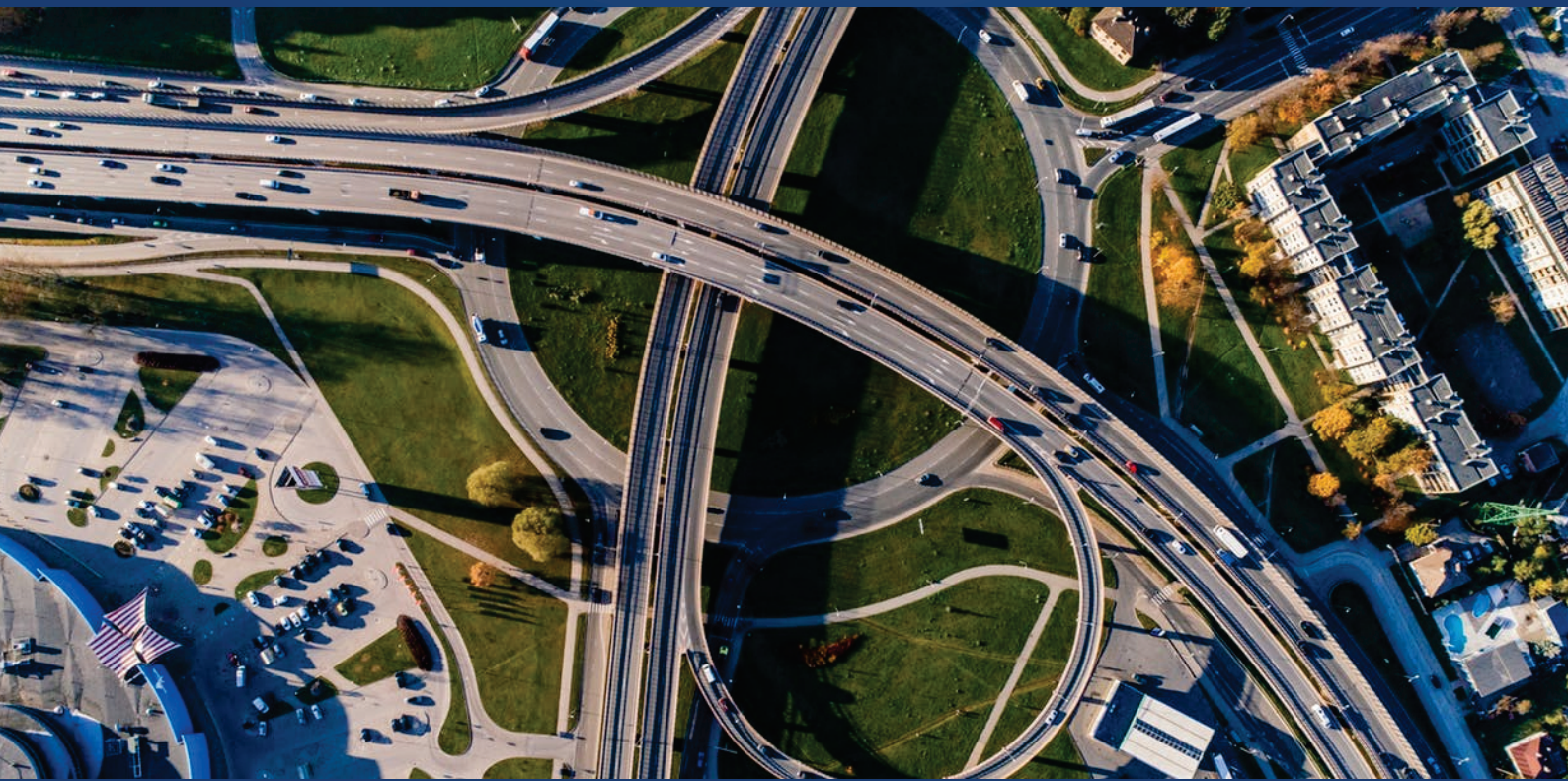




*The **AMERICAN CHAMBER** of Commerce in Mongolia*

Position Paper on Developing an Environmentally Friendly Auto and Machinery Industry



