Recommendations for Union Budget: 2022-23

Presentation to
Department of Revenue, Ministry of Finance
Government of India

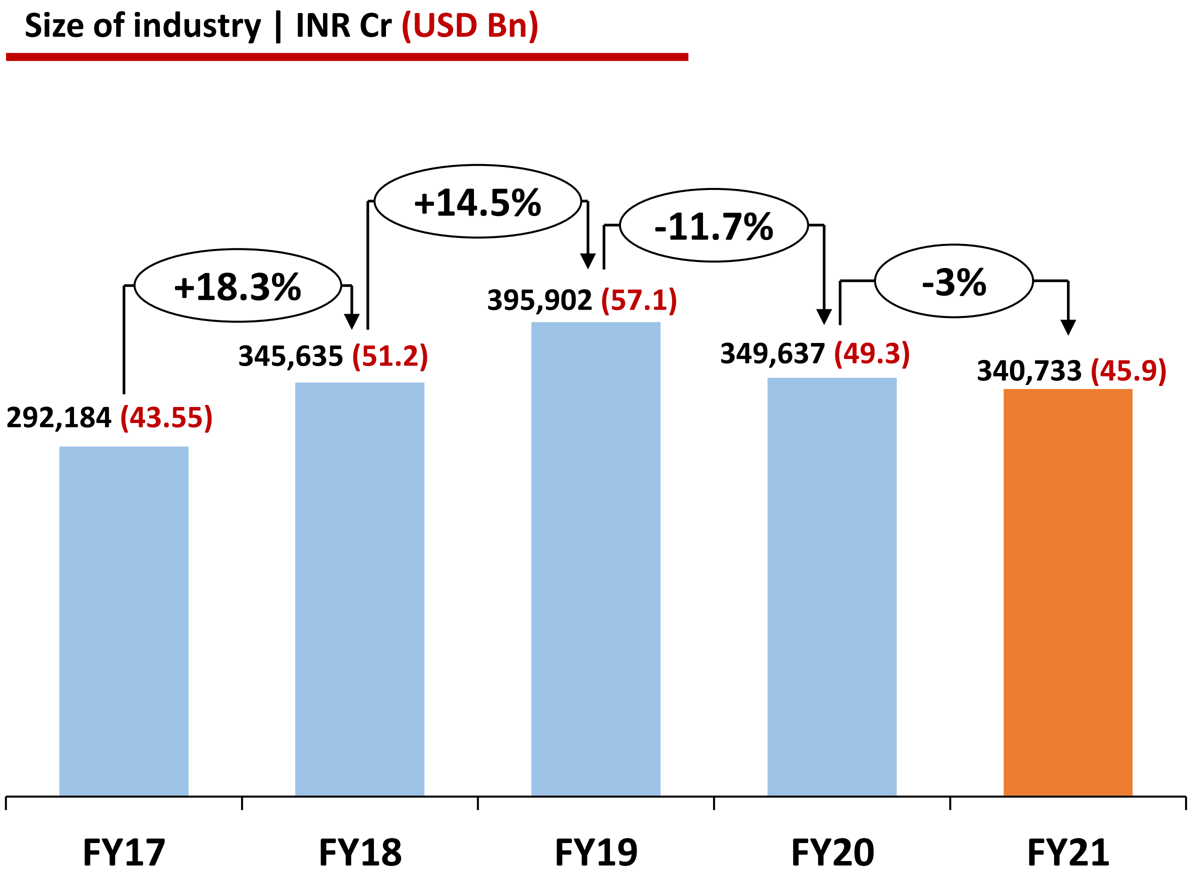
30th November 2021; New Delhi

Automotive Component Manufacturers Association of India

Auto Components Industry Update: FY 2021/ FY 2020

FY 2021: Auto Components Industry Performance

Sales to OEMs + Aftermarket + Balance of Trade



FY21 – Auto components industry performance

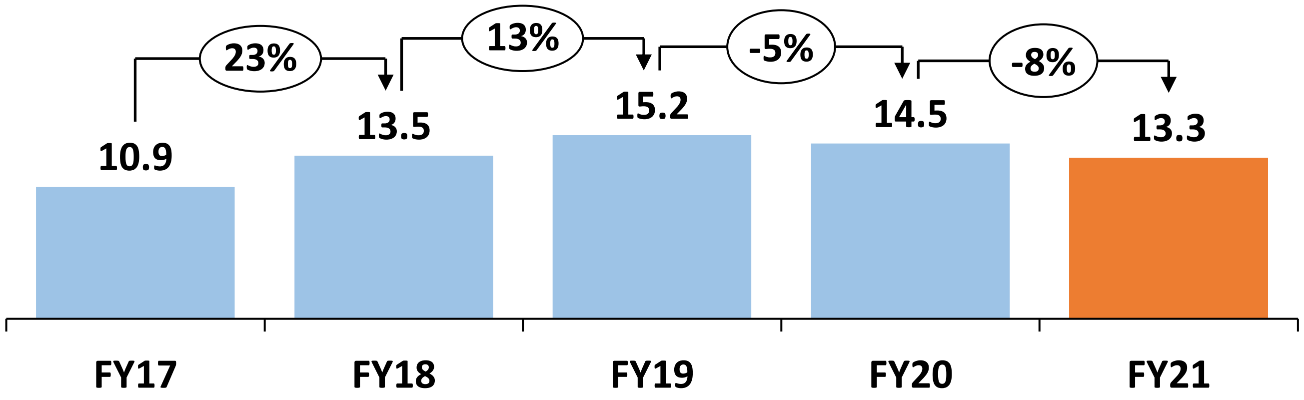
- Vehicle production recovery in H2 FY21 - **~1.7x** of H1 FY21
- Raw material cost per unit vehicle up by **~13%** (vs. FY20)
- Key commodities: Steel (▲22%) & Aluminum (▲31%) prices surged Y-o-Y
- Trade deficit narrowed down to **~$0.5B in FY21** from **~$1B** in FY20
- Rupee value ▼**5%** in FY21 Y-o-Y
- Aftermarket saw a **~7%** dip; e-commerce platforms are expected to witness a spike in demand.

