

POSITION PAPER OF AUTOMOTIVE WORKING GROUP

Prepared by
Automotive Working Group

I. ACKNOWLEDGEMENT

The Automotive Working Group acknowledges and expresses its gratitude to the government for listening to the feedback of the group and taking new initiatives to help the automotive industry. We remain hopeful for further support from the government to help grow the automotive industry in Vietnam to its true potential. In doing so we will serve the people, help the country and maintain the competitiveness of the industry.

II. BRIEF OVERVIEW OF THE VIETNAM'S AUTOMOTIVE INDUSTRY

Automotive industry in Vietnam

As in our earlier document, we again reiterate that the automotive industry is usually considered a symbol of the progress and development of a nation. In addition to providing and supporting the means of transportation for the citizens, the automotive sector plays a vital role in the enhancement of efficiencies of overall supply chain and growth in business and commerce. Some quick estimates:

- 1) Contribution to GDP of Vietnam : 3-5%
- 2) Industry size in 2013 ~
 - a. Two Wheelers : 3,000,000 units
 - b. Passenger & Commercial vehicles : 100,000 units
 - c. CKD & CBU ratio : CKD ~ 80%, CBU~ 20%
- 3) Direct and indirect employment/livelihood : 500,000

III. RELEVANT BACKGROUND (IN BRIEF)

Vietnam has a population of nearly 90 million that is expected to reach 100 million within a decade. The per capita GDP is US\$1,300, expected to rise to US\$4,000 by 2020. These two factors will impact on car spending habits, especially when the current car density per 1,000 Vietnamese citizens is less than two. Similar growth across other countries has resulted in an increase in consumption of automotive products leading to automotive industry growth.

Vietnam holds a strategic position within the Asean and Asian supply chain and manufacturing footprint plans. A number of automotive companies in Vietnam have underscored the nation's potential to become a major ASEAN production hub and export base. Furthermore, Vietnam's WTO and AFTA accession has laid the foundation for favorable legal conditions to entice investors. Besides, Vietnam is attractive with a dynamic and young population, which is a huge source of low labor cost and utilities.

The auto industry's growth has developed and promoted the skill sets of Vietnam's work force, while increased business opportunities with a higher volume and familiarization with international products will develop workers' skills. Meanwhile, the development of surface transportation infrastructure to link cities, ports, upcountry territories and industrial zones will further accelerate economic development.

Localization and attraction of investment in Vietnam's automotive sector should be seen from an ASEAN opportunity/exports-oriented manufacturing perspective. This is particularly important and relevant as the AFTA enters full implementation from 2018 onwards.

The two wheeler and four wheeler companies have continuously brought into Vietnam the latest technology in assembly and manufacturing processes. Investments have been made through the entire supply-chain and focus has been on training and skill set improvement of manpower.

IV. SUMMARY OF CURRENT SITUATION – HIGH LEVEL RISKS

- a) The four wheeler industry continues to operate at below true potential of Vietnam. It has yet to recover after the crash in 2012 when the four wheeler industry fell around 35-40%.
- b) The participants in the industry are facing a situation of excess idle capacity.
- c) Vietnam is amongst the high tax protected countries for automobiles within Asia.
- d) Limited supplier base of repute and quality make it difficult to expand local production.
- e) Logistic prices affect pricing of parts and finished goods. This further affects the competitiveness when compared to local sourcing in other Asean countries.
- f) Absence of an automotive industry growth plan deters increase in future investments.
- g) Different interpretations of certain proposals/ policies leading to confusion amongst participants.
- h) Poor and lack of transparency in enforcement of policies and controls – e.g. customs/ imports
- i) Absence of centralized data monitoring agency on registrations of vehicles and related records

V. OPPORTUNITIES FOR DEVELOPMENT OF THE AUTOMOTIVE SECTOR

The working group once again requests the Government take quick action to fully develop the industry to desired levels within the window of opportunity before 2018 and also sustain after 2018.

