Chapter 35 – Further DFP approval for RHI

DFP consideration of the Business Case Addendum

35.1 Following the Casework Committee meeting on 21 October, Mr Cooper formally submitted, on 27 October 2015, a copy of the Business Case Addendum to Ms Scott at DFP Supply Division for DFP approval.[1935] This was Version 4 of the Business Case Addendum.

35.2 The Business Case Addendum was sent with a covering letter from Mr Cooper.[1936] His covering letter asserted at paragraph 2 that "The scheme provides ***continuing*** (the Inquiry's emphasis) value for money."[1937]

35.3 At paragraph 11 the letter stated that:

> "As regards reacting sooner to increased uptake, the Business Case Addendum confirms that the Department could not have reasonably acted sooner. A sustained increase in application numbers was not achieved until March and April 2015."[1938]

35.4 Paragraph 3 emphasised that, for legislation to proceed in early November, approval was needed on scheme expenditure.[1939] At paragraph 9 Mr Cooper stated that, with low levels of uptake and underspends against allocation the domestic scheme had been given precedence over extension of the non-domestic scheme and cost controls measures and that implementing all of the 2013 consultation proposals would have caused significant delays.[1940] He advised, at paragraph 13, that the most recent update from Ofgem had shown uptake to be 4 times that forecast for October but the DETI Analytical Services Unit (ASU) had confirmed that the additional expenditure was value for money (VFM) on the basis that VFM was "scaleable".[1941]

35.5 The Business Case Addendum itself had a table included at paragraph 3.3 which showed that applications had risen from 9 in the year 2012-13 to 119 in the year 2013-14 and 435 in 2014-15.[1942]

35.6 The Version 4 of the Business Case Addendum forwarded to DFP on 27 October, as discussed previously, had been modified from the Version 3 used at Casework Committee and informally shared with DFP on 16 October 2015. It now included the following at paragraph 2.5, presumably the product of the undertaking given to Ms Scott at the Casework Committee to address what had been the trigger for cost controls to be introduced on the GB RHI scheme in 2012:

> "The NI Non-Domestic Scheme commenced one year after the GB scheme. But unlike the experience with the GB scheme where considerably higher tariffs triggered high levels of uptake from the outset, the performance of the NI scheme was poor. The high uptake on the GB scheme led DECC to consult on cost control

1935 DFE-149790 to DFE-149822
1936 DFE-149791 to DFE-149794
1937 DFE-149791
1938 DFE-149793
1939 DFE-149791
1940 DFE-149792
1941 DFE-149793 to DFE-149794
1942 DFE-149800

measures in Spring 2012 by which point the GB scheme had already received 533 applications (in six months) and forecast expenditure for 2012/2013 was £42 million. The NI scheme on the other hand had only received 21 applications in the first seven months. There was therefore no immediate need to follow DECC's proposals for budgetary control. In any event the 'budgetary controls' only related to deferral of applications and the measures were subsequently withdrawn by DECC. After two years DECC did introduce expenditure control measures in the form of digression [sic] arrangements."[1943]

35.7 The statement in paragraph 2.5 of the Business Case Addendum was not accurate. The introduction of an "interim cost control" or "stand-by mechanism for budget management" by DECC in relation to the GB RHI scheme has been discussed previously in this Report. It followed a public consultation initiated on 26 March 2012, a few months after the implementation of the GB RHI scheme.[1944] The Ministerial Foreword to the relevant consultation document recorded that the scheme was funded from Government spending and emphasised the need to maintain value for money and protect annual budgets. It also noted that, despite the fact that uptake levels were very low relative to the available budget, assurance was needed that the scheme would not exceed budget; taking into account the fact that it was a new policy in an immature market with a high degree of uncertainty in the short term.[1945] The GB RHI interim cost controls were not withdrawn; they were replaced by legislative amendment bringing into operation a more sophisticated long-term system of degression, something which had been explained in the March 2012 consultation document.

