

# **Environmental Externalities of Geological Carbon Sequestration Effects on Energy Scenarios**

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## Summary

Geological carbon sequestration seems one of the promising options to address, in the near term, the global problem of climate change, since carbon sequestration technologies are in principle available today and their costs are expected to be affordable. Whereas extensive technological and economic feasibility studies rightly point out the large potential of this 'clean fossil fuel' option, relatively little attention has been paid so far to the detrimental environmental externalities that the sequestering of CO<sub>2</sub> underground could entail. This paper assesses what the relevance might be of including these external effects in long-term energy planning and scenario analyses. Our main conclusion is that, while these effects are generally likely to be relatively small, carbon sequestration externalities do matter and influence the nature of future world energy supply and consumption. More importantly, since geological carbon storage (depending on the method employed) may in some cases have substantial external impacts, in terms of both environmental damage and health risks, it is recommended that extensive studies are performed to quantify these effects. This article addresses three main questions: (i) What may energy supply look like if one accounts for large-scale CO<sub>2</sub> sequestration in the construction of long-term energy and climate change scenarios; (ii) Suppose one hypothesizes a quantification of the external environmental costs of CO<sub>2</sub> sequestration, how do then these supposed costs affect the evolution of the energy system during the 21st century; (iii) Does it matter for these scenarios whether carbon sequestration damage costs are charged directly to consumers or, instead, to electricity producers?

**Keywords:** Geological carbon storage, External costs, Energy scenarios

**JEL Classification:** O33, O38, Q43

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## 1. Introduction

Today, overwhelming evidence exists that mankind is modifying the Earth's environment and is provoking an increase of the average global atmospheric temperature and the associated detrimental effects of regional and local climate change (IPCC, 2001). In order to minimize the risks induced by substantial climate change (UNFCCC, 1992), carbon dioxide concentrations should be stabilized, preferably during the 21<sup>st</sup> century and probably at a level not exceeding much more than twice the pre-industrial level (IPCC, 1996). Adaptation to the consequences of climate change will almost certainly be necessary. "Geotechnical engineering" of the atmosphere, to counteract the radiative effects of increased levels of greenhouse gases, is probably undesirable. Removal of carbon dioxide from the atmosphere through the employment of biological sinks may likely contribute to only a limited extent to mitigating climate change. Thus, reducing anthropogenic greenhouse gas emissions substantially below the levels that would be implied by a "business-as-usual" scenario is imperative. In order not to exceed a doubling of the atmospheric carbon dioxide concentration, global carbon emissions from fossil fuel combustion in 2050 must not exceed those in 1990, and should decrease to about a third of 1990 levels by the end of the century (see, for example, Fetter, 1999). Given current and likely near-term future energy consumption increases and corresponding emission evolution patterns, this challenge is large.

The challenge, however, can be met. Many different measures must be exploited simultaneously to realize it, among which a control of global population growth, decreasing levels of energy use per unit of Gross Domestic (World) Product (GDP or GWP), and decreasing levels of carbon emissions per unit of energy use. Whatever means may to some extent contribute to alleviating the global warming problem, most specialists view a (partial) decarbonisation of energy use a necessity. For decreasing the carbon intensity of energy consumption, no panacea exists. Hence, all non-carbon emitting options should probably, for the moment at least, remain part of an energy mix as diversified as possible. Among these are very different (both conventional and still relatively unconventional) energy resources, such as hydropower, nuclear energy, renewables and decarbonised fossil fuels. Hydropower possesses a number of environmental drawbacks and is unlikely to be expandable so as to maintain its current relative share in an increasing world energy supply. Nuclear energy's future is unclear, since it faces a variety of problems related to radioactive waste, reactor accidents, nuclear proliferation, economic competition and public perception (Sailor *et al.*, 2000). Renewables (such as wind, solar and biomass energy) seem promising in many respects, but when and to what extent they can significantly contribute to global energy supply remains to be seen, impeded for the moment by relatively high costs and/or large land-use or resource requirements, and because it is unresolved whether renewables can be effective in ascertaining energy supply security (Turner, 1999). Therefore, expanding the decarbonisation of fossil fuels to options beyond a transition from carbon-intensive fossil fuels (coal and oil) to carbon-poor ones (natural gas) is currently receiving enhanced attention (Reichhardt, 1999; EIA/DOE, 2004; IEA/OECD, 2000a and 2000b; IEA-GHG, 2004).

The decarbonisation of fossil fuels through carbon dioxide capture and sequestration in the ocean or deep underground could contribute significantly to reducing anthropogenic greenhouse gas emissions (Marchetti, 1977; Parson and Keith, 1998; UNDP, 2000; Gielen, 2003). Technologies for both pre- and post-combustion carbon dioxide capture in power stations, as well as pre-combustion capture fuel cell applications, are available and have already been demonstrated, notably through their use for a number of other industrial purposes (Hendriks, 1994; Williams, 1998). Technologies for carbon dioxide transport, via pipelines or with tankers, and for its compression or solidification, needed for storage, are all known in principle. Whereas deep-ocean storage is still at a relatively early stage of development and is likely to remain

controversial, it has been shown that geological carbon sequestration is feasible and probably acceptable today (Herzog *et al.*, 2000). The Earth's geological storage capacity, in depleted natural gas and oil fields, aquifers and coal-beds, is likely to be large (Socolow, 1997; Bachu and Gunter, 1999; Lako, 2002). Carbon storage might, already in the short term, play an important role in mitigating global warming and protecting mankind against the detrimental regional and local effects of climate change (UNDP, 2000; IPCC, 2001). Therefore, energy analysts start presently to include carbon capture and storage alternatives in abatement scenarios for their integrated assessments of climate change. Still, insufficient attention has so far been paid to possible external environmental effects of carbon storage.<sup>1</sup> This paper attempts to contribute to filling the gap existing in this respect in the current literature.

In section 2 of this article we recapitulate what we think could be some of the major environmental externalities of geological carbon sequestration. Leaving a detailed technology externality calculation for future research, in section 3 we postulate some rationalized hypotheses concerning the order of magnitude of possible environmental impacts, in terms of external costs, of CO<sub>2</sub> sequestration. In section 4 we present our analysis results regarding the nature of long-term energy and climate change scenarios if one accounts for CO<sub>2</sub> sequestration (i), if one incorporates external costs of geological carbon storage (ii), as well as concerning the way in which damage costs are included in energy models, i.e. whether they are charged to energy consumers or, instead, to electricity producers (iii). Section 5 provides our major conclusions, describes a few recommendations and lines for further research, and discusses possible implications of our findings for policy making *vis-à-vis* future large-scale geological carbon sequestration.

## 2. Environmental externalities of geological carbon sequestration

Whereas the prospective benefits of carbon sequestration are significant, notably because it possesses the potential to catalyse a transition to a hydrogen economy, a number of important questions related to environmental hazards and safety risks remain (for a taxonomy of the various risks involved with geological carbon storage and potential impacts, see also van der Zwaan *et al.*, 2001; Wilson *et al.*, 2003). In scientific, political and non-governmental communities, a closer inspection of these external effects now starts to receive momentum.<sup>2</sup> At present, information about the potentially detrimental external environmental effects of carbon sequestration is far from complete. Uncertainties associated with negative sequestration impacts – that ideally ought to be addressed before carbon storage is employed at a large scale – abound, and their nature and extent are insufficiently understood. Without attempting to be exhaustive, we indicate below some of the geological storage externalities that we suspect could play a role in the future. We do not try to assign probabilities to these various potential impacts, or to quantify the uncertainties dominating their significance, given the lack of our current understanding of carbon sequestration external impact mechanisms. However inadequate our present knowledge about the external effects of carbon storage may be, we do not judge that this inadequacy is reason for not trying to include external costs in energy policy analyses. Instead, we postulate in the next section some hypotheses on these environmental impacts (means lacking for the moment to do better), which we rationalize and that could thus be considered crude 'guesstimates' to at least some extent. Subsequently, in section 4, we include them in our scenarios.

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<sup>1</sup> The IPCC (Working Group III), in an envisaged Special Report on Carbon Dioxide Capture and Storage, is currently in the process of assembling a comprehensive overview of carbon storage options, including their detrimental environmental impacts.

<sup>2</sup> For a presentation on views and preoccupations of environmental NGO's regarding CO<sub>2</sub> capture and storage, see, for example, [www.ipieca.org/downloads/climate\\_change/Oct03\\_workshop/3\\_Anderson.ppt](http://www.ipieca.org/downloads/climate_change/Oct03_workshop/3_Anderson.ppt).

Deep geological carbon storage can acidify water present at large depths underground. Natural gas and oil fields have a proven containment integrity record for millions of years. Still, storing carbon dioxide in such fields (once depleted, or while depleting) could have an acidification impact on underground waters. In a similar way, water in deep underground aquifers could undergo acidifying effects by CO<sub>2</sub> injection (Chen *et al.*, 1999). In both cases, groundwater pollution of nearby freshwater aquifers may result, if the containment of the aquifers into which CO<sub>2</sub> is injected is breached. This could affect the quality of drinking water, if the latter is obtained from sources fed by the polluted groundwater. Enhanced Coal-Bed Methane (ECBM) recovery and Enhanced Oil Recovery (EOR) carbon storage can in principle pose similar groundwater pollution effects (Wong *et al.*, 1999; Liu *et al.*, 1999). A related problem is that the process of reservoir fluid/gas displacement by CO<sub>2</sub> insertion, and the resulting modification of the hydrodynamic properties of underground geological layers, can have a negative impact on the water extraction potential of certain sources. Perhaps more importantly, as a result of CO<sub>2</sub> injection in geological layers, their integrity could be disturbed. In the case of aquifers this could lead to the brine they contain migrating to other layers in contact with freshwater aquifers serving as source for drinking water.

As a result of underground carbon sequestration, structural changes could occur in geological formations, as well as modifications of the thermodynamic properties – and even dissolution – of underground geological layers. Both such geological modifications and the CO<sub>2</sub> injection process itself could involve seismic activity or soil cave-ins, with uncertain aboveground impact, depending both on site and option chosen.<sup>3</sup> Altered chemical properties of geological formations as a consequence of carbon sequestration, or the build-up of localized high pressures, could affect the stability of the geological layers above. Resulting from a large range of possible geo-chemical reactions of carbon dioxide with underground geological structures, cocktails of gases can be formed, the bearings of which to either the underground or aboveground environment (including plants, animals and humans) are largely unknown today. All these matters can affect or have pervasive consequences on habitat conditions.