1. IMMEDIATE CONCERNS

The recovery in 2013 vs. 2012 has been far from encouraging so far when compared to the operations in 2011 and the true potential. The automotive working group has summarized the concerns of the industry and also requests the government to support the recovery of the industry at the earliest through a list of recommendations below.

1.1. Taxation and Licenses

The high level of taxation has already been described in earlier submissions. To help in making ownership of a car more accessible for the population and in growth of the industry, the group has the following recommendations:

- a) Reduce SCT on the vehicles through a road map. Suggestion:
 - i. For four wheelers -reduce 50% immediately and then progressively each year till a ceiling of SCT of 0-15% based on engine and vehicle type is achieved. This will help to increase ability to own vehicles for Vietnam consumers. Increased purchases imply increased volume and helps to drive increased investments in the automotive industry by both OEM and component suppliers.

- ii. For two wheelers -remove SCT over 170 cc in line with the driving license requirements.
- b) Simplify categorization/ tax classification of definition for origin of vehicles and related bilateral treaties for taxes (example: tax for hybrid, tax for origin, trade treaty- JVEPA with Japan, ATIGA, AFTA, etc.)
- c) Road Map of Taxes and Duties
 - i. **Asean Alignment. CKD IMPACT** - Following agreement on tariff reduction commitments under AFTA, from 2018 Vietnam is expected to reduce import duties to zero for all vehicles manufactured within ASEAN and to adhere to the minimum level of AFTA's commitments. This is further extended based on ASEAN +2/3 Agreements. There is a concern about the unknown" about Government's plans to leverage and support current CKD operations in Vietnam after 2018. This has led to a "wait and watch approach" by global investors.
 - ii. **Asean Alignment. CBU IMPACT-** There has been raising concern on the impact to Import business based on the proposed Asean alignment of Vietnam's automotive business. The industry is seeking clarity on possible duty structures, quotas, additional tariffs if any etc.

A clear road map of different automotive sector taxes (SCT/ Import Duties -Asean integration, MFN etc.) and policies till 2018 and *beyond 2018* will benefit the industry. Further tax and policy stability will fortify investor confidence and growth in the industry. All of this will lead to increased customer choice and development of the country.

Consultation with automotive working group and other industry associations will be helpful to work together with the government.

- d) Uniform Taxes - The group thanks the direction on the attempt to have uniform "ownership tax" in the industry across all the provinces. While there exists some flexibility (up to 50%) of the value between the provinces and there is a clash with regards to tax on used cars, the overall move is well received and is a step in the right direction. We hope that the government can take the next step of having a uniform tax policy on number plate and ownership tax soon.
- e) Import Duty imposed on royalties and other payments for use of intangible assets. Currently, guidelines on how royalty and other payments for intangible assets may be considered as "conditions" of imports are unclear. There are some cases where tax audit team concludes that a payment is dutiable where no other countries consider similar payments made under similar contracts as dutiable. In some cases, an audit team treats a contract stipulating a payment as indicating that the payment under such contract is a "condition" of import, where the contract never explicitly says that it is a condition. In such case, both the parties suffer unproductive and tiring arguments, and company and State budget are exposed to a potential huge loss. On the other hand, the intention to add domestic royalty into dutiable price is not reasonable because:

Royalty comprised of fees for transferred technology and royalty for IP (trademarks, design & invention patents), then:

- (i) The fees for technology add value to the localization in Vietnam only and thus, by nature, they cannot be included in the imports' value, as well as they are already subject to FCT tax; and*
- (ii) The royalty for trademarks, design & invention patents appears only in Vietnam and thus, by nature, it cannot be included in the imports' value, as well as it is already subject to FCT tax.*

It will help to abolish import duties on royalties and other payments related to the usage of intangible assets made under similar contracts and accepted as non-dutiable expenses in other WTO participating countries.