35.8 The Business Case Addendum did record that the RHI AME funding might not be treated as normal AME and that there may be NI DEL consequences/penalties of "overspending".[1946] Clarification was needed from DFP/HMT, and if such consequences or penalties were to be visited upon the NI block for spending more than what was described as "the 'Barnett' allocation", then both schemes might need to be closed in 2016.[1947]

35.9 Upon receipt, Ms Scott, the DETI Supply Officer in DFP, submitted the Business Case Addendum to Christine Finlay, Deputy Principal Economist with the Economic Appraisal Branch (EAB) within DFP making it clear that she was coming under pressure from DETI to respond/approve the case by 30 October.

35.10 Ms Finlay had in fact looked briefly at the Business Case Addendum on 21 October 2015[1948] when Version 3 was submitted informally to DFP. At that time she made the point, having looked at the risks section, that the original Outline Business Case looked at risk of incorrect subsidy level and the risk of insufficient budget for administration or future payments. She then stated: "These must not have been well mitigated." She also made the point "the cost of the new commitments are huge."

1943 DFE-149796
1944 DFE-53097 to DFE-53121
1945 DFE-53098
1946 DFE-149804
1947 DFE-149804
1948 DOF-04584

35.11 In light of the timetable expected of DFP to deal with the approval Ms Morelli, the head of DFP Supply, made clear, on the evening of 27 October 2015, that "all we can offer at this time is prospective approval as discussed."[1949]

35.12 Ms Finlay spoke to Ms Scott over the telephone and, having had what she described as "a really quick look over the RHI Addendum", had her further comments transmitted to Ms Scott on 28 October.[1950]

35.13 In her written statement of evidence to the Inquiry, Ms Finlay pointed out that:

> "If I had have had more time to quality assure the addendum I could have looked further into the assumptions behind the modelling and various other tariff levels. With limited time and considering the status quo, it was important to do something, if even on a temporary basis and review further options and additional analysis further down the line."

35.14 Among other matters raised by Ms Finlay in her comments were: the fact that she was wary about employment benefits now being taken into account with regard to VFM; the need for continuous monitoring and a budget cap; the spike from poultry houses; and whether the scheme could be closed.

The DFP letter of 29 October 2015 granting prospective approval

35.15 Following a series of email exchanges between Ms Scott and Mr Cooper,[1951] where a number of issues were clarified, a DFP approval letter from Ms Morelli was sent to DETI on the morning of 29 October 2015 granting prospective approval only, and on a time-limited basis to 31 March 2016.[1952]

35.16 Ms Morelli recorded in the letter that the time allowed for DFP consideration was far from ideal to allow for scrutiny, especially since the intention to submit the addendum had first been discussed with DFP on 12 June.[1953] As noted earlier, Ms Morelli and other officials from DFP had been present at and participated in the Casework Committee discussion.

35.17 In her letter of approval Ms Morelli emphasised that, because of the very short time scale, DFP had prioritised the prospective element of the addendum and would return to the retrospective request (i.e. for the period from 1 April 2015 to the end of October 2015) in due course.[1954]

35.18 Ms Morelli did not question whether, or how, the fact that expenditure had reached four times the forecast was relevant to the assessment of VFM. Nor did she enquire as to why employment benefits had now been introduced in the VFM assessment when that had not been done in the previous consultants' studies, despite that concern having been raised earlier by Ms Finlay in her comments to Ms Scott. Ms Morelli told the Inquiry that "We weren't looking at optimal value for money in reading this business case – even prospectively." She said:

> "We had two days, really, to look at this, and, if you're asking should we have sought more information or challenged further or looked into this, I would say, "Yes,

1949 DOF-04582
1950 WIT-42617 to WIT-42622
1951 DOF-04579 to DOF-04581
1952 DFE-167354 to DFE-167356
1953 DFE-167354
1954 DFE-167354

> we should have" to make sure that we were giving optimal value for money, but, on the information that was provided, we were looking to see, "Well, is this the best case that's provided in this case?" and it was."[1955]

35.19 She accepted that she had not picked up or questioned the circumstances of the reference to reducing the risk of "gaming" mentioned under the heading 'Annual Payment Cap' in paragraph 4.16 of the Business Case Addendum stating:

> "In the consideration of this case and the prospective way forward, we were looking forward, and I suppose it's no excuse, but nobody -. Well, I personally didn't read that and ask those questions."[1956]

35.20 In the letter of 29 October Ms Morelli noted that, while approval was requested to December 2016, no budget had been confirmed beyond 2015-16 and there would only be certainty as to future funding following the November 2015 Spending Review.[1957] It was for this reason, given this lack of certainty beyond the end of the 2015-16 financial year, and as mentioned earlier, that DFP approval for new installations was limited to 31 March 2016.

