

## Chapter 55 – DETI systems of governance and control

### The issue of governance within DETI

- 55.1 One of the many issues which the Inquiry has had to investigate is why risks relating to the NI RHI scheme materialised, but yet were not sufficiently appreciated by officials or picked up sooner by DETI's systems of governance.
- 55.2 Officials working on the NI RHI scheme within DETI had identified some potential risks relating to the scheme from the outset. They were recorded on an initial scheme risk register. Several risks were also the subject of warnings to DETI from bodies like CEPA and Ofgem during the creation of the scheme, whilst the same or other risks became apparent to commercial entities in the renewable energy sector shortly after the scheme launched, some of which were drawn to DETI's attention.
- 55.3 Governance systems were the Department's safety net, there to ensure that commitments were met and to draw attention to any mounting problems, such as those of the NI RHI, before they went out of control. Shortcomings in the design and implementation of the NI RHI scheme, and the impact of the lack of project management, could and should have become visible to senior management through such systems; but this did not begin to become reasonably apparent until the middle of 2015 and not in a sufficiently structured form until the DETI Internal Audit report of May 2016.<sup>2977</sup>
- 55.4 Alongside arrangements for the management of civil servants (using mechanisms such as annual appraisals, objective setting and regular personal performance reviews), DETI's governance systems were intended to give assurance to the Permanent Secretary and senior management that the Department's activities were being well managed. Responsibility for making sure that these governance systems were in place and working satisfactorily rested ultimately with the Permanent Secretary.
- 55.5 Mr Sterling, in his written evidence to the Inquiry, explained that section 3 of 'Managing Public Money Northern Ireland' required him, as Accounting Officer, to ensure that the organisation operated effectively and to a high standard of probity, meaning specifically that he had to ensure his Department:
- had a governance structure which transmits, delegates, implements and enforces decisions;
  - had trustworthy internal controls to safeguard, channel and record resources as intended;
  - operated with propriety and regularity in all its transactions; and
  - used its resources efficiently, economically and effectively, avoiding waste and extravagance.<sup>2978</sup>

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2977 DFE-223638 to DFE-223682

2978 WIT-04049

## Previous similar issues – the BTI and Bytel cases

- 55.6 Governance within DETI was a topic of some considerable interest and activity during the years 2009-2016. Changes and intended improvements were introduced within the Department to the systems of risk management and governance reporting and, for a time, Internal Audit focused on improvements in project management. At the same time, as discussed in chapter 4 of this Report, there was external pressure, generated in particular by two reports produced by the Northern Ireland Audit Office (NIAO) which involved DETI: ‘The Bioscience and Technology Institute Report’, dated November 2011<sup>2979</sup> and ‘The Bytel Report’, dated March 2015.<sup>2980</sup> These reports were highly critical of aspects of DETI’s governance and approach to project management. While both reports referred to events pre-2010, they nevertheless resulted in discussions at DETI’s Audit Committee and hearings at the Public Accounts Committee in the Assembly, at least some of which occurred during the lifetime of the NI RHI scheme, albeit prior to DETI’s full awareness of its problems.
- 55.7 In respect of the Bioscience and Technology Institute (BTI), the NIAO report was published on 29 November 2011, at a time when the NI RHI scheme was being created. Amongst other things, it recorded that project monitoring and control was weak<sup>2981</sup> and its recommendations included the need for active monitoring of projects.<sup>2982</sup>
- 55.8 The Bytel project, being one which aimed to provide high-speed broadband connectivity linking Belfast, Craigavon, Armagh, Dundalk and Dublin,<sup>2983</sup> gave rise to a co-ordinated examination between the NIAO and the Office of the Irish Comptroller and Auditor General which was published in a report on 3 March 2015. This was at a time at which significant problems with the non-domestic RHI scheme were first beginning to be appreciated within DETI.<sup>2984</sup> That report highlighted DETI’s failure to deal effectively with information from a ‘whistle-blower’; a failure to keep proper notes and records; and a failure to employ relevant project management.<sup>2985</sup> A PAC hearing on 18 March 2015, attended by Dr McCormick and Mr Sterling, considered the NIAO’s report on Bytel and committee members were particularly critical of DETI.<sup>2986</sup>
- 55.9 Subsequently, on 1 July 2015, the PAC issued its report in respect of Bytel,<sup>2987</sup> the executive summary of which stated that warning signs were “effectively ignored” by the Department which “behaved as if nothing was wrong” and left “the impression that DETI hoped that silence and inaction would make these issues disappear.”<sup>2988</sup> The report also recorded that:
- “The Committee is very concerned that poor project management and disregard for value for money appear to have been endemic within the Department at that time.”<sup>2989</sup>