1.2. Strategic Car Policy for Vietnam

A strategic car approach for Vietnam has been a work in progress for many years. Individual organizations and the VAMA have provided inputs to various Government departments. However, as of now, no firm guidance on a strategic car is apparent. Clear direction would have a positive impact on the industry's growth potential. Strategic cars policy has helped other ASEAN countries' automotive industries rapidly grow, gain cost competitiveness and especially expand CKD operations. Clarity on a strategic car would allow OEMs to prepare and plan to support the Government's direction in a timely manner appropriately.

The consultation process on the strategic vehicle for Vietnam should be opened for discussion with interested parties such as automotive associations (e.g. VBF's automotive working group, VAMA), automakers, etc. We believe the inputs of private sector will help the Government to soon publish a clear direction on a potential strategic car. Besides, we think that compact eco-friendly models, people movers etc. could qualify as strategic cars for Vietnam.

1.3. Bonded warehouse, Duty Refund process, Export Processing Zone

Currently, more companies have chosen Vietnam to be their regional hub from which goods are imported and then re-exported and distributed regionally. However, the current import process does not allow for temporary transit. All import duties, SCT and VAT must be paid even though the goods are for re-export and the refund process is opaque and takes up to three months. This is too costly considering the current cost of finance.

We request for bonded warehouses for CKD assemblers and official importers (both Vietnamese and foreign-owned parties). It is also recommended that automotive goods such as cars, parts, tools imported into Vietnam purely for re-export are exempt from taxes. This would, however, generate revenue and foreign currencies for the Government.

To increase local content, Vietnam should allow quality automotive parts producers to work from export processing zones and allow them to sell a sizeable percentage of local production in Vietnam. Granting the same export rights to already existing world-class automotive OEMs in Vietnam would also benefit the local industry.

1.4. Clarity on government decrees/ circulars.

It has been observed that certain government decrees/ decision notices need additional clarification. Misinterpretation of these documents leads to severe consequences and affects the business sentiment. For example:

Prime Minister Decision 356 (356/QD/TTg)

Under this decision the government is aiming to limit the number of two wheelers to 36 million units. This information of imposed limit has impacted the confidence of investors and current players in the industry and they are reluctant to expand and invest in Vietnam.

1.5. Policy on maintaining and disclosing the registration data

Since registration data is handled by municipal governments, it is hard for manufacturing companies to obtain timely, updated and complete nationwide registration data. Furthermore, since the system may not have incentives on renewing nor penalizing for not renewing registration data, accuracy on the actual number of motorcycles being used may be questionable. Timely useful data is very helpful to all – government, industry and investors.

We recommend that the country would prepare a policy applicable throughout the country, and a body that oversees and collect all the registration data. Secondly, we recommend that a system to refine registration data at the time of renewing insurance policies obligated by law to be introduced, or to firmly operate the newly introduced road usage fee, and refine the possession data based on the payment of this tax. With this tax posed effectively and correctly, we may also give incentives for people to dispose old motorcycles/cars with low fuel efficiency, and also give more correct data on the number of motorcycles that are actually being used. We request being able to discuss in details of addressing the situation to help all impacted bodies.

1.6. Classification investments - in particular Engine/Power train investments as “Hi-Tech”

The Government seems to under-estimate or overlooks the contribution automotive industry is making towards tax revenue and employment. Furthermore, the automotive industry is not subject to any particular investment incentives, such as those enjoyed by “high tech” industries. The Automotive Working Group is of the opinion that the automotive industry should be defined as “high tech” and should be subject to the same incentive system. Strong evidence and international studies show that the automotive industry is a key player in technological development within numerous countries. Moreover, the industry’s development is strongly correlated with the development of skills, country know-how and ultimately its educational system. The numbers of engineers in a country is a key metric of innovation capability and competitiveness.

