



## **Comments of the Regulatory Action Center**

Re: NHSTA-2016-0068-0107

Reconsideration of Final Determination of Mid-term Evaluation of Greenhouse Gas Emissions Standards for Model Year 2022-2025 Light-duty Vehicles; Model Year 2021 Greenhouse Gas Emissions Standards

October 5, 2017

The Regulatory Action Center at FreedomWorks Foundation is dedicated to educating Americans about the impact of government regulation on economic prosperity and individual liberty. FreedomWorks Foundation is committed to lowering the barrier between millions of FreedomWorks citizen activists and the rule-making process of government bureaus to which they are entitled to contribute.

---

### **Summary of Position**

FreedomWorks Foundation's Regulatory Action Center appreciates the opportunity to provide comment to the National Highway Traffic Safety Administration (NHTSA) and the Environmental Protection Agency (EPA) regarding the reconsideration of Corporate Average Fuel Economy (CAFE) standards.

Our comments address these questions of NHTSA and EPA specifically:

- The cost on the producers or purchasers of new motor vehicles or new motor vehicle engines;
- The feasibility and practicability of the standards;
- The impact of the standards on reduction of emissions, oil conservation, energy security, and fuel savings by consumers;
- The impact of the standards on the automobile industry;
- The impacts of the standards on automobile safety;

It is our position that the CAFE program, and thus stringent standards set out by NHSTA and EPA under this program, has a negative impact on consumers and the automobile industry across each of these areas. The CAFE standards program rests on incorrect assumptions about the domestic energy market and creates a number of unintended economic outcomes which undermine the efficacy of the program,

destabilize the automobile market, unnecessarily burden automakers, and harm the financial and physical welfare of consumers. We are particularly concerned with the issues outlined in testimony delivered by Sam Kazman of the Competitive Enterprise Institute (CEI) before EPA and NHTSA on September 6, 2017 regarding CAFE reducing vehicle weight and size, posing a danger to Americans in general and to our members and their families specifically.

Therefore, on behalf of our 5.7 million members nationwide, FreedomWorks Foundation wishes to state our support for making CAFE standards for cars, SUVs and light trucks less stringent.

### **Background and Historical Perspective**

Corporate Average Fuel Economy standards, or CAFE standards, are federal regulations on vehicle fuel economy (miles per gallon or mpg) across the fleet of vehicles sold by a given manufacturer. While CAFE calculations are more complex than a simple average of the fuel economy of all the vehicles a company sells, the effect is still the same: automakers are forced to prioritize adherence to rapidly increasing mpg requirements as part of both the design of individual vehicle lines as well as the fleet of vehicles a company will produce in a given year.

CAFE standards were implemented in 1975 as part of the Energy Policy and Conservation Act. This law was a clear response to the oil crisis of 1973-74, when Americans experienced long lines for gasoline as a result of rationing and shortages. While many still blame the oil crisis on the Organization of Petroleum Exporting Countries (OPEC) embargo, the oil crisis actually resulted from prior government fiddling in the fuel market. Per economist Thomas Sowell:

“Many have blamed the gasoline shortages and long lines at filling stations in 1973 on the Arab Oil embargo of that year. However, the shortages and long lines began months before the Arab oil embargo, right after price controls were imposed.”<sup>1</sup>

The economics of the matter are simple. Controls kept prices low, encouraging over-consumption while discouraging production. Had prices been allowed to naturally fluctuate, two things would have happened to alleviate and perhaps avoid the crisis altogether. First, consumers would have self-imposed rationing at an earlier stage. While government-imposed rationing eventually became a feature of the crisis, had prices been allowed to rise consumers would have immediately begun to consume less gasoline, stretching the existing supply. However with price controls and looming shortages, consumers were incentivized to fill up with as much as they could versus just what they needed. Second, higher prices would have encouraged oil producers to increase exploration and tap reserves with higher production costs. We’ve seen evidence of this recently, with higher gas prices leading to the boom in domestic oil production, which is more costly for a number of reasons including regulations, wages, and the difficulty of resource extraction itself. Today the government does not directly control the price of gasoline. Price controls during the oil crisis kept more expensive supplies of oil in the ground instead of in gas tanks.

