SUBMITTED TESTIMONY OF

AMERICAN INTERNATIONAL AUTOMOBILE DEALERS ASSOCIATION

Hearing on Increasing U.S Competitiveness and Preventing American Jobs from Moving Overseas: How Border Adjustment and Other Policies Will Boost Jobs, Investment, and Growth in the U.S.

Tuesday, May 23, 2017
1100 Longworth House Office Building
10 a.m.

HOUSE OF REPRESENTATIVES

COMMITTEE ON WAYS AND MEANS

Hearing on Increasing U.S Competitiveness and Preventing American Jobs from Moving Overseas: How Border Adjustment and Other Policies Will Boost Jobs, Investment, and Growth in the U.S.

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This statement is submitted by the American International Automobile Dealers Association[1] (AIADA) in response to the hearing held on May 23, 2017 in the Committee on Ways and Means regarding the proposed border adjustment tax (BAT). Established in 1970, AIADA is and continues to be the only association whose sole purpose is to represent America's international nameplate automobile franchises that sell and service vehicles in the U.S. Our mission is to increase awareness in Washington, D.C., and around the country of our members' contributions to their communities and the American economy, and to preserve and promote a free market for international brand automobiles in the United States.

In cities and towns across our country, dealers of international brands operate 9,600 franchises and employ 577,000 Americans with a payroll of 32 billion dollars. Together they account for an additional 527,000 indirect jobs. In 2016, those same franchises sold 8.4 million vehicles, or 59 percent of total U.S. market share. Moreover, international nameplate auto dealers did not stop there; in 2016 they spent an overwhelming $4.8 billion on advertising and sold $54 billion in parts and services. International nameplate auto dealers are a large, visible, and vital cog in our nation's economy, and they rely on the competitive pricing of their products to maintain and grow their businesses.

AIADA's dealer members represent the retail side of the international auto manufacturing industry, which has also invested heavily in the United States. In fact, these brands have more than doubled their production in the U.S. over the past 15 years, making them responsible for 47 percent of all vehicles built here in America. In 2016 alone, 5.5 million vehicles were built by international nameplate manufacturers in the U.S., creating 1.29 million direct and indirect U.S. jobs. These same companies invest $75 billion in U.S. operations. Additionally, in 2016 international automakers contributed to the 265,000 jobs that were needed to produce and

[1] AIADA represents America's international nameplate automobile franchises that sell and service the following brands: Acura, Aston Martin, Audi, Bentley, BMW, Ferrari, Genesis, Honda, Hyundai, Infiniti, Jaguar, Kia, Land Rover, Lexus, Maserati, Mazda, Mercedes, MINI, Mitsubishi, Nissan, Porsche, Rolls Royce, Scion, Smart, Subaru, Toyota, Volkswagen, and Volvo. These retailers have a positive economic impact both nationally and in the local communities they serve, providing more than 500,000 American jobs. Visit AIADA online at www.aiada.org.

export the vehicles they built in the U.S. These exports totaled 925,000 vehicles, which were exported to over 140 countries.

AIADA highlights all this information to ensure that the committee members are aware of the economic impact of international auto dealers and automakers in the United States. As an industry we are very concerned with the proposed border adjustment tax provision currently being discussed by House Republicans in their "Better Way" tax reform proposal. If passed into law, the 20 percent tax on all goods and services crossing the border into our country would have a number of detrimental effects on American workers, consumers, dealers, and manufacturers.

Made in America

Contrary to what border adjustment tax proponents might say, there is no "Made in America" tax. Under the current tax system, both imported and domestically produced products are treated equally. When an American and foreign firm sell in another country, they both pay a corporate tax and a value added tax (VAT). American and foreign firms selling a product in the U.S. both pay just a corporate tax – the difference is that the American firm pays a 35 percent rate, while a foreign manufacturer might only pay a 17 or 20 percent rate. If American firms are at a disadvantage, it is due to the exorbitant American corporate tax rate, not a need to border adjust taxes.

Misconceptions also persist about what actually constitutes an American product. For example, the automobile industry is so globally integrated, that many automobiles traditionally thought of as "foreign" are actually built right here in the U.S. and with more U.S. parts than the traditional American brands. Not one car sold in America contains 100 percent domestically produced content. Therefore, the 20 percent import tax will increase the price on all new vehicles, not just imported vehicles.