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2979 INQ-05023 to INQ-05113

2980 INQ-90001 to INQ-90107

2981 INQ-05035

2982 INQ-05038

2983 INQ-90010

2984 INQ-90066 to INQ-90107

2985 INQ-90098 to INQ-90099

2986 INQ-90139 to INQ-90180

2987 INQ-90108 to INQ-90226

2988 INQ-90113

2989 INQ-90113

- 55.10 The fact that DETI had “provided unsubstantiated assurances over many years” was noted, and the report emphasised that “Important as systems and processes are, it is vital that these work in practice.”<sup>2990</sup>
- 55.11 These factors formed part of the context to the evidence this Inquiry heard on the question of governance. The Inquiry was particularly concerned to probe whether there were systemic problems with governance within DETI which contributed to, or failed adequately to identify or mitigate, the difficulties with the RHI scheme that are addressed in detail elsewhere within this Report.

### Five particular aspects of the DETI governance system

- 55.12 The Inquiry focused on five particular aspects of DETI’s governance systems: the forward looking Operating Plan (sometimes referred to as the business plan) and the linked divisional and branch plans; assurance statements; risk management; Internal Audit (particularly important, as its role was to ensure that DETI’s governance was in order); and the arrangements for ensuring quality of advice to the Minister. Each is discussed below.

#### DETI’s operating, divisional and branch plans and the planning process

- 55.13 DETI’s Operating Plan was derived from its longer-term Corporate Plan, which in turn was informed by the relevant Programme for Government of the Northern Ireland Executive. The DETI Operating Plan was produced annually and gave rise to further specific plans for each of DETI’s divisions – the ‘divisional plans’. Mr Sterling told the Inquiry that the Operating Plan included the 13 commitments which fell to DETI from the 2011-15 Programme for Government, three of which were shared with other Departments. The Operating Plan also set out the objectives for each business area of the Department.<sup>2991</sup>
- 55.14 As Mr Thomson stated, “the DETI operating plan would have been a combination of ‘top down’ objectives – key priorities of the Executive and minister and ‘bottom up’ – key objectives being identified by Heads of Divisions.”<sup>2992</sup> He explained that DETI’s Operating Plan “was the key driver of performance”; that “Heads of Division were required to formally report progress against each of the targets contained in the DETI Operating Plan on a quarterly basis”; and that, in terms of his own managerial practice, “I met with my respective heads of division at the reporting stage to review quarterly performance.”<sup>2993</sup>
- 55.15 References to RHI in the DETI Operating Plan, it turns out, were few in number and at a very general level. For example, in the 2011-12 Operating Plan there were 97 specific targets, with one relating to RHI that read: “By 31 March 2012, have in place all necessary arrangements to facilitate the operation of a Renewable Heat Incentive in Northern Ireland.”<sup>2994</sup> The 2012-13 Operating Plan again contained just one reference to RHI: “By 31 March 2013, have progressed all necessary arrangements for introduction of Phase II of the Renewable Heat Incentive in Northern Ireland.”<sup>2995</sup> In both years, the RHI-related target was one of more than twenty set for the Energy Division as a whole.