It is not improbable that carbon dioxide gas could gradually - and without being noticed - migrate and slowly leak from where it is stored (Ha-Duong and Keith, 2003). This threat ranks high among the potential risks of geological carbon storage, since it could seriously hamper its suitability as global warming mitigation alternative. Since natural gas has long been stored in geological formations, one could draw a parallel and conclude that long-term secure sequestration of carbon dioxide seems feasible. Given that the physical and chemical properties of CO<sub>2</sub> are different from those of CH<sub>4</sub> (the latter being chemically more inert than the former), however, it may not be guaranteed that its artificial storage underground retains integrity forever. Especially regarding options other than depleted gas and oil fields, such as aquifers and coal beds, long-term storage effectiveness aspects are uncertain. Migration times vary according to the sequestration option considered, and depend on the characteristics of the geological formation of the site specified (NITG, 2004). The leakage time frame that typifies each option and site, and the compatibility of that time frame with global warming mitigation efforts (determined by the features of the natural carbon cycle), is determinant for the option's suitability to preclude or postpone presumed climate change effects.

Probabilities for catastrophic well blowouts (e.g. during injection) may be exceedingly small and the associated risks negligible in comparison to those involved with carbon seeps, but the eventuality that artificially stored carbon dioxide gas could escape rapidly, in large amounts at once, may not be left unmentioned. Sudden carbon releases could in principle have global warming effects - if large enough - as well as severe accidents with human casualties. Although the hazards involved are likely to be only local and temporary, they could be pervasive. However

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<sup>3</sup> Note that, inversely, carbon dioxide sequestration could be employed to restore (re-pressurize) natural or artificial surface soil cave-ins, e.g. resulting from pressure decreases generated by fossil fuel mine/field depletion.

inappropriate a comparison may be between artificially stored CO<sub>2</sub> and amounts built up in some natural cases, a frightening phenomenon remains the natural disaster that occurred in Cameroon in August 1986. Carbon dioxide welled up from deep in Lake Nyos, and was responsible for killing, by asphyxiation, 1,700 people and their livestock (Holloway, 2000). This concerned a very unique and unfortunate case, different in many ways from CO<sub>2</sub> stored underground by Man, but it should not be fully neglected, and shows that one has in principle to be weary of unexpected potential risks.<sup>4</sup> Accidental releases of CO<sub>2</sub> should also be considered regarding high-pressure CO<sub>2</sub> transportation, which would become part of the carbon sequestration solution. CO<sub>2</sub> pipelines exist already, and specialists ascertain that their safety record can be considered better than that of natural gas pipelines. Multiple safety devices are built-in throughout the various stages of CO<sub>2</sub> transportation methods, but risks for personal accidents as a result of pipeline defaults and sudden CO<sub>2</sub> releases, e.g. for workers involved in network maintenance or for people living in the vicinity of pipelines or CO<sub>2</sub> compression installations, are not zero. If CO<sub>2</sub> transportation via pipelines is operationalized at large scales, such risks will augment accordingly. Land-use issues may then also increasingly play a role of significance.

### 3. Damage costs

How does one go about quantifying the qualitative observations made above regarding the potential externalities of geological carbon sequestration? In principle, to evaluate the impact and damage cost of any pollutant, one needs to carry out an “impact pathway analysis”, tracing the passage of the pollutant from the place where it is deposited or emitted to the affected population. The principal steps of such an analysis involve (1) a specification of the amounts disposed or emitted, (2) a calculation of the dispersion of the pollutants, (3) a calculation of the impact of these pollutants, and (4) the monetary valuation of the costs of these impacts. The impacts and costs must then be summed over all impact types and receptors of concern. For the fossil fuel chain including carbon sequestration, part of the damage cost arises from combustion in power plants (corresponding to the pollutants that are not captured but emitted into the atmosphere), while the other part arises downstream from power generation, that is, as a result of the environmental externalities of geological carbon sequestration. For most energy resources, such analyses of environmental damages have been performed in the ExternE (External costs of Energy) Project series of the European Commission (see e.g. ExternE, 1998). The ExternE studies, however, have so far not included calculations on externalities resulting from geological carbon sequestration. The scientific knowledge required for externality calculations for carbon sequestration, e.g. regarding migration of carbon-induced products through underground layers, is still largely absent. Without data on geological chemical diffusion, these calculations cannot be performed, and even if they were available today, it would fall beyond the scope of this paper to perform these (extensive and detailed) calculations here.

Still, however, we think it may be insightful to perform an energy scenario analysis including not only carbon sequestration technologies, but also the external costs that could be associated with them. Lacking either theoretical or experimental data regarding external impacts, we have chosen to make some hypothetical assumptions concerning their costs. By including these in our scenario analysis, we hope to trigger work directed towards the proper calculation of external costs of carbon storage, or at least towards a more careful, but perhaps still crude,

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<sup>4</sup> In the case of Lake Nyos, CO<sub>2</sub> rises up from deep volcanic activity and via groundwater beneath the lake dissolves in the lake's lower water layers. Lake Nyos does not turnover, however, so that CO<sub>2</sub> gas saturates the bottom water until some trigger (e.g. a storm or earthquake) provokes the deep water to suddenly move upward. This resulted in 1986 in CO<sub>2</sub> coming out of solution in large quantities, and erupting, like champagne uncorked, into an 80 m high jet of water and CO<sub>2</sub>. The CO<sub>2</sub> gas, heavier than air, subsequently rolled down the hills in a large cloud, asphyxiating everything it found on its way.

estimation of them. Deriving rough but reasoned guesses of what external costs of carbon sequestration could be would allow getting better feeling for their consequences for energy-climate modelling, as well as for their policy relevance. For the moment, however, we cannot do much more than simply postulating a set of numbers. We will, nevertheless, attempt to somewhat justify our 'manna-from-heaven' figures in this section. Thus, while avoiding to undertake a detailed geological carbon storage externality calculation *à la* ExternE – we will leave such work to future research activities – we attempt to somewhat validate our hypothetical quantification of the (order of magnitude of the) external costs associated with the environmental impacts of CO<sub>2</sub> sequestration.

For this justification, we rely on the numbers generated by Rabl and Spadaro (1999), which are based on ExternE (1998), for the externalities resulting from the use of the three fossil fuels based on technologies employed during the 1990s and 2000s. For these two time periods, the Rabl and Spadaro (1999) figures are quoted in table 1. We use these, as well as their comparison with the corresponding numbers for renewables and nuclear energy, as reference for our hypothetical figures on coal, oil and gas externalities for the 2010s and thereafter. For the latter time period we assume that geological carbon sequestration is added to the use of fossil fuels. Our postulated estimates for the damage costs, involved in fossil fuel use, of carbon sequestration are also presented in table 1. The figure of 0.2 ¢/kWh hypothesized for the external geological storage costs for fossil technologies in the 2010s is assumed neither to vary over the technology considered nor over time from 2010 onwards. The main reason is that externality costs at large, and our postulates in particular, are subject to great uncertainties and may vary by even an order of magnitude depending on the option under consideration. Since these uncertainties are dominant, we merely perform a "*suppose that... what then...?*" analysis with these fixed and constant figures.<sup>5</sup>

<b>Damage costs (¢/kWh)</b>	<b>Total</b>	<b>PM<sub>10</sub>, SO<sub>2</sub>, NO<sub>x</sub></b>	<b>Global Warming</b>	<b>CO<sub>2</sub> Sequestration</b>
<b>Coal 1990s</b>	13.3	10.5	2.8	-
<b>Coal 2000s</b>	3.8	1.1	2.7	-
<b>Coal 2010s</b>	<b>1.3</b>	<b>0.6</b>	<b>0.5</b>	<b>0.2</b>
<b>Oil 1990s</b>	10.0	8.2	1.8	-
<b>Oil 2000s</b>	3.2	1.4	1.8	-
<b>Oil 2010s</b>	<b>1.3</b>	<b>0.7</b>	<b>0.4</b>	<b>0.2</b>
<b>Gas 1990s</b>	2.8	1.6	1.2	-
<b>Gas 2000s</b>	1.5	0.3	1.2	-
<b>Gas 2010s</b>	<b>0.6</b>	<b>0.2</b>	<b>0.2</b>	<b>0.2</b>

**Table 1.** Damage costs for fossil fuel chains in the EU. Carbon sequestration is included in 2010.

Note that production cost of base load electricity in the EU is in the range of 2.5 to 5 ¢/kWh. Source: ExternE (1998), for 1990s and 2000s, and author's hypotheses, for 2010s and thereafter.

<sup>5</sup> For future work we intend to perform a proper sensitivity analysis, in which we vary our externality assumptions over e.g. an order of magnitude and analyse the effect of this variation on our scenario results. Within the present knowledge of uncertainty concerning these figures, we do not judge it sensible to distinguish between different external sequestration costs for e.g. gas and coal, although natural gas usage emits only about half of the carbon dioxide of coal power generation.

In postulating the figures of table 1 for the damage costs of coal, oil and natural gas with 2010 technologies, we have made the following assumptions. First, it is unlikely that all external costs in the two first categories can be avoided: not all particulate matter (PM<sub>10</sub>, of size smaller than 10 μ), SO<sub>2</sub>, NO<sub>x</sub> emissions, on the one hand, and global warming (mainly as a result of CO<sub>2</sub> emissions), on the other hand, will be eliminated when pollution removal and carbon capture are applied. This explains why non-zero figures remain for these two entries for 2010 technologies.<sup>6</sup> Second, it is supposed that in 2010 damage costs due to particulate matter, SO<sub>2</sub> and NO<sub>x</sub> will be further reduced to about 50% of current damage costs, given the improvement in capture technologies that still takes place. Third, it is assumed that in 2010 damage costs due to global warming will be reduced, through carbon capture and sequestration, to about 20% of current costs, given that 80% GHG emission reduction can probably be implemented relatively soon and cost-effectively (Hendriks, 1994). Technologies that can reach capture levels that near the 100%-level exist (IGCC seems the most likely route forward for new power plants, which reduces emissions at the plant by easily 95%): but we want to be realistic in that not all greenhouse gas emissions are likely to be avoided completely anytime soon, mainly for economic reasons.