In fact, the 2016 Cars.com American Made Index[2] (AMI), which looks at cars on a model-by-model basis, not by manufacturer, put the Toyota Camry at the top of their chart. The AMI recognizes cars that are assembled here, using a high percentage of domestic parts, and which are bought in large numbers by American consumers. The Toyota Camry is followed by: Honda

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[2] Cars.com's American-Made Index rates vehicles built and bought in the U.S. Factors include the percentage of parts considered domestic under federal regulations, whether the car is assembled in the U.S. and U.S. sales. We disqualify models with a domestic-parts content rating below 75 percent, models built exclusively outside the U.S. or models soon to be discontinued without a U.S.-built successor.
Domestic-parts content stems from Congress' 1992 American Automobile Labeling Act, which groups the U.S. and Canada under the same "domestic" umbrella. It's one of the bill's imperfections, but the AALA is the only domestic-parts labeling system car shoppers can find on every new car sold in America. Other domestic-content ratings — namely those used for the North American Free Trade Agreement and the corporate average fuel economy programs — are unpublished, give a simple over/under indication or lump even more countries, like Mexico, into the "domestic" pool. https://www.cars.com/articles/the-2016-carscom-american-made-index-1420684865874/

Accord (2), Toyota Sienna (3), Honda Odyssey (4), Honda Pilot (5), Chevrolet Traverse (6), GMC Acadia (7), and Buick Enclave (8).

Cars.com also studied employment and production figures to see how many U.S. assembly-plant jobs each model supports. The 2016 analysis shows that the Toyota Camry still supports more assembly-plant jobs of any vehicle studied. The remaining AMI autos followed in the same order as in the initial ranking; Honda Accord (2), Toyota Sienna (3), Honda Odyssey (4), Honda Pilot (5), Chevrolet Traverse (6), GMC Acadia (7), and Buick Enclave (8).

Finally worth noting, the Cars.com AMI used production numbers instead of sales figures as a measure of assembly-line employment. If using that data, the top two autos actually switch positions with the Honda Accord coming out on top. The remaining rankings follow as originally ranked: Toyota Camry (2), Toyota Sienna (3), Honda Odyssey (4), Honda Pilot (5), Chevrolet Traverse (6), GMC Acadia (7), and Buick Enclave (8).

In an increasingly global economy, it would be ill-advised and short-sighted to attempt to classify products, particularly automobiles, into categories of imports and exports and therefore pick winners and losers. Many Americans are employed as a result of the international nameplate automobile industry, including the 577,000 employed by international nameplate automobile dealers, and many more Americans benefit from being able to purchase quality products at affordable prices that result from this integrated supply chain.

Affordability

As mentioned before, ALL vehicles sold in the U.S. have non-U.S. parts content. Therefore, the 20 percent border adjustment tax will increase the price on all new vehicles, not just imported vehicles. The proposed border adjustment tax will significantly impact new car sales through higher prices, reduced demand, restricted choice, and an increased inability by customers to qualify for higher loans.

In fact, should the proposed border adjustment tax be implemented, a recent study conducted by the Center for Automotive Research[3] pegs the average price increase at about $2,000 per vehicle. Another study by Deutsche Bank says we should expect an increase of $2,300 per vehicle, reducing U.S. demand by 1.2 million units per year in the short term and 0.5 million units in the long term. That is a striking decrease in sales and would cause a dramatic downstream impact on the entire dealership operation.

The auto industry already has an affordability issue. Today's average vehicle transaction price hovers around $35,000. Given today's average new car loan rates and terms, with 2 percent down and 66 months financed, this could increase the payment for the average car buyer by

[3] CAR's mission is to conduct independent research and analysis to educate, inform and advise stakeholders, policy makers, and the general public on critical issues facing the automotive industry, and the industry's impact on the U.S. economy and society. http://www.aiada.org/sites/default/files/CARS%20Study.pdf

nearly $100 per month. The current average monthly payment, according to Cox Automotive,[4] is $424, and if the border adjustment tax was implemented, AIADA estimates it would increase to $509. A recent presentation by Cox Automotive states that according to Kelley Blue Book, 66 percent of car buyers are concerned with affordability, and are more concerned with the monthly payment than the overall price. A $100 per month increase in a new car payment will cause many consumers to be priced out of the car market all together. Furthermore, to arrive at that monthly payment, consumers would also need longer loan terms. Cox Automotive again finds that 75 percent of automotive loans in 2015 were longer than 5 years versus 51 percent in 2009.

The concern of affordability is not new to the auto industry. As the regulatory burden of manufacturing autos has increased with time, so has the cost of the vehicles they produce. But what has not increased for consumers is household income. Cox Automotive found that while the current average price of a new car has increased to $35,496, an increase of $2,280 since 2015, the median U.S. household income has only risen 3 percent in the last 20 years. That's a 35 percent increase for a new vehicle compared to a 3 percent income increase.

The impact of the proposed border adjustment tax would be felt throughout the entire dealership. In addition to the increase in the cost of the vehicle, servicing and repairing a car would also icrease. Analysts predict that the cost of gasoline would also rise approximately 30 cents per gallon[5]. Consumers least able to afford the added cost will be the most impacted. Customers need safe, new cars and trucks to transport their families and get to work. They don't need a new consumer tax. Nor do they need tax reform relying on untested economic models and the hope of a quick currency adjustment that would supposedly make the affordability problem disappear.

Currency Rates

The idea that currency will adjust and the dollar will appreciate by a significant amount, rendering the increase in costs of all imported goods negligible, is a central justification that has been used by border adjustment tax proponents. However, experts indicate this argument is flawed and lacking any real-world examples.

