

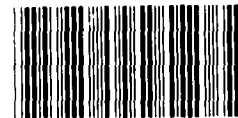
GAO

Report to the Chairman, Subcommittee on Oversight and Investigations, Committee on Energy and Commerce House of Representatives

December 1986

AUTO SAFETY AND EMISSIONS

No Assurance That Imported Gray Market Vehicles Meet Federal Standards



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Resources, Community, and
Economic Development Division

B-217842

December 11, 1986

The Honorable John D. Dingell
Chairman, Subcommittee on Oversight
and Investigations
Committee on Energy and Commerce
House of Representatives

Dear Mr. Chairman:

This report, prepared in response to your January 2, 1985, request, summarizes the results of our review of various issues relating to the importation of vehicles that do not conform to U.S. safety and emission standards. The report also discusses the manner in which the National Highway Traffic Safety Administration, Environmental Protection Agency, and U.S. Customs Service carry out their respective responsibilities regarding the importation of these vehicles.

As arranged with your office, unless you publicly announce its contents earlier, we plan no further distribution of this report until 30 days from the date of this letter. At that time, we will send copies to interested parties and make copies available to others upon request.

Sincerely yours,

A handwritten signature in cursive script that reads 'J. Dexter Peach'.

J. Dexter Peach
Assistant Comptroller General

Executive Summary

Purpose

Motor vehicles produced for foreign markets do not always conform to U.S. safety and emission standards. The National Traffic and Motor Vehicle Safety Act and the Clean Air Act allow these vehicles to be imported if they are modified to conform to these standards. The non-conforming vehicles requiring modification, or "gray market" vehicles, imported annually increased from about 2,400 in 1980 to 66,900 in 1985. Although the number dropped in the first half of 1986, it remains an issue of concern in the Congress.

The Chairman, Subcommittee on Oversight and Investigations, House Committee on Energy and Commerce, expressed concern about whether the growing number of gray market vehicles was being conformed to the standards. He asked GAO to examine the manner in which the regulatory agencies were carrying out their respective responsibilities.

Background

The federal regulatory agencies are the National Highway Traffic Safety Administration (NHTSA), Department of Transportation; the Environmental Protection Agency (EPA); and the Customs Service (Customs), Department of the Treasury. Motor vehicles operated on the nation's highways must conform to safety and emission standards established by the Secretary of Transportation and the Administrator, EPA.

Nearly all vehicles imported or built for sale in the United States conform with these standards as originally manufactured. However, some vehicles manufactured for foreign markets are not certified by the original manufacturers as being in conformity with U.S. safety and emission standards. Such nonconforming motor vehicles may be imported by private individuals and independent commercial importers for personal use or for resale on the condition that they be modified to meet U.S. safety and emission standards.

With few exceptions the importers must agree to modify the vehicles to meet the federal standards within a specified period and post bonds with Customs until they do so. Customs notifies NHTSA and EPA when gray market vehicles enter the country. They, in turn, notify the importers of the safety and emission standards applicable to the particular vehicles and of the documentation needed to support that the vehicles have been modified to meet the standards.

Upon notice from NHTSA and EPA that the vehicles have been modified, Customs releases the importers' bonds. However, if the vehicles are not

modified within the specified time, Customs is to take enforcement action—a fine, bond forfeiture, or vehicle exportation or destruction.

Results in Brief

The gray market program, as now operated by NHTSA and EPA, lacks sufficient internal controls to ensure that imported gray market vehicles are modified to meet U.S. safety and emission standards. The agencies neither inspect the firms that modify the vehicles nor test the vehicles to ensure that the standards are met.

GAO's analysis, as well as several government and industry surveys (although limited), suggest that substantial percentages of gray market vehicles approved by NHTSA and EPA do not conform to the federal standards.

During the 99th Congress the Senate and House of Representatives passed bills (S. 863 and H.R. 2248) tightening controls to ensure that gray market vehicles are modified to meet safety standards. The Congress adjourned before final action was taken on the proposed legislation. These bills did, however, address some of the control problems GAO identified.

Principal Findings

Improved Internal Controls Needed

GAO found that NHTSA does not inspect firms that modify vehicles to ensure that they have the capability to conform the vehicles to the safety standards. Moreover, NHTSA does not test the vehicles to determine that modifications were done properly. EPA has a certification program to recognize certain firms and laboratories that have demonstrated their respective capabilities to modify the vehicles to meet the emission standards or perform the federal emission test procedures. Thereafter, EPA accepts certificates from these firms and laboratories indicating that they have properly modified or tested the vehicles. While EPA's program has more internal controls than NHTSA's, it also has shortcomings. GAO found that EPA's certification program does not provide for periodic inspection of the modifying firms or testing of the vehicles. Although EPA began, in September 1985, a reinspection of the laboratories, it has no plans to include inspection of modifying firms.

**Indications of
Nonconformance to
Standards**

GAO randomly selected 50 vehicles for review to determine if the importers had met all NHTSA and EPA requirements. For safety standards GAO found that the documentation (including receipted work orders, photographs, and engineering calculations) for 21 of the 50 vehicles had not been submitted within the specified period of time, generally 120 days, from the date of vehicle entry. For the remaining 29 vehicles, questions arose as to the adequacy and accuracy of the documents substantiating that the vehicles conformed with the safety standards. GAO judgmentally selected 5 of the 29 vehicles for detailed review and, in conjunction with the original manufacturers, examined the documentation to determine if the vehicles had been modified to conform with federal safety standards. None of the five vehicles met all of the applicable standards.

For emission standards, GAO requested EPA to provide the documentation that the importers had submitted to substantiate that the vehicles had been modified to meet the standards. EPA was unable to locate any documentation for 26 of the 50 cases. In 12 of the remaining 24 cases, the importers had been granted exemptions on the basis of the age of the vehicles. In the other 12 cases, EPA had approved the vehicles on the basis of test results submitted by EPA-recognized testing laboratories.

In 1985, in about 90 percent of the cases, EPA based its approval of vehicles on test results provided by the recognized laboratories. GAO noted, however, a 1984 study conducted by EPA and California state inspectors on 27 gray market vehicles that EPA had initially approved on the basis of laboratory test results. Only one vehicle had passed all parts of the emission test.

Proposed Legislation

Although the Congress adjourned before final action was taken on S. 863 and H.R. 2248, both bills took similar approaches. Both restricted who could import vehicles that did not conform to safety standards and established eligibility controls over which nonconforming vehicles could be imported. In addition, both required NHTSA to provide greater assurances that gray market vehicles would be properly modified to meet safety standards. Neither of the bills addressed vehicle conformance with emission standards.

Under the House bill, with limited exceptions, only registered commercial importers could import gray market vehicles; and only designated vehicles, which could be readily modified to meet the safety standards, would be eligible for importation.

The Senate bill, while more flexible on who could import a gray market vehicle, also required registration and inspection of modification firms and periodic testing of vehicles that modifiers had certified as being in compliance.

Recommendations

GAO recommends that the Secretary of Transportation direct the Administrator, NHTSA, to improve controls over its program by establishing a process similar to EPA's program, whereby firms are recognized by NHTSA, through certification, as being capable of modifying gray market vehicles. In addition, NHTSA should periodically reinspect these firms and consider testing a sample of modified vehicles as a check on the firms' performance in ensuring vehicle compliance with the safety standards. In considering the appropriate scope, frequency, and amount of testing, NHTSA should take into account factors such as staffing constraints as well as the safety standards for which compliance testing is technically practical and cost-effective.

GAO recommends that the Administrator, EPA, improve EPA's controls over its program by periodically inspecting both the modifying firms and test laboratories that have been previously recognized and consider testing the vehicles, on a sample basis, to ensure compliance with federal emission standards. In considering the scope and amount of testing, various factors should be taken into account, including staffing constraints and the cost of such testing.

Agency Comments

GAO discussed its findings with agency program officials and included their comments where appropriate. However, GAO did not request official agency comments on a draft of its report.

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Abbreviations

AICA	Automobile Importers Compliance Association
BMW	BMW of North America, Inc.
CARB	California Air Resources Board
DOT	Department of Transportation
EPA	Environmental Protection Agency
GAO	General Accounting Office
MBNA	Mercedes-Benz of North America
NADA	National Automobile Dealers Association
NHTSA	National Highway Traffic Safety Administration
OVSC	Office of Vehicle Safety Compliance
RCED	Resources, Community, and Economic Development Division
VIN	vehicle identification number

Introduction

Motor vehicles used in the United States must conform to safety and emission standards established by the Secretary of Transportation and the Administrator, Environmental Protection Agency (EPA). Nearly all vehicles imported or built for sale in the United States conform with these standards as originally manufactured. However, motor vehicles that are not covered by a certificate of conformity with U.S. safety and emission standards may be imported by private individuals and independent commercial importers¹ for personal use or for resale on the condition that they be modified to meet U.S. safety and emission standards.² These imported nonconforming motor vehicles are often referred to as "gray market" vehicles.

Nonconforming motor vehicles are purchased abroad by private individuals and independent commercial importers from new and used car dealers, brokers, wholesalers, rental and leasing companies, large corporations, and private citizens generally at prices substantially lower than those charged for similar models by original manufacturers' authorized dealers in the United States. Such vehicles may lack accessories that are standard on models originally manufactured for sale in the United States. These vehicles may also differ mechanically and structurally from models certified for sale in the United States.

A purchaser who buys a nonconforming vehicle overseas pays for the vehicle itself, its shipment to the United States, modifications to the vehicle to meet federal safety and emission standards, and customs duties. The savings to the purchaser increase or decrease as the value of the dollar fluctuates relative to the value of the exporting country's currency (exchange rate) and as the foreign manufacturer adjusts its prices for similar vehicles originally built for and sold in the U.S. market. For example, according to EPA, in 1985 the price difference to consumers between one popular nonconforming vehicle modified to conform with federal safety and emission standards and a comparable model certified as having been originally built to conform with those standards was \$9,000.

¹The term "independent commercial importers" as used here means importers who do not have a contractual agreement with foreign manufacturers to act as their authorized representatives for the distribution of vehicles into the U.S. market.

²Motor vehicles include passenger cars, multipurpose passenger vehicles, trucks, buses, trailers, motorcycles, and motor-driven cycles, such as mopeds. However, essentially all imported nonconforming vehicles are passenger cars.

Requirements for Federal Safety and Emission Standards

The National Traffic and Motor Vehicle Safety Act of 1966, as amended (15 U.S.C. 1391 *et seq.*), requires that a motor vehicle manufactured on or after January 1, 1968, sold in or imported into the United States conform with all applicable federal motor vehicle safety standards in effect on its date of manufacture. These standards are intended to reduce traffic accidents, as well as deaths and injuries to persons resulting from such accidents. The Clean Air Act, as amended (42 U.S.C. 7401 *et seq.*), requires gasoline-fuel vehicles, beginning with those manufactured in the 1968 model year, and diesel-fuel vehicles, beginning with the 1975 model year, to be certified as meeting emission standards if they are sold in or imported into the United States. These standards affect emissions of air pollutants that may endanger public health or welfare.

The Secretary of Transportation has specified levels of performance for passenger cars and their components by issuing 36 safety standards as of December 31, 1985. The federal safety standards deal with those characteristics of vehicles that

- prevent crashes,
- affect and reduce the severity of injuries after a crash occurs (also referred to as crashworthiness standards, containing critical occupant survivability requirements), and
- relate to motor vehicle safety in various other ways.

The Administrator, EPA, has established vehicle emission standards for several types of air pollutants. These include hydrocarbon, carbon monoxide, oxide of nitrogen, evaporative, and, where applicable, diesel particulates.

Legislative and Regulatory Provisions for the Importation of Nonconforming Vehicles

Both the Safety Act, as originally enacted in 1966, and the Clean Air Act permit the conditional importation of motor vehicles not covered by a certificate of conformity with applicable federal safety and emission standards. Section 108 of the Safety Act and Section 203 of the Clean Air Act provide that nonconforming vehicles may be imported under terms and conditions to be prescribed in joint regulations issued by the Secretary of the Treasury with the Secretary of Transportation and with the Administrator, EPA, respectively.

One foreign automobile manufacturer observed that the purpose of the conditional importation provisions of the Safety Act and the Clean Air Act was to assist returning members of the armed services, diplomats,

and other Americans living abroad who had obtained foreign nonconforming vehicles while overseas and who would suffer a hardship by being forced to sell their vehicles before returning to the United States. Our review of the legislative history did not disclose that the Congress intended to limit conditional importations to these persons.