Furthermore, the damage costs of carbon sequestration are expected not to exceed the range of those for renewables and nuclear energy. The latter have been calculated to be about 0.2 ¢/kWh (Rabl and Spadaro, 2000).<sup>7</sup> We think it is reasonable to make conservative assumptions regarding the damage costs of carbon capture and sequestration – resulting from e.g. carbon dioxide dissipation, sudden releases of carbon dioxide, acidification of underground water, and the chemo-geophysical modification of underground geological layers – in which their level does not surmount (and is at most of the same order of magnitude as) the average damage costs of renewables and nuclear energy. Two main arguments can be given to back this assumption.

First, like with nuclear energy, the use of fossil fuels with carbon sequestration involves the geological storage underground of by-products of the energy chain (for the nuclear case, see, for example, Milnes, 1985). But that is probably where the comparison stops: for radioactive nuclear waste one has relatively small quantities of highly toxic products, whereas for carbon sequestration one has very large quantities of CO<sub>2</sub> with low toxicity. Indeed, the magnitude of material disposed is vastly less for nuclear energy and the material is vastly more dangerous than with fossil fuel use with carbon storage. For both, one multiplies a big number by a small one, but it is unlikely that the result of it equals in these two (inverse) cases. One cannot claim, therefore, that the corresponding costs could be the same, or even of the same order of magnitude. The nature of the products involved is too different, especially considering the health effects of chemically active reactants, for carbon storage, *vis-à-vis* those of radioactive substances, in the case of nuclear energy. Chemical acidification is likely to be much less hazardous to the environment and harmful to humans than radioactive contamination. Hence, damage costs for carbon sequestration are probably smaller than those for nuclear energy, that is, for radioactive waste disposal. Estimates for the latter (however controversial these might be) can be considered a pessimistic upper bound for guesses of the former, thereby justifying our conservative choice of 0.2 ¢/kWh for carbon storage damage costs.

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<sup>6</sup> Of course, in the case of SO<sub>2</sub> emission reductions, almost all SO<sub>2</sub> can technically be removed with either amine or IGCC systems (for PM<sub>10</sub>, NO<sub>x</sub> and CO<sub>2</sub> it is more difficult to achieve total removal). But it will not easily be considered cost-effective to reach such close-to-zero limits.

<sup>7</sup> For wind and PV, high and low estimates fall within a width of some 0.1-0.2 ¢/kWh, while for biomass damage costs amount to about 0.1-0.6 ¢/kWh, depending on the technology chosen. For nuclear energy, damage costs are distinguished between short-term and long-term, amounting to values below 0.1 and around 0.2 ¢/kWh, respectively. On average, therefore, a value of 0.2 ¢/kWh seems to be reasonable for the damage costs of these renewable and fission alternatives.



Our second argument derives from our assertion that the total costs of electricity (including all external costs) for different energy technologies will perhaps become the most important determinant for the permissible (internal and external) costs of sequestration. If external costs are to be internalised (this is now official EU policy), and if external costs for carbon sequestration prove to be – and remain – much higher than those for renewables (supposing that at least some renewable energy options will reach competitive break-even with fossil fuels including carbon storage in the not too distant future), carbon sequestration will not see the daylight on any large scale because of a lack in economic interest. Wind power, for example, is at present becoming competitive at various locations, while on average still being more costly to generate than conventional (fossil-fuelled) electricity. It can be reasonably expected that wind energy production costs continue to decrease over the coming years, while its external costs may remain about 0.2 ¢/kWh. Other renewable energy resources, such as PV, are still considerably more expensive than fossil-based electricity, but are also expected to continue to be subject to economic learning. Capturing, transporting and sequestering CO<sub>2</sub> may increase competitive fossil energy production costs by a factor of two, when e.g. about 80% of the CO<sub>2</sub> released is avoided. In other words, competitive costs of fossil-based power production including sequestration may approximate renewable energy production costs over the decades to come, so that - on the basis merely of production costs - a comparable electricity price results for these two distinctive alternatives. But this does not yet account for damage costs. Damage costs of carbon sequestration may then surely not exceed the (renewable) 0.2 ¢/kWh level of external costs, in order for carbon sequestration to remain competitive with these cheap renewable options (and given that fossil fuels with carbon sequestration still involve some of the remaining external costs other than those related to sequestration). We assume that those carbon sequestration technologies will emerge that are both environmentally attractive and are able to survive in competitive markets, which justifies our choice for the above quoted (conservative) upper-bound values of external sequestration damage costs.

#### **4. Long-term energy scenarios**

If in the future the energy system is going to be subjected to stringent climate constraints, the use of coal for power generation will be put into disadvantage, even in comparison to its fossil-fuel-based counterparts (oil and natural gas). Clearly, when ambitious global warming goals are to be met, the role of coal in our energy mix should be significantly reduced. Scenario analyses demonstrate that coal indeed loses importance under these conditions. With much of its emissions being avoided through carbon capture and storage, however, this picture dramatically changes: coal can largely continue to play the important role it does today. But with coal retaining a large share of global energy consumption, a proper analysis should be performed of its full external environmental impact, not only in terms of the generation of mining wastes and its continued contribution to global warming and local air pollution, but also in terms of the possible damage effects of geological carbon sequestration. What is the effect of including damage costs for carbon sequestration on the construction of long-term energy supply scenarios? To answer this question, we have used the MARKAL model. Before presenting our modelling results, the main features are described of the MARKAL version we employed.

##### **4.1 The MARKAL model**

MARKAL is a commonly used bottom-up model for energy system analysis based on cost optimisation. The model algorithm has been expanded over the years, resulting today in a number of possible extensions that can be employed in combination and in conjunction with the basic version. But its major characteristics remain: it is an ideal-market cost-minimisation

decision model with rational behaviour, perfect information and perfect foresight, that optimises and matches the supply and demand sides of energy for the entire modelling timeframe under consideration.<sup>8</sup> The version often used nowadays for policy analysis studies is the one with endogenised technological learning and price elasticities. Its geographical coverage is Western Europe (WEU), that is, the 15 EU countries *anno* 2003, expanded with Norway, Switzerland and Iceland. This area is treated as a single region, so there is no specific country dis-aggregation.

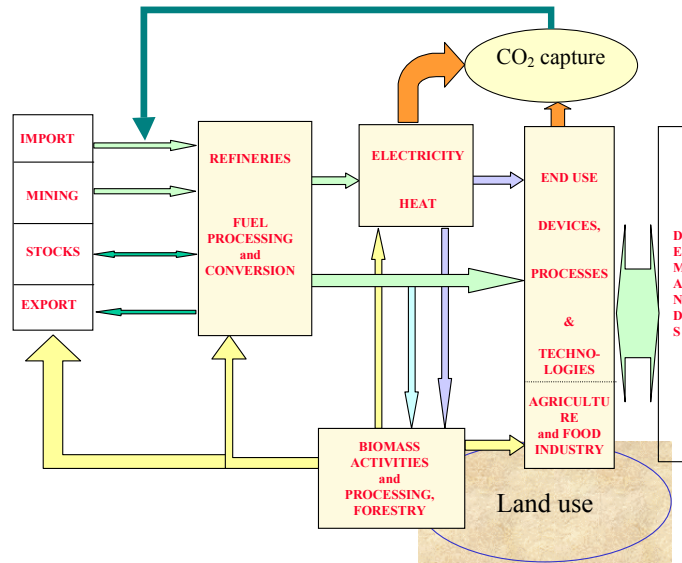
The emissions considered for this study are the CO<sub>2</sub> emissions from both fuel combustion and industrial processes. Emission removal is considered both through carbon sequestration in geological storage options and via uptake by land use, agriculture and forestry. The model distinguishes 6 geological CO<sub>2</sub> storage options: aquifers, Enhanced Oil Recovery (EOR), Enhanced Coal Bed Methane (ECBM) recovery (2 different options, at different depths) and depleted oil and gas fields (2 options: on-shore and off-shore). They are each characterised by specific data on storage potential, injection and storage costs, and the rate of energy recovery (for EOR and ECBM). Costs related to transportation, from the site where CO<sub>2</sub> is captured and compressed to the injection point, are also included. For the capture of CO<sub>2</sub> from large point sources 21 technologies are modelled: 10 in the electricity sector (coal, oil and natural gas based), 6 in industry (mainly in ammonia, iron and steel production), and 5 in the fuel conversion sector (in the production of hydrogen from fossil fuels).<sup>9</sup> Figure 1 illustrates the basic functioning of MARKAL, with the supply side at the left, the conversion and transformation phases in the middle, and the end use at the right.

Some features, assumptions and limitations of MARKAL deserve additional attention. The model does not incorporate trade, changes in import-export balances of electricity, rebound or other feedback effects at the macroeconomic level resulting from price changes, e.g. induced by the incorporation of external costs. Assumptions with respect to implementation barriers of technological options, as well as various socio-political considerations, can be inserted, but have not been regarded as relevant for this study. Although MARKAL may cover other pollutants and other greenhouse gases (GHGs) than CO<sub>2</sub>, within the context of the present study the analysis has been restricted to carbon dioxide only (accounting presently for about 80% of all GHGs in Western Europe). This implies that only the global warming and sequestration parts of the external costs of table 1 have been considered for our energy scenario inspection. For older technologies from the 1990s, these represent only the smaller part of total external costs. For recently and future installed technologies, however, the global warming impacts are expected to involve generally the largest among the three sources of external costs. Since the emphasis in the current analysis lies on the effects of the inclusion of CO<sub>2</sub> sequestration external costs in electricity production, it is the cost difference as a result hereof that matters mostly (rather than the absolute value of remaining external costs).

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<sup>8</sup> It is a linear programming bottom-up energy technology model, using GAMS and a linear solver (CPLEX or OSL). The time frame by the model version used covers the 1990-2100 period, and the programme is solved in 10-year steps. The database linked to the use of MARKAL contains about 70 different demand categories at the end-use-side, and in total more than 900 energy technologies at the supply-side (involving both existing and future options).

<sup>9</sup> Note that for the analysis presented in this paper, no carbon sequestration à la the Sleipner project is included, that is, in which CO<sub>2</sub> is captured from natural gas field exploitation and subsequently re-entered in underground layers.

