

SIAM Response on Feebates

Background

Automotive industry in India has come a long way and is fairly matured today. The industry contributes almost 50% of manufacturing GDP and employs around 32 million people directly and indirectly. It is one of the sunrise sectors contributing immensely to the economy in excess of 7% of overall GDP of the country.

This industry sector is perhaps the only large sector wherein a very high degree of local value addition has been achieved and where India is globally competitive. The growth of automotive industry will be critical in realising the Government objective of increasing the contribution of manufacturing to the national GDP from current level of 16% to 25%.

Sharp Focus on Sustainable Development

With fairly advanced eco-system of design, development and manufacturing, automobile industry is continually working towards environmental sustainability. Automobile industry would be moving to BS-VI emission norms jumping straight from BS-IV emission norms within a period of 3 years from 2017 to 2020. Similarly, oil industry would be gearing up to provide BS-VI compatible fuel across the nation from 2020. Both the industries have put in huge investments for this transformation to the tune of [Rs 100,000] Crore put together. The shift to higher emission norms has led to significant lowering of pollution from new vehicles. As per MoRTH regulations, the BS IV diesel cars and commercial vehicles have 50% and 80% lower PM 2.5 emissions as compared to BS III regulations. With introduction of BS VI norm, the reduction in PM 2.5 will be 90% as compared to BS III vehicles for both diesel cars and commercial vehicles. Further, fuel efficiency norms are challenging industry to develop and manufacture more efficient vehicles. As such, it may be noted that efficiency norms and emission norms double up the challenge as meeting higher emission norms often put a penalty on fuel efficiency of a vehicle due the impact of having additional aftertreatment devices.

Heavily Taxed Industry

Automobiles in India are taxed at an extremely high level as compared to most countries across the world. The basic GST rate on automobiles is pegged at the highest rate of 28% with an additional compensation cess levied to the tune of 22% for large cars and utility vehicles. Additionally, road tax on vehicles add to the purchase cost quite considerably. The State taxes are also based on either a) Size of the vehicle b) Price of the vehicle c) fuel type (different tax based on diesel, petrol and CNG). With all these Central and State taxes, the total burden of taxation on passenger cars can be as high as 70%. Further, fuel cost in India is also comparatively higher than other countries despite that these countries also depend on imported crude oil. Over and above these high tax burden, some segments of cars e.g. diesel cars are subjected to additional taxation. For example, even small diesel cars attract

3% cess, going upto 22% in big cars and all diesel cars having engine capacity of 2000 cc and above have to pay an additional 1% ECC to the Central Pollution Control Board. Furthermore, the States road taxes on diesel cars is usually higher as compared to petrol cars. In Delhi itself, the road tax on diesel cars is higher by 25% as compared to petrol cars. In addition, in NCT the registration period for new diesel cars has been reduced from 15 to 10 years, thereby in effect imposing a significant indirect tax on these vehicles. All these additional Cesses, Charges and Taxes being collected, and the revenues earned through these measures, can be used for pollution mitigation efforts.

Promoting EV Technologies

In 2011, Government together with the auto industry embarked on the initiative of drawing up a National Mission Plan to promote Electric and Hybrid Mobility in the country. This led to the formulation of the National Mission on Electric Mobility under which Government has been encouraging adoption of zero emission vehicles including electric vehicles through various measures.

Promoting EVs broadly involve the following three actions:-

- a) Creating an attractive and viable ecosystem that supports EVs. Industry to invest in EV technologies and produce vehicles that could be acceptable to the consumers.
- b) Establishment of the necessary infrastructure to support EVs e.g. charging stations, manufacture of Li Ion cells at a Giga Scale etc.
- c) Fiscal and non-fiscal incentives to make EVs affordable to the consumers.

Over the last 2-3 years, some specific actions have been taken to address some of the above issues, e.g. setting up charging stations, availability of preferential power for charging, amendment in building by-laws to mandate charging infrastructure.

Today, Battery electric vehicles and fuel cell electric vehicles attract preferential GST Rate of 12% without any additional Cess. Critical components of electric vehicles can be imported at nil basic customs duty. Government is also providing purchase incentives through its flagship scheme namely FAME India to different categories of EVs.

Indian EV Movement - at a Nascent Stage

However, it is to be appreciated that all these measures have been taken only very recently and we as a Nation are in the very nascent stages in our long journey towards EVs. As contrasted, most other countries of Europe, USA, Japan and even China have had decades of head start in the Electric/Hybrid vehicles space and through sustained long-term policies these countries have reached a certain level of maturity in EV technologies and their affordability and acceptability by the consumers. Moreover, many of the western countries are high per-capita income countries and the purchasing power of the consumers is considerably higher than an average Indian consumer. China has been a command economy and Government has put in Billions of dollars to promote EVs as well as to encourage a few Champion Chinese companies to take leadership in EV technologies that include Cell and Battery technologies, Motors and Motor Controllers, Charging Stations and to manufacture them at cheap prices. All these efforts made it easier for high cost EVs to become affordable

to the customer in these countries. Even after that, the low share of EVs even in these markets reflect the long gestation time needed to achieve desired levels of penetration, especially for a new technology such as EVs. This is necessary to allow technology maturation and development of key enablers such as charging infrastructure and manufacturing ecosystem.

