1. SUMMARY INFORMATION

Implementing Country/Technical Partner: Mexico

Reporting Period: From 09/30/2019 to 09/30/2020

Report Date: 01/10/2020

Implementing Agency: General Directorate for Climate Change Policies, Ministry of Environment and Natural Resources (SEMARNAT)

Contact Person:
• Yutsil Guadalupe Sanginés Sayavedra, General Director, SEMARNAT (Focal Point)
• Ximena Aristizábal C. (PMR Coordination)

Grant Executed By: World Bank

Grant Effectiveness and Closing Dates: 07/01/2017 – 06/30/2020

Grant Amount (USD):
Initial: USD 3,000,000
Updated: USD 2,700,000

Funding Mobilized (USD):
• Government of Mexico: USD 570,000 (last year estimate)
• IKI Project “SiCEM” (financed by BMU, implemented by GIZ in Mexico): EUR 4,200,000 (USD 4,920,700). From September 2017 to February 2023.

Funding Committed (USD) as of 09/30/20
USD 2,190,000

2. OVERVIEW
Please provide a general description of the progress made towards the Grant’s Objectives and Activities (as per the Project Development Objective(s) Indicator(s) and Intermediary Results Indicator(s) included in the World Bank’s Project Paper’s Results Framework). Please also highlight critical issues as well as pending actions that may require the PA or the PMR Secretariat’s attention.

The PMR Partnership Assembly endorsed Mexico’s Market Readiness Proposal (MRP) in 2013 and awarded funding for US$3 million to support market readiness activities. The focal point for the PMR is the Ministry of Environment and Natural Resources (SEMARNAT). The National Housing Commission (CONAVI) participated in PMR activities as coordinator of one of the three original components.

The grant was initially to be managed by the Climate Change Fund, but due to changes in the fund operation, SEMARNAT decided to proceed with a Bank-executed project in April 2017.

In 2018, the Climate Change Law was amended according to the goals and content of the Paris Agreement. Amongst other critical provisions, the amended Law mandates SEMARNAT to design and implement a National ETS, starting with a pilot phase. The regulation (“Bases Preliminares”) for the Pilot Phase of the ETS was published on October 1st, 2019, with the support of PMR. The pilot will run for three years, starting on January 1st, 2020.

Building upon Mexico’s MRP, the implementation work program was updated and refined into the support for the development of a National Emissions Trading Scheme (ETS), based on the following areas:

(i) Capacity building of private and public sector entities. Some of the results from this activity are:

- A Simulation Exercise in 2018 to give participants a firm grasp on ETS concepts and design elements to improve communication between authority and stakeholders.
- Execution of the ETS Academy 2019 to build capacities among government officers.
- ETS Academy 2020 building capacities on government officers, private sector representatives and the Consultative Committee for the ETS.
- Business oriented training for regulated entities in 2020 for all ETS covered sectors.
- Development of a medium and long-term Communication Strategy.
- Development of an ETS handbook with a basic and a technical component.

(ii) ETS pilot phase readiness, with a particular focus on an emissions registry and offsets. A general view of the implementation results, highlights the following activities:

- Design of a national Offset Scheme, with criteria for the assessment, review and approval of protocols and guidelines for mitigation outcomes verification.
- Design of rules and criteria for the approval of early action GHG reduction certificates and recommendations for the registration.
- Development of four demonstrative protocols in Forests, Agriculture, Livestock and Transport.
- Technical assistance for the design of a register tool for mitigation projects and certificates (RENE - mitigation).
(iii) Technical advisory for the implementation of the pilot phase. Some of the most relevant results are:

- Adaptation of an electronic platform to serve as a demonstrative Registry for the market.
- Policy mix analysis, including integration of vertical policies.
- Evaluation framework for the pilot phase of the ETS.
- Market monitoring framework.
- Assistance for the installation and 2020 sessions of the Consultative Committee.
- Assistance on the development an Allocation Table and Rules & Criteria for allocation and reserves use.

3. IMPLEMENTATION REPORT BY COMPONENT

**Differences between the Objectives/Activities in the Market Readiness Proposal and the Grant Agreement**

| Are there any important and material differences between the objectives/activities proposed in the Market Readiness Proposal and endorsed by the Partnership Assembly of the PMR and those agreed to in the Grant Agreement with the Delivery Partner and described in the Project’s Results Framework? | Yes

Please choose one of the above options.

*If yes, please explain the reasons for these changes and how the revised objectives/activities will contribute to market readiness (i.e., the establishment of core technical components and/or the piloting of specific activities related to carbon pricing and the use of market-based instruments). Please also provide details about when and how the PA was informed about and endorsed the change(s).*

The Government of Mexico (GoM) works on a carbon pricing strategy that goes beyond the initial efforts of adopting a carbon tax on fossil fuels importation and commercialization. The objective is to pursue further, and more ambitious mitigation goals aligned with the Climate Change Law and Mexico’s NDC.

Since the endorsement of Mexico’s MRP, the country has gone through various milestones related to carbon pricing. Some of them include the amendment to the Climate Change Law in 2018, the publication of the ETS pilot regulation in the official gazette, the publication of the cap for the first two years of the pilot and the sectoral allocation in 2019.

In 2020, several capacity building activities have taken place, in addition, Mexico has installed its Consultative Committee and has developed a Registry to perform the first allocation. In 2021 the first commitment period will close, and the first indicators of market performance will be available.