September 2018

Developing an Environmentally Friendly Auto and Machinery Industry

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Through its Auto and Machinery Committee, AmCham Mongolia and the Mongolian Automobile Distributors' Association (MADA) has developed a policy paper titled "Developing an Environmentally Friendly Auto and Machinery Industry". The policy paper outlines key challenges in promoting an environmentally friendly auto sector in Mongolia and proposes certain policy recommendations based on local initiatives and international best practices in handling these issues. The challenges and recommendations were developed with input from key stakeholders, raised and discussed during an Eco-friendly Auto Industry policy workshop held on May 11, 2018. The workshop was organized by AmCham Mongolia and MADA, in cooperation with the Ministry of Road and Transport Development of Mongolia and the Ministry of Nature and Environment of Mongolia.

AmCham Mongolia, namely its Auto and Machinery Committee, and MADA stand ready to discuss the challenges and suggested solutions with the state's authorities to make sure that necessary actions are taken to minimize risks and avoid potential negative impact on the industry and the environment, and to improve progress toward developing an eco-friendly auto industry in Mongolia.

The paper was prepared by the executive teams of AmCham Mongolia and MADA, under the leadership of the Chairman of AmCham Mongolia's Auto and Machinery Committee Garrett Wilson. The Auto and Machinery Committee operates under the authority of the AmCham Board.

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Preamble

Countries around the globe have gradually started focusing their efforts on advancing sustainable and environmentally friendly economic development. Adhering to a similar principle, Mongolia, the Government of Mongolia, state authorities, and the private sector are working together to contribute to the nation's sustainable development goals and the development of an environmentally safe society for current and future generations.

Valuing this critical objective, the American Chamber of Commerce in Mongolia (AmCham Mongolia) and its Auto and Machinery committee, in cooperation with the Mongolian Automobile Distributors' Association (MADA), have released a Position Paper on promoting an environmentally friendly auto and machinery industry to contribute substantially to further development in the sector.

The Position Paper outlines key challenges in promoting an environmentally friendly auto sector in Mongolia and proposes certain policy recommendations based on international best practices in handling these issues.

AmCham Mongolia actively supports private sector development in Mongolia. We believe that a strong and competent private sector will ensure the sustainable development of Mongolia and become a solid foundation for improved livelihoods.

AmCham Mongolia's 2018 policy and advocacy priorities are to support the growth of a strong private sector as the backbone of the country. In pursuit of this initiative, AmCham Mongolia has addressed common issues in the main sectors of the economy through its committees and suggested viable solutions for resolving problems.

The Mongolian Automobile Distributor Associations (MADA) is a non-governmental organization that unites the world's leading car brand's official distributors in Mongolia. These brands operate in the automotive sales and service procurement business according to internationally accepted service standards.

Members of MADA operate in accordance with international standards and are responsible for their customers and for the environmental and social responsibility of their own showrooms, which are fully compliant with quality and safety requirements.

MADA is working on comparing the policies, laws, projects, decisions, ordinances, and standards that are being implemented in Mongolia with international expertise, and to bring the development of the industry to international standards.

Industry Background

The auto and machinery industry is a rapidly growing sector in Mongolia. It is estimated that approximately 120,000 people (directly or indirectly) work in subsectors related to the industry, such as passenger transport services between and in provinces and the capital, as well as auto and machinery repair services.

Auto road development has greatly expanded in Mongolia, with 6,351 kilometers of paved road newly built or upgraded from 2011-2015. In addition, more infrastructure development works are due in 2016-2021, with the construction of an additional 5,770 kilometers of paved road.