Joint regulations governing the conditional importation of nonconforming vehicles were issued by the

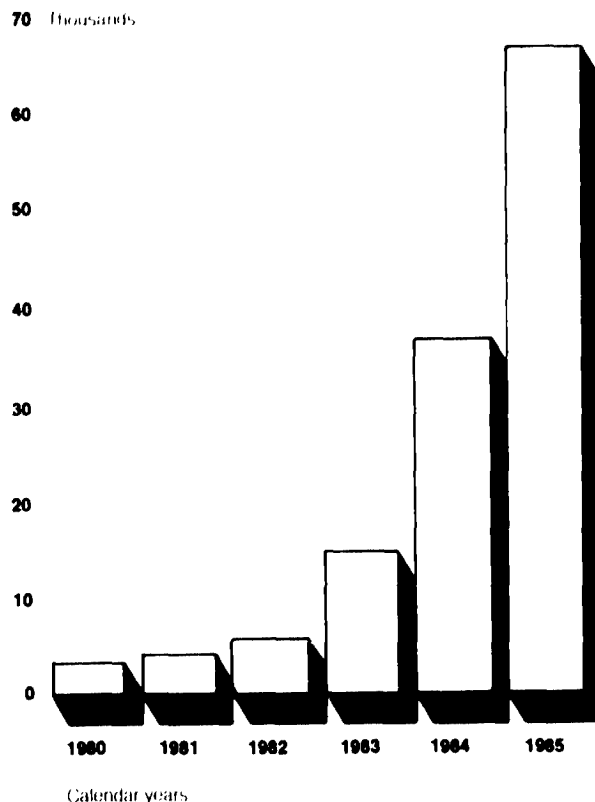
- EPA and Customs in 1972 and
- National Highway Traffic Safety Administration (NHTSA), Department of Transportation (DOT), and the U.S. Customs Service (Customs), Department of the Treasury, in 1978.

EPA also issued separate regulations in 1972 relating to such imports.

Increase in Importation of Nonconforming Vehicles

According to NHTSA the annual number of imported nonconforming vehicles increased from about 2,400 in 1980 to 66,900 in 1985—an increase of nearly 2,800 percent—as shown in figure 1.1. However, through the first half of 1986, only 15,500 gray market vehicles had entered the country, and industry forecasts are that, given the strength of the U.S. dollar in the foreign market, the downward trend will continue.

Figure 1.1: Number of Nonconforming Vehicles Imported Annually During Calendar Years 1980-85



Source: NHTSA

In 1985 foreign manufacturers imported 2.8 million vehicles and domestic manufacturers built about 7.8 million, a total of 10.6 million vehicles that conformed to all applicable federal safety and emission standards. As shown in figure 1.1, during that year 66,900 nonconforming vehicles were imported. Nonconforming vehicles accounted for less than 1 percent of the vehicles produced and sold in the United States in 1985.

Objectives, Scope, and Methodology

In a January 2, 1985, letter, the Chairman, Subcommittee on Oversight and Investigations, House Committee on Energy and Commerce, expressed concern about the growing number of nonconforming motor vehicles entering the United States. The Chairman requested that we examine the manner in which NHTSA, EPA, and Customs carry out their respective responsibilities regarding the importation and modification of these vehicles. The Chairman specifically asked that we examine

- the problems encountered by NHTSA, EPA, and Customs in administering the laws' provisions;
- the adequacy of each of the three agencies' personnel to administer the laws and regulations governing the importation of nonconforming motor vehicles and the costs associated with implementing the program;
- the extent to which each of the three involved agencies uses contractors for the program and the method used to award such contracts;
- the extent of coordination between NHTSA, EPA, and Customs;
- the extent to which the importation of nonconforming vehicles has become a commercial operation;
- the extent to which nonconforming motor vehicles can be and are made to conform to emission and safety standards, including applicable certifications by importers and modifiers; and
- the adequacy of Customs enforcement of the provisions governing the importation of nonconforming vehicles and its bonds to ensure that the vehicles are made to conform to applicable federal emission and safety standards.

The Chairman also requested us to examine several legal questions concerning the importation of nonconforming vehicles. We addressed these questions in a GAO opinion (B-217842, July 2, 1986).

Because of the complexity of the three agencies' programs, which is further complicated by their interrelationships, we have presented an overview of the programs and their weaknesses in chapter 2 and provide more detailed information on the individual agency programs in appendixes I, II, and III. Appendix IV provides additional information requested by the Chairman.

We performed work at NHTSA, EPA, and Customs headquarters in Washington, D.C., and at Customs district offices in Baltimore, Maryland, and Houston, Texas. This included (1) obtaining and reviewing NHTSA's, EPA's, and Customs' policies and procedures for monitoring and enforcing the requirements for importing and modifying nonconforming vehicles; (2) examining pertinent legislation and regulations; and (3) interviewing responsible agency officials.

We reviewed a random sample of importers' documentation submitted to NHTSA and EPA for 50 vehicles imported during calendar year 1984. We evaluated the documentation's reasonableness for substantiating that modifications for applicable federal safety and emission standards had been performed. We also reviewed an additional random sample of 30 cases for which NHTSA recommended that enforcement action be taken

against importers in calendar year 1984 to determine (1) the actions recommended to Customs and (2) the reasons for such recommendations. The results of these samples are not projectable to the universes because they were not statistical samples with a high confidence level. They were used to identify the control points in the process, rather than to evaluate program effectiveness. With concern to the extent to which nonconforming vehicles had been modified to conform to federal standards, we also obtained and reviewed various reports, studies, and investigations conducted by DOT, EPA, the National Automobile Dealers Association (NADA), and Mercedes-Benz of North America (MBNA).

We visited EPA's Motor Vehicle Emissions Test Laboratory in Ann Arbor, Michigan. The purpose of our visit was to review this laboratory's policies and procedures for (1) assessing private laboratories' capabilities to test individual modified vehicles' conformity to emission standards and (2) determining modifiers' qualifications to be issued a certificate of conformity that attests to their ability to modify a nonconforming vehicle to meet federal emission standards.

We also visited various automobile manufacturers to obtain their views on the nonconforming motor vehicle importation program. We visited the U.S. headquarters of MBNA in Montvale, New Jersey; BMW of North America, Inc. (BMW), in Montvale, New Jersey; Jaguar Cars, Inc., in Leonia, New Jersey; and Volvo North America Car Operations in Rockleigh, New Jersey. These manufacturers' European models represented the majority of the gray market vehicles imported into the United States. We also visited Ford Motor Company in Dearborn, Michigan, because it imports a vehicle manufactured in Europe. In addition, we interviewed the Executive Director, Automobile Importers Compliance Association (AICA), and the Vice President, Automobile Importers of America, to obtain their organizations' perspectives of the program.

We reviewed files and interviewed various NHTSA and EPA officials to determine the method of award and the costs of contracts awarded by these agencies for services related to the nonconforming motor vehicle program. NHTSA, EPA, and Customs provided us information concerning the estimated staffing levels and costs devoted to the implementation of the program in fiscal year 1985.

In the Customs Houston district office, we examined that office's practices for processing importers' nonconforming vehicle entry documents, bond release letters from NHTSA and EPA, and notices to redeliver that are sent to importers who fail to substantiate their vehicles' conformity to

applicable federal standards. We also obtained and reviewed a report on vehicles seized by that office in fiscal years 1984 and 1985. The Customs Houston district office was responsible for processing about 20 percent of the gray market vehicles imported in 1985.

Our review was conducted from January through December 1985. We discussed our findings with NHTSA's Associate Administrator for Enforcement; EPA's Director, Manufacturers Operations Division; and Customs' Deputy Commissioner and have included their comments where appropriate. However, in accordance with the Chairman's request, we did not obtain the views of these officials on our conclusions and recommendations, nor did we request official agency comments on a draft of this report.

Except as noted above, we made this review in accordance with generally accepted government auditing standards.

Federal Programs Lack the Internal Controls Needed for Regulating Gray Market Vehicles

The NHTSA, EPA, and Customs programs we reviewed lack sufficient internal controls needed for ensuring that gray market vehicles are modified to meet federal safety and emission standards. In addition, the limited scope studies conducted by NHTSA, EPA, and various private industry groups raise questions about the adequacy of the modifications being made to conform these gray market vehicles to the federal standards.

The Gray Market Vehicle Importation Process

The process for importing a gray market vehicle is complex. It begins at the port of entry, where Customs identifies the vehicle as a gray market vehicle because it does not have a certificate that it was manufactured to conform to U.S. safety and emission standards. Customs then requires that the importer post a bond (equal to the value of the vehicle plus duty fees) to ensure that the vehicle will be modified to meet the standards and advises the importer that NHTSA and EPA will provide additional information on the steps required to bring the vehicle into compliance with the standards.

Customs notifies NHTSA and EPA separately of the arrival of the nonconforming vehicle. These agencies each notify the importer of the specific standards to be met and what documents the importer must have completed and returned to them to demonstrate that the vehicle has been successfully modified.

The importer then has the vehicle modified to meet the safety and emission standards and returns the completed documents that NHTSA and EPA require. NHTSA and EPA examine the documents and make separate decisions on whether the vehicle meets the safety and emission standards.

The two agencies separately notify Customs of whether the vehicle has met the standards and direct Customs to either release the bond or initiate enforcement action. Customs does not notify NHTSA and EPA of the action it takes in response to their direction. Enforcement action may be a fine, bond forfeiture, or vehicle destruction or exportation. NHTSA may consider that some safety standards (other than the crashworthiness standards) have not been fully met. In such cases, NHTSA will generally recommend that penalties of a lesser amount be collected by Customs, rather than forfeiture of the full bond.

Manufacturers of vehicles built to meet the U.S. safety and emission standards have pointed out that gray market vehicles do not have to meet the same requirements. These include defect and 5-year/50,000-mile performance warranties, fuel economy requirements, "gas guzzler"

taxes, and defect notification and recall provisions of both the Motor Vehicle Safety Act and the Clean Air Act. Neither are gray market vehicles subject to crash tests to determine compliance with the crashworthiness safety standards. (Since February 1986 the gray market commercial importers have been liable for payment of "gas guzzler" taxes, according to the Internal Revenue Service.)

Weaknesses in the Agencies' Programs

We found problems in each step of the gray market import process. These problems were either in ensuring that the vehicles had been modified to meet the standards or in processing the associated paperwork within and between the three agencies.

Customs

Our visit to the Customs Houston district office, which had the greatest percentage of gray market vehicle imports, disclosed that Customs was experiencing delays in handling the associated paperwork flow with NHTSA and EPA and in initiating enforcement actions. Customs has decentralized its program to its district offices that are responsible for over 300 ports of entry. In addition, Customs had given the gray market vehicle compliance program a lower priority than some of its other programs.

The Customs Houston district office, responsible for processing about 13,000, or 20 percent, of the gray market vehicles imported in 1985, experienced delays and backlogs both in its notifying NHTSA and EPA that gray market vehicles had arrived at the port of entry and in processing the information received from NHTSA and EPA on whether to release the vehicle bonds or to take enforcement action. The district office also experienced delays in initiating enforcement actions.

As of August 20, 1985, the Customs Houston district office had 1,456 entry declarations for vehicles that were as much as 10 months old that had not been forwarded to NHTSA and EPA. Therefore, NHTSA and EPA had not been notified to begin exercising their responsibilities toward these vehicles.

The Customs Houston district office also had 3,896 bond release letters from NHTSA and EPA as much as a year old that had not been entered in the district office's computer system. As a result, the Customs Houston district office may have initiated enforcement actions against importers because they had not provided evidence of satisfactory modification within the allowed time period, when in fact NHTSA and EPA had notified

Customs that they were satisfied that the importers had brought their gray market vehicles into compliance. Although the Customs Houston district office provided us two examples that occurred at the time of our visit, it did not maintain records of the number of such cases.

Further, the Customs Houston district office had a backlog of 1,938 cases as of August 22, 1985, for which it should have sent the importers notices that enforcement actions were being initiated against them. These importers had not, within the prescribed time, provided evidence of conforming the vehicles to the safety or emission standards.

All backlogs were eliminated by the end of 1985. See appendix I for detailed information on the weaknesses in the Customs program and related information.