In FY22 shortage of semiconductors, high raw material and logistics costs and high fuel prices continue to hamper recovery in the automotive industry

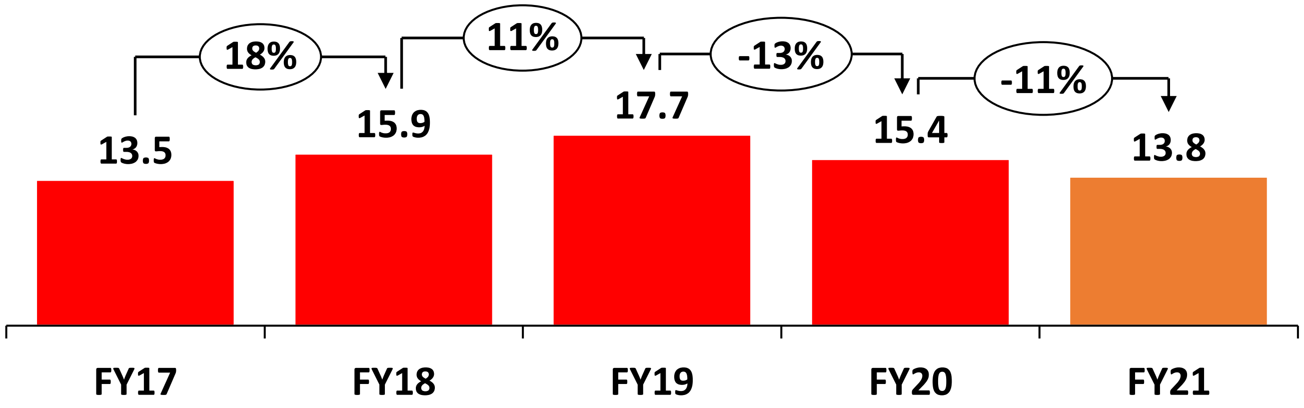
FY 2021: Exports & Imports - Balance of Trade

India's trade deficit for auto components reduced to ~ $0.5B in FY21

Total Exports | $ Bn.



Total Imports | $ Bn.



FY21 - EXIM performance

- Exports fell **~8%** on account of lockdowns in major global markets (United States, Germany, Mexico). Expected to grow ~10% CAGR from FY21-FY26 (CRISIL)
- **~11%** decline in imports Y-o-Y; reduced demand in the domestic market, supply chain deficiencies globally
- Government's PLI and other policies focused on export compositeness & increasing localization to further reduce trade gap
- In H1/FY22 exports grew by 78% to $9.25 bn; Imports grew by 73% to $ 8.69 bn resulting in modicum of trade surplus

Recommendations on Indirect Tax

1. Seeking Clarification on Classification of Automobile Components

- According to the recent ruling in Westinghouse Saxby Farmer Ltd. case, summons/notices are being issued by DRI/ Customs Department disputing the classification of parts of motor vehicles and demanding differential tax by proposing the classification under HSN 8708 wherein higher tax is applicable.

- Many vehicle parts such as engine & engine parts, rubber parts, auto electronics are classified under their respective chapters such as 84, 40, 85, etc.

- This will result in a.) mismatch of HSN in case of international trade, b.) claiming in FTA benefits, c.) collection of statistical data by department/s d.) Inability to control the supply chain, especially in case of B2C supplies, etc

Recommendations:

- Request that the department to file a review petition against the said Judgement for the benefit of Industry

- A Communication be issued to field formations/investigating authorities requesting them to wait for CBIC/MOF guidance before sending summons/ notices for physical presence, etc.