There are 900,127 registered vehicles in Mongolia: 65.1 percent of them are passenger cars (of which 83 percent are right-hand drive), 59 percent are in Ulaanbaatar, and 77.4 percent are more than 10 years old. From 2011 through the first half of 2018, Mongolia imported a total of 342,380 passenger cars valued at 2.4 billion USD. This data indicates that the pool of vehicles in Mongolia has increased by an average of 42,798 cars per year over the last several years. The import of these passenger vehicles has generated 1.13 trillion MNT for the state budget through VAT and excise tax revenue.

Challenges and Potential Solutions

The automotive and machinery industry in Mongolia is diverse and rich in terms of the pool of vehicles and the complexity of challenges faced. At a time when Mongolia's economy has been growing and the public's consumption has increased, proper development of the automobile industry is a rather important step. There has emerged a necessity to promote public safety and environmentally friendly practices in the automobile sector, as well as to fully meet and appropriately supply a continually increasing demand for vehicles.

The Position Paper addresses the aspect of eco-friendliness in the automobile and machinery industry of Mongolia, to keep advocacy efforts fruitful and optimal.

Challenges and Solutions

Challenge: Pollution emitted from old vehicles

As shown by reports, 56 percent of imported vehicles in Mongolia since 2011 are more than 10 years old, followed by 27 percent that are more than 7 years old, 9 percent that are between 4-6 years old, and a mere seven percent between the ages of 0-3 years.

The common use of old cars in Mongolia is creating a pressing problem of how to store, re-build, or dismantle secondhand vehicles, their parts, batteries, and waste oil. As a result, Mongolia has turned into a dumping ground for some countries' toxic hybrid vehicle waste. Because vehicle batteries are considered to be hazardous freight and Mongolia's neighbors don't permit the transportation of these items, the number of expired batteries being kept in storage by official dealers is increasing on a regular basis.

Solution:

It is essential to keep import taxes for new vehicles lower than those for older cars, to raise import tariffs for old cars, and thus encourage buyers to purchase new cars. This measure would not restrict a citizens' right to the ownership of a vehicle. This approach is the best international practice for reducing the number of environmentally damaging and potentially dangerous imports, in terms of health and safety, through economic means.

However, it is impossible for every citizen to buy a new car due to the current economic situation and limited purchasing power. Some European countries offer discounts and long-term financial leasing for purchases of new cars, given that a buyer yields their old vehicle to a recycling plant, where it will be dismantled or destroyed, and intends to buy a new automobile.

An interim solution could be to ban older vehicles that no longer meet emissions and production standards.

The proposed ban on older cars is a complicated issue, which has a direct impact on the livelihoods of many citizens. It is necessary to provide employment opportunities to people whose main source of income comes from having an older vehicle. For instance, the expansion of a more environmentally friendly public transport system would be an efficient alternative and increase the number of jobs for drivers. The ban would also lead to the more frequent use of public transportation services. In collaboration with internationally-known transport services, such as Uber, it is possible to resolve the matter, as well.

A renewed classification of vehicle ages and excise taxes could also trigger a change of course toward the appropriate level of automobile use. The over-use of vehicles would be reduced, thus mitigating the dangerous effects of vehicles on the environment.

The following recommendations are being presented to achieve this goal.

- a) Prohibit the import of vehicles that do not meet industry standards. For instance, vehicle inspection, the condition of batteries, the rate of pollutant emission, the depreciation of parts, and safety technology, etc., should be strictly enforced as part of customs entry checks so that low-performing vehicles will not be allowed entry into the country.
- b) Increase vehicle fees and taxes based on the age of vehicles.
 - Excise tax:
 - 1) Introduce a new age classification scheme, classified as 0-1 year, 2-3 years, 4-6 years, 7-9 years, and more than 10 years.
 - 2) Increase excise taxes for vehicles over 10 years old by 2 or 3 times.
 - 3) Combine the age classifications of 7-9 years and 10+ years after a certain period of time (a suggested five years) and reduce the age of the automotive pool step by step.
 - Vehicle excise tax:
 - 1) Introduce engine and age classifications and increase vehicle use fees in line with the law on excise taxes.
- c) Other policy recommendations:
 - Develop and organize cab services in line with international standards and improve access to and the convenience of public transport buses.
 - Create and improve the business and legal framework for car rental services.
 - Establish a car dismantling plant next to a metal processing plant.
 - Improve vehicle inspection procedures and standards in correlation with international practices.