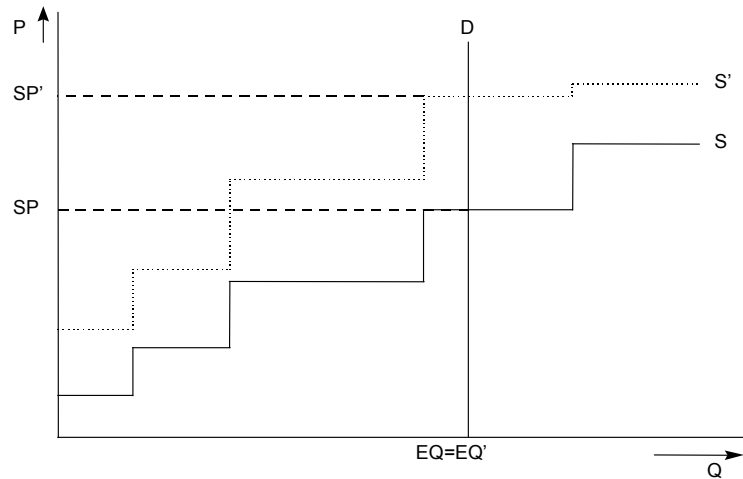


**Figure 1.** Flow diagram of MARKAL with carbon capture and sequestration. The upper (dark green) arrow indicates that some storage activities have energy recovery as co-benefit.

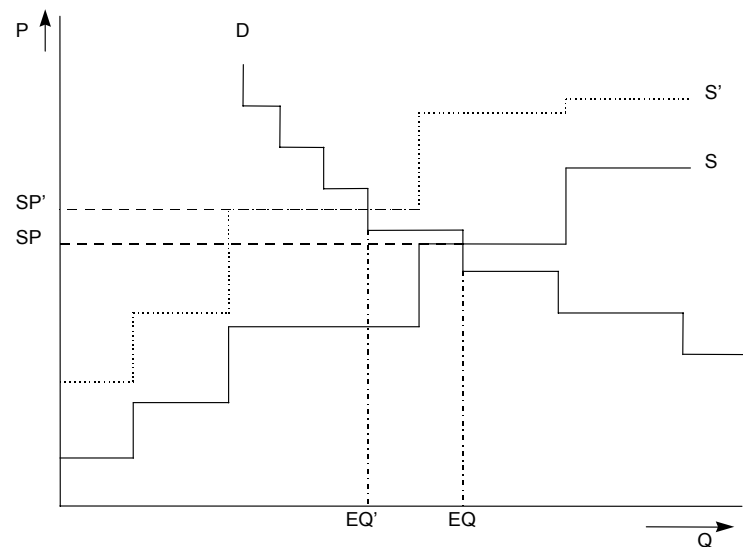
Cost reductions of technological options are assumed to evolve through learning curves. This assumption implies that the unit investment cost of a particular technology, or a particular technology component (such as a gas turbine or gasifier), decreases with increasing installed capacity. Learning curves are based on observed phenomena in the past, and applied in our MARKAL version to future technological cost developments. A fixed ratio (the progress ratio) exists between investment cost reductions and every doubling of cumulative installed capacity. For relatively mature technologies, progress ratios typically lie between values of 0.90 and 0.95, meaning a cost reduction of 10% and 5% respectively per doubling of installed capacity. Promising new technologies may have progress ratios as low as 0.70. In our MARKAL model, most learning technologies or components are found in the electricity production sector, while some appear in other sectors such as transport, and upstream oil and gas industries.

A weak point of traditional MARKAL models is that changes in prices do not affect demand, that is, demand is exogeneously defined. In recent years, the MARKAL algorithms have been extended to include price-dependent demand levels. Of the two approaches that have been developed (MARKAL-MACRO (see Hamilton *et al.*, 1992) and MARKAL-Elastic-Demand (MARKAL-ED, see Loulou and Lavigne, 1996)), we use the latter, mostly because of the significant differences that exist between the two in computer calculation times.<sup>10</sup> MARKAL-ED is a partial equilibrium model in which the common exogeneously defined demand relations have been replaced by price-driven demand functions. Energy demand decreases as a result of increasing energy and product service prices. A main advantage of the model is that it is still based on linear equations, allowing rapid calculations. With non-linear demand equations, with current machines and calculation capacity at least, it would not be possible to run our complex WEU model. Figure 2 shows the (simplified) equilibrium that is achieved in traditional MARKAL models. Figure 3 shows the equilibrium that is achieved in the model version we use, with elastic demands.

<sup>10</sup> Note that both MARKAL-MACRO and MARKAL-ED are attempts to bridge the worlds of bottom-up versus top-down modelling. For example, these models constitute a first step towards allowing for the study of welfare effects with the bottom-up approach, through a calculation of changes in consumer plus producer surplus.



**Figure 2.** Supply (S and S') and demand (D) price-quantity equilibrium in traditional MARKAL models. EQ=EQ' indicates the equilibrium quantity (Q); SP and SP' are the shadow prices (P).



**Figure 3.** Supply (S and S') and demand (D) price-quantity equilibrium in our MARKAL-ED model for Western Europe. EQ and EQ' indicate the equilibrium quantities (Q); SP and SP' are the shadow prices (P).

As depicted in both figures 2 and 3, all supply and demand curves are linearized in MARKAL (typically a 20-step function), allowing the use of a linear algorithm to solve the programme. Supply curves are derived from the database of supply options and their characteristics. In traditional MARKAL models (figure 2), energy demand is independent of its price, so that the demand function is a vertical line. In MARKAL-ED (figure 3), the demand decreases if the price increases, so that the demand function is a curve with a downward slope. Equilibrium between supply (S) and demand (D) is reached in point EQ, which is the same for both figures in the base case calculation without GHG emission penalties. If GHG penalties are introduced, the supply curve moves upward, because all emissions in the supply chain are penalised (S changes to S'). In the case of fixed demand (figure 2), this has no consequences for the demand (EQ=EQ'). However, shadow prices increase (from SP to SP') in both figures. In the case of elastic demand (figure 3), demand decreases and a new equilibrium price and quantity

are achieved, below the EQ' prices and quantities in the case of fixed demand (figure 2). The precise form of the demand function used in our analysis, applied to all energy resources and technologies, is:

$$D_{i,p}/D_{i,b} = (P_{i,p}/P_{i,b})^{e_i}$$

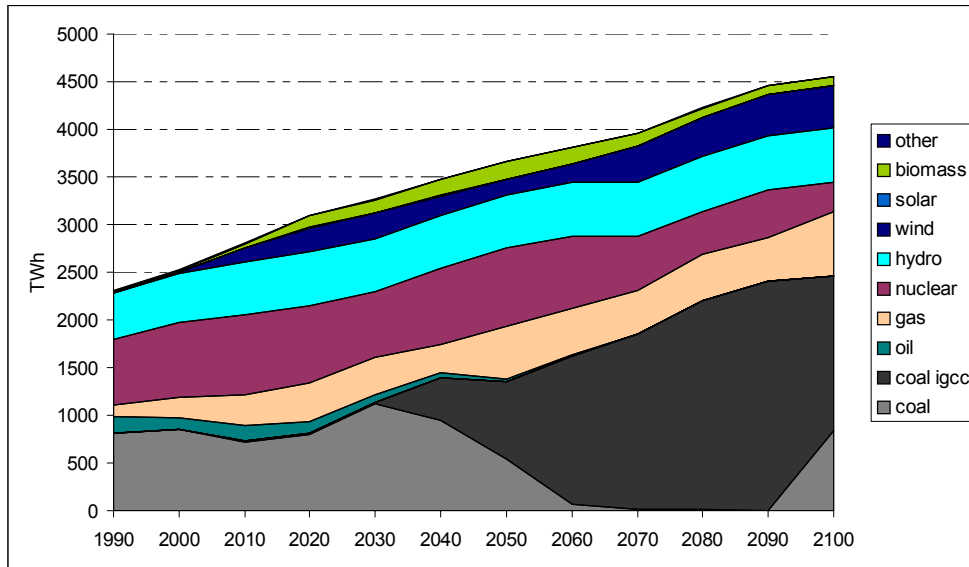
in which:

$D_{i,p}$	=	demand for energy i after introduction of GHG penalty
$D_{i,b}$	=	demand for energy i in the base case
$P_{i,p}$	=	energy price i after introduction of GHG penalty
$P_{i,b}$	=	energy price i in the base case
$e_i$	=	price elasticity for energy i

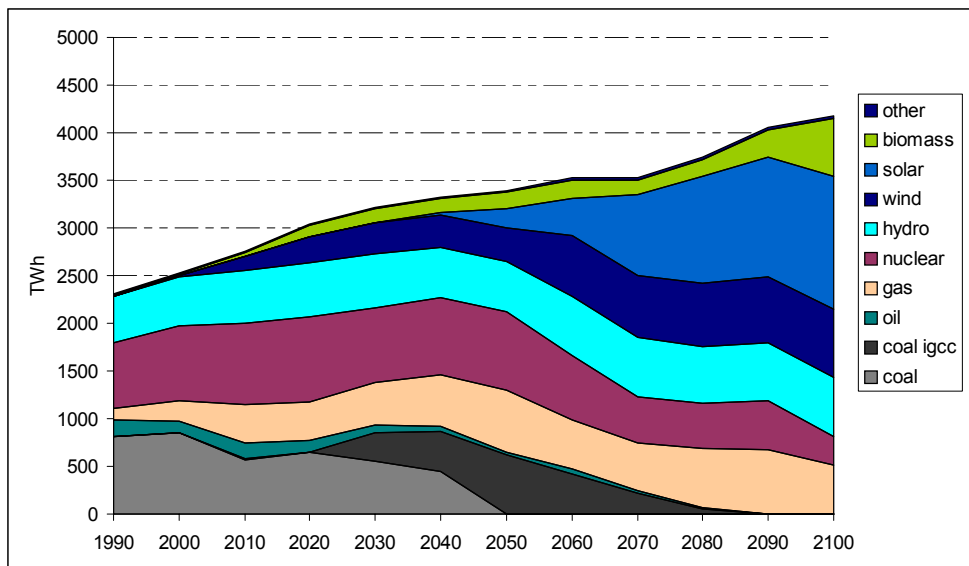
While it is known that price elasticities may diverge considerably (see, for example, Franssen 1999), even within a single demand category, we have assumed that all elasticities in our model are fixed at a value of -0.5. Long-term demand elasticities typically lie within bounds between -0.1 and -2.5. Still, most long-term demand elasticities usually range from -0.1 to -0.5. Our value of -0.5 is considered to represent an upper limit for the impact of demand elasticities, given the fact that our model also simulates other demand reduction and increase effects (e.g. through endogenised technological learning). The high value for elasticities is compensated by e.g. rather stringent limitations on the rate at which energy demand may vary.

