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6/18/79

HOLD:

BROCK ADAMS MEMO IS NOW OUT OF
DATE. SI LAZERUS IS CHECKING
AROUND TO SEE IF AN UP-TO DATE
REPORT CAN BE PUT TOGETHER ON
THIS FOR THE PRESIDENT.

RICK

A handwritten signature consisting of the letters 'D' and 'R' in a cursive, stylized font. The 'D' is on the left and the 'R' is on the right, with a long horizontal stroke extending from the top of the 'R' to the right.

Date: May 28, 1979

MEMORANDUM

6/0
w/SS
~~at Desk~~

FOR ACTION:

Stu Eizenstat - *w/SS comment*
Frank Moore / Les Francis *NC*
Jim McIntyre
Charlie Schultze *NC*
Fred Kahn *attached*
Charles Warren *NE needs return*

FOR INFORMATION:

Vice President
Bob Lipshutz

FROM: Rick Hutcherson, Staff Secretary

SUBJECT: Brock Adams memo re Coordination of Fuel Economy Standards

YOUR RESPONSE MUST BE DELIVERED
TO THE STAFF SECRETARY BY:
TIME: 12 noon
DAY: Wednesday
DATE: May 30

memo may be pulled

ACTION REQUESTED:

Your comments

Other:

STAFF RESPONSE:

I concur.

No comment.

Please note other comments below:

PLEASE ATTACH THIS COPY TO MATERIAL SUBMITTED.

If you have any questions or if you anticipate a delay in submitting the required material, please telephone the Staff Secretary immediately. (Telephone 7052)



THE SECRETARY OF TRANSPORTATION
WASHINGTON, D.C. 20590

MAY 25 1979

MEMORANDUM FOR THE PRESIDENT
Attention: Mr. Rick Hutcheson, Staff Secretary
From : Brock Adams *Brock Adams*
Subject : Coordination of Fuel Economy Standards

I am intending shortly to respond to the request by the U.S. auto manufacturers for review of the 1981-84 automobile fuel economy standards. While the manufacturers have not filed a formal petition for review, the Department agreed early this year to consider their claim that a slightly lower schedule for the standards would be more cost effective than the standards I issued in July 1977.

In accordance with the Congressional statutory directive, the standards issued in 1977 covered vehicles manufactured up through 1985. In issuing the standards, we used information from the manufacturers and all other interested parties and we took into account the other major automotive requirements for the 1980-1985 period, particularly the statutory emissions levels that were just being enacted by the Congress and the requirements for automatic restraint systems which take effect beginning in 1982. In doing all this, we responded to the manufacturers' request that standards be established far in advance to permit long-range planning. The manufacturers all said they could comply.

In reassessing the standards recently, we have been trying to determine whether the manufacturers' compliance plans reflect the most cost-effective measures available for improving fuel economy. On the cost side, we have been examining not only the costs associated with various schedules of standards, but also the industry's overall capital requirements and its cash flow situation. Thus, our consideration of the economic practicability of the standards extends to the compliance costs for all vehicle regulatory programs and not simply the fuel economy one. We have also been in consultation with Doug Costle about the effect of emissions standards and testing procedures on fuel economy.

We will decide our response to the manufacturers following one additional meeting with the Domestic Policy White House staff next week. They have been reviewing all of the pertinent figures and our analysis of them. I wanted to have the benefit of their review prior to acting on this matter.

I have also talked with John Riccardo of Chrysler and have told him that I would not hesitate to employ the provision in the statute to waive penalties should Chrysler at some future date not succeed in meeting the fuel economy standards. The law allows such a waiver, following consultation with the Federal Trade Commission, if imposition of the penalties would have an anti-competitive effect.

Our current reassessment of the standards builds on an extensive analysis in the Department's January 1979 Report to the Congress on the feasibility of the 1981-84 fuel economy standards. In addition to examining the available technology and potential fuel savings, the report also considers the effects on the industry's operational practices (such as vehicle re-design cycle) and overall capital requirements, including those for other vehicle regulatory programs.

In the same way that the standards were coordinated with other pertinent agencies when first issued in 1977, we have been working closely with the Environmental Protection Agency and the Department of Energy particularly in this reassessment. We have shared with the EPA and DOE all of the factual information we have and both technical staff and policy officials have discussed the various aspects of the issues raised by the manufacturers. In this reassessment, we have given particular consideration to the fuel economy effects of the EPA emissions requirements and of some changes in fuel economy measurement procedures made by EPA last winter. We also have carefully reviewed analyses from two other Departments, a Commerce Department document suggesting that the standards should be lowered and one from the Department of Energy suggesting that the standards should not be changed.