2990 INQ-90113 to INQ-90114

2991 TRA-06064

2992 WIT-13518

2993 WIT-13516 to WIT-13518

2994 DFE-386409

2995 DFE-386439

- 55.16 Some further detail about RHI was set out in the divisional plans relating to Energy Division. These divisional plans contained specific tasks which were assigned to the relevant branches within Energy Division, and the officials responsible for their respective completion. An example considered by the Inquiry was such a plan for 2011-12 (as at September 2011), where the Energy Division Renewable Heat Branch was listed, on one page, as having six tasks related to the NI RHI scheme including developing, clearing and consulting on the policy.<sup>2996</sup>
- 55.17 The following year, the format of the Energy Division’s divisional plan was changed to include a column on ‘Risks’, so that any issues which jeopardised the achievement of ‘key actions’ and ‘performance targets’ could be recorded. In that year, 2012-13, the Renewable Heat Branch (as at June 2012), was listed as having three ‘key actions’ related to RHI on one page of the plan: “Launch of Phase 1 of Renewable Heat Incentive”; “Development (with Ofgem) of systems to manage the administration of the RHI”; and “Development of RHI Phase 2 Policy”.<sup>2997</sup> Against these actions, in the risks column, and as explained by Mr Thomson, two risks were referenced as follows: “State Aid approval required” and “Secondary legislation required.”<sup>2998</sup>
- 55.18 In the 2013-14 plan for the division (as at September 2013),<sup>2999</sup> the RHI actions focused on the setting up of RHI Phase 2<sup>3000</sup> with only limited mention of Phase 1 in the context of administration. Monitoring the NI RHI scheme was not recorded.
- 55.19 In his written evidence to the Inquiry Mr Thomson explained that:
- “At departmental level therefore, the implementation and operation of the RHI, having been launched, was considered best handled at divisional level – it wasn’t either a Programme for Government or Operating plan objective.”<sup>3001</sup>
- 55.20 The Inquiry notes that plans at both the corporate and divisional level for 2013-14<sup>3002</sup> and 2014-15<sup>3003</sup> lacked a reference to the scheduled first review of the NI RHI scheme that was to take place in 2014. Mr Sterling accepted that the need for a review would have been more likely to have been recognised and acted upon:
- “If it was in the operating plan for 14/15 or, indeed, to have been flagged up earlier in the previous year, 13/14. And even if those charged with doing the review had concluded for whatever reason that they weren’t going to do it to the same timescale, the fact of it being included in our operating plan would’ve meant there would’ve been a challenge to why it wasn’t happening in line with the expected timescale.”<sup>3004</sup>
- 55.21 There was a third level of plan, at branch level, but branch plans were not in universal use. When he joined as the head of the Energy Efficiency Branch in the summer of 2014, Mr Wightman created and started using a plan specifically for his branch (the Energy Efficiency Branch plan, referred to earlier in this Report). He did not believe there had been such a plan at branch level since 2009. Mr Wightman explained to the Inquiry that branch-level plans were

2996 DFE-363984 to DFE-364017 at DFE-363993

2997 DFE-367854 to DFE-367893 at DFE-367870

2998 WIT-13516 to WIT-13517; DFE-367870

2999 DFE-374215 to DFE-374254

3000 DFE-374234 to DFE-374235

3001 WIT-13516 to WIT-13517

3002 DFE-386482 to DFE-386483; DFE-374234 to DFE-374235

3003 DFE-386537; DFE-377503 to DFE-377504

3004 TRA-06825

not a necessity, with branch teams often relying on the divisional level process. He, however, had been used to a branch level plan in his previous roles: “I found it good practice; I’ve always had branch plans.”<sup>3005</sup>

55.22 The Inquiry considered iterations of this Energy Efficiency Branch plan for 2014-15 and 2015-16, which were more detailed documents. In the early versions of the plan in the summer of 2014, Mr Wightman included actions brought across from the handover note left by Mr Hutchinson. As set out in Chapter 50, there was a reference to a possible “review of the biomass tariffs of under 100kW” and “consideration of tiered tariffs to prevent excessive payments”.<sup>3006</sup> In the event, no such actions took place in the summer or autumn of 2014. There was also an action for the team to speak to Mr Hutchinson, by now having left DETI and in his new role, to check their understanding about what was meant by the need to “consider tiered tariffs.”<sup>3007</sup> As noted earlier, while a meeting with Mr Hutchinson did happen, it focused on the domestic scheme; this particular action on tiered tariffs remained unaddressed until the middle of 2015.

