



STATEMENT OF

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AUTOMOBILE MANUFACTURERS, INC.**

**BEFORE THE
SENATE SURFACE TRANSPORTATION AND MERCHANT MARINE
SUBCOMMITTEE
SENATE COMMITTEE ON COMMERCE, SCIENCE, AND
TRANSPORTATION**

**REGARDING LEGISLATION AUTHORIZING
PASSENGER CAR FUEL ECONOMY STANDARDS**

May 9, 2006

Good morning. My name is John Cabaniss, Director, Environment and Energy for the Association of International Automobile Manufacturers, Inc. (AIAM).

AIAM is a trade association representing 14 international motor vehicle manufacturers accounting for over 40 percent of passenger cars and over 20 percent of light trucks sold in the United States annually.¹ AIAM appreciates the opportunity to offer its views regarding the need to reform passenger automobile CAFE standards. AIAM supports Transportation Secretary Mineta's request for additional legal authority to revise the structure of the passenger car CAFE standards. In addition to addressing this issue, we would like to stress the importance of adequate lead-time in achieving compliance with any new standards, suggest that supplemental market-based incentives would strengthen a national effort to reduce fuel consumption, and recommend the elimination of the "two-fleet rule" requiring the separation of a manufacturer's import and domestic fleets.

AIAM members are important stakeholders in the debate over passenger car fuel economy standards, representing 44 percent of all sales in this market segment last year. In addition, AIAM member companies have for many years been leaders in offering fuel-efficient vehicles for the U.S. market. Historically, vehicles produced by our member companies have headed EPA's annual list of most fuel-efficient vehicles. Member companies have achieved this fuel-economy leadership to a significant degree by pioneering the introduction of advanced automotive technology into their vehicles. Our member companies continue to introduce a variety of advanced technology models,

¹ AIAM members include Aston Martin, Ferrari, Honda, Hyundai, Isuzu, Kia, Maserati, Mitsubishi, Nissan, Peugeot, Renault, Subaru, Suzuki and Toyota. AIAM also represents original equipment suppliers and other automotive-related trade associations.



including hybrid electric vehicles, ethanol-capable flexible-fuel vehicles, hydrogen fuel cells, clean diesel, as well as advances in traditional gasoline vehicles.

AIAM believes that there are three guiding principles that Congress should follow when it addresses CAFE matters. First and foremost, when considering the form of the CAFE standards it is of the utmost importance that the structure or underlying approach is competitively neutral, and that all manufacturers are treated fairly and equitably under the standards system. Second, under any structure, the specific requirements of the standards must be technologically feasible and economically practicable. Third, it is absolutely essential that manufacturers are provided adequate lead-time to implement new standards.

In addition, standards should continue to establish performance requirements rather than specify or favor any particular technology. Reducing U.S. dependence on petroleum is a complex undertaking, and the greater the number of creative technologies that can be brought to bear, the better. In addition, performance standards allow manufacturers the flexibility to set their own research priorities based on their individual strengths and to develop the most effective and efficient approaches to meet consumer demand, while achieving the broader societal goals for which the standards are intended.

I. Reform of the Structure of the Passenger Car CAFE Standards

An April 28, 2006, White House Fact Sheet states that the Administration is requesting additional legal authority to enable DOT to reform the passenger car CAFE standards “consistent with the approach taken with the light truck rule issued March 29.”² AIAM supports authorizing DOT to establish attribute-based class standards for passenger cars, as is currently authorized for light trucks. This approach would be consistent with the recommendations of the National Academy of Sciences Committee and is generally consistent with the approach adopted by NHTSA in its recent light truck CAFE rulemaking. DOT should be given the flexibility to consider variations of the structure adopted in its light truck rule. Given our lack of experience with the new structure, it remains uncertain how the new structure will work in practice. Under no circumstances should the Department be authorized to adopt company standards based on past performance, such as uniform percentage increase (UPI) standards. We urge Congress to provide guidance to DOT by providing the underlying principles upon which the new standards must be based, including the three guiding principles discussed above.

Over the years AIAM has vehemently opposed any effort to authorize fuel economy standards based on the UPI approach. Respected analysts have consistently criticized the UPI approach, including the National Academy of Sciences, in its 2001-2002 study, which states:

The UPI system would impose higher burdens on those manufacturers who had already done the most to help reduce energy consumption. The peer-reviewed

² See <http://www.whitehouse.gov/news/releases/2006/04/20060428-9.html>.



literature on environmental economics has consistently opposed this form of regulation. It is generally the most costly way to meet an environmental standard; it locks manufacturers into their relative positions, thus inhibiting competition; it rewards those who have been slow to comply with regulation; it punishes those who have done the most to help the environment; and it seems to convey a moral lesson that it is better to lag than to lead. In addition to fairness issues, the change would not eliminate the problems of the current CAFE system, but would create new ones. Implementation of such rules provides strong incentives for manufacturers to not exceed regulatory standards for fear that improvements will lead to tighter regulations. Thus, such rules tend to create beliefs counterproductive for longer-term goals.³

In addition to these shortcomings, the UPI approach would have the effect of locking manufacturers into their current model mix, leaving them potentially unable to meet changing consumer demands.

We also believe that standards levels should be established by DOT through rulemaking. The complex technical and economic analyses necessary to set standards are better accomplished as part of an agency rulemaking rather than through direct legislation. DOT has substantial resources available to perform the required technology and economic analyses required for standard setting, and the use of an open, transparent, rulemaking process is needed to assure that the interests of all parties are considered in reaching a decision on the standards.