NHTSA

NHTSA's program does not ensure that imported nonconforming vehicles are modified to meet the safety standards. We found instances where NHTSA's program, which primarily depends on a review of documentation supplied by the importers, is not effective in identifying all nonconforming conditions. NHTSA neither tests the vehicles nor visits the firms that modify the vehicles to ensure that they have the capability to conform the vehicle to the safety standards.

We randomly selected 50 cases to review how NHTSA examines and approves the documentation submitted by importers. In 21 of the 50 cases, the importers had not provided the documentation within the required time frame. (In 1 case the vehicle was exported.) In the remaining 29 cases, NHTSA determined that the vehicles had met the federal safety standards. However, our initial review of the documentation for the 29 vehicles raised questions as to the adequacy and accuracy of the documents to substantiate that the vehicles conformed to the safety standards.

We judgmentally selected 5 of these 29 cases to review in detail the documents supporting the importers' certification that the vehicles had been modified to meet the safety standards. As part of our evaluation, we provided copies of the documentation to the five vehicles' original manufacturers for their comments. On the basis of our review and the manufacturers' comments, we believe that NHTSA accepted incorrect, incomplete, or inadequate documentation to substantiate that each of these five vehicles met all the safety standards.

We also found that as of June 30, 1985, NHTSA had a backlog of about 10,000 unreviewed statements of compliance and supporting documentation from importers. NHTSA applied additional resources to this backlog and, by December 31, 1985, had virtually eliminated it. There was no recurrence of this backlog through August 30, 1986.

See appendix II for detailed information on the weaknesses in the NHTSA program and related information.

EPA

EPA's program does not ensure that all imported nonconforming vehicles are modified to meet the federal emission standards. EPA does not routinely inspect the gray market vehicles but, rather, depends on documentation from EPA-recognized vehicle modifiers or from EPA-recognized laboratories that test vehicles modified by others. In fiscal year 1985, about 90 percent of the documentation provided to EPA was from EPA-recognized testing laboratories, and about 10 percent was from the vehicle modifiers.

EPA recognizes vehicle modifiers on the basis of its tests of prototype vehicle modifications performed by the modifiers. EPA recognizes testing laboratories on the basis of its review of their applications and supporting information on personnel and equipment. EPA accepts documentation supplied by either type of recognized firms as evidence of whether the vehicles have been modified to meet the emission standards. At the time of our review, EPA did not make routine tests or inspections of the firms, other than an initial inspection when recognizing the laboratories and a one-time test of each prototype vehicle modification. However, in September 1985 EPA began inspections of previously recognized testing laboratories, although not on a regular schedule. Between September 1985 and June 30, 1986, EPA reinspected 12 of the 46 recognized laboratories and began action to withdraw recognition from 3.

Using the 50 cases we had randomly selected when reviewing NHTSA's program, we asked EPA for the documentation supplied by the importers with respect to whether the vehicles had met the emission standards. EPA was not able to locate such documentation for 26 of the 50 vehicles. EPA was able to locate and provide us with documentation to show that its requirements had been satisfied in the remaining 24 cases. As of April 1986 EPA had instituted internal control procedures to track the progress of each case.

See appendix III for detailed information on the weaknesses in the EPA program and related information.

Indications That Gray Market Vehicles Do Not Meet All Safety and Emission Standards

Government studies and industry surveys conducted since 1983 indicate either that substantial percentages (from 50 to 95 percent) of imported nonconforming vehicles had not been modified to meet the federal safety and emission standards or that the modifications that had been made were not adequate. We did not examine the adequacy of the scope or the methodology used in these studies and surveys to determine their accuracy or whether their results may be projected to the universe of gray market vehicles. We do, however, believe that the results of these studies are an indicator of potential problems in the implementation of the gray market program as a whole.

Transportation Systems Center Study

In May 1985 DOT's Transportation Systems Center, Research and Special Programs Administration, issued a study entitled Safety Inspection of Foreign Vehicles. From its review of 63 vehicles, the Center found that 24 were not in full compliance with one or more of 12 different safety standards or regulations, including those for door locks and door retention components, windshield mounting, and seat belt retractors.

NHTSA's Inspection and Test of Two Vehicles

In February 1985 NHTSA negotiated a contract to purchase, inspect, and crash-test two randomly selected vehicles, purchased from independent commercial importers, to evaluate the importers' certifications that the vehicles conformed with all applicable safety standards. The crash tests were to evaluate whether the vehicles met the crashworthiness standards. In April 1985 the contractor reported that one vehicle did not conform with eight safety standards and the other did not conform with nine standards.

EPA's Study of Imported Vehicles in California

In 1984 EPA, in cooperation with the California Air Resources Board, had 27 gray market vehicles tested in California for compliance with the federal emission standards. Only 1 of the 27 vehicles was found to pass all the emission test requirements. The importers of these vehicles had previously had them tested by an EPA-recognized test laboratory and had test results showing that they met the federal emission standards.

Mercedes-Benz Survey

MBNA issued a report on May 14, 1986, on the results of a survey it conducted during the 18-month period from December 1983 through May 1985. MBNA asked its dealers to inspect and report on the modifications to each nonconforming vehicle brought in for service. The dealers performed no testing of the modified vehicles but rather made "simple visual inspections" to determine whether a particular required feature had been installed. The report was based on 1,114 dealer survey reports. MBNA's survey indicated that 95 percent of the vehicles failed to comply with all applicable federal safety and emission requirements.

**National Automobile
Dealers Association Survey**

NADA issued its Gray Market Vehicle Survey Results in January 1985. During 1984 NADA sent a questionnaire to its member dealers requesting information concerning the adequacy of modifications for safety and emission requirements on gray market vehicles. It received 393 responses. The responses showed that 82 percent of the vehicles were missing equipment relating to at least one safety standard. In addition, up to 53 percent were missing emission control equipment.

Proposed Legislation

Problems in the gray market vehicle program that pertain to compliance with NHTSA safety standards were addressed by proposed legislation. During the 99th Congress, the Senate and House of Representatives passed bills (S. 863 and H.R. 2248) tightening controls to ensure modification of gray market vehicles to meet safety standards. The Congress adjourned before final action was taken on the proposed legislation. We believe that both bills had considerable merit since they addressed some of the NHTSA program control problems we identified and would have made the NHTSA gray market program more efficient and effective.

While the provisions of these bills differed, their approaches were similar. Both restricted who could import nonconforming vehicles and established eligibility controls over which nonconforming vehicles could be imported. In addition, both bills directly addressed NHTSA's lack of assurance that the vehicles it approved for import had been modified to meet the safety standards. They required NHTSA, through tests and inspections, to provide greater assurances that gray market vehicles would be properly modified to meet the safety standards.

The bills would have provided for the

- registration of commercial gray market vehicle importers who would be subject to requirements similar to those imposed on manufacturers of automobiles manufactured for and imported to the United States;
- registration of gray market vehicle modification facilities;
- listing of vehicle makes and models, eligible for importation and modification, that are capable of being readily modified to meet the safety standards;
- inspection and testing of vehicles and modification facilities; and
- requiring of other importers of the listed vehicles to have the vehicles modified by the registered vehicle modification facilities.

Under the House bill, with limited exceptions, only registered commercial importers could have imported gray market vehicles and only designated vehicles, which could have been readily modified to meet the safety standards, would have been eligible for importation. The Senate bill, while more flexible on who could import a gray market vehicle—members of the uniformed services or the foreign service returning from overseas assignments—also required registration and inspection of modification firms and periodic NHTSA testing of vehicles that modifiers would have certified as in compliance with all safety standards.

Neither of the bills addressed EPA's enforcement of the emission standards. Neither required EPA to periodically (1) inspect modification firms that bring gray market vehicles into compliance with emission standards or (2) test the vehicles that are represented to have been modified to comply with such standards. EPA has administratively established requirements for the inspection of laboratories and has begun to monitor these laboratories through reinspection. EPA does not, however, test gray market vehicles for compliance with emission control standards.

Conclusions

In calendar year 1985, gray market vehicle imports appeared to have reached their peak with about 66,900 imports. Through the first half of calendar year 1986, only about 15,500 gray market vehicles had entered the country, and industry forecasts are that, given the strength of the U.S. dollar in the foreign market, the downward trend will continue. This situation could change as the strength of the dollar shifts. Regardless of the gray market vehicle import level, the gray market program as now operated does not, in our opinion, have sufficient controls to ensure that the vehicles are being modified to meet federal safety and emission standards.

We believe that the three principal agencies can revise their programs to more effectively and efficiently use their resources to ensure that gray market vehicles are properly modified. For example, we recognize that NHTSA cannot inspect or test every vehicle to satisfy itself that the modifications being made are adequate to meet the performance level requirements. NHTSA could, however, eliminate the paperwork reviews and adopt a program similar to EPA's for recognizing vehicle modification firms. More specifically, NHTSA could accept certificates provided by firms that it has determined to be capable of modifying the vehicles to conform to the safety standards. Such a program, however, should also provide for inspections and testing of samples of both the firms and the vehicles they modify. In considering the appropriate scope, frequency, and amount of testing, NHTSA should take into account factors such as staffing constraints as well as the safety standards for which compliance testing is technically practical and cost-effective.

While EPA's program has more internal controls, it could also be strengthened by providing for both inspection and testing of the EPA-recognized vehicle modification and emissions testing firms, as well as for testing the vehicles they have modified. Again, we recognize that this program could not be accomplished on each firm and vehicle. However, it could be implemented through a valid statistical sampling approach. In considering the scope and amount of testing, various factors should be taken into account, including staffing constraints and the costs of such testing.

During the 99th Congress, the Senate and House of Representatives passed bills that would have tightened controls to ensure that gray market vehicles would be modified to meet safety standards. The Congress adjourned before final action was taken on the proposed legislation. These bills (S. 863 and H.R. 2248) addressed many of the safety standard enforcement problems we identified. We believe that both bills had considerable merit since they addressed the major NHTSA program problems we identified.

However, neither of the bills addressed EPA's enforcement of the emission standards, nor did either lessen the continued need for the three agencies to coordinate their efforts closely in order to ensure an efficient and effective program. Customs, NHTSA, and EPA officials generally concurred in the weaknesses that we identified in their programs and agreed that action is needed to strengthen or modify their respective programs.

Recommendations

We recommend that the Secretary of Transportation direct the Administrator, NHTSA, to improve controls over its program by establishing a process similar to EPA's program, whereby firms are recognized by NHTSA, through certification, as being capable of modifying gray market vehicles. In addition, NHTSA should periodically reinspect these firms and consider testing a sample of modified vehicles as a check on the firms' performance in ensuring vehicle compliance with the safety standards. In considering the appropriate scope, frequency, and amount of testing, NHTSA should take into account factors such as staffing constraints as well as the safety standards for which compliance testing is technically practical and cost-effective.

We recommend that the Administrator, EPA, improve EPA's controls over its program by periodically inspecting both the modifying firms and test laboratories that have been previously recognized and consider testing the vehicles, on a sample basis, to ensure compliance with federal emission standards. In considering the scope and amount of testing, various factors should be taken into account, including staffing constraints and the costs of such testing.

Customs' Gray Market Vehicle Enforcement Program

Customs plays a major role in enforcing NHTSA's and EPA's regulations pertaining to importing nonconforming vehicles. Importers may import gray market vehicles through any one of more than 300 ports of entry. Customs has experienced backlogs of entry declarations for nonconforming vehicles and delays in processing both bond release letters from NHTSA and EPA and redelivery notices to importers who have failed to provide documentation to NHTSA and EPA.

Description of Customs Responsibilities

Customs' Director, Office of Cargo Enforcement and Facilitation, Office of Inspection and Control, told us that centralized data and records relating to how Customs has performed its responsibilities for the nonconforming motor vehicle program, in part in behalf of NHTSA and EPA, are not available at Customs headquarters. Each district office maintains files on those vehicles imported through ports of entry under its jurisdiction.

Under Customs regulations, district directors may initiate enforcement actions against importers who fail to substantiate that their vehicles have been modified to conform with federal safety and emission standards within the allowed times. Generally an imported vehicle must conform to all federal safety and emission standards that were in effect on the date of its manufacture. If the vehicle was not originally manufactured for export to the U.S. market, it will lack labels certifying that it was manufactured in accordance with all applicable federal safety and emission standards. With these labels Customs does not have to make a detailed inspection to ascertain that it is a nonconforming gray market vehicle.