Challenge: Smoke/Fumes

The widespread use of imported secondhand vehicles in transportation has had dire consequences for the environment and public health.

Mongolia allows permits for vehicles if they meet the Euro 2 emission standard, a process undertaken as part of the national vehicle inspection process. However, every day we see vehicles posing questions as to whether or not these cars really satisfied the standards upon entry. Additionally, Mongolia is one of a few countries left on the globe which enforces the Euro 2 standard for vehicle inspections. Most nations have completely transitioned to the Euro 5 standard, while some highly developed countries follow the Euro 6 emission standard or other clean engine technology standards. Vehicle exhaust fumes contain poisonous chemicals and cause health problems, particularly where the population concentration is higher.

The population of Ulaanbaatar reached 1.4 million in 2017, while the number of registered vehicles totaled 531,075, indicating that there is one car for every three city residents. Since there is no heavy chemical production in Mongolia, chemical elements in the air are solely derived from vehicle exhaust. According to air pollution reports for Ulaanbaatar, vehicle emissions and dust are found to be the second biggest source of air pollution in the city, constituting 10 percent of the pollution, 30 percent of the carbon dioxide emission, and 78.5 percent of the nitrogen dioxide emission. These elements are included in the list of hazardous greenhouse gases compiled by the World Health Organization. Even if it seems like a small percentage, vehicle exhaust emissions are more toxic than the ger area smoke produced from coal burning, and it lasts throughout the whole year.

Countries pay special attention to vehicle exhaust fumes and the role of state authorities in mitigating them, which is critical to resolving the matter. To see positive outcomes, government agencies need to be transparent and open, and work to ensure the participation of automobile producers, dealers, and sellers in defining effective policies.

International practices for promoting an environmentally friendly automobile industry

Developing Countries

In 2009, Mauritius became the first developing country to adopt a feebate tax structure that taxed inefficient and older vehicles at a higher rate and provided refunds for cleaner vehicles. This tax structure was instrumental in promoting the import of modern, more fuel-efficient vehicle technologies. Specifically, Mauritius enforces an age limit and a carbon dioxide emissions-based feebate scheme for imports, in place since 2011; a 50 percent discount on excise duty on hybrid electric vehicles; and a very recent higher reduction on duties for fully electric vehicles.

In the capital of Port Louis, the number of hybrid vehicles grew from just 43 to 1,824, and the number of electric vehicles went from none to eight, and the country saw emissions reductions of about 20 percent in nine years. The successful experience of Mauritius in implementing such policies and the proposed additional policy recommendations has been discussed not only on a regional level, but also globally.

Developed Countries

Electric car buyers in Norway do not pay import tax or VAT, and plug-in cars are exempt from numerous road tolls and city emission charges. Moreover, electric cars can park for free and bypass traffic by driving in some bus lanes. As a result, Norway has incontestably achieved the most successful deployment of electric cars in terms of market share, globally. The Norwegian government has set a clear target to end the sales of gas and diesel-powered vehicles by 2025.

Other developed countries have set forward the following measures and goals:

- *Barcelona will begin banning old polluting cars in 2019.*
- *Munich has started banning all kinds of projects and programs regarding diesel engines.*
- *Great Britain is planning to enforce regulations forbidding diesel engine vehicle use in transportation.*
- *The Netherlands and Switzerland will allow only non-diesel engine automobiles starting in 2025.*
- *Paris, Madrid, Athens, and Mexico City will ban diesel vehicles in 2025.*

Emerging international initiatives have been forcing automobile makers to stop production of engines prior to the Euro 5 standard and to move to the production of electric vehicles. On the other hand, state policies in these countries are prudently and consistently enforced, while producers and the public have begun taking active steps in exporting or dismantling their old diesel cars, since they are familiar with the exact timeline set by their respective authorities in implementing environmentally friendly initiatives. As a consequence, there is a marked surge in cheap Western secondhand vehicles being imported to Mongolia.