In the international arena, the country has joined various regional and multilateral initiatives related to carbon pricing. On December 12th, 2017, at the One Planet Summit in Paris, France, the governments of
Canada, Chile, Colombia, Costa Rica, Mexico, as well as the US states of California and Washington and Canadian provinces including Alberta, British Columbia, Nova Scotia, and Québec, announced the Declaration on Carbon Pricing in the Americas. In 2018, the state of Sonora joined the Declaration, as the first subnational government from Mexico choosing to be part of this unique regional collaboration mechanism. The Declaration and platform for cooperation remain open for more jurisdictions to join. The cooperation has identified three priority areas: governance, current work environment, and specific policy challenges.

Mexico became a member of the Carbon Pricing Leadership Coalition (CPLC) and an observer of the International Carbon Action Partnership (ICAP) and subscribed a Memorandum of Understanding with the State of California in the U.S. The country is member of the Pacific Alliance, an initiative comprised of Chile, Colombia, Peru and Mexico, in which every country is collaborating for deeper integration to drive further growth, development and competitiveness; while each country is pursuing carbon pricing policies that could converge in collaboration in that matter.

The adjustments to the original MRP allowed Mexico to focus on ETS design and implementation. The main elements of the updated and refined implementation work program were presented by Mexico and discussed with the PA during its 16th Assembly Meeting.

**Implementation Progress by Component**

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<th>A. Component 1: CAPACITY BUILDING</th>
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<td><strong>Status:</strong></td>
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*Please choose one of the above options.*

*Please describe the progress made towards the achievement of the expected results, as per the date of the Report, in relation to each of the Intermediary Results Indicators.*

Mexico is facing the first year of its ETS Pilot Phase; there is a continuous need to build capacities and develop skills among stakeholders.

On August 2016, the Government of Mexico signed an MOU with the Mexican Stock Exchange to launch an **ETS Simulation** as a capacity building exercise for the private and public sectors. The Simulation required the service of a software provider for an electronic tool to serve as a registry, auction platform, and trading platform for allowances issued within the Simulation. Participants were able to learn about the organization and operation of an ETS, and about the differences with other carbon markets (voluntary and CDM, for example).

The exercise started in December 2017, with introductory training workshops during November 2017; the Simulation ran for 7 months and was finalized in June 2018. The exercise included in-person trainings, webinars, and continuous support for the participants; the simulation was implemented through three simulated phases, each of them comprising compliance periods from 3 to 6 years.
Key Achievements:
- It was the first Simulation Exercise in the Latin American region gathered over 100 companies from: energy, power generation, aviation, chemical, iron and steel, mining, car manufacturing, cement, pulp and paper, glass, construction, food and beverages, finance and other sectors.
- Three exercises that simulated 12 calendar years in total.
- Training introduction workshops, call center for participants.
- Active engagement from all participants.
- Final exercise included award ceremony for top performers.


In 2019, Mexico carried out the **first ETS Academy**; a three-day workshop focused on learning the key steps to design the ETS pilot phase and how it should be adapted for Mexican reality, learning from international experiences.

Key Achievements:
- Over 30 participants from the Federal Administration, including Ministries of Environment, Finance and Economy, the National Forestry Commission (CONAFOR), National Institute of Ecology and Climate Change (INECC), Mexican Oil Company (PEMEX), Electricity Federal Commission (CFE), among others.
- Presence of international experts from, North America, Asia, and Europe to share lessons learned with their respective systems.
- Government discussion for next step planning.

A brief note and all presentations can be found at [https://www.thepmr.org/events/eventlist/other-events/ets-academy-mexico](https://www.thepmr.org/events/eventlist/other-events/ets-academy-mexico).

The **second ETS Academy** took place on September 2020. Originally designed as a face-to-face workshop, and later transformed into a virtual one, the objective of this training was to provide detailed capacity building on the implementation of the pilot phase for decision makers in the private, public, and social sectors as well as the academia. Among those audiences the **Academia del SCE** ran through four intensive weeks of up to 3 weekly sessions given by expert speakers of more than 15 countries. The **Academia** hosted as speakers a majority of the top technical public officials, advisors, and consultants from relevant jurisdictions and Mexico regarding carbon pricing policy experience.
The training was composed of both live and prerecorded lessons structured in topics by week. Prerecorded sessions and other materials like readings and graphical recordings were hosted in a learning platform. The 18 modules covered topics like general ETS design and implementation, detailed Mexican ETS pilot phase aspects, a keynote speech by the UNFCCC, experiences implementing initial phases of ETS around the world, market dynamics, MRV robust systems, strategies to incentivize compliance, governance structure of the Pilot phase, stakeholder outreach and communications, early action and offsets protocols, Latin America regional experience exchange in carbon pricing policies and Article 6.

The innovative structure of the *Academia* was accompanied with a friendly and highly graphical communication strategy that develop a strong channel to deliver messages for the audience but overall to keep participants interested in the training. Participation was always above 85% in every session.

Key Achievements (Appendix 2):
- Almost 80 decision makers trained from the relevant sectors involved in the ETS implementation.
- Lessons delivered by key experts from more than 15 jurisdictions with in-depth experience in carbon pricing policy and climate policy.
- First stakeholder capacity building training since the start of the pilot phase.

The **ETS training for business** is the first capacity building effort with a sectoral business-to-business approach specifically tailored to participating operators of the Mexican ETS. It started on August 2020 and will last 9 weeks. The content of every module is presented each week, led by national and international sectoral experts. The training includes pre-recorded and live sessions, interactive activities, educational videos, and expert-to-participant knowledge transfer.