This history of unintended consequences of government intervention in the fuel market is important to note in regards to CAFE standards for two reasons. First, it demonstrates that the original justification for CAFE standards is fundamentally flawed. In effect, CAFE standards are nothing more than long-term rationing mechanisms. The reality of the oil crisis and today’s domestic energy boom prove that government-imposed rationing is entirely unnecessary. Absent price controls, consumers would have

---

<sup>1</sup> Sowell, Thomas. 2004. *Basic economics: a citizen's guide to the economy*. New York: Basic Books.

naturally rationed gasoline in response to higher prices. In the short-term, consumers would have altered their behavior by driving less while in the long-term demand more fuel efficient vehicles, all without government intervention. Again, recent history serves as proof. When gas prices spiked in the late 2000s, Americans drove less and bought more fuel efficient vehicles. The current domestic energy boom further proves government rationing to be unnecessary. Oil producers, initially due to higher prices, were able to develop and deploy new technologies to detect and access previously unknown or inaccessible reserves. The United States is now a leading producer of oil and is projected to become a net-energy exporter in the near future; statuses unimaginable to Americans in the 1970s.<sup>2</sup>

The other reason to highlight this history of price controls is to emphasize that government economic intervention is all-too-often wrought with unintended consequences. Whereas price controls directly facilitated the oil crisis of the 1970s, CAFE standards now wreak economic havoc of their own.

### **CAFE Standards Are No Free Lunch**

At the core of the litany of economic issues associated with CAFE standards is the fact that the program is ultimately just another example of central planning. One of the many faults of central economic planning is the inability of planners to contemplate and account for all the various perverse incentives that reverberate from their designs. In their book, *Common Sense Economics*, economists James D. Gwartney, Richard L. Stroup, Dwight R. Lee, and Tawni H. Ferrarini share this anecdote about central planning in the Soviet Union:

---

<sup>2</sup> EIA's AEO 2017 projects the United States to be a net energy exporter in most cases, Energy Information Agency, January 5, 2017. <https://www.eia.gov/todayinenergy/detail.php?id=29433>

“In the former Soviet Union, managers and employees of glass plants were at one time rewarded according to the tons of sheet glass they produced. Because their revenues depended on the weight of the glass, most factories produced sheet glass so thick that you could hardly see through it. The rules were changed so that the managers were compensated according to the number of square meters of glass they could produce. Under these rules, Soviet firms made glass so thin that it broke easily.”<sup>3</sup>

There are several economic ripple effects of CAFE standards, some of which bear striking resemblance to those in the story of the Soviet glaziers. These unintended consequences and behavioral changes are at both the producer and the consumer level.

At the producer level are the problems of foreign replacement, market stability, and wasted resources. Foreign replacement refers to a CAFE- induced phenomenon that exploits the inherent differences between the historical production of foreign automakers and the domestic “Big Three” of GM, Ford, and Chrysler. The general trend is that foreign automakers produce smaller and more fuel-efficient vehicles than the Big Three.<sup>4</sup> Essentially this grants these firms greater flexibility in CAFE attainment. Thus, while the Big Three pull back on production of heavier and less fuel efficient vehicles, foreign firms are able to produce and sell vehicles to meet some of the leftover demand. In a 2012 study evaluating CAFE standards, Mark R. Jacobsen discusses this issue:

---

<sup>3</sup> Gwartney, James D., Richard L. Stroup, Dwight R. Lee, and Tawni H. Ferrarini. 2010. Common sense economics: what everyone should know about wealth and prosperity. New York: St. Martin's Press.

<sup>4</sup> Fischetti, Mark and Kevin Schultz, “Toyota and Honda Have the Most Fuel-Efficient Cars,” Scientific American, November 1, 2014. <https://www.scientificamerican.com/article/toyota-and-honda-have-the-most-fuel-efficient-cars/>

“I examine the effects of CAFE at the manufacturer level and find that almost all profit impacts of the current standard are felt by domestic firms. A key mechanism behind this result is substitution in the market for large, high-horsepower vehicles: When domestic firms cut production of these vehicles in order to meet the standard, the unconstrained and fine-paying firms will increase production in their place. The substitution pattern... harms the efficacy of CAFE in reducing gasoline use.”<sup>5</sup>

In short, much of the potential intended effect of CAFE is blunted by the substitution between domestic low mpg vehicles and foreign ones. This gets at the underlying issue of consumer demand for the kinds of vehicles that lower the average mpg of vehicle fleets. Quite simply, it's high. However, CAFE works exclusively on the supply side of this equation, creating the issue of foreign replacement as well as others.

