UNITED STATES ENVIRONMENTAL PROTECTION AGENCY
WASHINGTON D.C. 20460

OFFICE OF THE ADMINISTRATOR
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EPA-COUNCIL-10-xxx

The Honorable Lisa P. Jackson
Administrator
U.S. Environmental Protection Agency
1200 Pennsylvania Avenue, N.W.
Washington, D.C. 20460

Subject: Advisory on a Preliminary Draft of the Second Section 812 Prospective Study of the Benefits and Costs of the Clean Air Act Amendments

Dear Administrator Jackson:

The Advisory Council on Clean Air Compliance Analysis (Council) met on May 4-5, 2010 to provide advice on the Agency's preliminary draft report on benefits and costs of the Clean Air Air Amendments (CAAA) of 1990. The second prospective study of benefits and costs from the CAAA covers the period 1990 to 2020. In accordance with Section 812 of the CAAA, the EPA Project Team has undertaken a series of technical studies to evaluate air quality scenarios for futures with and without the CAAA, and to estimate the costs of compliance with CAAA provisions and the benefits associated with projected improvements in air quality. Section 812 also established the Council to review the data, methodologies, and validity and utility of the benefit-cost studies prepared under the section. At the meeting, the Council reviewed the preliminary draft report (dated April 2010) for the Second Prospective Study, and supporting reports on costs and benefits of compliance with the CAAA. The Council also considered the advice and recommendations of its subcommittees regarding stand-alone technical documents prepared by the EPA Project Team to support the Second Section 812 Prospective Study.

The Charge to the Committee requested the Council's advice on the Project Team's choice of data and methodologies, as well as on the overall utility of the preliminary draft integrated report. The detailed recommendations on data and methods used in the development of the various air quality scenarios, and in estimation of health and ecological effects under those scenarios, are contained in the Council subcommittee reports, being provided to the Agency under separate cover (list final report numbers when available…). Attention to these suggested improvements to data and analyses will enhance the validity of the final benefit estimates. In addition, the Council has asked its Air Quality Modeling Subcommittee (AQMS) to review the final adjusted PM emissions inventories (including application of the Modeled Attainment Test

Software, or MATS) when these are available from the Project Team. The focus of this advisory letter, therefore, is on the preliminary integrated report for the Second Section 812 Prospective Study, with some additional comments on the benefits valuation and direct cost analyses that support the integrated report.

The Council commends the EPA Project Team for its preparation of the second prospective analysis. This project is ambitious in scope, incorporates advances in analysis of environmental regulation, and should have significant impact on public understanding of the 1990 Clean Air Act Amendments (CAAA).

The second prospective analysis is intended to provide an overall perspective on the benefits and costs of the 1990 CAAA for the period 1990 through 2020. This is an ambitious undertaking that confronts many challenges due to limitations in scientific understanding, modeling, and relevant data. We offer several comments and suggestions for improving the analysis and presentation of the work.

Framing and Interpretation

The Council suggests that the framing and interpretation of the second prospective study should be clarified. The draft report could be misinterpreted as estimating the actual benefits and costs of the world as it exists (or will exist) in 2000, 2010, and 2020 compared with the world as it would have existed in those years had the 1990 CAAA not been adopted. In fact, the analysis is more circumscribed. First, it is concerned with decadal trends in pollution, health, and compliance costs, not with shorter-term variations that may result from variations in weather, economic growth, and other factors. Second, it takes many factors as fixed, even if they are likely to change over the 1990-2020 period, including climate and atmospheric emissions from Mexico and Canada. Third, it treats many factors as exogenously determined, neglecting any effects of the adoption of the CAAA. Examples include the growth, geographic distribution, and composition of population and economic activity, prices of oil and other resources, as well as climate and emissions from other countries.

Understanding the framing and boundary conditions of the analysis is important to interpretation of the report. First, because the analysis assumes constant (2002) meteorology, it is inappropriate to compare simulated and measured patterns of pollution in modeled years such as 2000 and 2010 without accounting for differences between simulated and realized meteorology. Similarly, it is inappropriate to compare the levels, distribution, and composition of population and economic activity in specific years with actual values without accounting for economic and other fluctuations. It may be useful for the project team to include additional analyses characterizing uncertainty about the overall benefits and costs of the CAAA or at least sensitivity to variation in the boundary conditions.