Feebates

In order to tip the scales in favour of EVs, many of these countries have in the past resorted to the system of Feebates as has been highlighted in the NITI Aayog Report. While incentives given for EVs represent the “carrot” approach, Feebates can be termed as the “stick”. Put together, any holistic system or Policy to promote EVs would have to be a judicious mix of carrot and stick, with the carrot coming first for a sustained period of time. If the necessary transformation expected does not take place, there could be a need for a “stick”.

Also, as per the Report on Feebates, the following are the pre-requisites to implement any form of Feebate structure:-

- a) It has to be based on fuel efficiency of the vehicle.
- b) It has to be “revenue neutral”
- c) It has to be “market based”
- d) It needs to be vehicle “size” neutral
- e) It has to be “technology agnostic”

Let us look at each of the above imperatives from the Indian perspective.

a) Fuel Efficiency of Vehicles

The Feebates system is effectively based on higher taxation on higher CO₂ emitting vehicles and less tax on lower CO₂ emitting vehicles. There needs to be a rationale and implementable mechanism within the Government system to be able to implement and monitor such a tax system on a dynamic basis because FE of vehicle models would be continuously improving. As a country we do not have a history of a taxation structure based on such dynamic factors. An ill managed system can result in a huge disruption in the smooth operations of the industry, which as mentioned earlier is one of the biggest contributors to the nation’s growth and economy.

b) Revenue Neutrality

Most of the countries whose examples and case studies are given in the NITI Aayog Report are either EU countries or Ontario (Canada). A scrutiny of the taxation rates in these countries reveal that automobiles attract the normal rate of taxation or the GST rates as applied to all other manufactured goods. Therefore, a marginally differential rate of taxation on vehicles based on CO₂ is a fair policy as well as acceptable to the auto industry. Moreover, the per-capita income of consumers and the maturity of the EV eco-system i.e. charging infrastructure, manufacturing base etc are also very different in these markets.

In India the rates of taxation on vehicles is extremely high. The basic rate of GST is highest in the GST schedule. Moreover, there is a Cess of upto 22% applied which makes the total taxation to a level of 70% in some cases (including State taxes). As explained above, over and above this, diesel cars face additional penalties of 1% ECC for more than 2000 cc cars and an additional road tax of upto 25% on all diesel cars in NCT on grounds of environment and pollution.

These taxes are already similar to Feebates and are serving the same purpose as the proposed Feebates. Therefore, industry feels that as long as the overall taxation on vehicles is so high and graded, there is no justification or rationale for imposing any additional taxes in the form of Feebates. Any additional tax will hurt the auto industry by making the existing technologies more expensive.

For the present, Industry would like to see whatever additional revenue that is being collected by Central/State Governments in the name of environment protection/pollution to be earmarked exclusively and used for providing rebates to the New Energy Vehicles (NEVs).

It is important to note that at present the issue of revenue neutrality is viewed in a very narrow framework of incentives provided to EVs being offset by additional taxes on ICE. However, this approach is not correct as impact on overall growth of the industry, new investments and higher import of EV parts at zero duty etc are not being factored. The experience of the other countries clearly shows how difficult it is to bring in revenue neutrality in any such scheme.

c) Market Based and Technology Agnostic

Feebate mechanisms are most effective when they achieve social goals without restricting or limiting “consumer choice”. However, in India, we have followed a policy under which consumer choice has been limited by design. The various actions against diesel vehicles is a case in point, which has led to a severe limitation being imposed on the consumers as regards diesel cars. When different goals conflict with each other, it is necessary for Government to remain technology agnostic and to work on the principles of mandated emission norms and regulated limits. If a policy limits the choice of technologies, it gives out conflicting messages to the consumer and blunts the impact of such policies.

Thus, if improvement in fuel efficiency of vehicles is a primary objective, it is contra-intuitive that Government has discouraged technologies that can offer fuel savings which is not in line with the principles of a technology agnostic approach, which the NITI Aayog Report itself espouses.

d) Size Neutrality

This is perhaps the one area where the Feebate System will have to face the biggest disruptions in the Taxation System. The current taxation system for vehicles which has been followed for decades is based on the size of the vehicle and engine capacity. Any change in this basic system will have far reaching implications on our taxation structure.

Conclusion

Feebates may make sense when we have made advancements in setting up the ecosystem, infrastructure and technology, and reduced the applied rates of taxation on vehicles to the normal GST levels. Any Feebates system before we reach that stage would be putting the “cart before the horse”, which can potentially do immense damage to the automotive industry.

We first need to create a solid platform of a strong and clear long-term policy framework to promote EVs, then implement the policy in earnest till we reach a minimum level of EV infrastructure and ecosystem support. Then we need to reduce the overall taxation on vehicles to a reasonable and uniform level.

In fact, from a standpoint of addressing the challenge of pollution and energy security, it would be far more efficacious if a holistic long-term policy is laid down by Government to promote electric mobility in the country over the next 15 to 20 years period. SIAM has already submitted a White Paper on Electric Vehicles for a long-term roadmap with specific recommendations in this regard covering a set of comprehensive fiscal and non-fiscal measures.