55.23 In summary, the planned review of the NI RHI scheme was not included on the Department’s Operating Plan or the relevant divisional plan; and whilst a more limited review was included on the relevant branch plan, it was not translated into action within an appropriate timescale.

#### Assurance statements on the system of internal control

55.24 Assurance statements, completed on a six-monthly basis, were another component of DETI’s department-wide governance system. Mr Thomson referred to this process as “a very important aspect of the governance arrangements.”<sup>3008</sup> He explained that the Permanent Secretary commissioned these statements from branches across the Department and, once completed (and after they had moved up through the divisions and been reviewed and signed off by the Deputy Secretary, who also provided his own accompanying statement), they were returned to the Permanent Secretary as well as being sent to Finance Division and to DETI’s Audit Committee.<sup>3009</sup>

55.25 The process involved completion of a template and a signature to affirm that “appropriate internal controls were in place and risks identified” across ten management procedures, including business planning, business cases, monitoring of expenditure and third-party organisations. The purpose was to seek confirmation twice a year that the required governance arrangements were in place and being used. There was also a section inviting comment on ‘other issues.’<sup>3010</sup>

55.26 The front cover of each assurance statement described the purpose of the system. For example, in the autumn of 2012, the front cover of an assurance statement signed by Mr Thomson stated:

“The system of internal control is based on an ongoing process designed to identify and prioritise the risks to the achievement of my Group’s policies, aims and objectives, to evaluate the likelihood of those risks being realised and the

3005 TRA-06921

3006 DFE-419562

3007 DFE-419562

3008 WIT-13519

3009 WIT-13519 to WIT-13520

3010 WIT-13519 to WIT-13520

impact should they be realised, and to manage them efficiently, effectively and economically.”<sup>3011</sup>

55.27 However, in his oral evidence to the Inquiry Mr Thomson further said of the assurance statements that:

“It became a very laborious system. I still think it was very good to ask heads of divisions to personally sign a statement to say that these things were all being done but...it has become too cumbersome and there is so much documentation that you don’t get the critical things out. But certainly some of the key things in the RHI were not flagged – being flagged to me.”<sup>3012</sup>

55.28 Yet the assurance statement system was not simply a matter of completing the template every six months because, as Mr Thomson also explained in his first witness statement to the Inquiry, the process involved conversations between senior managers:

“I discussed the individual statements with the respective divisional heads to receive assurance that internal controls were in place, that everything was operating as expected and to identify any particular issues of concern. On the basis of these discussions I made my own statement to the Permanent Secretary to confirm the efficacy of the systems of internal control in my areas of responsibility and, where appropriate, draw the attention of the Permanent Secretary to any significant internal control issues.”<sup>3013</sup>

55.29 The assurance statements and the discussions that surrounded their completion could have been a mechanism to identify, for example, that DFP’s approval of the RHI scheme was time-limited in the section of the statement (section 2.2) that invited an affirmation that all expenditure had DFP approval.<sup>3014</sup> It could also have been a mechanism to cause questions to be asked about the adequacy of the sponsorship arrangements of Ofgem as operated by the Renewable Heat Branch in the section (section 7.4) requiring assurance on the adequacy of monitoring systems over external delivery organisations that distributed money on behalf of the Department.<sup>3015</sup>

55.30 In May 2014, Mr Thomson signed off an assurance statement giving the Renewable Heat Branch a clean bill of health for the six month period up to the end of March 2014.<sup>3016</sup> However, the assurance document that had been provided to him did not contain any reference to CEPA’s warning in 2013 that Northern Ireland was unlikely to meet its target of 10% of heat from renewable sources by 2020, any reference to the need for a review of the non-domestic RHI scheme, any reference to the introduction of cost controls having been decoupled from development of the domestic scheme, nor any reference to the risks of significant staff turnover having occurred or about to happen at that time. It seems that none of these matters had been raised by Renewable Heat Branch or Energy Division in their contribution to the document; nor had they come to Mr Thomson’s attention through any other route, be it his own questioning or what was volunteered in management conversations.