## 4.2 Results

Before looking in detail into the consequences of adding damage costs for CO<sub>2</sub> sequestration in our model, we attempt to answer the first question we pose ourselves: how does energy production change if one includes carbon sequestration technologies in long-term scenarios? We look at the energy system, and the electricity generation scheme in particular, as calculated both before and after the introduction of carbon sequestration technologies. Two sets of scenarios are presented, to illustrate the effect of adding CO<sub>2</sub> sequestration options. The first set (figures 4a and 4b) includes a base case and a CO<sub>2</sub> reduction scenario, as derived before CO<sub>2</sub> sequestration was included in the MARKAL database. The base (or reference) case is a business-as-usual scenario, without the imposition of a climate constraint. The reduction case illustrates a stabilisation scenario by 2100 at 550 ppmv atmospheric carbon dioxide concentration, modelled through a cumulative limit on the total amount of emissions between 2000 and 2100, the year in which the required maximum concentration level is reached. The second comparative scenario set (figures 5a and 5b) involves the same two (business-as-usual, respectively stabilisation) scenarios, but this time with sequestration technologies included (but still without external damage costs). All four figures show the total amount of electricity production (in TWh) by means of production (fuel source). For each of them, the price-elastic version of MARKAL is used for the stabilisation scenario, in order to avoid rigid demand levels under a severe climate objective.



**Figure 4a.** Electricity production by energy source in the base case scenario (no carbon sequestration technologies included).<sup>11</sup>

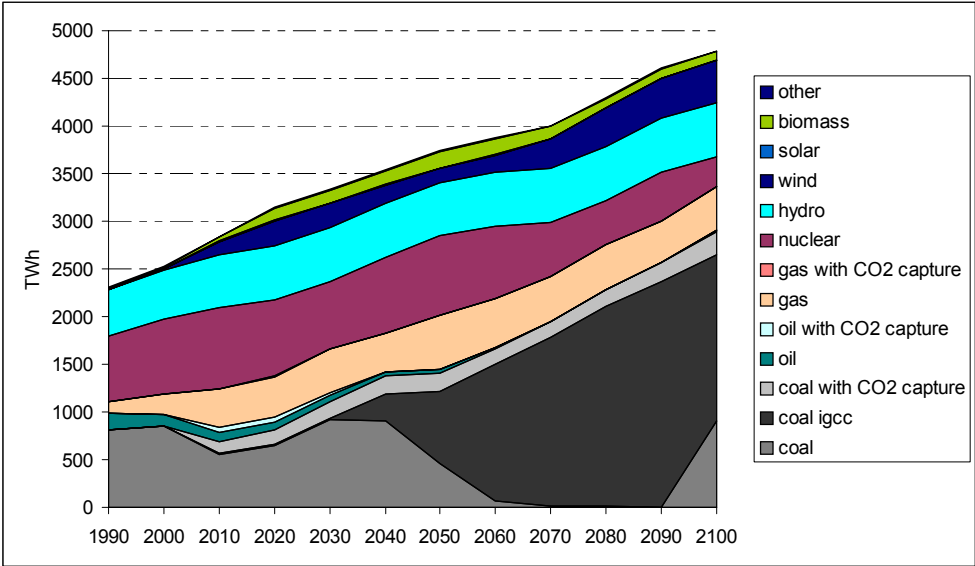


**Figure 4b.** Electricity production by energy source in the climate-constrained scenario (no carbon sequestration technologies included).

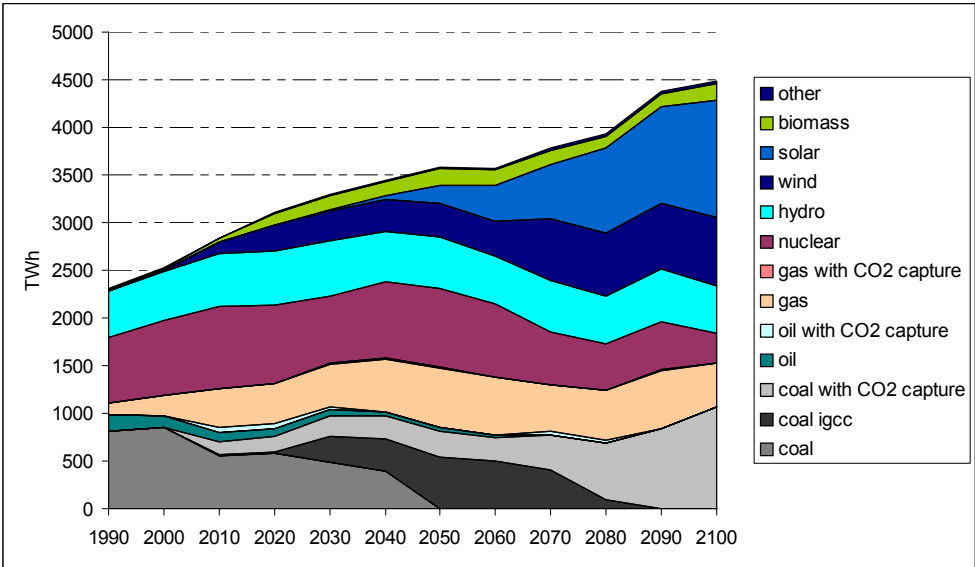
From figure 4a, one observes that in the reference case renewables (mainly wind and some biomass) emerge early, and subsequently remain almost constant at a relatively modest share. Hydropower remains roughly stable, while nuclear energy decreases slightly. The use of natural gas increases significantly, but by far the largest increase occurs in the production of electricity through cheap coal technologies. From 2030 onwards, the major production source is coal through the advanced type Integrated Gasification Combined Cycle (IGCC). In the 550 ppmv stabilisation case, depicted in figure 4b, both the total production decreases and the production mix changes. The decrease in energy demand, and thus production, results from the use of elastic demand curves, and is induced by an increase in energy prices that allows meeting

<sup>11</sup> Note that this and following figures should be interpretable in black-and-white: the energy contributions in the graph appear in the same order, from top to bottom, as in the corresponding explanatory box. Still, they remain most illustrative in full colour.

the climate constraint. Nuclear energy remains available because it involves zero carbon emissions. Hydropower remains roughly stable: it has no room for expansion within Western Europe, so it cannot contribute more to power production. Under the climate constraint, coal disappears completely, even with the advanced IGCC technology, while wind and solar energy increase substantially. To compensate for the increased power production from intermittent renewables like wind and solar energy, biomass and natural gas use also increases.



**Figure 5a.** Electricity production by energy source in the base case scenario (with carbon sequestration technologies).



**Figure 5b.** Electricity production by energy source in the climate-constrained scenario (with carbon sequestration technologies).

From figure 5a, one sees that even without climate constraint it becomes worthwhile to invest in coal with CO<sub>2</sub> capture rather early in time, while oil and natural gas based electricity production with capture remains marginal throughout the entire simulation period. The reason for the use of coal with carbon capture to become profitable is that the CO<sub>2</sub> captured is used for

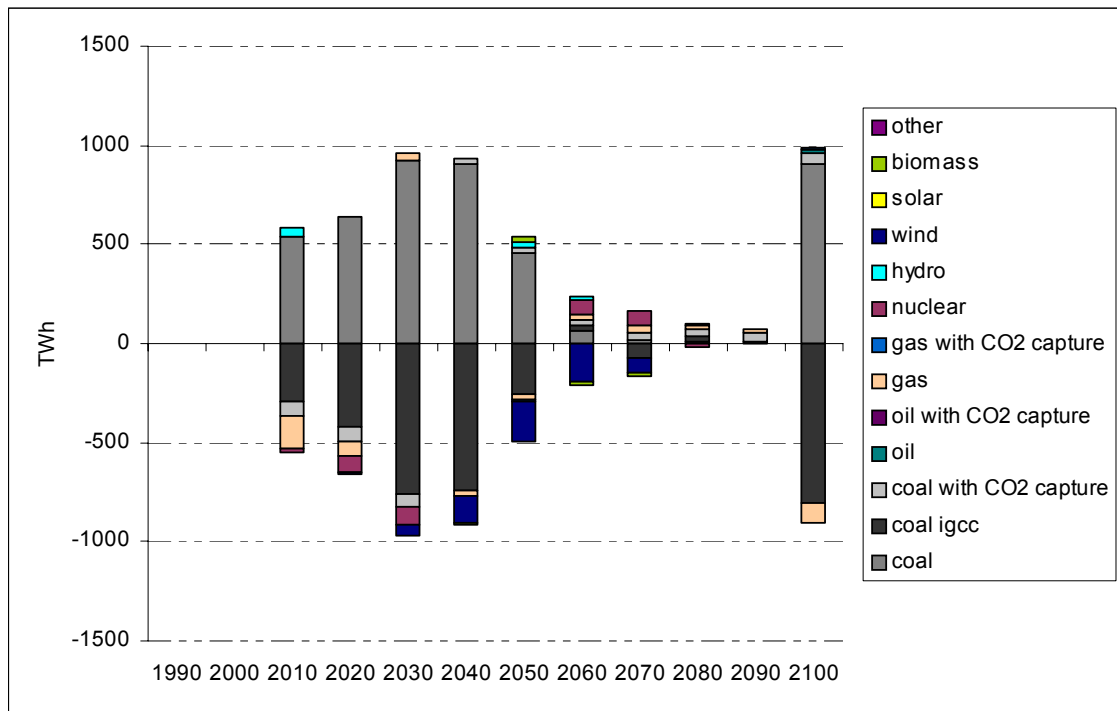
ECBM. Through the recovery of methane by the injection of CO<sub>2</sub> in coal beds, it becomes cost-effective to invest in coal power plants that include carbon capture and sequestration, in addition to the vast use of coal through IGCC. Otherwise, figures 4a and 5a differ little from each other. Note that one may judge it remarkable, and even unlikely, that ECBM will make carbon capture profitable without carbon constraints; in our case it appears as an opportunity largely as a result of our parametric assumptions on fuel prices. As can be seen from figure 5b, in the climate-constrained scenario, allowing for geological carbon storage implies that coal remains an electricity option for the rest of the century at a fairly constant share (and coal is not phased out like in figure 4b). Coal with carbon capture is developed to a large extent, especially during the last decades of the 21<sup>st</sup> century. Again, the reason is that CO<sub>2</sub> is injected in coal seams to extract methane, which on its turn is fed into the energy system. In this stabilisation case, compared to the stabilisation scenario without carbon capture, coal-based electricity production with CO<sub>2</sub> capture replaces some of the renewables (biomass and solar energy). Again, one observes that overall electricity supply in figure 5b is lower than in 5a. The reason is that in the 550 ppmv stabilisation case, a reduction has to be realised of up to 40-60% of annual carbon emissions by the end of the century. This reduction will affect seriously energy prices, and hence end-use behaviour, demand and production. A fixed price-insensitive demand would over-estimate future energy use under severe climate constraints, and also pose a heavier burden on the energy system as a whole in meeting these constraints.