Customs enforcement efforts on behalf of NHTSA and EPA are, in part, accomplished through its regular inspection and control functions. This enforcement effort generally consists of enforcing compliance with the admissibility requirements by

- inspecting imported vehicles for proper certification labels,
- checking entry documents to see that NHTSA and EPA declaration forms are completed, and
- forwarding the completed forms to NHTSA and EPA.

Customs must promptly forward the entry forms to NHTSA and EPA so that NHTSA can advise the importers of the procedures that must be followed in substantiating that their vehicles have been modified and EPA can begin its regulatory process.

Customs releases imported nonconforming motor vehicles to their importers before they meet the admissibility requirements. However, importers must post a performance bond, which guarantees that the requirements will be met. When NHTSA and EPA approve the documentation submitted by the importers to substantiate that their vehicles have been modified to conform to safety and emission standards, the agencies, by letter, notify the director of the Customs district where the vehicle entered the United States and give approval for release of the importer's performance bond.

Until February 1986 Customs conducted its enforcement program under regulations it had issued jointly with NHTSA and EPA. The procedures followed until February 1986 are described below. The revisions to the program, as discussed later, reduce the Customs enforcement role.

The joint regulations issued by NHTSA and Customs provide that if Customs does not receive a bond release letter from NHTSA within 180 days after the vehicle's entry, the district director should issue a notice requiring the importer to deliver the vehicle to Customs. The joint regulations issued by EPA and Customs are similar, allowing 90 days or such additional time as the Customs district director may allow for good cause. If the vehicle is not delivered to Customs within the time allowed, liquidated damages are generally assessed in the full amount of the importer's bond.

In an August 9, 1985, notice to the various Customs field offices, the Assistant Commissioner, Office of Commercial Operations, provided new written instructions for seeking redelivery of vehicles that had not been conformed to federal safety and emission standards. The notice stated that if the district director had not received timely notice of compliance, the district director must demand the exportation or destruction of the nonconforming vehicle. If the importer does not export or destroy the vehicle, the district director must demand liquidated damages in the amount of three times the vehicle's value or the full amount of the bond, if that is less.

After damages are assessed, the importer may submit a petition for mitigation of damages. The petition should contain the facts and circumstances the importer relied on to justify the action taken. Although the Secretary of the Treasury may cancel or mitigate damages, it is Customs policy to seek and follow NHTSA's and EPA's recommendations regarding mitigation. Importers who elect to pay these damages may operate the

vehicles on the nation's highways, even though they may not meet all federal safety and emission standards.

Customs may seize vehicles for nonconformance to federal safety and emission standards or for other reasons. In an October 16, 1985, letter to us, the Customs Deputy Commissioner told us that in fiscal years 1983, 1984, and 1985 (through August 1985), Customs seized 9,481, 9,347, and 8,990 vehicles, respectively. The Deputy Commissioner stated in his letter that approximately 5 percent of the total seizures were for violations of federal safety and emission standards.

Most vehicles are seized by Customs as a result of investigations involving other illegal activities, such as conveyance of narcotics, counterfeiting, and importing stolen vehicles. During our visit to the Customs Houston district office, we obtained a report on vehicle seizures for fiscal years 1984 and 1985 (through August 21, 1985). That report showed that in fiscal year 1984, the Customs Houston district office seized four vehicles—two of which were for violations of federal safety and emission requirements. Of the 11 vehicles seized during the first 11 months of fiscal year 1985, only 1 was seized for violations of federal safety and emission requirements (false declarations).

Customs Enforcement Practices for Imported Foreign Vehicles at Port of Houston

Customs district offices have discretionary authority to administer the program. Therefore, we were unable to make agency-wide observations on Customs administrative practices involving the importation of nonconforming vehicles. However, our visit to the Customs district office and port of entry at Houston, Texas, provided insight into Customs practices concerning Customs enforcement of requirements for gray market vehicles because this district office processed the single largest percentage of such imports.

Our review showed that the number of imported gray market vehicles processed through the Customs Houston district office grew from about 8,500 in 1984, or about 23 percent of all such vehicles, to approximately 13,000 in 1985, or about 20 percent of the total. By August 1985 the Customs Houston district office had a backlog of entry declarations for 1,456 nonconforming motor vehicles dating back to October 1984 (10 months) that it had not forwarded to NHTSA and EPA. Therefore, NHTSA and EPA had not been notified to begin exercising their responsibilities toward these vehicles.

In addition, the Customs Houston district office had a backlog of 3,896 bond release letters (1,287 from NHTSA and 2,609 from EPA dating back to November and August 1984, respectively) that it had not processed. As a result, the Customs Houston district office may have initiated enforcement actions against importers although NHTSA and EPA had notified Customs that they were satisfied that the importers' gray market vehicles had been brought into compliance with the federal standards.

The Customs Houston district office also had a backlog of cases in which Customs should have sent the importers notices to return the vehicles to Customs or export them. These importers had not, within the prescribed time, provided evidence of conforming the vehicle to the safety or emission standards. There were 1,938 such cases as of August 22, 1985. Customs instructions in effect at that time were that such notices should be sent 210 days after the vehicle had been imported.

**Delays in Processing
Imported Vehicle
Documents**

Our review showed that the Customs Houston district office had a large backlog of entry documents for imported nonconforming vehicles that had not been forwarded to NHTSA and EPA. A Supervisory Import Specialist and an Import Specialist at the Customs Houston district office advised us that the district office normally forwards all NHTSA and EPA forms to the respective agencies once a week. They also told us that after the imported vehicle arrives at the port, the importer has up to 3 days to complete the required declarations and it normally takes between 2 to 7 days to receive the completed forms from the Houston port.

As of August 20, 1985, the entry documents for 1,456 imported vehicles, dating back as much as 10 months, had not been forwarded to NHTSA and EPA. The age of this backlog is shown in table I.1.

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Customs' Gray Market Vehicle
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**Table I.1: Nonconforming Motor
Vehicles With Unprocessed Entry
Declarations as of August 20, 1985**

Month of entry	Number of vehicles
October 1984	1
November 1984	1
January 1985	2
February 1985	3
March 1985	14
April 1985	78
May 1985	67
June 1985	374
July 1985	586
August 1985	330
Total	1,456

Source: GAO compilation of data at the Customs Houston, Texas, district office.

The Customs Houston district office employees responsible for processing the forms told us that data from each form are entered in the district office's tracking system before the form is forwarded to NHTSA and EPA. The backlog of entry declarations shown in table I.1 had not yet been entered in the tracking system.

**Delays in Processing Bond
Release Letters and Notices
to Redeliver**

At the Customs Houston district office, we found that 3,896 NHTSA and EPA bond release letters had not been entered into the Customs tracking system as of August 20, 1985. Customs bond regulations, which became effective February 18, 1985, require that redelivery notices be sent to importers for whom bond release letters have not been received from NHTSA and EPA within 210 days after the imported vehicles entered the United States. Therefore, it is essential that NHTSA and EPA bond release letters be promptly entered into the tracking system when received from NHTSA and EPA so that Customs will not issue the importer an erroneous redelivery notice.

The Customs Houston district office's Fines, Penalties, and Forfeiture Officer told us that his office had sent notices of redelivery to importers and later learned that NHTSA and EPA had previously notified the district that the importer's bond could be released. For example, on June 7, 1985, the Customs Houston District Director issued a combined notice of redelivery and demand for payment of liquidated damages of \$2,800 to an importer. The individual had entered a nonconforming vehicle through the Houston port on May 24, 1984. NHTSA and EPA had notified the District Director on December 19, 1984, and January 15, 1985,

respectively, that their obligations against the bond could be released. In an August 20, 1985, letter to the importer, the Houston District Director acknowledged receipt of the NHTSA and EPA bond release letters and advised the importer that Customs' demand for redelivery of the vehicle and payment of liquidated damages had been cancelled.

On August 22, 1985, the Houston Customs district office issued 21 combined notices to redeliver and demand for payment of liquidated damages to importers for failure to substantiate that their vehicles had been conformed to safety and/or emission standards. Between 65 and 351 days had elapsed after the 210-day deadline until the issuance of these notices.

Eleven of those notices were for failure to substantiate conformance only to safety standards, two were for failure to substantiate conformance only to emission standards, and eight were for failure to substantiate conformance to both safety and emission standards. NHTSA furnished us information showing that it had notified Customs earlier that its obligation against the importers' bonds for six of these vehicles could be released. NHTSA's bond release letters for those six vehicles were dated between October 26, 1984, and August 15, 1985. We did not determine whether EPA had notified Customs before issuance of these notices that its obligation against the 10 importers' bonds could be released.

Table I.2 shows the large number of bond release letters at the Customs Houston district office that had been received from NHTSA and EPA but that had not been entered into the Customs tracking system as of August 20, 1985.

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**Table I.2: NHTSA and EPA Bond
Release Letters Not Entered into the
Customs Tracking System as of August
20, 1985**

Date of bond release letter	Months elapsed	Number of NHTSA letters	Number of EPA letters
August 1984	12	•	1
September 1984	11	•	1
October 1984	10	•	3
November 1984	9	3	11
December 1984	8	3	25
January 1985	7	6	72
February 1985	6	21	214
March 1985	5	73	181
April 1985	4	114	258
May 1985	3	226	592
June 1985	2	240	511
July 1985	1	350	528
August 1985	Under 1	251	208
Date not determinable		•	4
Total		1,287	2,609

Source: GAO compilation of data at the Customs Houston, Texas, district office.

In an August 23, 1985, meeting with the Customs Houston district office's Assistant District Director, Classification and Value, we presented our observations on that office's backlogs of entry declarations and bond release letters. After acknowledging the backlogs, he said that the office planned to assign additional staff and authorize overtime to the extent needed to eliminate these backlogs. He said that this may be a temporary solution because of the district office's position that the non-conforming motor vehicle program be assigned a lower priority than other activities, such as smuggling, child pornography, the exportation of high technology, and the importation of certain steel products. The backlog was eliminated by the end of 1985.

**Nonresidents Sell
Noncomplying Vehicles
in the United States**

Customs regulations permit nonresidents to import noncomplying vehicles without modifying them to conform with applicable federal emission and safety standards under certain conditions. The sale of vehicles by nonresidents has been identified by NHTSA, EPA, and Customs as a potential problem in the program's implementation.

Nonresidents, generally, are not required to post a bond. The nonresident importers must, however, complete both NHTSA and EPA motor

vehicle declaration forms. These forms require that the nonresident declare

"I am a nonresident of the United States and am importing the merchandise for personal use for a period not to exceed 1 year from the date of entry and I will not sell it within the United States."

During 1985 NHTSA received 571 nonresident declarations to enter nonconforming vehicles. Customs headquarters and district office officials advised us that they were not aware of the extent to which nonresidents sell their noncomplying vehicles to individuals in the United States. Customs does not have a system to determine whether these vehicles are exported within a year.

During our visit to the Customs Houston district office, we inquired whether the district was experiencing problems with nonresidents selling nonconforming vehicles in the United States. The Fines, Penalties, and Forfeitures officer told us that although they do not have a tracking system to monitor nonresidents' vehicles, they do from time to time follow up on any cases that come to the district office's attention and seek penalties from the importer and/or the purchaser of such vehicles.

Proposed Changes in Customs' Enforcement Role

Customs prepared a document entitled Briefing Paper—Importation of Automobiles in January 1984, which stated that Customs was experiencing several problems enforcing NHTSA's and EPA's regulations for gray market vehicles. Customs said that (1) lengthy response times from everyone concerned were slowing the processing time, (2) large backlogs of these cases were common at major ports, and (3) claims for redelivery of the imported vehicles and the assessment of liquidated damages against importers for vehicles entered under bond were taking too much time in Customs offices.

In letters dated June 5, 1985, to the NHTSA Administrator and the EPA Assistant Administrator for Air and Radiation, the Deputy Commissioner of Customs stated that their respective agencies were faced with a proliferation of nonconforming vehicle imports and resultant paperwork. The Deputy Commissioner stated that in an effort to speed up the paperwork and conformity process, Customs was prepared to change the procedures for handling imports. Customs proposed to extricate itself from the "middleman role" that has resulted from the use of a Customs entry bond to ensure conformance with federal safety and

emission requirements. More specifically, the Deputy Commissioner proposed that NHTSA and EPA assume responsibility for the issuance of redelivery notices to the importers. Further actions to have the importer substantiate conformance of his vehicle would be between NHTSA and EPA and the importer.