I have put particular stress in the last two years on making sure that the National Highway Traffic Safety Administration properly coordinates any significant safety or fuel economy regulatory actions with other interested agencies. I am pleased with the extent to which they have carried out this

directive, not only with regard to the executive agencies, but also in establishing effective working relationships with staff on the Council of Economic Advisors, the COWPS, and Fred Kahn's office. At the present time, the National Highway Traffic Safety Administration is working closely with the Environmental Protection Agency on several other important regulatory issues concerning motor vehicles, such as the health effects of diesel particulates, accurate fuel economy measurements, the increasing of engine octane requirements as engine compression is increased to improve fuel economy, and van and light truck fuel economy.

Recently, staff from the Department, the EPA, FTC, the Justice Department and the Regulatory Council met to discuss the sufficiency of motor vehicle regulatory coordination. There was a consensus that with regard to actions initiated by the agencies there is a cooperative spirit and effective coordination, but that when the automotive industry or one particular company initiates a variety of requests with different agencies, such as Chrysler has been doing in the last three to five months, there is a lack of knowledge among the agencies about the variety of incoming communications and requests. This may be a tactical move by the industry but we are working to assure future coordination on such matters.

THE WHITE HOUSE

WASHINGTON

June 12, 1979

MEMORANDUM FOR: THE PRESIDENT

FROM: STU EIZENSTAT *Stu*
SI LAZARUS *SL*

SUBJECT: Brock Adams' May 25 Memo on
Coordination of Fuel Economy
Standards

Subsequent to Rick Hutcheson's receipt of the attached memo, several senior Executive Office advisors, including myself, Charlie, Fred, Anne and Jack, received an extensive briefing on this important issue from Joan Claybrook, Administrator of DOT's National Highway Traffic Safety Administration (NHTSA) and her staff. After the briefing, the Executive Office advisors met and decided to recommend to Joan and Brock that NHTSA open a new formal rulemaking proceeding on the 1981-84 fuel economy standards to permit a full public airing of competing analyses of the effects of the current standards. This way, the auto companies will have to provide public justification for their assertion that the current standards will be prohibitively costly, and NHTSA will have to provide public justification for its contrary conclusion. Interested parties in Congress, industry, and elsewhere will have an opportunity to react, before the administration makes its decision.

If DOT were to institute proceedings, the rule probably could not be changed to affect the 1981 model year. But if changes for the 1982-84 model years appeared necessary they could be made.

Joan stated that she could not respond without consulting Brock who was then and is now in France. Brock will be returning on June 11, and we will report back to you after we confer with him and Joan at that time.

Brock's memo does not recommend any action on your part, and you need take no action until Brock responds to our suggestion to reopen the issue for comment.



THE SECRETARY OF TRANSPORTATION

WASHINGTON, D.C. 20590

MAY 25 1979

MEMORANDUM FOR THE PRESIDENT

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From : Brock Adams

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directive, not only with regard to the executive agencies, but also in establishing effective working relationships with staff on the Council of Economic Advisors, the COWPS, and Fred Kahn's office. At the present time, the National Highway Traffic Safety Administration is working closely with the Environmental Protection Agency on several other important regulatory issues concerning motor vehicles, such as the health effects of diesel particulates, accurate fuel economy measurements, the increasing of engine octane requirements as engine compression is increased to improve fuel economy, and van and light truck fuel economy.

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ALUMINUM USAGE AND FUEL ECONOMY STANDARDS

Based on an analysis performed by Chase Econometric Associates, the Department of Commerce (DOC) has concluded that the current passenger automobile fuel economy standards will exacerbate U. S. dependence on foreign sources of aluminum inputs (alumina and bauxite) during the early 1980s and that the increase in demand for aluminum will contribute to balance of trade deficits and inflationary pressures on the domestic economy. DOC believes that if fuel economy standards that increase linearly to 27.5 mpg in 1.5 mpg increments are substituted for the current standards, auto industry demand for aluminum will decline significantly, lowering aluminum imports and reducing the annual rate of increase in the price of aluminum. Based on data provided by Ford and Chrysler, NHTSA finds that (1) the DOC assumption about aluminum usage per car in the early 1980s is excessively high and (2) a reduction in the passenger automobile fuel economy standards would not significantly reduce aluminum demand by the domestic auto industry.

1. DOC assumes that under the current standards, the average car will contain 225 pounds of aluminum in 1982-83, while under the linear standards, the average car would contain 150 pounds (75 fewer pounds) in 1982-83. In either case, aluminum usage would range from 200-250 pounds per car in 1985.

