STATEMENT OF DIANE K. STEED, DEPUTY ADMINISTRATOR, NATIONAL HIGHWAY TRAFFIC SAFETY ADMINISTRATION, DEPARTMENT OF TRANSPORTATION, BEFORE THE SUBCOMMITTEE ON ENERGY CONSERVATION AND POWER, HOUSE COMMITTEE ON ENERGY AND COMMERCE, CONCERNING AUTOMOBILE FUEL ECONOMY, JULY 21, 1983

Mr. Chairman and Members of the Subcommittee:

I am pleased to appear before you today to discuss automobile fuel economy. With me today is Mr. Barry Felrice, Associate Administrator for Plans and Programs, Mr. Frank Berndt, Chief Counsel, and Mr. William Boehly, Office Director for Market Incentives. This hearing focuses on the Corporate Average Fuel Economy (CAFE) standards established under the Energy Policy and Conservation Act of 1975 (EPCA), Pub. L. 94-163. In your letter of invitation, you stated that you are interested in whether the Department of Transportation is contemplating any revision in the regulations or legislation governing the CAFE standards. You have asked a series of specific questions on projected CAFE figures, penalties and credits, and industry and Departmental views on the present and future status of the CAFE statute and regulations.

I know that there is a concern in some quarters that the domestic auto manufacturers may not be able to meet the CAFE standard for this model year (MY), i.e., MY 1983, or future model years, but I do not believe that the manufacturers will incur penalties under the passenger car CAFE standards.

DOT will be as responsive as possible to the Committee's questions. I also appreciate the forum this hearing provides others to express their views on this subject. The Department is interested in hearing their views.

The Fuel Economy program and the CAFE standards issued under it for cars and light trucks were mandated by Congress under the 1975 Act in an effort to restrain energy demand. Congress specified the fuel economy standards for passenger cars in MY 1978, MY 1979, MY 1980 and MY 1985 and thereafter and directed the Department to administratively set the standards for MY 1981 through MY 1984. As for light trucks, the statute directed the Department to set standards beginning in MY 1979.

In 1977, the Department set the MY 1981-1984 passenger car standards in compliance with the statutory requirement to achieve the maximum feasible fuel economy based upon four factors listed in the statute: technological feasibility, economic practicability, the effect of other federal standards (such as emission control and safety standards) on fuel economy, and the need of the Nation to conserve energy. The standards were also required to achieve steady progress toward the statutory 27.5 mpg standard for 1985 and thereafter.

In 1979, in part due to the turmoil in Iran, oil shortages again developed and the price of oil skyrocketed. The demand for very fuel efficient small cars increased dramatically, leading the domestic manufacturers to confidently predict that they would not only meet the CAFE standards through MY 1985, but exceed them by several miles per gallon. It appeared that market forces would bring about the desired increase in fuel economy independent of the pressure from government regulations, as nearly all domestic companies expected their CAFE to exceed 30 mpg by 1985.

However, the energy situation has continued to fluctuate. Since 1981, supplies of available oil have increased and oil prices have dropped. Oil shortages and oil embargoes do not seem as ominous to the public at large. Having invested billions of dollars in a massive redesign of their product lines, the domestic auto manufacturers continue to offer very fuel efficient cars, but a growing portion of the car-buying public is purchasing larger, less fuel efficient cars. The market for diesel cars has declined precipitously. This shift in buyer preference is one of the factors changing the manufacturers' CAFE levels. Still, the fuel efficiency of the domestic car fleet has greatly increased since the advent of the fuel economy standards in MY 1978. While the reported CAFE for the entire domestic auto fleet in MY 1976 was approximately 15 mpg, it had increased to over 24 mpg for MY 1983.

Despite the effect on the CAFE levels for some manufacturers, we believe, based upon confidential data submitted to us by the domestic automakers for model years 1983, 1984, 1985, 1986, and 1987, each of them will either meet the CAFE standards for passenger automobiles or have sufficient credits (carried forward or carried back) to offset a CAFE shortfall. Based upon their projections, we do not anticipate any penalties. Since standards for light trucks manufactured in MY 1986-88 have not yet been set, it is premature to evaluate the truck credit situation for 1984-85.