A related point concerns assumptions about compliance or “rule effectiveness” that can vary across domains. For local sources, the analysis includes assumptions about the costs of unidentified control measures that are needed to ensure compliance with the CAAA. It would be useful to state explicitly what assumptions are made about compliance, and how these affect estimated benefits and costs.

The second prospective report serves multiple purposes. One goal is to estimate the total benefits and costs of the CAAA over the study period (1990 – 2020). A second is to provide a comprehensive assessment of the benefits and costs of the CAAA, including effects that may be small relative to the total, but may be important to some stakeholders. A third is to develop methods for better quantifying benefits and costs that are not well estimated in previous Section 812 and other reports of the benefits and costs of air quality regulations. A fourth is to identify high-priority areas for research.

The tension among these goals has implications for the analysis and presentation of results. For example, the quantified benefits are dominated by the reduction in mortality risk associated with lower concentrations of fine particulate matter ($PM_{2.5}$). The total quantified benefits and uncertainty about their magnitude is determined almost entirely by the components of the analysis that estimate changes in annual $PM_{2.5}$ concentrations, the slope of the concentration-response function for mortality, and the monetary valuation of mortality risk. For the first goal, most of the emphasis in the report should be on these factors.

For the second goal, it is important to consider other benefits of the CAAA, including effects of other pollutants (e.g., ozone and hazardous air pollutants) and consequences other than mortality, including reductions in morbidity and a range of effects on agriculture, forestry, unmanaged ecosystems, and on construction and other materials. This aspect of the report is somewhat spotty in its coverage, reflecting limitations of scientific knowledge and data. Some effects are treated comprehensively (e.g., the relationship between ozone exposure and mortality) but others are treated only in the form of case studies that represent a tiny share of the total effect in some domain. For example, quantified effects on agriculture are limited to effects of ozone, and exclude acidification. Quantified effects on forestry and unmanaged ecosystems are for selected effects in or near the Adirondacks, and the only quantification of the effects of hazardous air pollutants (HAPs) is a case study of the health effects of benzene emissions in the Houston metropolitan area. There appears to be no reasonable basis to extrapolate from these case studies to the larger domains of which they are examples. Many of the non-fatal health effects are valued using cost-of-illness methods that do not fully capture the gain in well-being from improved health.

The incomplete coverage is largely justified by the absence of comprehensive data and estimates of exposure-response functions for various pollutants and endpoints, but it is difficult for the reader to have a sense of what share of benefits (and perhaps costs) of the CAAA are included in the quantified components. To a large extent, the report describes what can be seen under a modest number of lamp-posts, without attending to other existing lamp-posts (e.g., other case studies that could have been performed) or attempting to characterize what may be concealed in the territory not illuminated by lamp-posts. The Council recommends that the report should be written to help readers understand what effects are, and are not, quantified, and to explain why it is not possible to generalize from the limited case studies.

A third purpose of the report is to develop and illustrate improved methods for quantifying the benefits and costs of air-quality regulations. One improvement compared with the first prospective analysis is the adoption of a "one-atmosphere" approach using a single model (CMAQ) to simulate (virtually) all of the air quality parameters needed for the project. In addition to the case studies (e.g., ecosystem effects in the Adirondacks, benzene in Houston), the report includes supplementary analyses using a computable general equilibrium (CGE) model and a dynamic population-simulation model. Each of these analyses demonstrates a theoretically superior method for quantifying the effects of the CAAA, but these methods have not been sufficiently well-developed to provide the levels of geographic and other detail that are of interest and can be provided using the primary analytic tools. The Council supports the development of these improved methods and encourages EPA to continue to improve them so that they may be used in future analyses.

Concomitant to the attempts to provide a comprehensive description of the benefits and costs of the CAAA and the development of methods for better quantifying these effects, the report helps to highlight areas in which new research would be valuable for quantifying (or better quantifying) certain effects. The Council suggests that implications for research priorities be described directly in the report and that the Project Team consider the merits of conducting an explicit value of information study to help rank research priorities.