Key achievements (Appendix 3):
- Active engagement from participants of all sectors.
- ~300 participants from the food and beverage, glass, paper, power generation, cement, lime, mining, iron and steel, chemical, and “other” sectors; from ~80 companies.

This component is also supporting the design and development of a **communications strategy** and a handbook. The communication strategy is being developed as a key instrument to help SEMARNAT in the design
and implementation of public interactions with audiences such as the public, ETS participants, public officials, legislative branch, technical experts, and other stakeholders. This strategy developed a series of research methods including interviews, round tables, focus groups, national surveys to gather information on the Mexican public, the appropriate type of narratives and messages to be developed and communicated, relevant channels, appropriate spokespersons. Aside from the communication aspects the strategy will contain in depth information on current opportunities to strengthen stakeholder’s capacities.

Another project focuses on the design of a Mexican ETS handbook. This document represents a cornerstone of the materials to be developed under the recommendations of the Communications Strategy. It is inspired by other handbooks but uniquely tailored to showcase the developments under de Mexican ETS. It is aimed to become the main source of introductory and detailed information for public and regulated entities. It is structured in two subsections: a general handbook and a technical handbook. Along with the handbook it was designed an institutional graphical identity for the ETS, with a main feature in the official logo, two videos for public, banners, templates, and infographics.

Key achievements (Appendix 4):
- First of its kind communications strategy for a national relevant climate change policy instrument in Mexico.
- First communication materials package (2 short videos, 2 infographic guides for participants) since the official start of the ETS according to the institutional graphical identity.
- ETS branding (logo, Power Point templates, Word templates, banners, etc.).
- Social media strategy.

Further training activities to facilitate the kick-off of the pilot phase include a Registry training.

Comments: Please describe the reason(s) for the early/timely/delayed achievement of the expected results.

Results have come on time. It is relevant to mention that communication and capacity building activities are a constant need. The PMR has helped to build strong basis for government representatives with a role in the ETS, for regulated entities, private sector associations and chambers and for the Consultative Committee. All stakeholders will require strengthening their abilities to participate in the market, and government participants will require additional training to foresee needs and be
prepared for the design and implementation of the operational phase of the ETS. Communication and training are the fundaments to achieve a full engagement, commitment and a focused participation when providing recommendations and changes to the system.

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<th>B. Component 2: ETS PILOT PHASE READINESS</th>
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This component supports the design and development of the ETS through 4 sub-components. In turn, these sub-components are part of a comprehensive ETS Design & Piloting Roadmap prepared by SEMARNAT to guide the ETS development process (see section 5).

**a) Support for the design of a pilot ETS Registry**

The emissions reductions Registry will support the ETS by providing the platform for trading emission allowances and allow offsets to enter the program. It will cover emissions reductions as stated in the Climate Change Law as well as reductions from sectors not regulated by the ETS. The registry development was based on an existing SEMARNAT software, adapted to the market needs.

The demonstrative registry will be administered by the SEMARNAT and follows international best practices that could eventually allow international linking with other trading systems. The registry will allow for the allocation, tracking, management, and trading of units that could be used towards compliance of mitigation obligations under the ETS.

This demonstrative registry is the first platform developed in the region; different aspects will be proved during the pilot phase such as reliance, completeness, security, among others. It is expected that the initial registry will be subject to improvement during the operational phases of the ETS.

The registry shall be in its implementation stage in October 2020, when the first allocation period takes place. See Appendix 5.

**b) Support the design of offsets protocol schemes**

This activity operationalizes the flexibility mechanisms stated into the ETS regulation. The PMR is supporting the following activities:

- Drafting specific rules and processes for recognition of early action offsets (Appendix 6), crediting of GHG reductions as Mexican offset credits and specification on their usage and trading under the Mexican ETS.
• Supporting technical definitions of processes (project life cycle) and criteria (eligibility, principles, validation, etc.) for the review and evaluation of existing protocols or new protocols proposals.
• Supporting the development of demonstrative offsets protocols for selected mitigation activities in priority sectors (Forestry, Agriculture, Livestock and Transport). See Appendix 7.
• Analyzing the feasibility of incorporating the transport sector as a regulated sector under the ETS or as an offset provider.
• Supporting the provision of technical input and guidelines for the Verification of emission reductions from eligible offset projects. In the medium term, Verification Bodies shall seek accreditation to verify emission reductions to be considered as offset credits. SEMARNAT will seek the usage of international existing standards as reference.

The development of those protocols has included a participatory approach from different government entities like: CONAFOR, INECC, Protected Areas Commission (CONANP) and Ministry of Agriculture (SADER).

Three different technical virtual workshops were organized to receive feedback and insights from the above-mentioned government entities about the potential mitigation activities identified and their prioritization.

c) Support the design of implementation rules and processes
This activity will support SEMARNAT to develop a reliable database of verified emissions to properly identify regulated entities and develop a National Allocation Table to pursue the allocation process.

Key development tasks:
• Develop a communication channel with participating operators. PMR has supported SEMARNAT to engage in +50 one on one meetings with participants to verify their emissions, validate their threshold for participation, understand the corporate structure (company and subsidiaries) according to the number of participant installations per company and sector, among many others. In March 2020, previous to this activity, SEMARNAT had confirmed the emissions from ~35% of the participant installations; with the PMR support, by August 2020, this had increased to ~75%, and as an ongoing task the percentage is expected to continue to rising.
Under this component, technical, institutional and legal advice is provided to SEMARNAT in order to prepare internal processes and interactions with regulated entities (official procedures to open an account in the Registry, Know your Customer (KYC), official rules for allocation and reserves management, among others).