These assumptions imply that aluminum usage increases are extremely "front-loaded" during the early 1980s to comply with current fuel economy standards, presumably because manufacturers do not have time to use more cost-effective techniques to improve fuel economy. Projected aluminum usage data provided to NHTSA by Ford and Chrysler refute these assumptions. NHTSA asked General Motors for similar data, but GM has not supplied it to the Agency. Based upon GM information previously submitted to NHTSA, it appears that if all of the difference in vehicle weights between the alternate standards in 1982-83 was made up of aluminum, the aluminum usage would only differ by 25-30-pounds per car. A more recent Wall Street Journal article reported that GM plans to reduce projected aluminum usage per car in 1985 from 250 pounds to 200 pounds, due to rising prices. Thus, NHTSA believes that GM's current plans for aluminum usage are comparable to Ford's and Chrysler's.

The Ford and Chrysler projections show a steady, rather than sudden, increase in the amount of aluminum used per car during the early 1980s. Neither company plans to use aluminum to the extent assumed by DOC. Ford and Chrysler expect to use about 160 pounds per car in 1982-83 rather than the 225 pounds per car assumed by DOC. Chrysler does put ranges around its projections, because Chrysler would consider developing aluminum cylinder heads and engine blocks if aluminum prices do not rise dramatically.

Since the industry estimates for aluminum usage under the current fuel economy standards are similar to DOC estimates for aluminum usage under linear standards, it is likely that aluminum usage per car would only decline marginally if linear standards replaced current standards. Accordingly, NHTSA estimates that the replacement of current fuel economy standards with linear standards to 27.5 mpg would reduce aluminum usage by no more than 10-15 pounds per car in 1982-83. The total aluminum usage should differ negligibly in 1985 since the fuel economy standard for that year is the same under both schedules.

2. The Chase analysis projects primary aluminum capacity to grow by less than 500,000 metric tons annually during the early 1980s, while demand will grow by more than 800,000 metric tons annually. This difference in growth rates will lead to extremely high capacity utilization rates and force aluminum prices up considerably faster than the general rate of inflation.

A Chase graph of projected aluminum consumption by cars indicates that Chase expects aluminum consumption by the domestic auto industry to increase by approximately 100,000 metric tons annually, or about 12 percent of the annual increase in total demand. During 1977, the domestic passenger car market used less than 12 percent of all aluminum shipments, or about 670,000 metric tons (data in millions of pounds

are shown in the attached table). Since this proportion is only slightly lower than Chase's projected auto industry share of demand growth, passenger car usage is not a primary contributor to the expected growth in aluminum demand, but is just one contributor out of many. Even with Chase's assumptions, the auto industry would only be maintaining its current share of this growing market.

It should be noted that while shipments of aluminum to the automobile industry are significant, only a very small percent of these involve imports. Auto shipments account for 37 percent of all domestic shipments of aluminum ingots and 5.2 percent of all domestic products. Of these, only 34.0 and 2.0 percent, respectively, are imported. The last column in the attached table shows that roughly 12.7 percent of imported ingots and 0.1 percent of the imported mill products are used by the domestic auto industry -- not a very large amount.

3. DOC estimates that with the current passenger automobile fuel economy standards aluminum prices will rise at an average rate of 14 percent annually between 1979 and 1982. If linear standards replace the current standards, DOC estimates that aluminum prices will rise at an annual rate of 12 percent annually during the same time frame.

DOC has not yet provided an explanation of how these figures were derived, but it appears they assumed that with lower standards, domestic auto industry demand for aluminum would not grow at all. If the annual demand growth rate for aluminum was reduced by the auto industry's 12 percent share, future annual price increases would be ameliorated by this fraction of DOC's projected 14 percent, or by about 1.7 percent annually. The average annual price increase would thus be 12.3 percent.

It seems very unlikely that lower standards would eliminate additional demand for aluminum by the auto industry. The long-run growth rate for automobile demand is about 1.5 to 2 percent annually. With a constant level industry demand for aluminum, aluminum usage per car would decline 1.5 to 2 percent annually during a time period when fuel efficiency requirements would be rising 1.5 mpg annually. NHTSA finds this rather difficult to believe, but this is the only way that the Agency could replicate DOC's estimates.

4. DOC estimates that, without a recession, the price of aluminum per pound would be 3-4 cents lower in 1982 if linear standards replaced current fuel economy standards. In the 1982 recession scenario, Chase estimates the price of aluminum per pound would be 7 cents lower with the linear standards.

NHTSA suspects that DOC has reversed its economics. With the aluminum industry running at full capacity, additional demand for aluminum to meet fuel economy standards should command significant price premiums. During a recession, however, NHTSA would expect the aluminum industry to have excess capacity. Under these circumstances, the additional demand should have little effect on aluminum prices.

5. DOC states that

"...the shortfall between the quantity of aluminum demanded in this country and U. S. - produced supplies will be about 1.5 million metric tons (annually in 1982-83) with front-end loading and about 1.1 million metric tons without. Given Chase's estimates of prices (\$1625 per metric ton) this difference (400 thousand metric tons) amounts to about \$650 million in the country's balance of trade (annually)."