If one applies the external costs from table 1 to electricity production costs, and assumes 0.2 €/kWh external costs for all other production options (renewables, nuclear and hydropower), it is not surprising that both the overall production level and the electricity production mix changes. The differences between scenarios with and without external costs prove important. For our purpose, most interesting is to look at the results in two external cost cases, namely with and without CO<sub>2</sub> sequestration costs. Figure 6 illustrates (in the BAU case) how the introduction of global warming external costs influences the total production of electricity, as well as the nature of the resulting production mix. The figure depicts in particular how the share (or rather, contribution) of some energy resources decreases (options that result in bars above the 0-line) and the share of others increases (bars below the 0-line).<sup>12</sup> As can be derived from the difference between the bars above and below the x-axis, the total power production is lowered slightly as a result of incorporating external global warming costs (between 0.5 and 2.0%). As can be seen from the figure, in terms of the production mix, the use of coal with conventional technologies is reduced, but the part lost is mainly replaced by the use of coal through IGCC. Also the use in production of natural gas and wind is increased modestly. The use of nuclear energy is slightly increased in the short term, but loses in importance in the longer run, according to our modelling results.

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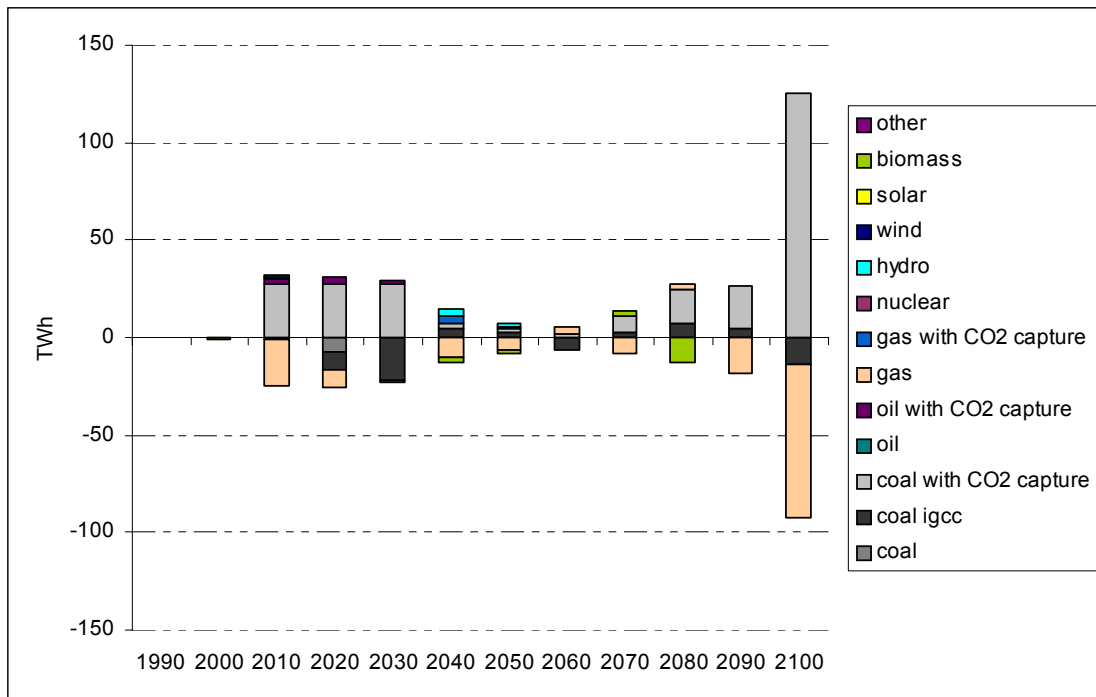
<sup>12</sup> Note that in figures 6, 7 and 8, we want to present the effect (on electricity supply, resulting from including external costs) in terms of the *reduction* of contributions from different energy resources, so that *decreases* appear as *positive* columns (and *vice-versa*).





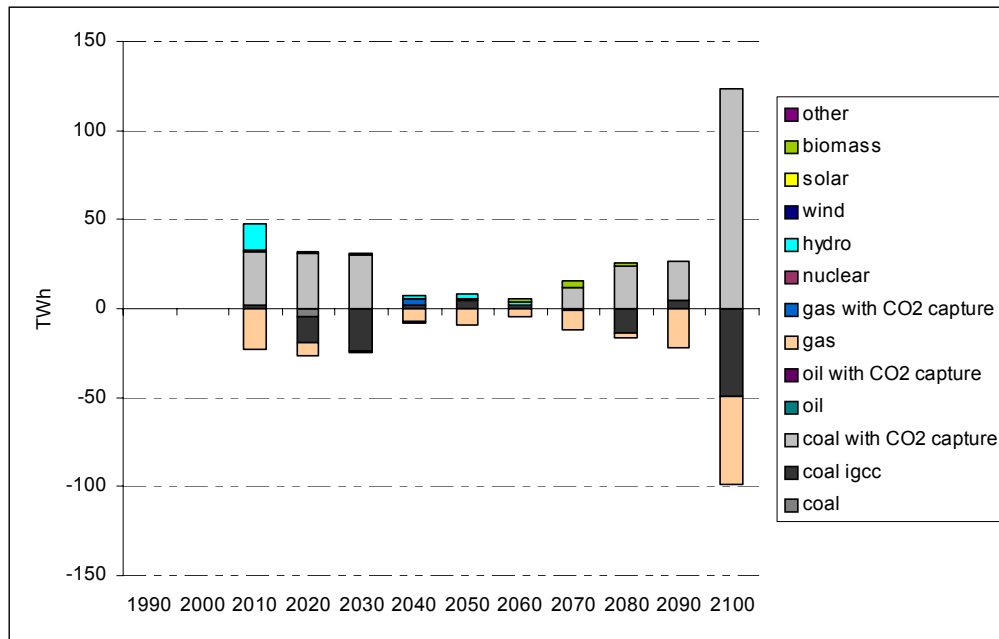
**Figure 6.** Overall and energy-specific reduction in electricity production after applying global warming external costs (BAU case).

Figure 7 displays the changes induced when, in addition to global warming external costs, also external costs for CO<sub>2</sub> sequestration are applied (again for the BAU case). First of all, one observes that the total change in electricity generated (all externalities in comparison to global warming externalities only) is relatively small, about an order of magnitude smaller than in the case of figure 6 with the introduction of global warming costs only (in comparison to no external costs). Both in the cases of no inclusion of external costs and the incorporation of global warming external costs only, the use of coal with carbon capture and sequestration was able to develop to some (rather small) extent. When also sequestration external costs are accounted for, coal-based production with CO<sub>2</sub> capture loses part of its share, as can be seen from the bars above the 0-line in figure 7. The share lost is mostly replaced by coal based on IGCC and the use of natural gas (and to a lesser extent also biomass). Overall (and understandably), the shift of technologies results in a total production level that is lower than in the case with only global warming external costs, the difference being on average 4 TWh/yr. This reduction comes on top of an average reduction of 35 TWh/yr after the inclusion of global warming external costs only. Thus, the inclusion of external costs for CO<sub>2</sub> sequestration has a further dampening effect on power generation, while the price difference between various electricity generation sources becomes less pronounced. As can be seen from figure 7, the overall electricity production reduction is largest at the end of the time horizon, and lowest in the very beginning. This means that, while the effects of including external sequestration costs are felt during the entire modelling time frame, the effects are significantly larger at the end of the 21<sup>st</sup> century than when they start being applied. This is a specific feature of our version of the MARKAL model used.



**Figure 7.** Additional overall and energy-specific reduction in electricity production after also including CO<sub>2</sub> sequestration external costs (BAU case, producer-side).

For both figures 6 and 7, the external costs are implied at the producers level as add-on to the fuel cost used as input in power plants. However, two variants can be considered, one where the external costs are distributed over power producers by adding it to fuel costs (as done for figures 6 and 7), and one where the external costs are distributed over the end-users as add-on to electricity prices. In the second case, the system not only optimises demand, but does so while taking into account increased delivery prices of electricity as set by producers. This, naturally, results in a lesser demand, and, as a consequence, a lower level of production. The difference, like in the first case, in total power generation (in a business-as-usual scenario) between with and without (global warming plus carbon sequestration) external costs lies in the order of 40 TWh/yr, or about 2% of total production. As a matter of fact, since the overall reduction in demand as a result of additionally including carbon sequestration is about 8 TWh/yr on average in the second case, the production level change as a result of the inclusion of all externalities lies this time slightly above 40 TWh/yr. The detailed results are depicted in figure 8. One sees that the features observed in this (consumer) case are roughly similar to the ones as found in the first (producer) case (compare figures 7 and 8). For example, coal-based power production including carbon sequestration is partly substituted by IGCC coal power production, the latter becoming more attractive due to the smaller impact of external sequestration costs on the output price of electricity. Also natural gas based production profits from the changed difference in production costs per kWh, and increases its share. If IGCC technologies gain in importance, it indeed seems logical that the use of natural gas should do so too, given the comparability of these two technologies.



**Figure 8.** Additional overall and energy-specific reduction in electricity production after also including CO<sub>2</sub> sequestration external costs (BAU case, consumer-side).