Regarding market stability, Economics 101 teaches us that free markets work to drive supply and demand towards a point of equilibrium or balance. CAFE inherently restricts supply and thus distorts the entire market. This creates serious issues for both producers and consumers.

In order to continue selling the vehicles consumers demand, automakers must produce and sell more vehicles with higher mpg averages. Producers face enormous compliance costs in this pursuit. The EPA's own estimates put CAFE compliance costs at roughly \$200 billion between 2012 and 2025.<sup>6</sup> Undoubtedly, automakers are investing heavily to increase the mpg of popular vehicles. Yet, due to the

---

<sup>5</sup> Jacobsen, Mark R., “Evaluating U.S. Fuel Economy Standards In a Model with Producer and Household Heterogeneity,” March 2012. [http://econweb.ucsd.edu/~m3jacobs/Jacobsen\\_CAFE.pdf](http://econweb.ucsd.edu/~m3jacobs/Jacobsen_CAFE.pdf)

<sup>6</sup> Bainwol, Mitch, Letter to G. Scott Pruitt, RE: Final Determination on the Appropriateness of the Model Year 2022-2025 Light-Duty Vehicle Greenhouse Gas Emissions Standards under the Midterm Evaluation, February 21, 2017. <https://autoalliance.org/wp-content/uploads/2017/02/Letter-to-EPA-Admin.-Pruitt-Feb.-21-2016-Signed.pdf>

structure of CAFE, automakers don't exclusively seek to comply with the standards in this way. Some automakers actually produce and sell vehicles at a staggering loss in order to drive up the average of the fleet. A recent example is the all-electric Chevrolet Bolt. Reports from late 2016 suggest GM would sell each Bolt at a \$9,000 loss.<sup>7</sup> While various state incentives play into this math, CAFE creates a clear incentive for companies to pursue this strategy.

Producing and selling things at a loss weakens the financial stability of any company. This is an obvious concern following the recent federal government bailout of the domestic auto industry in 2009 at a cost of \$79.68 billion.<sup>8</sup> There is also the more nuanced yet equally pertinent economic problem of the misallocation of resources.

When automakers are forced to devote resources to supply vehicles that ultimately aren't demanded at a price sufficient to cover costs, the resources used to produce those vehicles are being wasted. This is the economic concept of opportunity cost. If the vehicle is sold at a loss, all the labor, raw materials, electricity, factory floor space, etc., that went in to producing that vehicle undoubtedly had more valuable uses elsewhere in the economy. Instead, CAFE standards distorted the market and diverted those resources to the production of a vehicle that is valued less than the price of producing it. The other uses for the workers, steel, plastic, electronics, etc., put in to the vehicles automakers produce simply to meet completely arbitrary standards cannot be ignored.

---

<sup>7</sup> Ferris, Robert, "GM stands to lose \$9,000 per car on Chevy Bolt," CNBC, November 30, 2016. <https://www.cnbc.com/2016/11/30/gm-stands-to-lose-9000-dollars-per-car-on-chevy-bolt.html>

<sup>8</sup> Snavely, Brent, "Final tall: Taxpayers auto bailout loss \$9.3B," USA Today, December 30, 2014. <https://www.usatoday.com/story/money/cars/2014/12/30/auto-bailout-tarp-gm-chrysler/21061251/>

These staggering compliance costs always find their way back to the pockets of consumers. According to a meta-analysis conducted by Salem Furth and David Kreutzer, both economic research fellows at the Heritage Foundation, “The quality-adjusted price of an average new vehicle sold in the U.S. is about \$6,200 above trend.”<sup>9</sup> These researchers contend CAFE standards are the primary reason why, stating, “If rising U.S. vehicle prices were due to material costs, technological changes, or global demand changes, similar trends would be occurring abroad. There is nothing to show that such is the case.”<sup>10</sup>

An extra \$6,200 on average would go a long way for most American families. Yet, again, there are more problems beneath the surface.