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3011 DFE-265835 to DFE-265837

3012 TRA-05781

3013 WIT-13520

3014 DFE-265844

3015 DFE-265860

3016 DFE-179862 to DFE-179865

- 55.31 The assurance statement for the six months up to the end of September 2014, when invited to affirm that all DFP approvals for expenditure were in place, recorded ‘yes’ and the accompanying ‘comments’ box stated, “Approvals already in place for RHI Phase 1.” No reference was made to the fact that the non-domestic RHI approval had less than six months left to run.<sup>3017</sup>
- 55.32 The assurance statement process could also have been a route for officials to flag up particular problems, for example in section 12.6, which provided an opportunity to raise any significant control or other matters not covered elsewhere in the six-monthly return,<sup>3018</sup> although, as discussed elsewhere in this Report, it did cause some consternation when used in this way by Mr Mills over attempts to clarify RHI funding in 2015.
- 55.33 Mr Sterling told the Inquiry that the Operating Plan, the six-monthly assurance statements and his regular dialogue with both grade 3s and with his grade 5 Heads of Division was the way he kept abreast of what was going on in the Department.<sup>3019</sup> He also told the Inquiry, however, that he endeavoured to give the message that teams should not wait for this six-monthly process to raise a problem:<sup>3020</sup>
- “I would have wanted to have a culture in place where people felt free to flag up concerns quickly so that they could be addressed before they become [sic] a bigger problem than they need to be.”<sup>3021</sup>
- 55.34 Mr Sterling accepted in his evidence to the Inquiry that there were issues that he now recognised ought to have been escalated through this system of assurance statements, but which were not. He could not satisfactorily explain why that was, other than to say it was as much about culture as about process.<sup>3022</sup>
- 55.35 The Inquiry has considered, by way of further example, the assurance statement for the six month period ended 31 March 2015, which was signed by Mr Stewart on 29 May 2015 in response to a request from the Permanent Secretary, Dr McCormick, who emphasised that completion of the statement required due diligence. This particular statement is interesting for two reasons:
- Firstly, because of the clear and positive assurances it offered about the way things were being run within the Policy Group, including Energy Division, up to that point in 2015; and
  - Secondly, because in his cover note to this statement, Mr Stewart repeated in fairly stark terms the point raised by Mr Mills in his contribution to Mr Stewart, about the need for clarity around the RHI budget for 2015-16.
- 55.36 The positive assurances from Mr Stewart on behalf of the whole Policy Group included the answer ‘yes’ to the statement that:
- “Programmes and projects are managed in accordance with good practice including, where appropriate, Gateway Reviews, Prince 2 Methodology and guidance that issues from Central Procurement Directorate.”<sup>3023</sup>

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3017 DFE-388307  
3018 DFE-388321  
3019 TRA-06065  
3020 TRA-06149  
3021 TRA-06150  
3022 TRA-06150  
3023 DFE-277250