A comparison of both base-case variants of figures 7 and 8 – with external costs accounted for via either fuel input for power plants or for the end-users of electricity – shows that in an optimisation model like MARKAL the difference between these two distribution systems induces little change. This could be expected, because the model optimises simultaneously the supply and demand side, while taking into account price-elasticity effects on the demand side. Also, the model does not take into account behavioural effects, but merely takes a rational approach to meet constraints and to cope with cost increases, so that no large differences are to be expected between the two cases. Nevertheless, some small effects were found. These are hard to explain because of the complex interactions and competitions between technologies and energy carriers. For example, applying external costs to output power prices generates a little bit more coal IGCC electricity, and a little less biomass and natural gas. In this case, there is also a little less hydropower in the earlier periods; the system uses its maximum hydropower potential only in the case when externality costs are charged on fuel as input to power generation.

Figures 6, 7 and 8 all present our comparison results in the BAU scenario. For the 550 ppmv stabilisation case, the introduction of external costs for global warming and CO<sub>2</sub> sequestration has been briefly inspected as well. In most respects, our findings are very similar as in the BAU case. Including carbon sequestration externalities induces, likewise – whether accounted for at the production level or at the level of end use – an overall production that is on average slightly lower than in the case without these sequestration externalities. Also in the production mix there are changes similar to the ones encountered in the base case. Coal-based production with CO<sub>2</sub> capture decreases over the whole time frame, while IGCC and natural gas show a slight increase in production, especially over the first few decades. Also other production means gain in interest in this case (predominantly later in time), among which solar, biomass and hydro energy. Of course, like previously observed, the shifts in the production mix remain modest compared to the overall production level. While the shifts in the stabilisation case are perhaps slightly larger than in the base case, they show a very similar trend, indicating the robustness of our analysis results.

We end by presenting analysis results through which some final findings can be derived regarding both the effect of including externalities and the difference between the producer and consumer cases: the evolution over time of the amount of sequestered carbon dioxide and the total (remaining) amount of emitted CO<sub>2</sub>. The amount of sequestered CO<sub>2</sub> is, of course, influenced by the inclusion (or not) of external costs. Figure 9 shows the annual amount of geologically stored CO<sub>2</sub> for each of the different scenarios assessed so far. As observed earlier, carbon sequestration already appears in the base case where no climate constraint is imposed. But the amount of CO<sub>2</sub> sequestered becomes significantly larger when a stringent climate policy is introduced. In both cases, the incorporation of external costs, either with or without sequestration externalities, lowers the amount of carbon sequestered in the long run. Including additional sequestration externalities lowers the amount of carbon sequestered further in comparison to the case where these externalities are not included. In the base case, it does not matter whether one charges these externalities at the producers or consumers side, while in the stabilisation scenario one can discern a small difference as a result of using these different accounting schemes.

Applying global warming external costs has the largest impact: a total cumulative reduction of sequestered carbon dioxide of 150 Mton in the base case and 420 Mton in the 550 ppmv stabilisation case (hence, over the 21<sup>st</sup> century modelled, on average 1.5 and 4.2 Mton/yr, respectively). Also adding sequestration external costs reduces the cumulative amount of carbon sequestered further with 190 Mton and 300 Mton (1.9 and 3.0 Mton/yr) for the base and 550 ppmv cases respectively. Applying external costs on end-users or fuel input involves a change in the amount of carbon sequestered, in the 550 ppmv case, of the same order of magnitude as the change incurred as a result of whether or not including carbon sequestration externalities. Overall, with an accounting for environmental externalities, sequestration becomes less part of the solution to meet climate change targets, while demand reduction, energy switches and technological change take a more important role. This illustrates the significant sensitivity of our model to price changes, even when these are small.

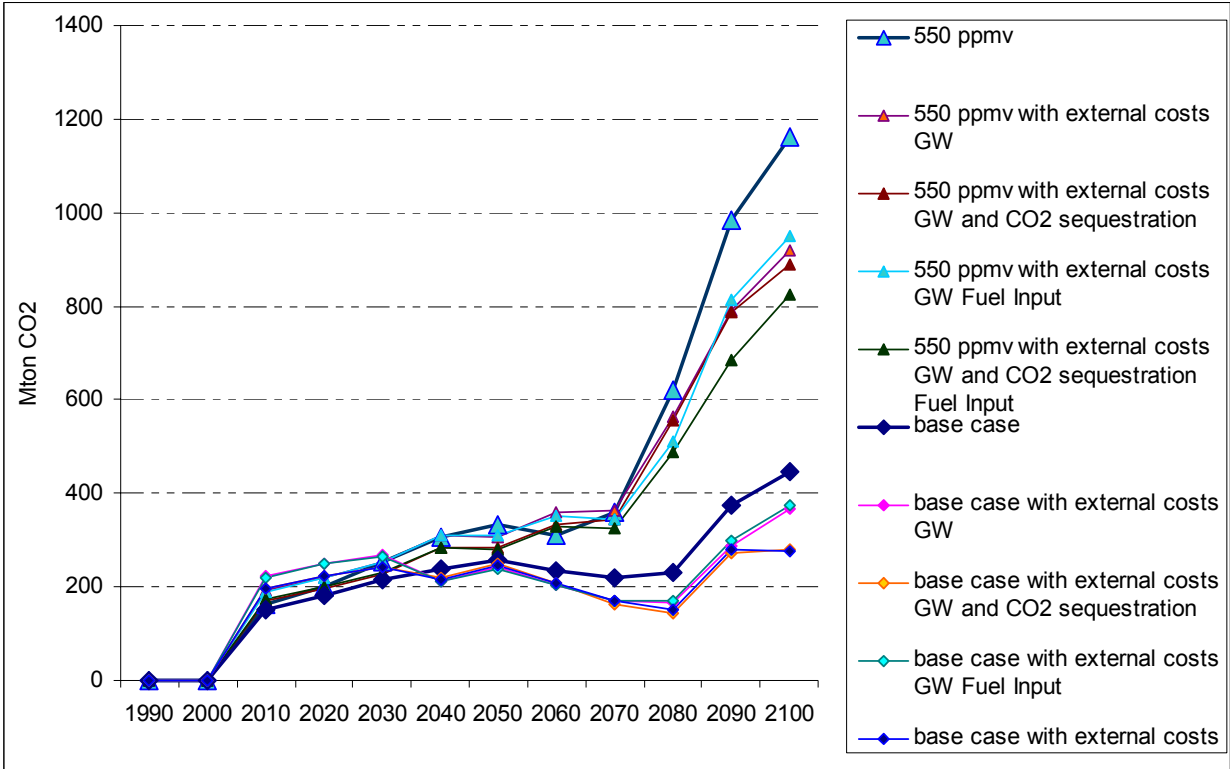
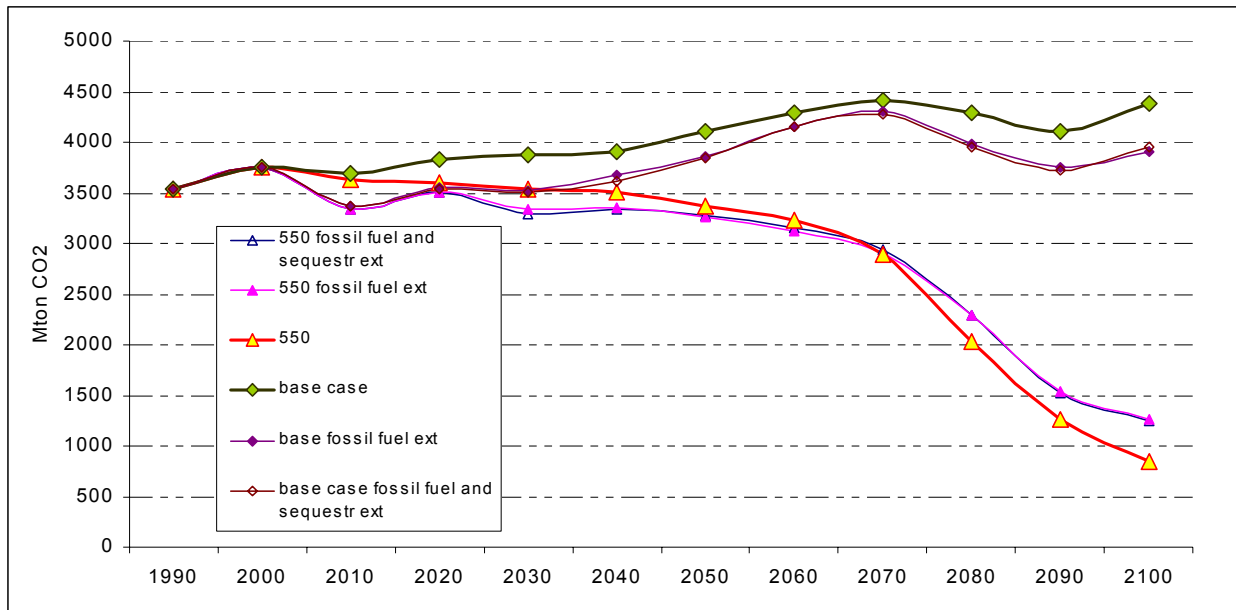


Figure 9. Total annual amount of sequestered carbon dioxide in Mton/yr.

As can be seen from figure 9, the inclusion of external global warming costs significantly lowers the amount of carbon sequestered in the long run. At first sight, this result may appear counter-intuitive, as one would perhaps expect the higher the damage provoked by carbon dioxide, the larger its sequestration. The mechanism driving the result, however, is: accounting for external costs implies in practice an increase of the costs (for either producers or consumers) - and hence in principle a decrease in attractiveness - of using fossil fuels as input for power plants. This implies that other energy options may play an enhanced role, or that the overall demand for electricity decreases due to the cost increase of electricity through the inclusion of external global warming costs. With the internalisation of climatic external costs, the use of important emitters of greenhouse gases, such as fossil-fuelled power plants, is most heavily affected, in the sense that gains are obtained in terms of avoiding detrimental greenhouse gases, but higher costs are incurred as a result of implementing carbon capture processes (that are unlikely to ever become 100% efficient). In our scenario analysis, it appears that the gains in terms of carbon emission mitigation through carbon capture are not high enough, or the additional involved costs for fossil fuels too elevated, in comparison with non-fossil options that are free of carbon emissions. A lowering of total energy production, and consequently of carbon emission and sequestration, and/or an increase in e.g. electricity from renewables might explain why we find lower carbon sequestration when including external global warming costs.

