

SSMT – written evidence (AUT0029)

TOPICS: AUSTRALIA LUXURY CAR TAX AND CPTPP ORIGIN REQUIREMENTS

Thank you for the opportunity to give evidence to the International Agreements Committee on 16 June 2021, in its Inquiry into the Comprehensive and Progressive Agreement for Trans-Pacific Partnership (CPTPP). During the evidence session, we offered to update the committee members on the potential impacts of Australia's Luxury Car Tax (LCT) on UK exports of passenger cars and to provide further insights on CPTPP origin rules.

Australia Luxury Car Tax

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The SMMT only collects data on UK exports by volume. The lack of data by value for each UK-assembled model exported to Australia does not allow us to quantify the financial impact for each manufacturer facing the LCT.

However, taking into consideration the LCT value thresholds applicable over this period (see Annex B), all premium and luxury vehicles exported from the UK to Australia are at risk of facing the tax. If we exclude exports of some volume manufacturers – all likely to be valued less than the LCT thresholds (estimated at £43,000 for low emission car and £38,000 for others) – the tax could apply to all other UK cars shipped to Australia. Accordingly, SMMT estimates that more than 38% of units exported from the UK were at risk of paying the LCT in 2019.

After the Covid-19 outbreak in 2020, the total volume of car exports to Australia dropped by more than 20%, with premium vehicles particularly affected by the slowdown and volume manufacturers performing relatively better. With exports of high-value vehicles underperforming compared with 2019, the LCT incidence is significantly reduced, with an estimated 26% of all UK exported cars at risk.

The future impact of the tax will depend on several factors. In the short-term, exports of luxury and premium vehicles will continue to face the LCT. Longer-term, progressively higher thresholds could slightly reduce LCT exposure for premium vehicles, but with value threshold increases of 1%-2% per year the SMMT expects these types of vehicles to be subject to the LCT for the foreseeable future.

CPTPP ORIGIN REQUIREMENTS FOR PASSENGER CARS

Should the UK accede to CPTPP without negotiating specific origin requirements through side letters, passenger cars could qualify for preferential tariffs if:

- The UK-CPTPP combined value content is at least 45% of the net-cost of the cars; or

- The UK-CPTPP combined value content is at least 55% under the so-called “build-down method”.

The two alternative rules are based on knowing the value of non-originating materials used in the production of each model to determine the proportion of the regional value content (RVC). The difference between the two options is that the net-cost method determines the RVC as a proportion of total cost, while the build-down method determines the RVC as a proportion of the value of the good.

Through the net-cost method, sales promotion, marketing and after-sales service costs, royalties, shipping and packing costs, and non-allowable interest costs that are included in the total cost are deducted. On the other hand, the value of the good is calculated as the price actually paid or payable for the cars when sold for export excluding any costs incurred in the international shipment of the good.

A complete assessment would require access to highly confidential data, including the bill of materials for each model, manufacturing costs, the transaction value of exported units, shipping costs, a complete picture of originating and non-originating materials of production, value added through manufacturing operations in the UK and in CPTPP countries. The SMMT does not have access to commercially sensitive data that would allow us to provide such assessment.

The UK automotive sector comprises a large portfolio of manufacturers with different sourcing footprints and some commonalities. While UK content is likely to vary from manufacturer to manufacturer, all UK car makers source a large number of materials from the EU. Only few manufacturers have supply chains stretching to CPTPP countries and source a large number of materials from the CPTPP region.

Accordingly, the SMMT can only provide an illustrative example on the basis of several assumptions. For the purposes of this illustrative example, we are using the net-cost method, with UK cars qualifying for preferential treatment if a 45% RVC threshold is met. There are four key determinants to qualify for preferential treatment under CPTPP net-cost method: UK content, content from Japan, EU content and rest of the world content as a proportion of total costs of production. The value of content from the EU and the rest of the world should be deducted.

With all UK manufacturers sourcing a large number of components from the EU, it is likely that only car makers with a significant proportion of UK content can meet the 45% RVC threshold. UK-centric producers are likely to be exporting high-value luxury and premium vehicles to the CPTPP region under preference, although there might be some models and variants unable to qualify.