Solutions:

- a) Introduce and stringently enforce emissions standards by revising existing rules and regulations. As part of this initiative, it is necessary to strictly monitor older public transportation vehicles, freight trucks, and passenger cars, and to conduct national vehicle inspections in compliance with the Euro 5 emission standard, at minimum.
- b) Increase and update the air pollution fee in conjunction with engine and age classifications set out in the excise tax law. Definite monetary values should be determined based on the state budget allocation for reducing air pollution.
- c) Encourage the public to purchase environmentally friendly electric or gas engine vehicles and build the infrastructure they require.
- d) Create financial and import incentives to support the purchase of electric cars.
- e) Introduce tax discounts or other incentives such as:
 - Electric cars up to six years should be completely exempt from customs duty, excise tax, and VAT
 - Charging devices to be tax exempt
 - Electricity used at charging stations should be exempt from electricity fees
 - Electric cars should be exempt from other types of usage fees

Challenge: Fuel Quality

In 2017, Mongolia imported nearly 1.5 million tons of petroleum products. Out of which:

- Euro 2 fuel made up roughly 92 percent of all imports, while Euro 5 fuel accounted for 4.8 percent,
- Diesel fuel made up 55 percent, while octane gasoline made up 25 percent, and
- Russia supplied 97 percent of the imports, while China and South Korea provided 2 percent and 1 percent respectively.

Mongolia is one of a few countries which use low quality fuel below the Euro 5 standard. For instance, Angarsky Oil Chemicals Plant, one of the major petroleum suppliers in Russia, sends its Euro 2 production line only to countries like Mongolia and Kyrgyzstan, but has stated that it is possible to provide Mongolia with Euro 5 fuel. High quality petroleum products would not only contribute to solving Ulaanbaatar's air pollution problem, but would also have a positive impact on the main economic pillars of the country, such as mining equipment, heavy machinery, cross-border freight transport, and consumer vehicle needs.

On the other hand, the government frequently regulates fuel prices through tax policies. High quality diesel fuel costs 1 EUR, or approximately 2,800 MNT per liter in Germany, while the price for diesel currently amounts to 2,010 MNT in Mongolia. Even if petroleum importers in Mongolia offer Euro 5 fuel in the domestic market, the public may not buy Euro 5 fuel on a wider scale due to limited purchasing power.

The government identified specific objectives and passed policy documents to increase sales and the adoption of Euro 5 fuel as a main petroleum product consumed, although progress has been slow and the means to implement the objectives has only been partially defined.

Solution:

It is imperative to pay special attention to this issue and to implement the Euro 5 standard completely and consistently.

- a) Carry out a campaign to establish reserves of diesel and AI 92 Euro 5 fuel at every gas station
- b) Complete planned actions to encourage the use of Euro 5 fuel
- c) Non-governmental organizations, rather than petroleum importers and sellers, should initiate this work
- d) Government agencies and related organizations should publicize the benefits of Euro 5 fuel and support import companies



Ways Forward

Certainly, addressing the identified policy issues is a complex and a time-consuming process that may face resistance from different stakeholders. But the timely and consistent actions in tackling these challenges will greatly contribute to the sustainable social and economic development of Mongolia and the public's secure and healthy lives.

The process will require a comprehensive approach from stakeholders and setting clear timelines to implement the proposed solutions.

AmCham Mongolia and MADA's members are eager to support the government in addressing these challenging issues. We will be able to provide expert views and share international experiences by, for example, co-organizing a public-private dialogue to discuss solutions to the challenges facing the auto and machinery industry.





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