The inclusion of external costs makes a difference as well in terms of the overall carbon dioxide emission path, the impact being slightly larger in the base case than in the 550 ppmv case (see figure 10, in which external costs are accounted for at the level of the fuel input to electricity production). In the former case, carbon emissions are lowered over the entire time frame considered, as a result of including these externalities, with little difference as to whether one includes carbon sequestration external costs or not. In the latter case, a shift in time occurs in the calculated emission path, while the overall cumulative amount of emitted CO<sub>2</sub> (calculable through an integration over the area under the emission evolution curve) remains approximately the same. Again, there is little impact on the calculated emission level from an inclusion or not of external costs resulting from carbon sequestration. Obviously, a sharp decline in emissions results (in comparison to the base case) when one imposes the 550 ppmv carbon concentration constraint. As can be seen from figure 9, this decrease in emissions coincides with an increase in the amount of carbon sequestered underground. As we can see from a comparison between figures 9 and 10, in 2100 the amount of sequestered carbon dioxide is about the same as the remaining level of carbon dioxide emissions.



**Figure 10.** Total amount of remaining CO<sub>2</sub> emissions.

## 5. Discussion, conclusion and recommendations

Given the preceding presentation of our main results, the prime conclusion of this analysis is that, while external environmental effects of carbon sequestration are generally likely to be relatively small, these externalities matter, and influence the nature of future world energy supply and consumption significantly enough to pay due attention to them. More importantly, since geological carbon storage (depending on the method employed) may in some specific cases have very substantial external impacts – in terms of both environmental damage and health risks – it is recommended that extensive studies are performed to quantify these effects. As explained, the numbers postulated in table 3.1 do not involve any detailed calculation. The proper way to proceed would be to determine more precise data for all damage costs of geological carbon sequestration. Ideally, a complete impact pathway analysis would be performed, along the lines for other energy resources and technologies of the EU ExternE project (see, e.g., ExternE, 1998). We thus recommend that external damage cost calculations for carbon sequestration are included in the next phase of ongoing ExternE analyses. Also the fossil fuel cycle including carbon capture and sequestration should be analysed according to the method by which its effects are calculated in terms of emissions, dispersion, impact and the total monetary value of this impact, resulting in an overall environmental damage cost in terms of \$(or €)-cents per kWh. As long as detailed calculations remain absent, and until the moment that appropriate calculations will have been performed, we think that the numbers presented in table 3.1 can be considered rough but reasonable guesstimates.

In the beginning of this article we posed ourselves three main questions. The first one – on the nature of energy supply if one accounts for CO<sub>2</sub> sequestration in the construction of long-term energy scenarios – we have addressed by the presentation of the scenario results as produced with MARKAL-ED. The second question concerned the inclusion of hypotheses regarding the level of external costs, and the effect hereof on the calculation of long-term energy scenarios. As mentioned, the effect is unlikely to be very large. It certainly does not seem to be negligible, however, so that we judge it necessary that detailed calculations are performed for a proper quantification of the external environmental costs of large-scale CO<sub>2</sub> sequestration. Once

such calculations have been made, the question of how these costs may affect the construction of long-term energy and climate change scenarios – which we answered at a first and preliminary approximation – can be revisited. Responding to our third question: it does not seem to matter significantly whether carbon sequestration damage costs are charged directly to energy consumers or, instead, to electricity producers. Surely in comparison to the inclusion of external global warming costs, the effect of choosing either of these two accounting schemes is small. The effect is expected to be of the order of magnitude of the incorporation of external costs for carbon sequestration.

It is commonly expected that without the imposition of a climate constraint the use of coal will be continued, and even considerably expanded, during the entire 21<sup>st</sup> century. Among the reasons are that coal is relatively cheap and readily available in large quantities at many locations the world over, notably in various large developing countries. Because of its polluting nature, however, both regarding local air pollution and as important contributor to global warming, the use of coal will probably be slowly discontinued over the decades to come when stringent climate objectives are to be met. An important conclusion of our analysis is that the role of coal probably remains important, even under a strict climate constraint, if carbon capture and sequestration is implemented on a large scale. Other research has come to similar conclusions (see, for example, McFarland *et al.*, 2002), the main reason being that, among the three fossil fuels, carbon capture is most easily implemented for coal technologies, thus allowing its continued use when reductions of carbon emissions are aimed at. Another finding, not reported so far in the literature, is that coal power plants may be simultaneously operated for both electricity generation and the production of CO<sub>2</sub> to be employed for methane extraction. Through the use of ECBM, natural gas (the cleanest of all fossil fuels) is then produced as by-product of the carbon dioxide injection process in coal seams, and can thereby be advantageously fed back into the energy system. If external damage costs for global warming are included, these findings remain roughly unchanged, the only difference being that coal with IGCC technologies (which will increasingly gain importance over the decades to come irrespective of the scenario assumed) is further favoured to the debit of conventional coal technologies. If also carbon sequestration damage costs are included, a small change can be observed from the use of coal plus carbon sequestration to the use of, predominantly, natural gas.

Some further analysis has resulted in preliminary answers regarding a number of other questions, not reported in section 4, such as what the origin of the total sequestered amount of CO<sub>2</sub> is. It proves that in both the base case and the climate-constrained scenario, the geologically stored CO<sub>2</sub> mainly originates from two sources: coal power generation and fuel conversion (that is, the production of hydrogen). Coal power generation is in both scenarios the most important source of sequestered CO<sub>2</sub>. As we have seen, accounting for external costs induces changes in the electricity production mix. If external carbon sequestration costs are included in the analysis, especially mixes that include options with CO<sub>2</sub> capture and storage change. This affects, naturally, the composition of the sources of CO<sub>2</sub> capture. From our preliminary analysis, however, it follows that the effect of this inclusion is not very large, probably because of the relatively small expected external sequestration cost level. It may still be worthwhile to explore this subject matter further.

Where will CO<sub>2</sub> be sequestered? Again, we have not fully explored this question yet, but some preliminary study suggests that coal beds become the main recipient of CO<sub>2</sub>, since this sequestration method, through ECBM, involves the beneficial recovery of methane. This finding is surprising, since ECBM is currently not seen as one of the most evident options for carbon storage. It results from our various modelling assumptions regarding (fuel) prices, and needs to be further investigated. Even in a base case scenario, ECBM is mostly followed by EOR, because of the advantageous oil recovery it implies. In a climate-constrained case higher sequestration levels should be attained, so that one is likely to observe an exhaustion of both the

ECBM and EOR potentials. This implies that storage in aquifers, as well as in depleted oil and natural gas fields, starts being employed by the end of the modelling horizon. Biological sinks are only likely to play a modest role throughout the entire 21st century. As shown from a quick inspection of the matter, the inclusion of external costs affects the sequestration options chosen in the system. The impact, however, does not seem to be very significant: in all cases, ECBM remains the predominant favourite and is used as first storage option, given the interesting option of energy recovery, while EOR comes second in line and appears later in time. Storage in aquifers and depleted oil and gas fields remains, it seems, a backstop solution. Since non-negligible effects of external cost internalisation on the nature of carbon sequestration recipients are observed, especially in the 550 ppmv stabilisation scenario, this constitutes a window for further research.

Among the other topics for future research is an analysis of welfare effects. In MARKAL, the surplus of consumption and production means can be interpreted as some measure of the welfare level of the economic system. For the short term, the imposition of a climate constraint and the inclusion of environmental externalities in energy costs involve a loss of this welfare measure. As a result of these conditions, the energy system evolves in a way different than without them, so that in the long run the welfare loss implications may not be trivial. The marginal cost of electricity, to be paid by consumers, is one of the determinants of the welfare (loss) level. This electricity cost is affected by both the climate constraint and the inclusion of externalities. External costs are thought to typically increase the marginal cost of electricity by 1.0 to 1.5 €cent/kWh, in the base case scenario. For the 550 ppmv climate-constrained scenario, the picture is more complex, as a result of the interplay between shifting investments and the presence of learning phenomena. Also this matter may be subjected to future research.

It is likely that geological carbon sequestration is going to be applied on a large scale over the decades to come. Among the various reasons is the fact that this allows continuing the present use of fossil fuels and that of their supporting infrastructures. However, carbon storage is neither a sustainable nor a renewable energy option: “true” renewables remain preferable over the longer run. The long-term deployment of renewables, however, might be negatively affected by the development of carbon sequestration today. It is therefore important, in both the scientific and policy-relevant discussion around this matter, that possible external environmental impacts of carbon sequestration are not discarded, in the same way as externalities of renewables should not be left out in assessments of their potential and desirability. In the discussion around carbon sequestration, the energy price paid for the carbon capture and storage process should also be included, as should be the observation that it prolongs the fossil fuel *époque* (fossil fuels remaining constrained by their limited abundance), with all the detrimental side-effects the continued use of carbon-based energy may entail. Although geological carbon storage is inherently not renewable, carbon sequestration could be considered a useful solution to bridge the 21<sup>st</sup> century, and create the time needed to let real renewable and sustainable energy sources evolve into competitive alternatives. It may thus prove a suitable technology for the development of paths leading to the sustainable use of energy.



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- (lix) This paper was presented at the ENGIME Workshop on “Mapping Diversity”, Leuven, May 16-17, 2002
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- (lxi) This paper was presented at the Eighth Meeting of the Coalition Theory Network organised by the GREQAM, Aix-en-Provence, France, January 24-25, 2003
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- (lxvi) This paper has been presented at the 4th BioEcon Workshop on “Economic Analysis of Policies for Biodiversity Conservation” organised on behalf of the BIOECON Network by Fondazione Eni Enrico Mattei, Venice International University (VIU) and University College London (UCL), Venice, August 28-29, 2003
- (lxvii) This paper has been presented at the international conference on “Tourism and Sustainable Economic Development – Macro and Micro Economic Issues” jointly organised by CRENoS (Università di Cagliari e Sassari, Italy) and Fondazione Eni Enrico Mattei, and supported by the World Bank, Sardinia, September 19-20, 2003
- (lxviii) This paper was presented at the ENGIME Workshop on “Governance and Policies in Multicultural Cities”, Rome, June 5-6, 2003
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