An economic report released in May 2017 by the international macroeconomics firm Capital Economics titled, *Border adjustment taxation - the implications*[6], finds the economic theory behind the border adjustment tax to be a "gross simplification" of today's currency markets.

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[4] Cox Automotive is a leading provider of products and services spanning the automotive ecosystem. No matter the stage of the auto buying or selling process, we have a solution for clients of any size.

[5] The Brattle Group, Border Adjustment Import Taxation Impact on the U.S. Crude Oil and Petroleum Product Markets, http://www.brattle.com/system/publications/pdfs/000/005/384/original/FINAL_Border_Tax_Paper_2016_12_16.pdf?1481912863

[6] *Border adjustment taxation – the implications*, https://www.rila.org/Public-Policy/Documents/Capital%20Economics%20-%20Border%20adjustment%20tax%20analysis%20Final%20-%20May%202017.pdf

The report concludes that even in the long-term, the dollar will appreciate no more than 8 percent in response to the House proposed border adjustment tax—well short of the 25 percent it has been suggested will be needed to offset higher costs on the thousands of items Americans buy every day.

Additionally, in congressional testimony in February, Federal Reserve Chair Janet Yellen herself noted that "a strong set of assumptions is needed to believe that markets would fully offset"[7] the price increases which would result from the border adjustment tax. Respected financial institutions CITI[8], Goldman Sachs[9], and J.P. Morgan Chase[10] have all also called into question the currency assumptions made in the plan.

In reality, there is just no way to tell if or how currencies will react, and it is too much of a gamble to risk real-world jobs and incomes on uncertain economic theory.

Closing

The automotive industry in the U.S. is constantly evolving, and international nameplate automobile manufacturers and dealers are designing, building, and selling more vehicles across the U.S. than ever before. In the process, they are redefining the meaning of an "American" car. International nameplate dealers are growing their investment in the American economy and communities in a variety of ways and today provide the majority of America's auto retailing jobs and vehicles for American consumers, selling 59 percent of the new cars purchased by American consumers in 2016.

AIADA strongly supports a pro-growth comprehensive tax reform bill, but we believe the proposed border adjustment tax provision will have unintended consequences that will cause harm to our dealerships, their employees, and their customers.

AIADA and its 9,600 American auto dealers strongly oppose the proposed border adjustment tax.

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[7] Bloomberg Markets, *Currency Traders Spot Fatal Flaw in Republicans' Border Tax Plan*, https://www.bloomberg.com/news/articles/2017-04-18/currency-traders-spot-fatal-flaw-in-republicans-border-tax-plan

[8] Willem Buiter, "Exchange Rate Implications Of Border Tax Adjustment Neutrality," Citi Research, 2/22/17

[9] Brian Faler, "Border Adjustment Debate Giving Washington A Crash Course In Currency Markets," Politico Pro, 2/1/17

[10] Brian Faler, "JP Morgan: Border Adjustment Tax Plan Will Shake Wall Street," Politico Pro, 12/20/16

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Border Adjustment Tax: Estimated Impact on U.S. Vehicle Prices

Overview

This analysis highlights the immediate impacts of implementing a border adjustment tax on U.S. vehicle prices.

- The border adjustment mechanism is being considered as an integral part of the major corporate tax reforms that are expected to be introduced in the 115th Congress.
- Border adjustment is being considered as a way to generate sufficient tax revenues to offset the impact of lowering the overall corporate tax rate.
- The border adjustment mechanism functions by excluding cash-inflow from overseas (export revenue) and cash- outflow to foreign countries (import costs) in the taxable profit calculation.
- Automakers and suppliers that sell and manufacture in the United States are part of a highly globally-integrated industry.
- The automotive industry would see significant changes to their tax base under a border adjustment; the tax would be highly disruptive to U.S. vehicle sales and production.

Methodology

- This analysis is based on confidential financial data received from automakers representing over 50 percent of U.S. light vehicle sales.
- This analysis holds exchange rates constant, and examines only a price response to the implementation of border adjustment.
- The estimates are based on the impact of the proposed border adjustment tax on imported vehicles as well as parts used for vehicle production in the United States.
- This analysis estimates a price increase with no change in unit sales or domestic production—both of which would be affected by a price increase of this magnitude.

Findings

In response to the border adjustment:

- U.S. light vehicle prices would increase 5.6 percent in immediate response to border adjustment.
- Since the current U.S. average transaction price for new vehicles is $34,968 (Kelley Blue Book, 2017), average per vehicle price increases are estimated at $1,970.
- Assuming U.S. sales at 17.5 million vehicles in 2016, the light vehicle price increase represents $34.6 billion in higher costs to consumers.
- The $1,970 price increase resulting from the proposed border adjustment masks the turbulence and churn in the market which would significantly impact models, segments, and even entire companies.

http://mediaroom.kbb.com/2017-02-01-New-Car-Transaction-Prices-Remain-High-Up-More-Than-3-Percent-Year-Over-Year-In-January-2017-According-To-Kelley-Blue-Book

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