

Stavins' Informal Observations  
regarding  
"Identifying and Calculating Economic Benefit that Goes Beyond Avoided and/or Delayed  
Costs: An SAB Draft Advisory"  
dated March 23, 2005

March 31, 2005

For April 29<sup>th</sup> Phone Call: Trudy Cameron, Rick Freeman, Larry Goulder, Rob Stavins (chair),  
Tom Miller

- We're asked to reflect on three questions:
  1. Has the Panel adequately responded to the questions posed in the Charge?
  2. Are any statements or responses made in the draft unclear?
  3. Are there any technical errors?

In my view, this is an excellent advisory, which adequately responds to the charge questions, although given the nature of the questions and the nature of the Panel's perspective, it is inevitable that most of the Panel's response is outside of the narrow bounds prescribed by the specific questions. There are a few places where the Panel's thinking could be expressed more clearly, and there are a few typographical errors.

My comments below are not necessarily in order of importance. Rather I follow the page and line numbering of the draft Advisory.

Page 3, lines 24-26: This is the first time this issue arises. Isn't there an additional category that is not included in the two mentioned by the Panel? I'm referring to a dynamic one: as a result of being out of compliance a firm is able to acquire some degree of market power it did not previously have, and thereby evolves from being a price-taker in a competitive market to a somewhat monopolistic position in which it is able to reduce its output to drive up price, thereby increasing its profits. I'm prepared to be told that this doesn't make sense, but if it does make sense and the Panel believes that it is a trivial case that is unlikely to occur then they might at least acknowledge that in a foot note. This issue comes up several times subsequently. Below I will refer back to this note as the "dynamic market power issue."

Page 5, line 24: OECA appears for the first time, but has not been defined. The first time it appears, it should be written out in full so that the reader does not have to search for the appendix.

- Page 6, lines 16-19: Delete, this is repetition from previous paragraph.
- Page 9, line 3: OECA is identified as the “Office of Compliance and Assurance.” What is the “E” for?
- Page 9, line 20: Substitute “review” for “critique.”
- Page 9, line 21: At end of sentence, after “draft report,” insert “and the process used to produce it.”
- Page 15, footnote 1: Be careful. This can confuse EPA, because the Department of the Interior has used cost as a proxy for a benefit in Natural Resource Damage Assessments.
- Page 19, line 3: Need brief text to explain to the reader that the Panel’s responses to the four specific charge questions come later (in section 4.4).
- Page 19, lines 24-26: See my comments above regarding “dynamic market power issue.”
- Page 20, line 12: Why is the case of a monopolist used? The Board will want to know why not use a price-taking competitive firm as the benchmark case.
- Page 21, line 11: I suggest you explain that in the first situation A and E are both trivially small.
- Page 22, line 1: I suggest you explain that in the second situation A and E are both zero.
- Page 23, lines 6-10: We can’t really review this without seeing the EPA White Paper. I suggest that Rick explain this in our telephone conference.
- Page 26, line 6: I suggest you insert the word “significantly” between “revise” and “the White Paper,” because if EPA takes to heart the Panel’s critique, it will have to produce a very different document (I would think – I can’t be sure, since I haven’t seen the Agency’s White Paper).
- Page 26, line 17: Back to the “dynamic market power issue” again.
- Page 27, line 2: Was this established above for competitive markets?
- Page 28, lines 4-5: How about a graph? This seems like a significant case. I’m sure the Board will want to hear about this.
- Page 28, line 21: Typo: “the profits on increases sales are...”

Page 32, lines 19-21: Explain the intuition: the expected value of the penalty to polluter is equal to the harm done by polluting.

Page 33, lines 1-4: I fear that you are going beyond the scope of the Advisory, by giving policy advice to the Agency. I say this because what you are recommending would undermine Congressional intent, as validated by the Supreme Court. Not only environmentalists, but the courts would go nuts if EPA decided to circumvent what the statutes specify in regard to setting the level of standards by implementing economic efficiency through the back door of “lax enforcement.”

Page 33, line 21: This first sentence renders the section irrelevant: “if the goal of environmental policy is economic efficiency...” The goal of environmental policy, at least in the context of major sections of the Clean Air Act, Clean Water Act, and several other statutes, is decidedly *not* economic efficiency.

Page 37, lines 31-32: Do you really wish to go on record as endorsing empirical measurement of actual court damage awards as a measure of economic damages? If so, perhaps a third edition of *The Measurement of Environmental and Resource Values* should be produced.

#### Appendix A

Page A-2, lines 162-171: Did the committee actually cover all of these areas? Very impressive.

#### Appendix B

Page B-1, lines 232-233: Typo separates lines.

Pages B-1 - B-5: Why are sources of funds for sponsored research listed? Presumably EPA is concerned about potential conflicts of interest or other sources of bias, but if this were the case, they might ask about consulting income, which they don't.

Pages B-1 - B-5: Fantastic panel, which presumably explains why the advisory is excellent!