A characteristic of the analysis is that it attempts to base estimates of particular effects on specific papers in the peer-reviewed scientific literature, and refrains from making estimates when no specific papers are available. This feature is commendable, in that it seeks to ensure that results are based on solid evidence, but it has the drawback of producing spotty coverage, treating similar effects using inconsistent methods, limiting the analysis to incomplete models, and perhaps providing too much weight to idiosyncratic error in a particular study. To some extent, it might be preferable to adopt a smoother approach in which estimates of similar effects are treated more similarly, drawing on a broader literature.

The tension between these approaches is analogous to a common question in statistical estimation: to what extent does the quality of an estimate improve or worsen as one moves from a very small but relevant sample to a broader and more diverse sample? As an example, in estimating direct costs, estimates of learning-curve effects in some industries are based on a single paper studying that industry, whereas it might be more credible to assume similar learning curves across a set of industries and use a common estimate for all industries in that larger set. In valuing changes in visibility, values for national parks are restricted to the parks included in a particular study while values for residential visibility in metropolitan areas without direct estimates are assumed to be similar to values estimated for comparable areas with direct estimates. (Moreover, visibility is measured using different concepts – visual range and deciviews – in the two contexts, because those were the measures used by the original studies.) Exposure-response functions for materials damage appear inconsistent and incomplete as they differ substantially in form by the affected material and do not incorporate humidity or acidity.

Presentation

The Council supports the Project Team’s plan to report the results of the 812 analyses using several documents (and possibly websites) rather than as a single volume. The primary integrated report should be accessible to knowledgeable readers and provide a clear explanation of the framing, primary analytic methods, and interpretation of the study results. Many of the technical details should be provided in subsidiary reports, with clear linkages to the integrated report.

The Council suggests it is important to provide sufficient context for understanding the primary results. The estimated benefits of the CAAA are on the order of $2 trillion per year in 2020, on the order of $5,000 per capita or 10 percent of income. To put these benefits in context, it would be useful to summarize the extent to which they reflect improvements in air quality subsequent to 1990 and to what extent they represent preventing deterioration of air quality that is assumed would have occurred in the absence of the CAAA. The report could discuss the possibility that, had the 1990 CAAA not been adopted, other federal or state regulations or voluntary actions might have prevented some of the degradation that is modeled in the without-CAAA scenario, and so some of the benefits of the CAAA would have been achieved. However, it should also note that these actions would have entailed costs, and so some of the costs of the CAAA would have also been incurred. The Council concurs with the EPA Project Team that it would be quite difficult to specify any alternative to the without-CAAA scenario other than the assumption that no further control measures would have been implemented.

It would also provide helpful context to compare the simulated air quality with and without the CAAA with actual air quality in prior years (e.g., 1960, 1970, 1980) and particular locations (e.g., the six cities included in the Harvard cohort study).

The report also should provide some interpretation of the distribution of benefits and costs across components, both endpoints and control measures. As already noted, the quantified benefits are dominated by PM-related mortality, but other benefits that may be large are not well quantified. A substantial share of total compliance costs is associated with measures that regulate emissions from non-EGU industry, primarily to control ozone. Simple comparison suggests that the benefit-cost ratio is much more favorable for controlling PM than ozone, but this does not imply that future ozone controls are not cost-justified.

In presenting an overall summary, the project team may wish to include the benefits (and costs) of aspects of the CAAA that have not been analyzed as part of the second prospective report, but are available from the first prospective or retrospective reports. These include regulations on lead and on CFCs and other stratospheric-ozone depleters.

Comparison between the results of the second and first prospective reports are helpful for understanding the implications of the new analysis, but these are likely to be of more interest to technically oriented readers, and might better appear in an appendix or subsidiary report rather than in the primary integrated report.

Characterization of Uncertainty

The second prospective report characterizes uncertainty about the estimates using a variety of approaches, including probabilistic uncertainty analysis, sensitivity analysis, tables reporting qualitative evaluation, and alternative analyses. Some sources of uncertainty are evidently ignored (e.g., climate change).