II. Lead-Time

The law provides that CAFE standards must be set at least 18 months prior to the start of the affected model year. However, the 18-month period is adequate to enable automakers to implement only the most minor of design changes. For more substantial changes, greater lead-time is necessary, not only to develop new technologies but also to deploy existing technologies into the fleet through normal product redesign cycles. It is instructive to note that the National Academy of Sciences Committee projected the need for up to 15 years lead-time to meet significantly higher standards. It is also desirable to our planning efforts to have standards set for multiple years in a single rulemaking, as NHTSA did with the recent light truck rule. Automakers generally plan major vehicle redesigns on a 5 to 8 year cycle, with individual model changeovers staggered to allow the best use of limited engineering resources. Significant changes in fuel economy require a stable and predictable set of requirements that corresponds to this 5 to 8 year product cycle. We urge Congress and the Administration to consider the need for lead-time beyond the statutory minimum in order to implement new vehicle technology.

³ “Effectiveness and Impact of Corporate Average Fuel Economy Standards,” National Research Council, 2002, pages 92-93.



III. Market-Based Approaches to Facilitating Higher Levels of Fuel Economy

CAFE standards mandate the production of more fuel efficient vehicles but provide no incentive for consumers to purchase such vehicles. The most direct market signal to encourage consumers to demand fuel efficiency is an increase in the cost of driving. Recent record-high gasoline price increases encourage consumers to value fuel saving technologies. However, motorist interest in fuel savings often dims when fuel prices decline. Therefore, other types of incentives may be useful to maintain demand for fuel efficient vehicles when fuel prices are lower or to reinforce the market signal provided by high fuel prices. Such incentives include extending and expanding current tax credits and tax deductions for the purchase of fuel efficient and alternative fueled vehicles, access to preferential parking areas, and mandates for government fleet purchases. These and other incentives would further encourage manufacturers to develop and introduce advanced technologies by enhancing the market for vehicles that use such technologies. Advanced fuel-efficient technologies are frequently costly, particularly in their first years of introduction, and such incentives can facilitate the introduction of advanced technologies by helping to bridge the price differential between these vehicles and conventional vehicles. Congress has considered a variety of technology-based incentives in recent years to encourage consumers to purchase advanced technology vehicles. AIAM member companies have generally supported these incentives and support the President's call to lift the current manufacturer cap on tax credits for hybrids and diesels to allow more consumers to be eligible for the full tax credit. Ideally, we believe that such incentives should be performance-based and technology-neutral, i.e., they should be designed to encourage the production and sale of fuel-efficient vehicles, regardless of the specific advanced technology selected by the manufacturer or where vehicles are manufactured.

AIAM supports new authority for credit trading under the CAFE program. Allowing credit trading would provide manufacturers with increased compliance flexibility and encourage fuel economy improvements. The 1992⁴ and 2001⁵ NAS CAFE Committees suggested this approach. Allowing such trading would also enhance the overall efficiency of the CAFE system. We believe that the rulemaking should examine credit trading among manufacturers and between a manufacturer's passenger auto and light truck classes.

IV. Domestic/Import Separate Fleet Requirement

The current law requires dividing a manufacturer's passenger car fleet into domestic and import classes that must comply separately with fuel economy standards. There is no similar requirement for light trucks. This requirement was originally intended to encourage domestic production of smaller vehicles by eliminating any compliance benefit for U.S.-based manufacturers from simply importing foreign

⁴ "Automobile Fuel Economy, How Far Should We Go?", National Research Council, 1992, page 184.

⁵ "Effectiveness and Impact of Corporate Average Fuel Economy (CAFE) Standards," National Research Council, 2002, page 114.



produced, fuel efficient vehicles. Supporters of the “two-fleet” rule argue that the rule prevents manufacturers from shutting down U.S. production facilities for smaller, fuel efficient vehicles. In our view, the current record-high fuel prices and growing demand for fuel efficient vehicles indicates there is a strong incentive for maintaining or increasing U.S. production of fuel efficient vehicles by all manufacturers. Moreover, the “two-fleet” provision has created the unintended consequence of providing a disincentive for foreign-based companies to increase the U.S. content of their vehicles to levels above 75 percent, since doing so would place the vehicles in a separate compliance fleet. This disincentive is real, not theoretical, and has cost U.S. jobs. There have even been cases where a company has decreased the U.S. content of certain domestic vehicles to a level below 75 percent to allow those vehicles to be averaged with the manufacturer’s more efficient import fleet adversely impacting U.S. suppliers.

The 2001 National Academy of Sciences study of the CAFE program⁶ states that “since the two-fleet rule increases costs to consumers, the committee believes it is no longer justifiable and should be eliminated.” The 1992 NAS CAFE committee⁷ concluded that the separate fleet requirement “has no obvious or necessary connection to the achievement of fuel economy” and encouraged Congress to consider its repeal. We strongly concur in these assessments.

V. Conclusion

The auto industry is not the same as 30 years ago when the CAFE program was established. Since that time AIAM members have invested over \$33 billion in U.S.-based vehicle, engine and parts manufacturing plants, and research and development facilities and developed a production capacity of 3.7 million vehicles annually. Combined, international automakers directly employ 103,000 Americans and generate 1.7 million U.S. jobs in dealerships and supplier industries nationwide. Approximately 60 percent of all the cars and light trucks sold each year in the U.S. by international automakers are made in the United States.

Thank you.

⁶, Id., page 89-90.

⁷, Id., pages 183-4.