35.21 Approval was given subject to a number of conditions, including a review that should include a "comprehensive, evidence-based assessment of all aspects of the RHI intervention, including tariff levels, banding and the duration of tariff payments."[1958]

The DFP letter of 21 December 2015 refusing retrospective approval

35.22 The legislative changes to the NI RHI scheme were subsequently approved by the Northern Ireland Assembly on 17 November 2015, and came into effect on 18 November 2015.

35.23 On 7 December 2015[1959] Mr Cooper wrote to DFP to explain that there had been 983 applications to the NI RHI scheme in the two and a half months leading up to the tariff changes on 18 November, and that the previous forecast of £22.8 million for 2015-16 (in November 2014 it had been around £12 million), now had to be increased to £30 million for 2015-16, and it would be £42 million in 2016-17. He also pointed out that any decision to close or restrict the NI RHI scheme could trigger another spike in demand and committed expenditure.

35.24 On 21 December 2015 DFP issued its decision on DETI's application for RHI retrospective approval for the period April to October 2015. DFP refused retrospective approval. The consequence of that decision was that all spending arising from the period not covered by an approval would remain "irregular" in Government accounting terms.

35.25 In the 21 December refusal letter[1960] Ms Morelli set out the rules relating to the grant of retrospective approval, and confirmed that, since DFP had not been afforded the opportunity to review or influence the policy decisions being taken at the time, March 2015, she could not conclude that DFP would have been satisfied with the decision not to amend the scheme and that, consequently, retrospective approval should be refused. The level of irregular expenditure would therefore be £17.7 million in 2015-16 and £355 million across the 20-year life of the scheme, to reflect the accreditations occurring between April and October 2015.

1955 TRA-15083
1956 TRA-15088
1957 DFE-167355
1958 DFE-167355 to DFE-167356
1959 DFE-152858 to DFE-152859
1960 DOF-04726 to DOF-04728

35.26 She explained that DFP Supply would write to the Audit Office to notify it of the refusal, indicating that DETI's management of the NI RHI scheme had raised a number of concerns. This led to the involvement of the Northern Ireland Comptroller & Auditor General and the production of the NIAO report of June 2016.[1961]

35.27 In her letter refusing to grant retrospective approval Ms Morelli referred to the level of annual expenditure being around £10 million per annum higher than the costs reported in the October Business Case Addendum and that the number of applications received in October alone was double the amount of applications received in the first 20 months of the scheme. She expressed the view that such a development "clearly warrants further investigation to test both the origin and authenticity of the additional applications."[1962]

35.28 She noted that the level of irregular expenditure was "of considerable concern for DFP" but those concerns were "dwarfed by the very immediate and long term budgetary implications."[1963] She explained that the HMT AME profile for the forthcoming Spending Review period was considerably lower than the level of expenditure DETI was now committed to, and, while discussions were ongoing, a possible and, indeed, probable outcome was that the Northern Ireland Executive would have to fund all costs above the HMT AME profile.

35.29 She concluded the letter in the following terms:

> "It would be useful to discuss the affordability concerns in more detail. My office will be in contact to arrange a suitable time to discuss both the budgetary and value for money implications of the operation of the non-domestic RHI scheme."[1964]

35.30 It appears to the Inquiry that the only reason why such reasonable enquiries were not made prior to approval was the concern about pressure of time.

1961 CAG-01680 to CAG-01697
1962 DOF-04727
1963 DOF-04727
1964 DOF-04728

Findings

199. The Inquiry takes into account the time pressures, the need to be fair to those concerned and the risks represented by hindsight. Nonetheless the Inquiry finds that although action was urgently needed in the autumn of 2015, the imperative of finding a solution outweighed the normal process within the civil service for independent scrutiny and challenge, and thus DFP approved the seriously flawed Business Case Addendum in circumstances in which it might not otherwise have done so.