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Mexico ETS at a Glance

Years in operation	<p>Mexico's ETS began its pilot phase in January 2020, and it was expected to be fully operational in 2023, although the main market rules had yet to be published. The Mexican ETS has three phases:</p> <ul style="list-style-type: none"> • Pilot phase (2020-2022) • Transitional phase: (2022)* • Operational phase: 2023 onwards** <p>*The transitional period aimed to enhance the quality of emissions data and build capacity in emissions trading for covered entities, ultimately improving the design of the operational period.</p> <p>**The Mexican regulator has declared that the rules for this phase will be defined in 2024 or 2025.</p>
Overall cap & trajectory	<p>2020: 271.3 million tCO₂ (1% CO₂ reduction over the emissions reported in the Emissions National Registry)</p> <p>2021: 273.1 MtCO₂</p> <p>2022: N/A</p> <p>2023: N/A</p>
Target(s)	22% below BAU by 2030
Emissions reduced to date	No data available yet
Sectors covered	Facilities with annual emissions of and greater than 100,000 direct tCO ₂ emissions from the energy (electricity generation and fossil-fuel extraction and production) and industrial sectors (cement, chemicals, automobiles, glass, steel, metallurgical, mining, petrochemicals, pulp and paper subsector, among other industrial subsectors that generate direct emissions from stationary sources)
GHGs covered	CO ₂
# of covered entities	Approximately 300 entities were covered by the pilot phase, representing around 37% of national emissions.
Allocation method	Grandfathering based on historic emissions
Trading rules	N/A
Use of offsets and linking	The use of offsets is limited to 10% of the compliance obligation and credits from non-ETS sectors during the pilot and transitional phase.



	The approved methodologies have not yet been published.
Other features	<p>In the pilot and transitional phase, banking was only allowed if participants fulfilled their obligations properly and on time. Credits issued in the pilot phase will only be valid in that phase. For the operational phase, the use of this flexibility mechanism has yet to be defined.</p> <p>There are three reserves within the cap: one for new entrants (10% of the cap), one to adjust supply if needed (5%), and an auction reserve (5%).</p>
Penalties for non-compliance	<p>In the pilot phase and transitional phases, there were non-economic penalties for non-compliance to encourage participation.</p> <p>For the operational phase of the ETS, installations that did not comply on time during the pilot phase will receive two fewer allowances for each allowance not submitted during the pilot phase.</p>
Use of revenues	Mitigation actions and ETS management

Major Developments

Although the implementing regulation of the Mexican pilot was published in October 2019 and the 2020-21 caps and allocations in November 2019, participants of the ETS only received their first allowance allocations in October 2021, and the SEMARNAT announced a 97% compliance rate for the year 2020 in April 2022.

In March 2022, the 3rd Emissions Trading Academy in Mexico was developed for high-level members of SEMARNAT to keep building and strengthening capacities to handle technical issues for the implementation of the Mexican ETS: financial regulation, carbon leakage, MRV, flexibility mechanisms, among other topics. A book capturing the ETS experience of Mexico is expected to be published.

Market Commentary

The fully operational phase was intended to start in January 2023, and facilities would potentially trade allowances and acquire carbon credits for compliance, however the main market rules for this phase have yet to be published. The Mexican regulator has declared that the operational rules for this phase will be defined in 2024 or 2025.

Since 2014, Mexico has had a federal carbon tax on fossil fuels, which applies to the production, import, and sale of fossil fuels intended for combustion processes, except for natural gas. This tax is subject to the Special Tax on Production and Services (IEPS) Law and establishes a tax rate based on the amount of carbon contained in the fuels.

In its first year of operation, the tax collected US\$538,000, while by the end of 2022, the cumulative revenues in Mexico from this instrument amounted to US\$3,421,696.56, according to data from the Ministry of Finance (SHCP, 2023). Currently, no mechanism

earmarks the use of the revenues collected through the IEPS for any specific purpose, so all the proceeds go into the general national budget.

SUBNATIONAL CARBON PRICING IN MEXICO

Since 2017, diverse federal entities have implemented carbon taxes within their jurisdictions. Currently, multiple instruments are in force in the states of Zacatecas, Durango, Querétaro, Yucatán, Estado de México, and Guanajuato. Several other states have expressed their interest and have initiated the development of subnational carbon pricing instruments, such as Tamaulipas, Colima, and Jalisco.

The taxes currently in force follow a uniform scheme that focuses on downstream regulation and is limited to direct emissions from fixed sources. Carbon prices range from US\$2.50 to \$40 per tonne. In some cases, such



as Querétaro and Guanajuato, they incorporate flexibility mechanisms such as tax incentives and offsets to enable obligated entities to reduce direct emissions. For example, 341,619 carbon credits were used in Querétaro towards the 2022 carbon tax obligations.

Under this operating model, significant revenue has been generated. It is important to note that, in all cases except Durango, these

funds have been specifically allocated to address issues related to climate change (mitigation and adaptation) and the environment.

Additionally, it is worth noting that states like Tamaulipas and Colima are implementing measures to enhance resource efficiency through climate change-related trusts, which are incorporated into their respective legislations.

Useful Links

[Mexico GIZ](#)

References

ICAP [archives](#) and [fact sheets](#)

[SEMARNAT Cap announcement](#)

[Federal Official Gazette: Emissions Trading System Pilot Phase](#)

[SEMARNAT statement on allocation rules – December 2020](#)

[SEMARNAT statement on allocation – January 2021](#)

[TECHNICAL NOTE: Emission Trading System in Mexico](#)

SHCP. (2023). Recaudación: Ingresos tributarios del Gobierno Federal. IEPS. Secretaría de Hacienda y Crédito Público.

AUTHORS

Camilo Trujillo
LAC Lead, IETA
trujillo@ieta.org

Paloma Vázquez
Technical Director, MÉXICO2
pvazquez@mexico2.com.mx

Denitza González
Operations Director, MÉXICO2
denitzag@mexico2.com.mx

MÉXICO₂
Plataforma Mexicana de Carbono