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The aim of the EU's new block exemption regulation governing the way vehicle manufacturers distribute their products is to give vehicle dealers more independence from manufacturers and create a fairer market, Europe-wide, for the consumer.

One of the likely results is that prices will fall for both new and used cars. The wider effect of this regulation will change the way business is done in the automotive industry and will be felt for many years to come. It must be applied in countries joining the EU from the date of their accession, subject to the negotiation of a derogation.

Since dealers and retailers will no longer be tied to a single vehicle manufacturer and can source the product from a range of suppliers, it is likely that their stocking and back-office systems will need revising because many have been designed for a single manufacturer.

For manufacturers this will only increase the pressure for cost reduction in an industry concerned with cost efficient supply chain management. For this reason the automotive industry is pushed to the vanguard of eastward expansion in the hunt for cheap labor resources. The holistic approach to cost-effective structuring must take into account tax efficiencies.

Tax changes

EU accession is and will continue to alter the tax landscape in central Europe. A car manufacturer will typically create a complex tapestry of cross-border transactions. Take as an example a company headquartered in Germany. It has sent tools on loan to a subsidiary in Poland and has goods stocked there for later sale to the Polish subsidiary from a customs warehouse. The Polish subsidiary ships completed parts to the manufacturing plant back in Germany.

Currently customs borders operate between countries of the current EU and the accession countries. On May 1, 2004, these will disappear. The reporting requirements in relation to goods moving between countries of the single market will become primarily the responsibility of the owner. In the above example, the German manufacturer after May 1, 2004, will find himself holding goods in another EU country. Customs warehousing will not be applicable to goods moving between EU countries, and the German manufacturer will find himself with a VAT registration requirement in Poland.

Car manufacturers will often send goods to be processed to a country in central Europe under a duty suspension or relief regime known as inward processing relief (IPR). One of the conditions of operating this regime is that the goods, once processed will be (re-) exported. This relief will no longer be applicable to goods coming from or destined for another EU country. In fact goods, which are sitting under an IPR regime on May 1, 2004, are potentially liable at that point to importation into free circulation in the EU and an immediate cash-flow cost can arise.

As car manufacturers venture eastward with production plants to territories such as Ukraine, the question of where to import goods into the EU is a matter for renewed consideration. Which of the new countries will become the Netherlands of the region? The Netherlands has long since implemented a simplification measure open to any EU member state that allows traders immediate recovery of VAT incurred on imports where they are entitled to it under the usual rules. This has enormous cash-flow benefits and has been a crucial factor in making the Netherlands the distribution center for Europe.

None of the accession countries have finalized their EU compliant legislation in this area as yet, but our most recent update indicates that none of the first-wave accession countries, including the Czech Republic, have sought to implement this measure.

End-of-life directive

EU legislation will also have a significant effect via the "end-of-life directive." Member states should ensure that the last holder and/or owner can deliver the end-of life vehicle to an authorized treatment facility at no cost. This is meant to reduce the number of junk cars going into a landfill. Under this directive producers must meet all-or a significant part-of the costs of the implementation of these measures, depending on national implementation. The response to the introduction of this measure in the EU was for some manufacturers to ship vehicles east to Poland, Hungary and the Czech Republic at their defined end of life. However, east is now about to become the EU, and these goods will be caught again.

The transition to a new EU will be more difficult for operators in the automobile industry than for many in other sectors. But as they're accustomed to change and heavy regulation, we expect it to be one of the industries best positioned to adapt. The key to success will be ensuring that its key people are properly informed in time of changes just around the bend.