In a reply dated July 2, 1985, the NHTSA Administrator sympathized with Customs' desire to change the import procedures and to eliminate Customs' middleman role. The NHTSA Administrator stated that the problem should not be approached through temporary measures such as proposed by Customs. Instead, the Administrator recommended that a comprehensive review of this matter be conducted at the staff level directed toward appropriate changes in the joint regulations designed to alleviate the administrative burdens on both agencies.

Similarly, in a reply dated July 16, 1985, EPA's Acting Assistant Administrator for Air and Radiation stated that he agreed with the goal of speeding the process and eliminating useless tasks. He stated that EPA was working on new regulations that may radically change the process. In addition, the purpose of the proposed regulations was to focus on enforcement and eliminate or greatly reduce routine administrative duties, and EPA did not agree that it should send out redelivery notices. It would appear inefficient and confusing to importers to get two notices, one from NHTSA and one from EPA.

On September 11, 1985, NHTSA, EPA, and Customs representatives met to discuss the revisions proposed by Customs. A Customs memorandum of the meeting pointed out that discussion centered upon Customs' proposal that NHTSA and EPA generate the redelivery notice simultaneously with their notice of noncompliance to the importer. The memorandum noted that EPA could not do this because it does not have a tracking system for imported noncomplying vehicles. EPA relies solely on Customs' redelivery notice and liquidated damage notice to the importer.

On February 18, 1986, Customs unilaterally made the following changes in its enforcement program:

- issues a notice, effective 180 days from the date of entry, demanding redelivery within 30 days if the vehicle has not been brought into compliance with the safety and emission standards;
- requires that all requests for extension of time or mitigation of penalties be directed to NHTSA and EPA; and

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- takes no further enforcement action unless directed by NHTSA and EPA to do so.

The Deputy Commissioner, Customs, advised us that under the new procedures, if Customs has not heard from NHTSA or EPA within a year after the vehicle was imported, Customs will release the importer's bond on the assumption that the vehicle has met the safety and emission standards. This means that Customs is expecting only negative feedback from NHTSA and EPA. That is, the agencies have a year to let Customs know in cases where the importer has failed to modify the vehicle to meet the safety and emission standards. This puts the pressure on NHTSA and EPA to complete their process on a timely basis.

NHTSA's Program for Ensuring That Gray Market Vehicles Conform to Federal Safety Standards

NHTSA does not routinely test or inspect gray market vehicles. Instead, it performs a desk review of the importer's entry declaration and supporting documentation of vehicle conformance to applicable safety standards. However, our review indicated that NHTSA accepted importers' documentation that was incorrect, incomplete, and inadequate. In addition, government tests and industry surveys of safety modifications made to imported nonconforming vehicles raised concerns about the adequacy of those modifications in achieving compliance with the safety standards.

NHTSA's Program, Procedures, and Requirements

NHTSA decides whether gray market vehicles conform to the safety standards on the basis of its analysts' desk review of the importers' entry declaration and supporting documentation. NHTSA's Chief, Verification Division, Office of Vehicle Safety Compliance (OVSC), said that the desk review usually takes 15 to 20 minutes.

The importer states that the nonconforming vehicle will be brought into conformity, to be evidenced by a statement of compliance submitted by the importer. The statement of compliance is due within 120 days of the vehicle's entry or such additional time (not to exceed a total of 180 days) as NHTSA may allow. The importer also agrees to observe the NHTSA requirement that the vehicle not be sold until the bond posted to ensure modification of the vehicle to all applicable standards has been released.

The importer is sent instructions describing the specific standards applicable to the vehicle and a statement-of-compliance form to be used by the importer to substantiate that the vehicle conforms to all applicable individual standards as originally manufactured or as modified. Material to support the compliance statement—such as vouchers and receipted work orders, photographs, mathematical calculations, and diagrams—should be attached to the importer's statement of compliance.

Eight of the 36 federal safety standards for passenger vehicles are referred to as crashworthiness standards. These standards contain critical occupant survivability requirements. Samples of models manufactured for sale in the American market are crash-tested to determine if they meet the requirements for these standards. Obviously, gray market vehicles cannot be individually crash-tested to determine whether they meet the requirements of the crashworthiness standards. Therefore, the importers provide NHTSA with engineering data and mathematical calculations, regarding the design and installation of structural modifications,

to establish that the vehicles have been modified to meet the performance levels required by the crashworthiness standards.

NHTSA's analysts perform a desk review of the importer's statement of compliance and supporting documentation to evaluate their adequacy to demonstrate conformance of the imported vehicle to applicable safety standards, either as originally manufactured or as modified. The analysts may determine that a statement of compliance and supporting documentation does not conclusively demonstrate that the vehicle conforms to all applicable safety standards. In such cases, NHTSA generally asks the importer for additional information. After examining any additional information from the importer, NHTSA makes its recommendation to the Customs district office on the disposition of the case. If NHTSA is not satisfied with the documentation, it may recommend that Customs (1) seek redelivery of the vehicle or (2) impose damages ranging from forfeiture of the full bond to lesser mitigated damages based on NHTSA's view that the vehicle is in "substantial" conformance with applicable standards. Customs does not generally advise NHTSA of its enforcement actions in individual cases.

The schedules of damages for individuals and commercial importers differ. For individuals, NHTSA's schedule provides for damages as low as \$25 for each standard to which the vehicle is not conformed (to a maximum of \$250). Up to \$200 may be added if the importer is more than 12 months late in filing his statement of compliance. However, if the individual does not file a statement of compliance to substantiate that the vehicle conforms to the specific crashworthiness standards and the vehicle cannot be exported, NHTSA may recommend damages of 25 percent of the bond, but not less than \$350. If a commercial importer does not substantiate a vehicle's conformance to the crashworthiness standards, NHTSA may recommend damages as high as the full value of the bond, with a minimum of \$600.

In those cases where the importer fails to submit a statement of compliance to substantiate a vehicle's conformance to other than the crashworthiness standards, NHTSA may recommend that Customs assess damages ranging from 5 percent to 25 percent of the bonds posted. The exact percentage depends on (a) the vehicle's age, (b) the safety standards for which conformance has not been demonstrated, and (c) whether the vehicle is for personal use or resale.

If the importer sells the vehicle before NHTSA has determined that the vehicle conformed to the safety standards, NHTSA can recommend that

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Market Vehicles Conform to Federal
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Customs seek redelivery of the vehicle. If the importer requests mitigation of these damages, NHTSA may recommend mitigation to Customs.

NHTSA estimated that as of June 30, 1985, it had a backlog of about 10,000 unreviewed statements of compliance and supporting documentation. In September 1985 NHTSA began temporarily assigning additional analysts to review the importers' documents while it considered revisions to its program. According to the Chief, Verification Division, OVSC, the backlog represented about a 10- to 12-week work load for the analysts who reviewed these documents. The Chief told us that, as of October 21, 1985, the backlog had been reduced to about 4,000—a 4- to 6-week work load—and as of December 31, 1985, the backlog had been eliminated. This backlog had not recurred through August 30, 1986.

NHTSA recommended that Customs assess liquidated damages in 2,225 cases in 1984. We randomly selected 30 of those cases for review to determine the specific actions recommended by NHTSA. Our review showed that NHTSA recommended that Customs seek redelivery of the vehicles in 25 of the 30 cases because the importer had not submitted documentation to substantiate that modifications had been made within the 120 days allowed by NHTSA regulations. In the five remaining cases, NHTSA recommended specific liquidated damages. Information on the enforcement action taken in specific cases was not available in NHTSA's files.

NHTSA's recommendation for liquidated damages in one case was made to Customs within the 120-day period allowed for the importer to supply the documentation. The other 29 recommendations were made from 103 to 837 days after the 120-day period had expired, as shown in table II.1.

Table II.1: Time Taken to Make Recommendations After the 120-Day Period

Range beyond 120 days	Number of cases
103 to 180 days	1
181 to 365 days	5
366 to 730 days	19
731 to 837 days	4
Total	29

Note: In only one of the 29 cases did the importer ask for and receive a 60-day extension to the 120-day period for submitting the statement of compliance.

**Gray Market Vehicles
 Not Effectively
 Regulated**

NHTSA's program does not ensure that all imported nonconforming vehicles are modified to meet federal safety standards. We randomly selected 50 vehicle cases at NHTSA to review how NHTSA examines and approves the documentation submitted by importers. The vehicles entered the country in calendar year 1984 through 13 Customs ports of entry. The sample included 24 different models from model years 1971 to 1985.

In 29 of the 50 cases, NHTSA analysts determined that the importers had demonstrated that the vehicles met the federal safety standards. However, we made a detailed review of five of these cases to examine the adequacy of the NHTSA reviews and found that none of the five met all the standards. In addition, in 20 of the 50 cases, the importers had not provided the statement of compliance and supporting documentation to NHTSA within the required time period, and 1 of the 50 vehicles was exported.

**Extent of Compliance as
 Originally Manufactured**

A federal motor vehicle safety standard is applicable to vehicles manufactured on or after the effective date of the standard. From 1968 to July 1985, when we reviewed our sample of 50 cases, the number of safety standards applicable to passenger vehicles had increased from 22 to 36. Our review of the 29 vehicles in our sample for which documentation had been provided found that the vehicles conformed to between 21 and 36 of the standards as originally manufactured and required modifications to conform with between 7 and 13 standards, as shown in table II.2.

Table II.2: Number of Federal Safety Standards to Which Sampled Gray Market Vehicles Conformed as Originally Manufactured

Number of vehicles	Range of standards	
	Conformed with	Requiring modification
19	21 to 25	11 to 13
9	26 to 30	7 to 10
1*	31 to 36	•
29		

*This was a domestic vehicle being returned to the United States that had been originally manufactured to conform with all applicable safety standards.

Source: GAO analysis.

**NHTSA Accepted Incorrect,
Incomplete, or Inadequate
Documentation**

Our initial review of the documentation furnished by the 29 importers raised questions as to the adequacy and accuracy of the documents to substantiate that their vehicles conformed with applicable safety standards as originally manufactured or modified. NHTSA had reviewed the documentation for these vehicles, determined that it was sufficient to demonstrate conformance with applicable standards, and notified Customs that the importers could be released from all liability under the bonds posted to ensure that the vehicles would be conformed.

To evaluate NHTSA's review of the importers' documentation, we selected 5 of the 29 cases for detailed review. NHTSA had furnished information to these importers that indicated that between 33 and 35 safety standards were applicable to these 5 vehicles. We found that these vehicles required modifications to conform with between 9 and 11 standards and conformed with between 23 and 30 standards as originally manufactured. As a part of our evaluation, we provided copies of the importers' documentation to the five vehicles' original manufacturers for their comments.

On the basis of our review and the manufacturers' comments, we believe that NHTSA accepted incorrect, incomplete, or inadequate documentation to substantiate the conformance of each of these five vehicles to some applicable standards. We met with the Chief, Verification Division, OVSC, to obtain NHTSA's basis for accepting the importers' comments or documentation to substantiate that their vehicles conformed to those standards where our review or the manufacturers' raised questions. He told us that the same type of omissions identified in the examples are generally noted by the analysts and additional information is requested from the importers.

The chief also said that the analysts often consciously accept some deviations and questionable statements by the importers. Many requirements of the federal safety standards, according to the chief, do not individually justify Customs and NHTSA's time and effort to pursue with the importers when their statements of compliance appear questionable or incorrect. OVSC accepts importers' statements of compliance even though they may contain minor discrepancies or deviations.

The chief said that the analysts must use judgment in deciding whether to accept the importers' statements. Before the analysts seek clarification of the documentation submitted or request additional documentation, the analysts consider whether the importers appear to have made a reasonable effort to bring their vehicles into substantial conformance

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with the federal safety standards. However, NHTSA had not established written guidelines for the analysts' use in deciding whether one or more noted deficiencies are serious enough to justify rejection of an importer's statement. The analysts' supervisor stated that he does not have time to routinely review all the decisions made by the analysts.

Table II.3 shows the reasons for and the number of standards for which the importers' documentation was questioned by GAO and the manufacturers. Following table II.3, cases are presented to illustrate the reasons why the vehicles' conformance with standards was questioned. Where applicable, comments of the Chief, Verification Division, are included.