2. Enhance RoDTEP Rates and extend the benefit to EOUs, SEZ, etc

- RoDTEP Rates, including those with the weight cap (Rs/kg), announced in August 2021 are not as per the industry expectations
- Majority of auto components attract lower rate - less than 0.8 % / 1% while cost incurred on taxes that cannot be offset is 3-4%
- Diesel cost has risen by 44% in comparison to the diesel cost considered while fixing the rates;
- No benefits for auto components falling under chapter 72 and 73 and to exporters operating under Advance Authorization, EOU and SEZ

Recommendation:

- Enhance the rates of Duty remissions as per the data provided by the Industry
- Remove weight cap for auto components & Extend RoDTEP rates for chapter 72 and 73 auto components
- Extend the scheme to Exporters operating under Advance authorisation, EOU/SEZ

3. GST - 18% for Chapter 84, 85 and Chapter 87 auto components and 5% for xEVs auto components

- Auto Components attract two different rates- 18% and 28%, 2.5-3 X compared to other emerging & developed markets
- GST Council reduced rate to 18% on approx. 60% auto components tariff lines over a period of time, rest continue to attract higher GST rate of 28%
- 28% GST on aftermarket- encourages Grey market; Challenge of compliance
- Difference is leading to unnecessary litigation and harassment of assessee due to department interpretation
- Majority of critical and safety items falls under chapter 84, 85 and 87
- GST rate on Electric Vehicles are at 5% whereas xEV components for it are at 18% and 28%

Recommendations:

- Auto component industry is an intermediary - Uniform GST rate of 18% across all product categories
- 5% GST rate for xEV components to avoid unnecessary credit over-flow at the end of value chain

Recommendations on Direct Tax

1. Incentivize Auto Components Sector to incur capex expenditure

- It is an imperative for Auto components sector to invest in R&D and manufacturing of newer technologies viz. Electric Vehicles (EV), and Advanced technologies to stay relevant.
- Accordingly, it is strongly recommended that Government should incentivize the industry to strengthen the supply chain.

Recommendations:

- Re-introduce additional investment allowance provision (section 32AC) of 15% of capex expenditure on plant and machinery. Minimum amount of investment for such allowance should be INR 5 crore for MSMEs.
- Reinstate deduction of at least 200% of the expense incurred on R&D
- Increase depreciation rate on plant & machinery to 25% from 15%
- Above benefits should also be available to taxpayers opting for lower corporate tax rate of 15%/ 22% to ensure industry’s global competitiveness.

2. Rationalization of provisions related to Equalization Levy (EL) on non-resident e-commerce operator

- EL @2% to be paid for online supply of good & services under Finance Act 2020 w.e.f. 01.04.2020.
- Sale / purchase transaction of a MNC group covered under amended Finance Act 2021, where even small step in ordering good is undertaken via any ERP / other digital system seems also to be covered in its ambit.
- Additional tax cost & compliance with such provisions is causing hardships to the taxpayers.

Recommendation:

- EL should be restricted only to those cases wherein all or substantially all activities take place online and carve out exception for typical manufacturing/ trading companies who have nil/ limited digital footprint
- Some activities should be exempted, e.g:

  -Order received by non-resident via email or common portal using internet

  - Intra group transaction / activities using online system like ERP etc.

  - For offline transaction in which payment takes place online
- Terms like "owns", "operates", "manages", "Digital or electronic facility or platform" used in the definition of e-commerce operator should be appropriately defined by CBDT.
- Further, it should be clarified that EL should be levied on 'net sales/ consideration' i.e. after adjustment of sales return & credit notes

Proposal for preventing GST leakage & incorrect Input Credit

Proposal for preventing GST leakage & incorrect Input Credit (1/3)

Proposal Statement:

- Some GST Assessees claim Input Credit for purchases made by them but the supplier may not deposit the GST with the authorities promptly

- Exchequer faces revenue shortage due to the mismatch between the input tax credit claimed and the actual GST received into the treasury

- Cases have come to light wherein assesses have fraudulently taken refunds for export turnover using GST Input that was never deposited in connivance with the supplier itself

- Creating more checks and barriers with additional regulations in the system will only lead to further formalities for scrupulous businesses leading to operational problems and more red tape

Proposal for preventing GST leakage & incorrect Input Credit (2/3)

Proposal of Split Payment System:

- The Government may mandate all banks to open GST accounts in parallel with current accounts of all GST assessees.
- Therefore, an assessee “ABC Co.” having a current account will have two accounts : “ABC Co. Current Account” and “ABC Co. GST Account”
- When a customer makes a payment to a supplier, the amount in split between the “Value of goods” and the “Amount of GST”
- The Value of Goods goes to the current account and the amount of GST goes to the GST Account of the supplier.
- The amount lying to the credit of the assessee in the GST account can only be used to pay GST into the GST account of another assessee or to deposit GST with the authorities.

Proposal for preventing GST leakage & incorrect Input Credit (3/3)

Risk Mitigation:

- The split payment system is running well for VAT in Poland successfully, and perhaps also in other countries where tax compliance needs to be approved.

- The system can be implemented in stages so that the existing system does not go into a “shock”. Poland implemented it chapter wise based on HS codes starting with sectors where the compliance challenges where the highest

- The transition to the split system can be incentivized for each industry by offering exemption from TCS, lower GST rates and other procedural measures that lead to operational issues

- Auto Component Industry would be pleased to be included in the first phase of implementation if this system is adopted

Thank you!