**Technical advice on legal aspects** has been constant in the formulation of rules and criteria for allocation and reserves, and the opening of an account. Both content and format of such elements have represented an opportunity for the design of the ETS regulation. Based on the principle of legality as well as the approach of the General Directorate of Climate Change and communication with the legal area of SEMARNAT, the meetings held have achieved progress and opportunities for improvement. Likewise, due to the communication among PMR projects (as with the ETS training for business), potential flaws have been detected and addressed.

An updated analysis of the **ETS interaction with other carbon pricing instruments** is taking place. In addition to the carbon tax, other instruments such as energy subsidies and sub-national initiatives (state level taxes) are included into the policy mix analysis.

SEMARNAT is preparing an **evaluation framework** to inform decision makers on the available methods and international experience on ETS evaluation processes. This framework will compare and extract relevant experiences of mature ETS in different jurisdictions, to further support the development of key concepts regarding performance in the ETS, consider dimensions to be evaluated as intended in the regulation and propose other relevant dimensions and indicators. The products from these tasks will be inputs for the Consultative Committee decision making process to host the evaluation of the ETS that will take place starting July 2021. The impact of this project is crucial for the further development of the operational phase of the ETS, as its results will inform and shape the new regulation.

The PMR is supporting the technical design of a **mitigation register**. The aim of this tool is to keep record of mitigation outcomes from different sources (e.g., offsets, early action offsets, ITMOs, voluntary projects, etc.) in a SEMARNAT’s managed tool. Technical advice goes beyond the platform, it includes the definition of eligibility criteria, processes and formats to register a project in this new component of RENE – mitigation. This technical support also includes the considerations to ensure a harmonious bonding among projects, procedures, protocols and accredited bodies, as well, capacity building with SEMARNAT.
In terms of institutional arrangements, it is relevant to highlight the installation in June 2020 of the Consultative Committee and its ordinary sessions.

d) **Analysis of enabling conditions to engage in Article 6 Cooperative Approaches**

Mexico has the potential to be an important player in the international carbon markets developing under Article 6, taking advantage of the potential economic gains. An ongoing study is analyzing Mexico’s current climate policy environment, including the legal and institutional framework, and its suitability to fulfill institutional and governance functions that are required to engage in Article 6 cooperation. The analysis addresses the opportunities, challenges, and needs that the Cooperative Approaches of the Paris Agreement present for Mexico’s climate policy.

The study identifies competing interactions and linkages between Mexico’s domestic carbon pricing instruments with internationally transferred mitigation outcomes (ITMOs), among others. It will address methodological considerations to facilitate Mexico’s participation in Cooperative Approaches and to address national development policy and environmental integrity considerations. Besides, it will generate a consolidated proposal for an Article 6 engagement strategy which aims to summarize opportunities, conditions, and challenges for Mexico and provide country-specific recommendations.

Some achievements have been reached since the project began. The interaction between SEMARNAT, INECC, PMR and the Consortium has been regular and meaningful. There is a right attitude towards sharing information from both SEMARNAT and INECC. Effective engagement can be seen in the already agreed, scheduled and longer-lasting bi-weekly calls. Besides, extra meetings were proposed and accepted by all members due to the shared acknowledgement of capturing all the correct information, sharing more reflections and being in contact with what the project needs.

The importance of this project for the future of Mexican capacities is related to the implementation of Mexico’s NDC and overall long-term low carbon development goals. Expected outcomes such as the elaboration of a generalized framework for cooperation that can serve as a template for identifying Mexico’s most appropriate cooperation approach will be essential. Besides, depicting how countries will interact under Article 6 is relevant to provide the context of how Mexico could potentially fit within the international scene in the short and mid-term. (Appendix 7)
Comments: Please describe the reason(s) for the early/timely/delayed achievement of the expected results.

This component is meant to support the ETS efforts in Mexico managed by the Climate Change Office in SEMARNAT. Improve technical capacities of the team in charge of the policy and support them to be prepared to operate the market. This is a relevant component, also considering government changes, with the documentation and preparation of tools and processes, it is expected for SEMARNAT to get sustainability in their activities. Nevertheless, for this component to be highly effective, it would require continuous support with more detailed contents in the next steps of the ETS implementation.

C. Component 3: MANAGEMENT AND ADMINISTRATION

Status: Under implementation

Please choose one of the above options.

Please describe the progress made towards the achievement of the expected results, as per the date of the Report, in relation to each of the Intermediary Results Indicators.

This component supports the contract for five national PMR consultants and an international PMR consultant, that will carry out activities to help SEMARNAT with the implementation of the activities described above.

Comments: Please describe the reason(s) for the early/timely/delayed achievement of the expected results.

All contracts will finish on February 2021.

If necessary, please add components in the table above.

4. PROGRESS, CHALLENGES, AND LESSONS LEARNED

Important policy or regulatory developments related to the Grant’s objectives and activities:

Developments: Please describe important policy and regulatory developments related to carbon pricing that have occurred during the Reporting Period and/or that are expected in the future.

