General Law of Climate Change
Agreement on the establishment of the preliminary basis of the Pilot Program of the Emissions Trading System (implementing regulation of the pilot)
Notice on the cap for the years 2020 and 2021
Notice on the reserve and sectoral allocation of allowances for the years 2020 and 2021
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