Comprehensive uncertainty characterization is a huge challenge, and the Council commends the project team for its attention to this issue. It suggests providing a more comprehensive discussion of the strategy for characterizing uncertainty, explaining when different approaches are adopted, and how the approaches should be interpreted. For example, probability distributions associated with Monte Carlo analysis account for uncertainty in the factors for which input distributions are provided (e.g., slope of the exposure-response function for $PM_{2.5}$ and mortality) but are conditional on other factors treated as fixed (e.g., the difference in $PM_{2.5}$ concentrations between with-CAAA and without-CAAA cases in 2020).

The attempt to qualitatively characterize uncertainties with respect to the likely sign and magnitude of their effects, in the tables concluding each chapter, is laudable, although the Council suggests the project team may be able to better explain the magnitude (e.g., a 5 percent of net benefit cutoff for major effect may be too small given the scale of some of the uncertainties).

Lessons Learned

The Council is impressed with the scale of effort the EPA Project Team has devoted to the series of Section 812 reports. It encourages the team to reflect on these efforts and to document lessons learned regarding allocation of effort, types of analytic tools, and other choices from which subsequent efforts would benefit.

Health Benefits

Overall, the Council notes that the studies relied on to value changes in health risk are rather dated. For mortality risk, the estimates of value per statistical life (VSL) continue to be drawn from the 26 studies originally identified for the retrospective analysis, most of which rely on data from the 1980s or earlier. For morbidity risk, many of the studies are similarly dated and some endpoints are valued using cost-of-illness methods. Particularly for mortality risk, there are questions about the extent to which VSL varies by age, health status, and characteristics of the risk (such as whether the exposure is voluntary or controllable and whether it causes traumatic injury or disease), and a number of newer studies address these issues. Given the importance of VSL for total benefits, the Council suggests that the report discuss the extent to which there is evidence supporting variation in VSL by these factors and how much affect that could have on the total benefits (see, e.g., the symposium on age-dependence of VSL in the Review of Environmental Economics and Policy[1]).

In addition, if the difference in risk between the with-CAAA and without-CAAA scenarios is large, it may be inappropriate to use marginal estimates of rate of substitution between wealth and mortality risk. As noted above, the average per capita benefit is on the order of 10 percent of income in 2020. This value is large enough that the difference between willingness to pay to reduce exposure from the without-CAAA scenario (compensating variation) and willingness to accept compensation to forgo the exposure reduction (equivalent variation) may be significant.

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[1] Symposium: Mortality-risk Valuation and Age. 2007. Review of Environmental Economics and Policy 1(2):228-282.

Estimates of the slope of the exposure-response function for PM and mortality are based on two well-studied epidemiological cohorts and an expert elicitation study. The Council agrees with its Health Effects Subcommittee that these studies are a good foundation for the health benefit estimate for PM (see the HES report[2]). The evidence concerning this parameter could be bolstered by discussion of several additional epidemiological studies (e.g., medicare, nurses health – please supply references).

Some members of the Council believe it would be worthwhile to conduct sensitivity analysis concerning the possibility of differential toxicity among PM components. Absent such a sensitivity analysis, the project team might discuss the extent to which different components of PM exposure are differentially affected, whether evidence that some components are less toxic than average implies others must be more toxic, and the likely effect of differential toxicity on estimated benefits.

The dynamic population model is a significant advance over conventional static methods for estimating consequences of changes in mortality risk, especially when they are as large as those estimated for the CAAA. The Council encourages further development of this approach.

Welfare Benefits

A subset of welfare benefits was selected for analysis and inclusion in the primary estimate of benefits from the CAAA, namely improvements to visibility, ozone-related benefits for agricultural crops and commercial timber, and benefits from reduced materials damage. Additional, limited estimates also were developed for recreational fishing benefits in Adirondack lakes (discussed in the EES report[3]).

Visibility. As noted above, residential and recreational visibility benefits were valued using different approaches (e.g., recreational WTP took into account household income, whereas residential WTP did not) because those approaches were used in the evidently only relevant studies. This inconsistency suggests a need for additional research to improve methods and estimates. In addition, the use of annual average visibility for the valuation includes nighttime hours (when visibility is less relevant) and does not capture large visibility improvements on extreme days with the most severely impaired visibility. For future analyses, the Agency should consider using an upper percentile of restricted visibility during daylight hours in valuation of visibility benefits.