During 2017, Mexico’s Congress discussed amendments to the Climate Change Law, after the entry into force of the Paris Agreement. The amendment proposals focused on harmonizing the content of the law with the Paris Agreement and the Mexican NDC. The amendment was initially approved by Cámara de Diputados (Lower Chamber) in December 2017, and by the Senate in April 2018. The bill was finally signed by the President and enacted by publication in the Official Gazette on July 13, 2018.

On 12 December 2017, at the One Planet Summit in Paris, France, the governments of Canada, Chile, Colombia, Costa Rica, Mexico, as well as the US states of California and Washington and Canadian provinces including Alberta, British Columbia, Nova Scotia, and Québec, announced the Declaration on Carbon Pricing in the Americas. In 2018, the state of Sonora joined the Declaration, as the first subnational government from Mexico choosing to be part of this unique regional collaboration.
mechanism. The Declaration and platform for cooperation remain open for more jurisdictions to join. The cooperation has identified three priority areas: governance, current work environment, and specific policy challenges.

The Mexican Government published a regulation for the pilot phase of the Mexican ETS. After a first draft put for public consultation in October 2018, the Government of Mexico issued a second draft of the regulation guidelines (“Bases Preliminares”) for public consultation in May 2019. The third draft addressing comments received was finalized by September, and on October 1st, 2019, the regulation guidelines for the pilot phase of Mexico’s ETS were published by the GoM in the Official Gazette.

The pilot program started in January 2020 and will have a duration of 36 months, followed by the full operative phase starting in 2023. Both the cap and the sectoral allocation plan were published, as stated in the regulation, by December 2, 2020.

In the upcoming months, SEMARNAT will publish the allocation rules and criteria as well as the official processes for regulated entities to interact with the Authority (opening account process, processes for reserves management).

Rules for the offset scheme are under preparation, they might be published in 2021.

Challenges: Please describe how such developments might affect the achievement of the Grant’s objectives and/or the implementation of specific activities under the Grant, either positively or negatively, and how possible policy and regulatory challenges may be addressed going forward. Please also refer back to any potential policy and regulatory challenges that may have been identified in the previous PMR Project Implementation Status Report and, if applicable, explain how such challenges are/have been handled.

The policy and regulatory developments had a positive impact in the grant’s objectives, by giving a strong and better legal framework for carbon pricing in Mexico. The legal mandate for an ETS had a positive impact in terms of engaging international agencies and jurisdictions in supporting the process for the ETS, including the PMR, GIZ, ICAP, WCI and New Zealand. Their support focuses on data reporting and verification, data analysis, legal advice, cap setting, technical studies, among others.

The big challenge for such an ambitious project (ETS implementation) has been political changes and time constraints, revisions and approvals are time consuming, SEMARNAT had to work together with changing staff among government agencies to socialize the ETS design and operation. Being the top priority, SEMARNAT worked together with the PMR team to dedicate the PMR project funding to the ETS pilot phase preparation and implementation. Mexico moved from a readiness status to implementation during the PMR project, therefore the changes to the work plan. Also, as the regulation was revised numerous times, the implementation of activities was also affected. SEMARNAT will be able to complete implementation of remaining funds by 2020. Having a regulation in place, and a Pilot officially started, implementation will remain a challenge, but with a strong political support.

Lessons learned: If applicable, please provide a brief description of the lessons learned regarding carbon pricing policy and regulatory developments during the last Reporting Period.
One of the main lessons learned and achievements from the programme is the engagement process with stakeholders from the private sector. The PMR support to the Simulation Exercise opened the door for more direct and technically focused exchanges with private sector representatives, an opportunity that led way to a Working Group. It was through the working group that both parties, government and private sector, were able to discuss their interests when drafting the ETS regulation. The ETS Simulation exercise and the Working Group helped in finding common ground on usually divergent positions and positioned the ETS as a feasible option for GHG mitigation in Mexico.

This effort was strengthened with the different capacity building and communication activities, directly reaching around 400 people with a high level of understanding of the process. Once the handbook and other communication materials are published, the scope is expected to be higher.

Despite on the time constraint, another important lesson learnt is that having a due date (in their regulations) for processes to be completed, has secured political support to make progress on aspects that otherwise would be longer, for instance, the development of the offset scheme or the ETS registry.

### Important changes in the technical design or approach related to the Grant’s activities:

**Developments:** Please describe any important change in the technical design or approach related to the Grant’s activities that have been made during the Reporting Period or that are expected in the future.

Due to the amendments to the Climate Change Law, the ETS regulation was adapted to be compliant with the new legal framework, as first step to implement an ETS in a Pilot Phase.

The Pilot will run for three years, from 2020 to 2022 as the work plan indicates. Some aspects for the ETS are being pushed to the operational phase, such as benchmarking, and auctions (although it is possible to start in 2021).

The offset program is under development during the pilot; however, it is foreseen for the first credits to enter the market during the operational phase. During the pilot phase it is expected to have early actions credits to be recognized and enter the market. This process is dependent on the readiness on the RENE mitigation platform and the publication of the offset rules.

**Challenges:** Please describe how such changes might affect the implementation of the Grant’s activities, either positively or negatively, and how possible technical design challenges may be addressed going forward. Please also refer back to any potential technical design challenges that may have been identified in the previous PMR Project Implementation Status Report and, if applicable, explain how such challenges are/have been handled.

Non risks are expected, all the activities committed under the grant are progressing according to the plan and are expected to close by the end of 2020 with few activities running on January 2021. Intense management and operational task force are deployed to ensure activities are developed and finished withing the tight deadlines.