## **Consumer Safety**

There are real safety concerns presented by CAFE standards. Higher new vehicle prices mean that Americans are more likely to drive older vehicles, generally less reliable and with fewer safety features, for longer. Should a consumer actually decide to buy a new vehicle, the hidden CAFE tax means consumers will purchase smaller cars with fewer features, particularly safety features, than they otherwise could afford.

On the production side, CAFE standards present a serious safety issue as it pertains to the size and weight of new cars. This issue is outlined in detail in the testimony of Sam Kazman, general counsel at the Competitive Enterprise Institute (CEI), before an EPA public hearing on CAFE standards on September 6th, 2017. Quoting at length:

---

<sup>9</sup> Furth, Salim, and David Kreutzer, “Fuel Economy Standards Are a Costly Mistake,” The Heritage Foundation, March 4, 2016. <http://www.heritage.org/government-regulation/report/fuel-economy-standards-are-costly-mistake>

<sup>10</sup> *Ibid.*



“In 1992 a federal appeals court ruled that [the National Highway Traffic Safety Administration (NHTSA)] had illegally evaded the fact that CAFE reduces auto safety... The model year (MY) was 1990; the passenger car standard was 27.5 mpg. The court found that ‘the 27.5 mpg standard kills people.’... By comparison, the standards now scheduled through MY 2025 are far more stringent than 27.5 mpg. In fact, the estimated small-car standard for MY 2023 will be more than twice as high as that 27.5 number. So where are we today on the issue of CAFE and safety? ... The EPA-NHTSA Draft Technical Assessment Report (July 2016) admits the ‘relationship between vehicle mass and safety’ and the fact that ‘mass reduction continues to be an important technology option ... in meeting future ... standards’. These were the two primary facts underlying the DC Circuit’s finding that CAFE kills, and those facts remain unchanged to this day. In the face of these facts, NHTSA and EPA cross their fingers and hope for the best. They hope that mass reductions will ‘be concentrated in the heaviest vehicles’, or that ‘careful changes in design and/or materials used might mitigate some of the potential increased risk from mass reduction ....’. Note the key fudge words here: ‘*careful* changes ... *might* mitigate *some*’ of the risk. This is wishful thinking. Even worse is EPA’s January 2017 pronouncement on this issue, in which it claims that its MY 2022-25 standards ‘will have no adverse impact on automobile safety.’ EPA, Final Determination, p. 27. In comparison, look at what the Insurance Institute for Highway Safety (IIHS) says. Its message is the same, whether you’re choosing a car for yourself or your teenaged children: bigger, heavier vehicles are safer. NHTSA and EPA pin much of their no-safety-effect argument on the notion that vehicle size is more important than weight. But an IIHS study compared hybrid cars with their conventional, nonhybrid twins and

found that the 10% increased weight of the hybrids was associated with a 25% lower risk of occupant injury. The issue may not be fully resolved, but this is one strong indicator that, to the extent you can differentiate, weight is more important.”<sup>11</sup>

To summarize, automakers have been consistently reducing the size and weight of vehicles to assist in CAFE standard attainment while EPA and NHTSA have failed to consider the acknowledged risk this poses to consumer safety in their evaluations of the program.

## **Conclusion**

As an organization dedicated to lower taxes, less government, and more freedom, FreedomWorks Foundation finds the CAFE standards program to be a particularly egregious example of the perils of economic central planning. As outlined above, the program substantially burdens both consumers and automakers in a flawed attempt to achieve an obsolete policy objective. Of particular concern is the continued negligence of EPA and NHTSA towards the issue raised by CEI regarding the safety of vehicles.

For these reasons, FreedomWorks Foundation calls on EPA and NHTSA to thoroughly re-evaluate the CAFE standards program to include a review of its impact on vehicle safety and ultimately impose the least stringent standards permissible under law.

---

<sup>11</sup> Kazman, Sam, “Fuel Economy Regulations Threaten Vehicle Safety,” Competitive Enterprise Institute, September 7, 2017. <https://cei.org/blog/fuel-economy-regulations-threaten-vehicle-safety>

Respectfully submitted,

A handwritten signature in black ink, appearing to read 'Patrick Hedger', with a long horizontal flourish extending to the right.

Patrick Hedger  
Foundation Program Manager  
FreedomWorks Foundation  
400 N Capitol Street NW Suite 765  
Washington, DC 20001