Agricultural and Forest Yield. The benefits of decreased ozone exposures are based on fairly well-understood concentration-response relationships that indicate improved yields in specific agricultural crops and commercial timber species (see the EES report[4]). The draft

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[2] Health Effects Subcommittee of the Council. Review of EPA's Draft Health Benefits of the Second Section 812 Prospective Study of the Clean Air Act. (EPA-COUNCIL-10-xxx).
[3] Ecological Effects Subcommittee of the Council. Review of Ecological Efects for the Second Section 812 Prospective Study of Benefits and Costs of the Clean Air Act (EPA-COUNCIL-10-xxx).
[4] Ecological Effects Subcommittee of the Council. Review of Ecological Efects for the Second Section 812 Prospective Study of Benefits and Costs of the Clean Air Act (EPA-COUNCIL-10-xxx).

prospective report indicates that these changes in yield will be valued using the Forest and Agricultural Sector Optimization Model (FASOM), which allows optimization across crops and between agricultural and timber land uses. However, no FASOM results were available for the Council's May meeting. The Council expects that a more detailed description of the model, and the model results, will be provided in the next version of the integrated report so that the details of the methodology can be evaluated.

Materials Damage. Unlike other air quality effects that are modeled using CMAQ (see the AQMS report[5]), the materials damage effects are modeled using the Air Pollution Emissions Experiments and Policy (APEEP) model (which incorporates results of a source-receptor matrix). It would be useful to report on the consistency between APEEP and CMAQ estimates of SO_2 concentrations. As noted above, the exposure-response functions used for materials damage appear incomplete (they do not depend on humidity and acidity) and vary substantially across materials. As in other areas, the literature is evidently thin, providing little basis for credible and comprehensive estimates.

Direct costs

Most of the direct cost estimates are based on an engineering approach that may reflect ideal operating conditions and fail to capture input-substitution possibilities. For some components (e.g., EGUs), econometric estimates of the cost of compliance with at least part of the CAAA (Title IV) are available and could be usefully compared with the simulated results.

As discussed above, the learning-curve estimates are partly based on different studies and there is limited evidence for overall magnitude or extent of variation by industry.

CGE modeling

The Council endorses the use of CGE modeling in the second prospective analysis. The effects of the CAAA on firm and consumer behavior are large enough that general-equilibrium effects are likely to be important. In the past, CGE models have been employed to identify some of the "hidden costs" associated with environmental regulation. The EPA project team has done this, and also provided an estimate of some of the "hidden benefits" that result from reduced mortality and morbidity risk, increasing time available for labor and leisure and decreasing some medical costs.

While the Council endorses the use of CGE modeling, it has concerns about the particular model and its implementation, at least as described. First, the model seems to require that consumers purchase greater quantities of market goods to maintain their utility, as opposed to paying higher prices for the same quantities (e.g., a car may provide the same utility with and without the CAAA, but costs more in the with-CAAA case because of the required pollution control equipment). One symptom that this implementation may be misleading is the result that oil consumption is higher in the with-CAAA case.

[5] Air Quality Modeling Subcommittee of the Council. Review of Air Quality Modeling for the Second Section 812 Prospective Study of Benefits and Costs of the Clean Air Act (EPA-COUNCIL-10-xxx).

The description of the model and results should be improved. First, the description of one case as "benefits-adjusted" may be easily misinterpreted – it includes the benefits of greater time availability (among the labor force) and reduced medical expenditures, but does not include the major non-market benefits represented by VSL that dominate the partial-equilibrium analysis. The Council suggests this case be described as "labor-force adjusted" or some other alternative. Second, there should be more comparison between the cost estimates from the CGE model and the direct cost estimates including discussion of the various factors that account for the differences (e.g., labor/leisure tradeoff, tax interaction effects, changes in investment). This comparison would elucidate the types of adjustment that are incorporated in the CGE but not the direct cost estimates, and clarify which are the most important.

Conclusion

In sum, the Council commends the EPA Project Team for its work on the second prospective analysis and looks forward to reviewing an improved integrated report.

Sincerely,

Dr. James K. Hammitt, Chair
Advisory Council on Clean Air
Compliance Analysis

NOTICE

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U.S. Environmental Protection Agency
Advisory Council on Clean Air Compliance Analysis

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