Since DOC has overstated the difference in aluminum usage per car in the 1982-83 time period between the two sets of fuel economy standards by a factor of at least 5 (15 lb vs. 75 lb), DOC's projected balance of payments deficit is similarly overstated. The trade deficit contribution due to 15 lb/car would be less than \$130 million annually during 1982-83 if all the additional aluminum were imported.

DOC also neglects the reduction in oil imports under the existing fuel economy standards. Currently, imported oil averages about \$18 per barrel. If the average imported oil price rose with the general level

of inflation in the U. S., it would be approximately \$23 per barrel in 1982-83. The difference in automobile fleet fuel consumption between the current and linear standards is 11.2 million barrels (31,000 barrels/day) in 1982 and 19.3 million barrels (53,000 barrels/day) in 1983. This difference works out to a \$260 million improvement in our balance of trade in 1982 and a \$440 million improvement in 1983 alone without even considering the benefits in future years. This reduction in oil imports would more than offset increases in aluminum imports.

In conclusion, NHTSA believes that DOC has overstated the effect of auto industry demand on aluminum prices and import levels. In addition, DOC has overstated the difference in aluminum usage per car between alternate fuel economy standards by at least a factor of 5. This has led to erroneous conclusions concerning the balance of trade implications of the existing passenger car fuel economy standards.

ALUMINUM USAGE IN AUTOMOBILES
1977--SHIPMENTS AND IMPORTS
 Millions of Pounds

Product Categories	Shipments to Auto Industry	Total Domes. Shipments	Auto Shipments as a % of Total	Total Exports	Total Imports	Total Supply Imports and Shipments ^{4/}	Total Imports as a % of Total Supply	Rough Estimates of
								Auto Imports as a % of Total Imports ^{5/}
Ingot	954	2,575	37.0	204	1,341	3,916	34.2	12.7
Total Mill Products	527	10,054	5.2	522	166	10,220	2.0	0.1
Sheet & Plate	378	5,821	6.5	344	113	5,934	1.6	0.1
Foil	35	791	4.4	26	11	802	1.4	0.1
Rolled & Continuous ^{1/}	11	221	5.0	28	18	239	7.5	0.4
Cast Rod & Bar								
Extruded Shapes	58	1,904	3.0	9	22 ^{2/}	1,906	0.1	negligible
Extruded Pipe & Tube	14	165	8.5	20	--- ^{3/}	---	--	--
Drawn Tube	13	103	12.6	1	--- ^{3/}	---	--	--
Bare Wire	1	74	1.4	15	--- ^{3/}	---	--	--
Forgings	14	100	14.0	6	---	---	--	--
Impacts	3	15	20.0	--	---	---	--	--

SOURCE: Aluminum Association, with the exception of import data which comes from D.O.C.

¹ Imports of rods under 0.375" are included with wire. Includes extruded rod and bar.

² Includes angles, sections, miscellaneous.

³ Not comparable.

⁴ Shipments do not include exports.

⁵ Estimate derived by multiplying automobiles as a percent of total shipments of each category by imports as a percent of total supply for the same category.

Date: May 28, 1979

MEMORANDUM

FOR ACTION:

Stu Eizenstat
Frank Moore /Les Francis
Jim McIntyre
Charlie Schultze
✓ Fred Kahn

FOR INFORMATION:

Vice President
Bob Lipshutz

FROM: Rick Hutcheson, Staff Secretary

SUBJECT: Brock Adams memo re Coordination of Fuel Economy Standards

YOUR RESPONSE MUST BE DELIVERED
TO THE STAFF SECRETARY BY:

TIME: 12 noon

DAY: Wednesday

DATE: May 30

ACTION REQUESTED:

Your comments

Other:

STAFF RESPONSE:

I concur.

No comment.

Please note other comments below:

I advise holding this memorandum. All of the President's principal advisors met with Alan Butchman and Joan Claybrook of DOT on May 29, to review their latest analysis of the cost-effectiveness of the automotive Fuel Economy Standards. The advisors have asked DOT to reopen the record in this rule-making to obtain the views of the automotive industry and the public.

DOT has promised to respond to this request by close of business May 31.

Whether they agree or disagree, the May 28 memorandum to the President from Secretary Adams is out of date. The Secretary should reflect these more recent consultations and decisions in a revised memorandum to the President, as soon as they produce either agreement or disagreement: in the latter event, what would go to the President would be an options memorandum for his decision.

Fred Kahn

PLEASE ATTACH THIS COPY TO MATERIAL SUBMITTED.

If you have any questions or if you anticipate a delay in submitting the required material, please telephone the Staff Secretary immediately. (Telephone 7052)