**Lessons learned:** If applicable, please provide a brief description of the lessons learned regarding the technical design or approach related to the implementation of the Grant’s activities during the last Reporting Period.
Many of the technical guidelines and needs established in the regulation required a lot of processes for them to become operational. The PMR funding has been key on providing a better level of detail for every specification and determining the needs. For instance, allocation itself was a challenge, since SEMARNAT’s database was not completed. During 2020, an extensive effort on contacting every regulated entity and completing the database with verification reports was pursued, it was highly demanding and not considered in the initial plan. This effort was key on having now a consistent database to deliver the first allocation with reliable and complete information.

Following that example, many of the activities under the Grant’s plan could not be achieved without solving administrative impasses and information gaps.

### Key capacity issues (implementation, technical, financial management, procurement) related to the Grant’s activities:

#### Developments:

*Please describe key capacity issues (institutional, technical, financial management, procurement) related to the implementation of the Grant’s activities encountered during the Reporting Period or that are expected in the future.*

One of the biggest challenges is the change of government representatives, at the beginning of 2020, SEMARNAT lacked a team to administrate the ETS. Now there is a team but with a very reduced number of members to oversee every aspect of the ETS.

On top of that, the Ministry suffered from a budget cut and they have limited resources to allocate on this activity, making them reliable on international cooperation. Many of the timely progress would not have been possible without external funding.

#### Challenges:

*Please describe how such issues are affecting the implementation of the Grant’s activities, either positively or negatively, and how possible challenges may be addressed going forward. Please also refer back to any potential challenges that may have been identified in the previous PMR Project Implementation Status Report and, if applicable, explain how such challenges are/have been handled.*

SEMARNAT is open to receive the support, the current team although small is highly committed and has notably increased its technical capacity. The need of international assistance has positively impacted the PMR project implementation, since the internal and external consultants have been welcomed to provide guidance and the PMR team performs as an extension if the internal capabilities.

A challenge of the timely implementation is the different timing between the PMR program and Mexico’s regulation. The implementation of the ETS pilot was not aligned with the PMR process as they vary in their length and time coverage. The grant period will conclude before the pilot ends, there is uncertainty on the continuity of the actions.

#### Lessons learned:

*If applicable, please provide a brief description of the lessons learned regarding the key capacity issues related to the implementation the Grant’s activities during the last Reporting Period.*

Have an open channel and continuous communication with the decision-makers makes an effective implementation of the activities. None of the activities are unknown or undesired by the country. At
every stage, technical discussions are held, and different stakeholders are invited. This strong relationship and mutual trust foster a smooth implementation.

### Coordination with other carbon pricing initiatives, including those funded by other donors:

**Developments:** Please describe any developments related to other carbon pricing initiatives, including those funded by other donors, that have occurred during the Reporting Period or that are expected in the future.

#### a. Coordination with other carbon pricing initiatives:

There is an ongoing study on potential interrelations among different carbon pricing policies currently running in the country: carbon tax, state-level taxes, energy subsidies and the ETS. This analysis will provide insights about the complementarity and potential opportunities to increase efficiency.

Mexico launched a Carbon Tax in 2014. The carbon tax regulation indicates that certified emission reductions from the Clean Development Mechanism may be used to compensate the carbon tax. In the future, once the ETS is fully operational, the offsets that are originated under the ETS could be used to compensate the carbon tax.

There is a strong relation between RENE (National Emissions Register) and the ETS. All participants in the ETS will be required to estimate, verify and report their annual emissions to the RENE. This register provides the backbone on MRV matters.

SEMARNAT is preparing a second branch of RENE, meant to register mitigation outcomes from voluntary and regulated mechanisms in Mexico. This centralized system, administered by SEMARNAT will allow to transparently record and track national and international transactions with other mechanisms, such as the potential ones related to the Article 6 of the Paris Agreement.

#### b. Coordination with other donors:

The policy and regulatory developments had a positive impact in the grant’s objectives, by giving a strong legal framework for carbon pricing in Mexico. The legal mandate for an ETS had a positive impact in terms of engaging international agencies in supporting the process for the ETS, including GIZ from Germany, ICAP, and WCI. Their support focuses on data reporting and verification, data analysis, legal advice, cap setting, competitiveness studies, among others.

SEMARNAT oversees the general coordination with other donors, safeguarding the most cost-effective use of resources and the compliance with all the requirements of the regulation, while avoiding duplication of activities. One of the principles SEMARNAT is following is that the government of Mexico keeps all the capacities that come through the activities from different donors and technical cooperants.

**Challenges:** Please describe how such developments might affect the implementation of the Grant’s activities, either positively or negatively, and how any coordination challenges may be addressed going forward. Please also refer back to any potential coordination challenges that may have been
identified in the previous PMR Project Implementation Status Report and, if applicable, explain how such challenges are/have been handled.

The policy mix analysis and the design of the RENE in its mitigation component are activities funded and guided by the PMR. The main challenge is the coordination with an extensive group of stakeholders, the scarcity of written and public information (especially in the case of the subnational initiatives) and the lack of time to design and test all the desirable components. Aside of that, all the activities are running, and their results are expected by January 2021.

Lessons learned: If applicable, please provide a brief description of the lessons learned regarding coordination with other carbon pricing initiatives during the last Reporting Period.

Ensuring the right coordination among carbon pricing initiatives results key for the achievement of the ETS goals, some participants are aware of this need and are asking questions about possible double regulation.