Table II.3: Reasons for and Number of Standards for Which Conformance Was Questioned by GAO and Manufacturers

Reasons for questioning conformance to standards	Number of standards					Total
	Case 1	Case 2	Case 3	Case 4	Case 5	
Accepted incorrect claim that vehicle conformed as manufactured	2	6	8	1	4	21
Failed to require modification after noting nonconformance	•	1	•	•	2	3
Accepted modifications without assurance of conformance to standards	1	•	•	2	1	4
Manufacturer stated modified vehicle's conformance cannot be determined from documentation	2	6	4	•	2	14
Incorrect claim of standard's inapplicability not questioned	1	•	•	•	1	2
Total	6	13	12	3	10	44

Source: GAO's and manufacturers' analyses of importers' documentation.

Incorrect Claim That Vehicle Conformed as Originally Manufactured

The importer certified that the vehicle conformed, as originally manufactured, to the hydraulic brake system standard that requires a red light on the instrument panel that lights in the event of a brake system failure. The NHTSA analyst did not question the importer's certification.

However, in its July 15, 1985, letter to us, the manufacturer stated that this make and model year vehicle did not comply with the standard as originally manufactured. When we questioned the Chief, Verification Division, OVSC, he agreed that technically the vehicle may not conform to this provision of the standard as originally manufactured.

**Vehicle Did Not Conform but
NHTSA Did Not Require Its
Modification**

An importer certified that the vehicle conformed, as originally manufactured, to the provision of the theft protection standard that requires that a vehicle be equipped so that a warning device will be activated whenever the key is left in the locking system and the driver's door is opened. The manufacturer stated in its July 1985 letter to us that no warning device was activated in the vehicle as originally manufactured. The NHTSA analyst had noted this deficiency in his original review of the importer's statement but did not require any corrective action by the importer or seek additional support that the vehicle conformed to the standard.

**Modification Accepted Without
Assurance That the Modifications
Were Adequate**

The importer certified that the vehicle, as modified, conformed with the fuel system integrity standard. The standard requires that the fuel system must prevent loss of fuel at a rate greater than 1 ounce per minute after a front barrier collision test at 30 miles per hour. In addition, in a rollover test following the impact test, the fuel loss shall not exceed a total of 5 ounces for the first 5 minutes of testing at each 90-degree increment of the test. The importer indicated that the vehicle met the standard through the installation of a rollover valve. The manufacturer told us that compliance with this standard can be determined only by crash tests and that the installation of a rollover valve by itself is not sufficient to conform the vehicle to the standard.

The NHTSA analyst told us that the critical part of the standard can be met by the installation of a rollover valve. He added that the installation of a rollover valve—which is designed to limit fuel spillage during and after crashes—is the only modification required of this manufacturer's vehicles to conform them to the fuel system integrity standard.

The Chief, Verification Division, OVSC, supported the analyst's position. The Chief said that European models and the models certified for sale in the United States are basically the same structurally. He said that the only difference is that the fuel line on the European models is vented to the atmosphere. He said that it is OVSC's position that the European model vehicles can be conformed to the standard by installing a rollover valve. However, he agreed that European models' conformance to the standard—as modified—can be actually verified only by crash tests.

**Compliance With Standard
Through Modification Cannot Be
Determined**

The importer certified that the vehicle, as modified, conformed with the standard for side door strength. The standard specifies strength requirements for side doors to minimize the safety hazard caused by intrusion

into the passenger compartment in a side impact accident. NHTSA accepted the importer's statement. However, the manufacturer, in its reply to us, stated that, according to the standard, compliance can be determined only by crash testing.

Importer Claimed Inapplicability of Standards

The importer indicated that the standard for windshield zone intrusion did not apply to his vehicle. However, the manufacturer said that the standard actually did apply. The standard regulates the intrusion of vehicle parts from outside the occupant compartment into a defined zone in front of the windshield during a frontal barrier crash test. The NHTSA analyst did not question the importer's position.

Studies of Safety Modifications Made to Imported Nonconforming Vehicles

DOT, MBNA, and NADA had conducted four studies since 1983 of the modifications made to nonconforming vehicles. These studies raised questions about the adequacy of such modifications to bring the vehicles into compliance with the federal safety and emission standards. The portions of the studies addressing safety standards are discussed below. Those addressing emission standards are discussed in appendix III.

DOT's Transportation Systems Center's Study

In May 1985 DOT's Transportation Systems Center, Research and Special Programs Administration, issued a study entitled Safety Inspection of Foreign Vehicles. From its review of 63 vehicles, the Center found that 24 were not in full compliance with 1 or more of 12 safety standards or regulations, including those for door locks and door retention components, windshield mounting, and seat belt retractors.

The objective of the study was to assess, through field inspections, the conformance status and reliability of the information provided by importers of 186 vehicles in their compliance statements to substantiate conformance to federal safety standards. The Center was able to contact the importers of 141 of these vehicles. Of these, only 63 vehicles were made available by the importers for inspection. Of the remaining 78 "unavailable" vehicles, 54 had been sold and 24 were considered unavailable because the importers made statements such as "too busy to have vehicle inspected; vehicle out of state; [or] vehicle in shop."

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The Center's team inspected the 63 vehicles to determine whether the vehicles had been modified as indicated by the importers on their statements of compliance submitted to NHTSA. The team determined that 39 of the 63 vehicles were in full compliance with applicable federal safety standards and 24 vehicles were not. The deficiencies noted in the importers' modifications of the 24 vehicles are shown in table II.4.

Table II.4: Deficiencies Noted in Importers' Modifications of 24 Vehicles

Items determined deficient or missing	Standard	Number of vehicles^a
Rear door locks	206	13
Belt retractors or seat belts	208	5
Windshield adhesion	212	4
Certification label	49 C.F.R 567	4
Headlights or rear side markers	108	4
Rollover valves	301	3
Vehicle identification number plate	115	2
Speedometers	101	1
Wheel nuts	211	1
Tire placard	110	1

^aThe numbers do not total to the 24 vehicles because not all vehicles failed to comply with each of the standards.

Source: DOT Transportation Systems Center, Safety Inspection of Foreign Vehicles, May 1985.

The Center found that 77 of the 141 vehicles had been sold prior to NHTSA's approval of documentation submitted by the importers to substantiate their conformance to safety standards and its issuance of approval letters to Customs stating that the conditions of importers' bonds had been satisfied. The sale of those vehicles violated the agreement signed by the importer when entering the nonconforming vehicle into the United States—namely that the vehicle will not be sold until NHTSA advises Customs that the importer may be released from all liability under the bond posted at the time of entry. NHTSA requested that the appropriate Customs district offices assess liquidated damages or issue a notice of redelivery for those vehicles that either failed or were not made available for inspection. As previously noted, Customs does not generally advise NHTSA of its enforcement actions in individual cases.

NHTSA's Inspection and Testing of Nonconforming Vehicles

In February 1985 NHTSA negotiated a \$103,795 firm-fixed price contract with a California firm to purchase, inspect, and test two randomly selected vehicles to evaluate the importers' certification that the vehicles conformed with all applicable safety standards. The vehicles were

purchased from independent commercial importers. In April 1985 the contractor reported that both vehicles did not conform with several safety standards.

The two vehicles were tested to determine their conformance with standards for hydraulic brake systems, power-operated window systems, and bumpers. One vehicle was also tested to determine its conformance with the standard for side door strength. The other vehicle was tested for conformance to standards for windshield mounting, windshield zone intrusion, and fuel system integrity. Both vehicles were visually inspected for conformance with seven standards, including those for theft protection, door locks, door retention components, and certification labels regarding month of manufacture, gross weight ratings, and vehicle type.

The contractors' tests and visual inspections showed one vehicle did not conform with eight standards and the other did not conform with nine standards. For example, neither vehicle conformed with

- the power-operated window standard because the windows operated with the key removed from the ignition,
- the theft protection standard because the driver was not warned when the key was left in the locking system and the door was left open, and
- the door locks and door retention components standard because the inside rear door handles were not inoperative when the doors were locked.

During crash testing,

- One vehicle failed the fuel system integrity standard when it was crash-tested. The fuel line broke, allowing fuel spillage.
- Both vehicles failed the bumper strength standard.

Visual inspections showed that neither vehicle met the standards for controls and displays, tire rims, and certification labels.

Mercedes-Benz Survey

MBNA issued a report on May 14, 1986, on the results of a survey it conducted during the 18-month period from December 1983 through May 1985. MBNA asked its dealers to inspect and report on the modifications to each nonconforming vehicle brought in for service. MBNA's survey indicated that 95 percent of the vehicles failed to comply with all applicable federal safety requirements. MBNA dealers performed no testing of

the modified vehicles. The dealers made "simple visual inspections" to determine whether a particular required feature had been installed. For example, the dealers determined whether the vehicle had

- European or U.S. standard headlights,
- reinforcement of any European bumpers,
- bolts in the sides of its doors to indicate their reinforcement,
- seat belts having DOT markings and production date, and
- a vehicle identification number visible from outside the vehicle.

The report was based on 1,114 dealer survey reports. The MBNA report stated that 3 percent of the 1,114 vehicles were in compliance with the above 5 federal safety standards. With respect to the remaining vehicles, the report indicated, in part, that

- about 60 percent did not have conforming headlights,
- about 90 percent did not have conforming bumpers,
- more than 40 percent did not have bolts in the sides of the doors,
- more than 50 percent did not have proper DOT markings and production dates on the seat belts, and
- more than 40 percent did not have a vehicle identification number plate or conform with other safety standards.

In addition, as discussed in appendix III, MBNA found safety hazards caused by improper installation of emission control equipment.

**National Automobile
Dealers Association Survey**

NADA issued its Gray Market Vehicle Survey Results in January 1985. The survey showed that 82 percent of the vehicles were missing equipment relating to at least one safety standard.

During 1984 NADA sent a questionnaire to its member dealers requesting information concerning the adequacy of modification for federal safety and emission requirements on imported nonconforming vehicles. NADA received 393 responses to the vehicle survey. NADA's survey results are shown in table II.5.

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Table II.5: Vehicles Reported Missing Safety Standard Equipment

Equipment ^a	Vehicles	
	Number	Percent
U.S. bumpers	322	82
U.S. headlights	237	60
VIN at windshield pillar	176	45
Side door reinforcements	168	43
U.S. version seat belts	155	39
Nonflammable seats	125	32

^aA vehicle could be missing more than one item of equipment.
Source: NADA, Gray Market Vehicle Survey Results, January 1985.

In a March 19, 1985, letter, NADA's Associate Chief Counsel and Director of Regulatory Affairs transmitted the above survey results to NHTSA. He stated that, on the basis of those results and other available evidence, NADA believed that importation of nonconforming vehicles posed a growing threat to highway safety.

Importers Late in Providing Documentation

Our analysis of the 50 cases we randomly selected showed that half of the importers had not provided NHTSA documentation to substantiate that the gray market vehicles had been conformed to the safety standards on time. As shown in table II.6, NHTSA received documentation for 5 vehicles after the 120-day deadline and had not received the documentation for 20 vehicles when we completed our review of the files on July 1, 1985.

Table II.6: Importers' Timeliness in Providing Documentation of Conformance With Safety Standards

Documentation	Vehicles
Received on time	24
Received: Late by 5 to 73 days beyond the deadline ^a	5
Not received: Deadline exceeded by 27 to 377 days	20
Not expected: Vehicle to be exported	1
Total	50

^aIncluding one case late after a 60-day extension.

As of July 1, 1985, NHTSA had requested Customs to seek redelivery of only 1 of the 20 vehicles for which it had received no documentation from the importers. The Chief, Verification Division, told us that NHTSA had concentrated its resources on reviewing the adequacy of the documentation submitted by importers rather than on importers who had not

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submitted documentation. However, the Chief told us that NHTSA often requests Customs to seek redelivery of vehicles because of the importers' failure to submit a statement of compliance, although NHTSA had no systematic process for identifying such importers.

NHTSA furnished us information as of July 24, 1985, that showed there were 13,681 cases in which the importers had not submitted the documentation over 180 days after the vehicles' entry. The range of overdue cases is shown in table II.7.

Table II.7: Cases in Which Importers' Documentation Was Overdue

Days since entry	Number of cases
180 to 360	4,187
361 to 541	2,602
542 or more	6,892
Total	13,681

Source: NHTSA.

Customs may have issued notices to the importers to redeliver these vehicles. However, from its records, NHTSA could not determine how many notices had been issued because Customs district offices do not generally provide NHTSA with that information.