Particular supporting industry investments in certain high value added components such as engines, engine parts and electrical systems is of paramount importance to transition the country from a pure cost base advantage to a more sustainable technological advantage. Metallurgy, machining and high precision assembly are key automotive manufacturing processes that currently are slow to grow in Vietnam due to its lack of available know-how. A strong incentive system will lower the risk for new entrants and could over time help Vietnam develop a cluster advantage recognized regionally.

We request the Government consider special incentive support for the automotive sector as a “high tech” business sector.

2. MEDIUM TERM CONCERNS

2.1. Facilities to support vehicles on roads & overall economy

It has been observed that lack of parking affects the industry. A reasonable percentage within new real estate developments should be dedicated as underground multi-storey car

parks. Such operators should be able to sub-rent access to such car parks to outsiders to alleviate inner city car parking shortages. The development of such facilities will support vehicle users and stimulate the automotive industry and overall economy.

2.2. Direction and special support to Hybrid/Alt Fuel/Electric vehicles and low CO2 emission vehicles

Thailand enjoys local production of the Toyota Prius, Camry Hybrid and Honda Jazz Hybrid and has recently created environmentally-friendly concept cars. Meanwhile, Malaysia is pushing green technologies. In some countries in Europe, Governments have set-up taxes based on vehicle emission levels, whilst in other countries Government incentives support alternative power trains such as hybrids or electrical.

It will be in the interest of the government of Vietnam to have more aggressive support for the above vehicles.

- More supportive tax criteria for hybrid vehicles, for CKDs and CBUs
- Different government bodies to build a co-owned and co-developed plan towards environmental protection across areas such as emissions, fuel consumption, component recycling and end-of-life vehicles
- Start engaging OEM/Associations/Technical centers and develop a road map with several steps as follows:
 - (i) Establish a reliable basis and set of criteria to measure a vehicle's fuel consumption or adopt and promote higher standards in fuel consumption, fuel quality, emissions and environmental awareness. This goal will only be reached by focusing on high-technology vehicles
 - (ii) Work out a plan which is in consistent with ASEAN neighbors and Europe, if Vietnam is to follow the Euro emission pattern
 - (iii) Define a fuel efficiency improvement plan based on country achievements
 - (iv) Define emission levels to comply with international low-carbon emission standards. Particularly with regard to new CBU cars' homologation, the Vietnam Register should simplify the homologating procedure without the need for any additional local emission test cars with EU4 and EU5 emission standards, which are more stringent than EU2.

2.3. Vision 2020+ & Stability of policies

Currently the vision 2010+ to 2030 has still not been finalized. The government should share ideas and a clear industry policy roadmap to 2025 with OEMs and industry associations to offer investors a long-term horizon and better predictability for future growth.

VI. CONCLUSION

To sustain the industry's development, we would like to re-iterate that the Government should:

- Consult automobile manufacturers' associations such as the VBF Automotive Working Group and VAMA for inputs into key proposals and policies affecting the automotive industry. Through prior consultation and discussion with the private sector, Government policies will be more practical, better understood and implemented.
- Maintain control on leakage of draft proposals in the media as they lead to inefficient reactions
- Take the method of pre-testing and piloting new proposals/policies into consideration since this is the most effective and less disruptive method.
- It is worth emphasizing that a clear road map for different automotive sector taxes and policies to 2025 will benefit the industry, customers and Vietnam. Taxation scheme and

policy stability drives investors' confidence to grow the industry and leverage Vietnam's development.

Industry players are still wary after the crash of industry in 2012. Coupled with the cost of rising inventory for both assemblers and dealers, business operations have become unviable and unsustainable in the short to medium term. Medium term stability remains a challenge to long term growth. We have seen in other countries that Governments have come to the rescue of automotive industries to help them recover and continue to provide employment. The industry, in return, will make good contribution to the State exchequer.

We plead with the Government to introduce **some quick measures to accelerate the revival of the industry** as soon as possible. **We sincerely request the Government quickly act to support the industry and help it recover during 2013.**