Manufacturers with higher levels of integration with our closest trading partner and a lower domestic UK content are likely to struggle to meet the CPTPP origin

requirement for passenger cars. EU-centric producers are also unlikely to source a significant proportion of materials from the CPTPP region, further reducing the chances for their exported cars to benefit for tariff preferences under CPTPP.

UK car makers with global supply chains are likely to incorporate a larger proportion of materials manufactured in the CPTPP region in UK-assembled vehicles. In particular, materials from Japan could represent a significant proportion of the value of the finished vehicle and the associated value can increase the RVC percentage thanks to CPTPP regional cumulation provisions. However, this third group of UK global manufacturers is also fully integrated into the EU and broader European regional supply chain. Their ability to meet CPTPP origin requirement will depend on the proportion of UK and EU content incorporated in their vehicles, given that CPTPP materials alone are largely insufficient to qualify. Accordingly, we cannot assume that all UK-based manufacturers sourcing materials from the CPTPP region will meet the CPTPP origin criteria for passenger cars.

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Even on the basis of this illustrative example, it is not possible to quantify the number of UK cars that might fail to qualify for preferential treatment under CPTPP. We can assume that, in volume terms, it is likely that the majority of UK-assembled cars would be at risk of not meeting CPTPP origin criteria, with all EU-centric manufacturers and some major global manufacturers potentially struggling to qualify.

The illustrative example does not take into account different types of vehicles and future trends. Given the current dependence on batteries and related parts manufactured in Asia, CPTPP materials might represent a higher proportion of the net-cost of electric vehicles, plug-in hybrids and other electrified vehicles. However, it is unclear whether such proportion will increase in the future. With the UK-EU Trade and Cooperation Agreement (TCA) setting very ambitious origin requirements for battery packs from 2024 onwards, UK manufacturers might reduce sourcing from CPTPP countries to increase the combined value of UK-EU content incorporated into finished batteries. UK manufacturers that will not source batteries originating in the UK or in the EU are likely to face tariffs on electrified vehicles exported to our closest trading partner in the next future. It is too early to assess how the creation of a stronger Anglo-European supply chain for electric powertrains could impact the ability of UK exporters to qualify for preferential treatment under CPTPP. A larger proportion of UK content in finished batteries would likely help to meet CPTPP origin requirements, but additional sourcing of batteries and battery parts from the EU might have the opposite outcome.

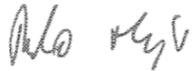
Failing to qualify under CPTPP origin requirement does not necessarily mean tariffs will apply. Manufacturers that cannot meet CPTPP origin rules might be able to export UK-built passenger cars under preference thanks to existing

continuity deals with CPTPP parties or new upcoming agreements with Australia and New Zealand. However, it is unlikely that CPTPP will offer the same opportunities to all UK car makers, with only some manufacturers and some models benefiting from the deal either as an alternative to bilateral FTAs or in trade with new partners covered only by CPTPP such as Malaysia.

Finally, some of the manufacturers that are unlikely to use CPTPP preferences for UK-built passenger cars might still find value in joining the deal. For example, CPTPP and its associated origin requirements might present some opportunities for UK-manufactured engines and parts. Given that relaxed origin requirements apply to these commodities, there is a possibility for UK-based producers to supply these products to assembly plants located into other CPTPP parties for further processing and final incorporation into finished vehicles.

Please do contact us directly if you would like further information.

Yours sincerely,

A handwritten signature in black ink, appearing to read 'Alessandro Marongiu', written in a cursive style.

Alessandro Marongiu
Senior Trade Policy Manager

ANNEX A: [CONFIDENTIAL]

ANNEX B: LCT Thresholds

Financial year	Fuel efficient vehicles	Other vehicles
2021-22	AUD 79,659	AUD 69,152
2020-21	AUD 77,565	AUD 68,740
2019-20	AUD 75,526	AUD 67,525
2018-19	AUD 75,526	AUD 66,331