As I've already suggested, the statute does provide a safety valve for any manufacturer which cannot meet a CAFE standard for one or more model years in the form of carry forward and carry back credits. A manufacturer can use these credits to offset the CAFE shortfall. It does not incur a penalty nor does it violate the CAFE law until all accumulated credits are exhausted. In their pre-model year report, GM and Ford have indicated the likelihood that they will need to use their 1980 credits to offset a 1983 shortfall for passenger cars. Since MY 1979, the manufacturers have accumulated the following credits: General Motors has accumulated credits of $685.5 million, Ford of $272.3 million, Chrysler of $293.5 million and American Motors of $11.9 million. None of them has requested the Department to modify CAFE penalties. Based upon manufacturers' projections for passenger cars, it appears unlikely that any of them will incur a penalty even if they fail to meet the standard since they can use credits. Even if a penalty were to be incurred, it should be noted that the statute also provides the Department with some latitude in enforcing the CAFE standards. The Department has the discretion to modify penalties incurred by a manufacturer to prevent bankruptcy, preserve competition in the auto industry, or allow for the effects of an extraordinary event such as a strike.

If the trend toward larger, less fuel efficient cars grows beyond present projections, the Department may have to reevaluate its position regarding the existing standards. If the manufacturers project themselves as being unable to offset the CAFE shortfall with credits, the Department may have to look at the regulations and the statute. We certainly would be open to the views of others on these matters.

For the post 1985 period, this Administration favors adopting a free market approach to the maximum extent possible to the manufacture and sale of fuel efficient cars. In 1981, the Department reviewed relevant data and projected that the auto manufacturers' response to car buyer demand would improve fuel economy over and above that required by the CAFE standards. The Department therefore terminated the rulemaking on post-1985 fuel economy standards initiated under the Carter Administration, leaving the MY 1985 standard of 27.5 mpg as the standard for post-1985 cars. The Department, however, is currently engaged in a rulemaking on fuel economy standards for light trucks for MY 1986 and 1987 mandated by statute.

With regard to the Department's administrative authority to lower the standard for MY 1985 and thereafter below 26 mpg or raise it above 27.5 mpg, the question has been asked whether the Department retains that authority in light of the recent Supreme Court decision on legislative veto. Under section 502(a)(4) of the CAFE statute, the Department's rulemaking action to lower the passenger car CAFE standard below 26 mpg or above 27.5 mpg is subject to Congressional review and disapproval by either House of Congress. While it is obvious that the legislative veto power in this statute has been nullified by the Supreme Court opinion, we and the Department of Justice are studying what effect such nullification has on the remainder of the fuel economy provision. The Department will follow provisions that require us to report and wait.

A question has also been asked about the Department's recommendations, if any, on a government role in encouraging, by incentives such as low interest loans or tax credits, the purchase and manufacture of fuel efficient cars. While incentives provide an alternative to regulation, in this case, they may introduce more distortions into the economics of car-buying. Low-interest loans, taxes or tax credits, aimed at changing purchasers' automobile buying habits are likely to introduce other problems into the economy, including possible distortions in international trade patterns, which might then require further government action. The Federal Government fostered low fuel prices in the 1970's and the Department believes that is at least one reason automobile fuel economy was so low in the early and mid-1970's models. The low fuel prices distorted the market signals transmitted to both consumers and manufacturers. In fact, the CAFE standards were adopted in part to reduce the overconsumption of gasoline due to the domestic price of gasoline being below the world market price, a second best solution. Without the price distortion, the domestic manufacturers might have designed their vehicles for a market that desired fuel efficiency years before before being forced to do so by the CAFE statute. As long as the price of gasoline reflects its true cost to society, people do not need other incentives to conserve; they will conserve to the point where it costs society more to conserve than to consume. Further, the cost of such incentive programs would likely be astronomical.

This concludes my statement. I would be happy to answer any further questions that you may have.

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