### Stakeholder engagement related to the Grant’s activities:

**Developments:** Please describe any developments related to stakeholder engagement (consultation, participation and disclosure), that have occurred during the Reporting Period or that are expected in the future.

Stakeholders are fundamental for the overall ETS process. SEMARNAT coordinates the engagement with regulated entities. In January 2018, SEMARNAT established a Working Group with different chambers and associations. The Group met every two weeks, in average, to discuss various aspects and elements of the ETS; the group participates in the drafting of the ETS regulation by providing and feedback to the content of the draft.

With the support of the PMR, SEMARNAT installed a Consultative Committee as established by the ETS regulation. This advisory body composed by members of the regulated sectors, civil society and the academia, will serve as a common ground for regulated entities and authorities to meet and discuss the effectiveness of the system and will allow them to propose changes and improvements, subject to authorities’ approval.

The Consultative Committee is an innovative institutional arrangement for environmental issues; similar frameworks are in place in Mexico for economic or competitiveness matters, but not for dealing with climate challenges. It opens the opportunity for the Government and stakeholders to improve communication and commitment with the national climate goals.

As previously mentioned, there is a component in Mexico’s MRP to develop communication and capacity building activities. Its implementation includes the simulation exercise in 2018, two ETS Academies in 2019 and 2020, and a business-oriented training for around 300 people from the regulated entities in the country. On the communication side, the development of a communication strategy and an ETS handbook complete the stakeholder engagement work.
Under the development of the communication strategy, different exercises took place: interviews, round tables, phone and online surveys, among others, that served to inform the views and needs of a variety of stakeholders. With that information on hand, the strategy aims to cover specific needs for targeted audiences and achieve greater engagement.

Challenges: Please describe how such developments might affect the implementation of the Grant’s activities, either positively or negatively, and how any stakeholder engagement challenges may be addressed going forward. Please also refer back to any potential stakeholder engagement challenges that may have been identified in the previous PMR Project Implementation Status Report and, if applicable, explain how such challenges are/have been handled.

A pending exercise that is currently being addressed is the appropriation of this carbon pricing policy by stakeholders beyond those directly impacted by the ETS. For instance, after the issuance of the amendment to the Climate Change Law that made the SCE mandatory, the continuous dialogue with the legislative branch has been intermittent; at the same time, general society has not been informed of the benefits of the SCE and how it will contribute in achieving the goals of the country's NDC. These processes require an increase in engaging efforts.

Lessons learned: If applicable, please provide a brief description of the lessons learned regarding stakeholder engagement during the last Reporting Period.

The main achievement of the public consultation process when designing the ETS regulation was to find common ground between stakeholders and the authority, which in the end helped to create the Consultative Committee. A lesson learned for future processes is to continue with the dialogue which has proven to be the most effective way to communicate and provide answers to questions from the future regulated entities.

Aligned with that, is key to involve key stakeholders early in the definition process for them to be engaged and act as owners of the mechanism. Having an informed regulated sector facilitates interactions with the government, since a sufficient level of knowledge and strengthened capacities foster interactions and encourages the development of more complex and refined solutions and, reaching a common ground-level for policy discussions. After all these efforts, stakeholders are fully aware of the challenges and the way to overcome them. There are also agreements on next steps to continue improving the reliability of the system.

Specific lessons may include:

- Start with a basic structure, simplified and accessible to participants and build the complexity of the system along with capacities of the participants.
- Continue capacity building efforts with specialized content as the needs of interested stakeholders evolve.
- Establish close, transparent, and sufficiently informed communication with stakeholders, this will help the policy to be appropriate by different actors.

Other issues related to the Grant’s activities
Please describe any developments, challenges and lessons learned regarding any other issue related to the achievement of the Grant’s objectives and the implementation of the Grant’s activities.

5. ADDITIONAL INFORMATION

In this Section, please provide any additional information that may be relevant for the achievement of the Grant’s objectives and/or the implementation of the Grant’s activities. Please also provide any relevant information related to carbon pricing and the use of market-based instruments for climate change mitigation.

Mexico ETS Design & Piloting Roadmap prepared by SEMARNAT to guide the ETS development process

The next roadmap was prepared by SEMARNAT and adjusted according to the current progress of the ETS.

2017
- Preparation for ETS Simulation: Development of TORs, Planning, and Procurement Process
- ETS Design: Contracting, development and/or conclusion of projects regarding: Legal analysis, competitiveness, carbon pricing policy mix, cap setting, among others. Stakeholder engagement.
- ETS Simulation started on December 2017.
- Climate Change Law Amendments Proposal and approval by Cámara de Diputados

2018
- ETS Design: ETS Working group meetings (stakeholders and government). Conclusion of projects: cap setting, competitiveness.
- ETS Simulation ended on June 2018.
- Regulation: Drafting of regulation for pilot program and standard for verification.
- On December 1st, President Andrés Manuel López Obrador took office.