EPA's Program for Ensuring That Gray Market Vehicles Conform to Federal Emission Standards

EPA, like NHTSA, does not routinely test or inspect gray market vehicles. Instead, it determines the vehicle's conformance to emission standards through either test results from an EPA-recognized laboratory or a certificate of conformity provided by an EPA-recognized firm that performs the necessary modifications. However, EPA was unable to supply the documentation supporting its acceptance of conformance for about half of the 50 randomly selected cases that we reviewed. In addition, government tests and industry surveys have raised concerns about the adequacy of modifications made to comply with emission standards. In September 1985 EPA proposed revising its gray market program to address the possible inequity of the requirements on independent commercial importers and alleged improper modifications and falsification of data.

EPA's Program, Procedures, and Requirements

Customs notifies EPA when a nonconforming vehicle enters through a port of entry. When the importer has satisfied EPA that the vehicle has been modified to meet the federal emission standards, EPA notifies Customs to release the importer's bond. The importer may satisfy EPA with either test results from a testing laboratory recognized by EPA or a certificate of conformity from a firm that EPA has recognized as able to conform the particular vehicle to the emission standards. If the importer does not provide documentation of conformity to EPA within the established time frame, EPA advises Customs to seek redelivery of the vehicle or assess liquidated damages against the importer's bond.

Responsibilities of EPA and the Importers

EPA's Manufacturers Operations Division, Office of Mobile Sources, Air and Radiation, is responsible for ensuring that imported nonconforming vehicles are modified to conform to applicable federal emission standards. The Division's monitoring and review process begins with the receipt of an importer's declaration of importation from the Customs port of entry where the vehicle entered the country. The importer indicates on the entry form that the vehicle is not in conformity with applicable federal emission standards but that it will be brought into conformity and is being imported under bond to ensure that it will be conformed. (An individual may import one nonconforming vehicle for personal use and not for resale without bringing it into conformity with federal emission requirements, if the vehicle is at least 5 model years old or if the importer is an individual who is permanently immigrating to the United States.)

The importer has 90 days to demonstrate to EPA that the vehicle has been modified to meet federal emission standards. EPA advises the importer that the vehicle cannot be operated on a public street or highway or sold until EPA advises Customs that its liability against the bond may be released. The vehicle can be driven only to a modifier and to a facility that tests whether the vehicle meets federal emission standards.

If the importer provides EPA documentation showing that the vehicle conforms to the federal emission requirements, EPA notifies Customs that EPA's liability against the bond can be released and sends a copy of the letter to the importer. If EPA is not satisfied with the importer's documentation, EPA notifies the importer that the test report has been rejected, noting the reasons for its rejection. EPA also advises the importer that its obligation on the bond cannot be released until the importer demonstrates compliance with federal emission requirements.

Options for Substantiating Conformance to Emission Standards

EPA gives importers two options for demonstrating that a nonconforming vehicle has been modified to conform to applicable federal emission standards.

First Option

Under one option, importers may have their vehicles modified and have them tested by a laboratory recognized by EPA as being capable of conducting the applicable federal test procedures. The laboratory then sends the packet of test results to EPA.

The test determines a vehicle's hydrocarbon, carbon monoxide, oxides of nitrogen, evaporative, and diesel particulate emissions, as appropriate by the engine type. The purpose of the test is to demonstrate whether the vehicle, as modified, conforms to EPA emission standards. As of April 11, 1986, EPA had recognized 46 laboratories as capable of testing modified vehicles in accordance with the applicable federal test procedure.

A laboratory must submit information on its equipment and technical capabilities to EPA for review in determining whether the laboratory will be recognized as capable of performing the test. From September 1985, when EPA began on-site inspections of laboratories requesting EPA recognition, through June 1986, EPA inspected and recognized eight laboratories.

When making such inspections, EPA also makes unannounced visits to inspect previously recognized laboratories in the same area to determine whether their operations meet EPA standards. In cases where the laboratory would not allow the unannounced visit, EPA scheduled an inspection date. EPA's Chief, Programs Testing Branch, told us that EPA did not know whether it had authority to demand unannounced entry. No laboratories have lost EPA recognition as a result of the unannounced visits although EPA has initiated action to withdraw recognition from three. Through June 1986 EPA had made 12 such unannounced visits.

Except as noted above, EPA does not perform on-site inspections of EPA-recognized laboratories unless it receives allegations that they are not operating properly. EPA does not accept packets of test documents from laboratories while it has them under investigation. Through April 1986 EPA investigated five laboratories because it had received allegations concerning problems with test documents submitted to EPA relating to vehicles modified to conform with emission standards. EPA had withdrawn recognition from four of the laboratories and was still investigating the fifth as of June 2, 1986.

Second Option

The second option allows the importer to have the vehicle modified by a firm to which EPA has issued a certificate of conformity. A certificate of conformity attests to the firm's capability to modify designated makes, models, and model year vehicles using specified components so that they will conform to the federal emission standards.

As part of the certification process, an applicant provides a prototype vehicle to EPA for testing at its Motor Vehicle Emissions Test Laboratory in Ann Arbor, Michigan. If the vehicle passes all of EPA's requirements, a certificate of conformity is issued to the applicant. The certificate holder can certify that all imported nonconforming vehicles of this type, which he subsequently modifies, are identical to the prototype vehicle and conform to applicable emission standards. EPA does not subsequently test the modifiers or the vehicles they modify. As of April 30, 1986, there were eight certificate holders. A certificate holder can sell other modifiers its modification kits and provide a certificate of conformity to cover the modification. According to the Director, Certification Division, Motor Vehicle Emissions Test Laboratory, EPA, the certificate holder is responsible for such modifications' meeting the federal emission requirements, but EPA is not aware of the number of kits sold or the number of modifiers to whom they were sold.

A vehicle modification firm may qualify for a certificate under the small-volume-manufacturer portion of the certification regulations. The requirements for small volume manufacturers are less stringent than for large volume manufacturers because they call for a single test by EPA of whether the prototype vehicle meets the emission standards, to be conducted within 4,000 miles after the modification. The requirements for large volume manufacturers (the vehicle manufacturers) include both the initial test plus tests at 5,000-mile increments up to 50,000 miles to evaluate the durability of the emission equipment originally installed. The large volume manufacturers are also subject to EPA's making assembly line tests or recalling modified vehicles for testing to determine whether the emission equipment continues to meet the federal emission standards.

If an importer has the vehicle modified by a certificate holder, a statement of compliance from the certificate holder is sent to EPA. After it receives the notarized statement, EPA notifies Customs and the importer that its liability against the bond can be released.

According to the Chief, Investigation/Imports Section, EPA processed 24,848 test packets for vehicles tested at recognized laboratories and about 2,470 statements of compliance for vehicles modified by certificate holders in fiscal year 1985. The remainder of the gray market vehicles imported in the fiscal year were either granted an exemption on the basis of being 5 model years old or their test packets were in process. In fiscal year 1986, through April 25, EPA had processed 13,384 test packets and had a backlog of about 1,400 unreviewed test packets. The Chief, Investigation/Imports Section, said that this represented a 2- to 3-week work load.

EPA Had No Documentation for About Half of Randomly Selected Cases

Using the 50 cases we randomly selected when reviewing NHTSA's program (see app. II), we requested the documentation that importers had submitted to EPA to substantiate that the vehicles had been modified to meet federal emission standards. EPA was unable to locate any documentation indicating whether 26 of the 50 vehicles conformed to federal emission standards.

EPA's Director, Manufacturers Operations Division, advised us that specific files may be unavailable because of the following reasons:

- EPA did not receive the importation information (declaration form) from the importer or Customs.

- Laboratories do not always submit test documentation promptly because their file is incomplete (the modifier did not supply the proper photographs), the lab has not been paid for the tests, or the lab is under EPA investigation.

EPA was able to locate and provide us with documentation to show that its requirements had been satisfied in the remaining 24 cases. In 12 of the 24 cases, the test laboratories had submitted test packages, which EPA accepted as adequate substantiation. The test report forms for these 12 cases indicated that the vehicles' emission of hydrocarbons, carbon monoxide, nitrogen oxides, and evaporation of hydrocarbons met EPA's standards. In the remaining 12 cases, EPA had granted the importers exemptions from its requirements because the vehicles were 5 years old or older at the time of entry.

The Director, Manufacturers Operations Division, advised us that EPA began to track test packets in December 1985 by entering test packet information into a data base and assigning an EPA file number for each vehicle. Entry forms filed with Customs for each vehicle and 5-year-old releases are also entered, beginning in April 1986, and are assigned a case number for tracking purposes. The Director said that the current tracking system allows EPA to track imported vehicles efficiently by having entry information entered into the computer shortly after the time of entry. Consequently, this allows EPA to more efficiently assist Customs in enforcing the joint regulations and to ensure that each vehicle complies with applicable federal emission requirements.

Government Tests and Industry Surveys Questioned the Adequacy of Modifications

EPA, MBNA, and NADA each conducted studies of the adequacy of modifications made to bring imported nonconforming vehicles into compliance with the federal emission standards. Each study raised questions about the adequacy of the modifications.

EPA's Study of Imported Vehicles in California

In 1984 EPA, in cooperation with the California Air Resources Board (CARB), had 27 gray market vehicles tested in California for compliance with the federal emission standards. The importers of these vehicles had previously had them tested by an EPA-recognized test laboratory and had

test results showing that they met the federal emission standards. However, only 1 of the 27 vehicles was found by the CARB personnel to pass all the emission test requirements.

In February 1985 EPA, in cooperation with CARB, issued a report entitled Joint Program to Inspect and Test a Sample of Imported Nonconforming Vehicles—September-October 1984. The study presented the results of tests of nonconforming vehicles certified as being in conformance with applicable federal emission standards.

Twenty-seven vehicles were tested on the basis of EPA's "Federal Test Procedures." Three inspection teams comprised of EPA and CARB personnel were established. CARB personnel tested the 27 vehicles at the Haagen-Smit Laboratory, El Monte, California, completing the testing before the end of October 1984.

The EPA/CARB team developed a sample plan that was expected to yield a statistically representative sample from the normal flow of imported vehicles' test packets in EPA's gray market vehicle program. These packets represented vehicles reported to EPA as having been satisfactorily tested by EPA-recognized private testing laboratories, according to the applicable federal test procedure, but for which EPA had not recommended to Customs that the importers' bond be released.

The 27-car sample was composed of 3 makes distributed as follows: 24 Mercedes-Benz, 2 BMW's, and 1 Rolls Royce. The group contained 4 diesels and 23 gasoline-fueled vehicles. Individuals imported 19 vehicles and commercial importers imported 8.

On the basis of our comparison of the CARB test data with the federal emission standards, 26 of the vehicles failed some portion of the test for (1) hydrocarbons, (2) carbon monoxide, (3) nitrogen oxides, (4) evaporation of hydrocarbons, and (5) diesel particulates. Only 1 of the 27 vehicles tested passed all the emission test requirements.

Mercedes-Benz Study

During the 18-month period from December 1983 through May 1985, MBNA asked its dealers to inspect and report on the modifications to each nonconforming vehicle brought in for service. The MBNA's May 14, 1986, report pointed out that the surveys were "simple visual inspections" to determine whether a particular required feature, such as a catalytic converter in its exhaust system, had been installed. The dealers performed

no actual testing to see whether the modified vehicles conformed to the standards.

The report described hazards and other problems the dealers observed, including the following:

- The exhaust gas recirculation system had been improperly routed to dump exhaust gas into the brake booster vacuum line. The brakes failed, resulting in a collision.
- Vehicle fuel tanks had collapsed, usually because of modifications that sealed off the fuel system in order to reduce evaporative emissions. The fuel used in the engine created a vacuum in the tank. The ensuing collapse may have caused fuel leakage into the vehicle, fuel odor, or a fire hazard.
- The wiring harness had been routed over the exhaust gas recirculation valve, which melted the harness and caused a fire.
- An engine fire had occurred when fuel leaked from a valve installed by a modifier. This fire spread over the entire engine compartment, stopping only when the fuel supply burned out and the vehicle stalled, causing the fuel pump to stop.
- One exhaust pipe of a dual pipe system had been welded shut, forcing all exhaust gas through a single pipe and increasing back pressure in the engine.

**National Automobile
Dealers Association Study**

The NADA study entitled Gray Market Vehicle Survey Results was issued in January 1985. During 1984 NADA surveyed its member dealers requesting information concerning the adequacy of modifications to meet federal safety and emission requirements performed on imported nonconforming vehicles. NADA received 393 responses to the vehicle survey. As shown in table III.1, the survey found that from 20 to 209 vehicles (or up to 53 percent) were missing emission control equipment or certification labels (certifying conformity with U.S. emission standards).

Table III.1: NADA Member Dealers' Report of Missing Emission Control Equipment and Labels

Missing equipment/labels ^a	Number of vehicles
Catalyst	119
Oxygen sensor	209
Carbon cannister	149
Tank filler restrictor	146
Unleaded fuel labels	149
Exhaust gas recirculation (diesel)	20
Certification label	203

^aA vehicle could be missing more than one item of equipment.
 Source: NADA, Gray Market Vehicle Survey Results, January 1985.

EPA's Proposed Rules for Revising the Nonconforming Vehicle Program

In September 1985 EPA issued a supplemental notice of proposed rule making for revising its imported nonconforming vehicle program. EPA had begun this rule-making effort in July 1980. The notice indicated that EPA was proposing the revisions as a result of comments submitted at or in response to workshops held by the agency in late 1983. Most of these comments dealt with two major issues associated with the current "modification and testing" approach.

EPA's notice stated that the first issue was whether the current regulations are equitable since they arguably impose less stringent requirements on independent commercial importers of nonconforming vehicles under the "modification and testing" approach than those imposed on original equipment manufacturers or their distributors, pursuant to the certification process.

According to the notice, original equipment manufacturers generally alleged that the regulations are unfair because they result in lower costs of compliance to independent commercial importers and because gray market vehicles cause widespread problems, such as warranty claims and unavailable parts for models not originally sold in the United States, which adversely affect the manufacturers' reputations. (This is discussed further in app. IV.)

The second major issue discussed in the notice was the extent to which alleged improper modifications and falsification of data occur under the existing approach. EPA stated that many commenters alleged that these problems were significant and widespread. On the other hand, EPA stated that some representatives of independent commercial importers

have claimed generally that such abuses are not as extensive as their opponents indicate.

EPA held public hearings on the supplemental notice in Washington, D.C., on October 9, 1985, and in San Diego, California, on October 24, 1985. EPA requested that written comments be submitted by December 6, 1985. EPA expects to revise its regulations by the end of 1986.

The Director, Manufacturers Operations Division, advised us on August 18, 1986, that the proposed regulation was under final review within EPA. He said that EPA has considered a wide variety of options in this rule-making process. "The Supplemental Notice of Proposed Rule Making of September 9, 1985," proposed three options for comment that EPA was considering most seriously. The first was prohibiting altogether the importation of nonconforming vehicles. The second was permitting essentially only certificate holders (with some exceptions) to import nonconforming vehicles. The third was identical to the second except it also provided for a revised modification and test provision for a limited number of vehicles whose low rate of importation did not warrant the costs of obtaining a certificate.

The Director also said that EPA is leaning toward the adoption of one of these options in order to address effectively the enforcement and administration problems associated with the current EPA program.

Other Observations on Gray Market Vehicles

The Chairman of the Subcommittee on Oversight and Investigations, House Committee on Energy and Commerce, asked GAO about several additional matters. They pertained to

- the extent to which the importation of nonconforming motor vehicles has become a commercial operation,
- the resources devoted by federal agencies to nonconforming motor vehicle programs, and
- manufacturers' and importers' views on conforming gray market vehicles to federal safety and emission standards.

Extent to Which the Importation of Nonconforming Motor Vehicles Has Become a Commercial Operation

The importation and conformance of gray market vehicles has become a relatively large commercial operation. In a January 1985 preliminary regulatory evaluation on its notice of proposed rule making for the Motor Vehicle Theft Law Enforcement Act of 1984, NHTSA discussed the nonconforming motor vehicle market. In that evaluation, NHTSA stated that roughly 400 firms engaged in one or more aspects of importing and modifying vehicles for federal emission and safety standards. These firms included shippers, modifiers, testing laboratories, retail sales outlets, bonding agents, parts suppliers, and equipment designers. The Executive Director, AICA, stated in public hearings held by EPA on October 9, 1985, that more than 550 AICA members participated in the importation and modification of 70 percent of the nonconforming vehicles brought into the United States. He also has stated that the businesses providing services related to the importation of nonconforming motor vehicles employ about 10,000 persons.

NHTSA stated in its evaluation that gray market vehicles' retail prices in the United States ranged widely from about \$20,000 to \$60,000. For purposes of its analysis, NHTSA assumed that an average gray market car sold for \$30,000. NHTSA estimated that 30 percent of the nonconforming vehicles were imported by retail firms. Using that percentage, we estimated that these retailers had sales of about \$600 million in 1985. The total value of nonconforming vehicles imported in 1985, including those brought in by commercial importers for resale and by individuals for their personal use, is estimated at \$2 billion.

According to NHTSA, the cost of shipping and modifying a vehicle to conform to emission and safety standards can range from \$6,000 to \$12,000, with most costing between \$6,000 and \$8,000. If an average cost of \$7,000 was incurred for modifications and related services for each of the 66,879 vehicles imported in 1985, we estimate that a total of

about \$468 million would have been generated by the firms involved in providing the services. However, this does not consider the number of these vehicles that were exempt from modification to conform to emission standards because they were 5 model years old or older or were imported by nonresidents or immigrants. Information provided by EPA indicated that about 50 percent of the nonconforming vehicles imported in calendar year 1985 were 5 model years old or older and the cost of modifying and testing a vehicle for federal emission standards compliance is about \$3,500. Therefore, because of the EPA exemption, these firms' revenues in 1985 may have totaled about \$350 million.

Resources Devoted by Federal Agencies to Nonconforming Motor Vehicle Programs

Precise information is not available to determine the federal government's total cost for administering the nonconforming vehicle program. For NHTSA and EPA, we were able to identify staff and contract cost data. Customs headquarters provided us with the estimated staff years and costs devoted to the program nationwide. Table IV.1 shows the estimated resources being devoted to the program by NHTSA, EPA, and Customs.

Table IV.1: Estimated Federal Resources Devoted to Nonconforming Motor Vehicle Program for Fiscal Year 1985

	EPA	NHTSA	Customs	Total
Personnel:				
Government employees	17	11	80	108
Contractor employees	11	18	•	29
Total	28	29	80	137
Salaries and expenses	\$512,500	\$394,300	\$2,818,200	\$3,725,000
Contract costs	292,300 ^a	1,016,200	•	1,308,500
Total	\$804,800	\$1,410,500	\$2,818,200	\$5,033,500

^aThe contract's initial period of performance was from November 1984 to November 1985.
Source: NHTSA, EPA, and Customs.

As shown in table IV.1, NHTSA and EPA incurred estimated costs totaling about \$1.3 million during fiscal year 1985 for contractor services related to the administration of the importation of nonconforming motor vehicles. EPA has awarded a negotiated contract to review and process documentation submitted by importers to substantiate their vehicles' conformance to federal emission requirements. NHTSA had awarded a negotiated contract to provide data processing support and analysts to review documentation submitted by importers to substantiate safety modification work.

Manufacturers' And Importers' Comments on Conforming Gray Market Vehicles to Federal Safety and Emission Standards

Manufacturers claimed that modification of their nonconforming vehicles to meet the federal safety and emission standards is either impossible or cost-prohibitive. Importers stated that EPA and NHTSA impose less stringent requirements on the importers of nonconforming motor vehicles than they impose on the original equipment manufacturers who manufacture and certify vehicles that they import as conforming to the federal safety and emission standards.

Representatives of BMW, Ford, Jaguar, and Volvo told us that it is possible to modify the European models of the vehicles that they manufacture so as to conform to all applicable federal safety and emission standards. They believe it is impractical, however, because—even though the technical knowledge may be present—the costs would be prohibitive. Volvo representatives told us that they estimated the costs to modify its models would be between \$10,000 and \$12,000. Jaguar officials estimated that the cost to properly modify one of its models would be between \$18,000 and \$20,000. We did not assess the reasonableness of these estimates. Ford, BMW, and MBNA had not estimated the costs that might be involved in properly modifying their vehicles. MBNA representatives told us that no modifier can modify and certify its European model vehicles to meet federal safety and emission standards.

European motor vehicle models' conformance to many safety standards may be substantiated by photographs or physical inspection—as originally manufactured or as modified (an example is whether the vehicle's speedometer shows miles per hour). On the other hand, there are several other safety standards relating to vehicles' crashworthiness with which NHTSA generally accepts European models' conformance as originally manufactured or—in the case of fuel system integrity—as modified by the installation of a rollover valve that prevents spillage of fuel in the event of an accident that results in the vehicle rolling over. Representatives of BMW, Jaguar, Mercedes, and Volvo told us that their European models either (1) generally conform to these crashworthiness standards or (2) have not been crash-tested to determine their conformance. The manufacturer representatives' comments on these crashworthiness standards are summarized in table IV.2.

Table IV.2: Four Manufacturers' Positions on Their European Models' Ability to Meet Certain Crashworthiness Safety Standards as Originally Manufactured

Federal motor vehicle safety standard		Meet the standard as originally manufactured	Must be tested to determine compliance
203.	Impact protection for the driver from the steering control system	4	•
204.	Steering control rearward displacement	4	•
212.	Windshield mounting and retention	2	2
216.	Roof crush resistance	4	•
219.	Windshield zone intrusion	2	2
301.	Fuel system integrity	•	4 ^a

^aEach of the manufacturers' representatives told us that major differences exist in the fuel systems of European and U.S.-certified models of their vehicles because of the differences in the emission requirements with which the vehicles must conform.

Source: Representatives of BMW, Jaguar, MBNA, and Volvo.

These manufacturers' representatives also told us that there is no assurance that their European model vehicles imported into the United States will meet the side door strength standard and the bumper regulation after being modified. In their view, destructive tests must be performed on prototype vehicles to determine whether the modifications made to nonconforming vehicles will permit their achieving the performance levels required by the standard and regulation. NHTSA relies on engineering data submitted by importers regarding the design and installation of structural modifications made to vehicles to decide whether the vehicles conform to the standard and regulation.

BMW and MBNA representatives told us that numerous major parts affecting emissions either are not available on European models of their vehicles or are significantly different in design and emission characteristics. These differences include pistons, spark plugs, ignition timing, compression ratios, and evaporative emission systems.

In testimony before the Subcommittee on Telecommunications, Consumer Protection, and Finance, House Committee on Energy and Commerce, a spokesman for the National Automobile Dealers Association stated:

"In order for major manufacturers to import vehicles for resale in the United States, such manufacturers must develop, manufacture and certify vehicles to conform with applicable federal emissions and safety standards. Certified automobiles must be covered by emission design, defect and five-year/50,000 mile performance warranties. Furthermore, such vehicles are subject to fuel economy requirements, gas guzzler taxes and the defect notification and recall provisions in both the clean air act and motor vehicle safety act.

"On the other hand, current EPA and Department of Transportation regulations do not impose such extensive requirements on conditional importers (importers of non-conforming motor vehicles). Simply put, foreign manufacturers and their franchised dealers have made substantial investments to insure that vehicles sold in this country are properly designed, built, serviced and maintained during operation. Gray market importers have none of these responsibilities.

"Such differential treatment has placed manufacturers and dealers in an unfair competitive situation in which they must sell against their own products imported through the gray market, in many cases at a price disadvantage. In other cases, they must sell against products which were never designed and produced for resale in the United States."

In April 30, 1985, comments to the Subcommittee on Telecommunications, Consumer Protection, and Finance, House Committee on Energy and Commerce, the Executive Director, AICA, indicated the following, in part, with respect to whether nonconforming motor vehicles represent a significant safety or emission compliance problem:

- A March 1985 NHTSA report of safety complaints provided to AICA indicated that NHTSA has received no safety-related complaints for these imported vehicles.**
- Safety modifications, including those for side door impact protection, bumpers, rear door locks, for most nonconforming vehicles are straightforward and impose no substantial technical challenge.**
- Statements of compliance, accompanied by descriptions and photographs of safety modifications, must be filed with, and accepted by, NHTSA for each vehicle.**
- All nonconforming vehicles (not exempted by EPA from emission standards) must be tested for compliance with, and must meet, emission standards. For conventional imports, only prototypes must be tested, and if production vehicles are tested, only 60 percent need meet the standards.**

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