2019
- ETS working group meetings (stakeholders and government). A new series of consultations and workshops were carried out
- Regulation: Drafting of regulation for pilot phase is finalized (May 2019)
- Public consultation (May-July 2019)
• ETS Academy, July 2019
• ETS regulation published on October 1, 2019.
• Publication of the cap and allocation plan to be published no later than December 2

2020

• ETS Pilot Program: Starting on January 1, 2020
  o Design of rules & criteria for allocation
  o Development of a National Allocation Plan
  o First Free Allocation: October 2020
• Design of a national ETS Registry
• Capacity building exercises: ETS Academy and business-oriented training
• Development of a medium- and long-term communication strategy
• Design of an Offset program: Early action, development of demonstrative offset protocols
• Other technical studies: policy mix, market monitoring, ETS evaluation
• Analysis of Article 6 readiness
• Design and publication of handbooks

2021

• ETS Pilot Program:
  o Second free allocation: October 2021
  o First Compliance: November 2021
  o Pilot evaluation
  o Drafting of regulation for future phases

2022

• ETS Pilot Program:
  o Transition year: Second and last compliance for the pilot phase
• ETS Operational Phase:
  o Emissions from 2022 will be subject for regulation for the operational phase.
APPENDIX 1 ETS TIMELINE

1st RENE period
- 2016
- 2017
- 2018

2nd RENE period
- 2019
- 2020

Pilot Phase
- 2021

Transition phase
- 2022

Operational Phase

RENE Verification
- > 1,000,000 tCO₂e
- 100,000.1 a
- 999,999.99 tCO₂e
- 25,000 a
- 100,000.09 tCO₂e
- > 1,000,000 tCO₂e

Annual Verification

Last year

Template (v.3.0 – March 2016)
APPENDIX 2 ETS ACADEMY

ETS Academy México
18/08/2020-10/09/2020

Edo. peruano: S delivers compliance (Public sector only)

Week 1
Module | Date | Duration | Session |
--- | --- | --- | --- |
Welcome and introduction | 18/08/2020 | 9:00-10:00 | L1 |
Mexican Risk | 19/08/2020 | 9:00-10:00 | L1 |
Carbon pricing | 20/08/2020 | 9:00-10:00 | L1 |
Emissions and learning from the first phase of ETS around the world | 21/08/2020 | 9:00-10:00 | L1 |
Global carbon markets | 24/08/2020 | 9:00-10:00 | L1 |
Introduction to ETS | 25/08/2020 | 9:00-10:00 | L1 |
Practice session | 26/08/2020 | 9:00-10:00 | L1 |
ETS in the private sector | 27/08/2020 | 9:00-10:00 | L1 |
ETS in the public sector (Public sector only) | 28/08/2020 | 9:00-10:00 | L1 |
ETS in the public sector (Private sector only) | 29/08/2020 | 9:00-10:00 | L1 |
ETS Risk Governance | 31/08/2020 | 9:00-10:00 | L1 |
Stakeholder Outreach, Involvement and Communication | 02/09/2020 | 9:00-10:00 | L1 |
Early actions in the offset scheme | 03/09/2020 | 9:00-10:00 | L1 |
Designing the Compensation Scheme in Mexico | 04/09/2020 | 9:00-10:00 | L1 |
Strengthening national cooperation around market instruments | 05/09/2020 | 9:00-10:00 | L1 |
Prospects for participation in Article 6 of the Paris Agreement | 06/09/2020 | 9:00-10:00 | L1 |
Closing remarks and next steps | 07/09/2020 | 9:00-10:00 | L1 |

James Grabert
Director de la División de Mitigación
Convención Marco de las Naciones Unidas sobre el Cambio Climático (CMNUCC)

Conferencia Magistral
En la Academia del Sistema de Comercio de Emisiones de México 2020

Sesión abierta al público
25 de agosto de 2020
9:00 am (hora de Ciudad de México)
Acceso libre en:
APPENDIX 3  ETS TRAINING FOR BUSINESS

- Active engagement from participants.
APPENDIX 4 COMMUNICATIONS STRATEGY AND HANDBOOK

¿Qué es el Sistema de Comercio de Emisiones?
El cambio climático es real y nos está afectando a todos.

El Sistema de Comercio de Emisiones (SCE) es un instrumento para ayudar a reducir la velocidad con la que crecen las emisiones de gases de efecto invernadero que causan el cambio climático.

Esta herramienta busca apoyar a las empresas para que cambien sus actividades productivas a modelos de desarrollo sostenibles que integren el bienestar social y el cuidado al medio ambiente.
10 gobiernos están evaluando implementar un SCE

México es el primer país en Latinoamérica en implementar un SCE a nivel nacional

¿Qué puede hacer la Planta SIMGEA para obtener derechos de emisión adicionales?

Opción 1. Comprar los derechos de emisión de participantes que tienen excedentes (Laboratorio Medimex)

Opción 2. Comprar de las subastas del gobierno

Opción 3. Créditos de compensación (aplica máximo al 10% de sus emisiones verificadas)

Opción 4. Acciones tempranas

Planta SIMGEA

3 derechos de emisión asignados
5 toneladas de CO₂ emitidas

Emisiones extra

Toneladas de CO₂ cubiertas por los derechos de emisión
APPENDIX 5 SCREENSHOT OF THE DEMONSTRATIVE ETS REGISTRY
### APPENDIX 6 POTENTIAL EMISSION REDUCTIONS FOR EARLY ACTION SCHEME

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<td>Climate Action Reserve</td>
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| Gold Standard | |}

1.1 M tCO₂e from 5 different carbon standards and programs identified that are potentially eligible for the early action scheme.
## APPENDIX 7 DESIGN OF OFFSETS PROTOCOLS

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**Transport**
- Government entities involved in the workshops and bi-weekly calls: CONAFOR, INECC, CONANP and SADER.
- +25 Stakeholders from forestry sector were reached by the forestry survey.
# APPENDIX 8 ARTICLE 6 COOPERATIVE APPROACHES

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