- 55.37 ‘Yes’ was also the assurance given to the statement that “Divisions, Branches and Units within the Group have obtained necessary DFP approvals for expenditure (where appropriate).”<sup>3024</sup> A further ‘yes’ was recorded against “Divisions, Units and Branches within the group that distribute money via External Delivery Organisations (EDOs) / Third Party Organisations (TPOs) have adequate monitoring systems in place.”<sup>3025</sup>
- 55.38 There was no reference to the lack of project management in respect of the RHI scheme and no reference to the fact that the DFP approval for expenditure on the non-domestic RHI scheme had lapsed on 31 March 2015 and not been renewed (although this had not at that time been realised by those in Energy Division). In addition, an assurance was given that implied confidence in the adequacy of the monitoring of Ofgem. The assurance statement also asserted that authority, responsibility and accountability within the Group were clearly defined and that staff were made fully aware of their job responsibilities.<sup>3026</sup>
- 55.39 Yet under a heading ‘Significant Internal Control Problems’, Mr Stewart in his cover note to the assurance statement wrote:
- “Despite repeated requests for information from Finance Division (and DFP) the Division has yet to receive any clarity around the maximum available RHI budget going forward. ...Without this clarification both schemes may need to be closed to prevent overspends.”<sup>3027</sup>
- 55.40 By contrast, in the aggregated governance statement for the Department as a whole for the year to 31 March 2015, signed by the Permanent Secretary on 24 June 2015, the non-domestic RHI scheme was described under a heading “other governance issues” as “a UK-wide scheme” and, rather than any suggestion of closure, the report stated simply that “The Department is currently working to address governance and financial requirement issues arising with the scheme.”<sup>3028</sup>
- 55.41 As previously acknowledged by the Inquiry, at this point it appears that this carefully guarded reference in the annual governance statement, to be included in DETI’s Annual Report, was motivated by a concern amongst relevant officials that a clearer statement of the problem could create an unwanted spike in applications. In his written statement of evidence Mr Cooper explained that the paragraph had been developed by himself, Mr Rooney and other departmental colleagues, including Dr McCormick, with a key factor being the tension between the details that could be provided and the potential for the market to react in such a manner, with an unwarranted spike in applications, as to aggravate the problem.<sup>3029</sup> The Inquiry has already discussed elsewhere in the Report how, in reality, extensive information had already been, or was to be, passed on to market participants by more junior Energy Division officials.
- 55.42 In any event, by 24 June 2015 it was known by senior management that approval for the scheme had lapsed and that the intended review had not taken place.<sup>3030</sup> In his oral evidence to the Inquiry, Dr McCormick accepted that he did not test sufficiently whether the system of assurance statements (and the operation of Internal Audit, considered later in this chapter)

3024 DFE-277245

3025 DFE-277253

3026 DFE-277251

3027 DFE-277239

3028 DFE-394651 to DFE-394660 at DFE-394660

3029 WIT-19060 to WIT-19061; DFE-146867 to DFE-146870

3030 DFE-279565 to DFE-279570

which on their face were good processes, were actually working, but rather “assumed a bit much” that these were indeed robust processes on the basis of his expectation that lessons had been learned from previous difficulties.<sup>3031</sup> He later observed, principally in relation to the system of risk management, but also more generally – and correctly in the Inquiry’s view – that it is “not enough to have a system; you have to continually apply it. It’s the continuous present application of stress-testing” which is required.<sup>3032</sup>

### Risk management

- 55.43 In terms of risk management within DETI, risks could be raised by officials with senior managers either when reporting on progress against targets contained in the Operating Plan or when completing six-monthly assurance statements, or both. Indeed, Mr Thomson explained that the six-monthly assurance statements were an important source document for keeping the departmental risk register up to date.<sup>3033</sup>
- 55.44 In addition, there was an exercise within the Department, initially on a quarterly basis but becoming half-yearly in 2011, to gather ‘key divisional risks’ and to update risk registers held at both divisional and at departmental (corporate) level. Mr Thomson explained that “those [risks] which were considered as having a high or medium impact or a high likelihood of occurrence were reported to the Departmental Board.”<sup>3034</sup>
- 55.45 Risk registers existed within DETI at a number of levels in the organisation: there was a single corporate risk register (which would have been the one used at the Departmental Board), divisional risk registers and branch risk registers. Also, there were risk registers for individual projects and, as noted elsewhere in this Report, an initial risk register for the RHI scheme was created in 2012 but never updated and the risks it articulated were never translated into any of the mainstream risk registers in the Department. In his evidence, Dr McCormick described “having a risk register that is kept alive and is observed and checked” as one of the “obvious things” that should have been in place.<sup>3035</sup>
- 55.46 As to why the risks of the RHI scheme were not flagged during his time at DETI, Mr Sterling said:
- “... I can’t explain satisfactorily why the risks that were inherent in this project weren’t managed and monitored more frequently and, indeed, escalated to the divisional risk register and, in due course, to the corporate risk register.”<sup>3036</sup>
- 55.47 The Energy Division risk register of autumn 2013, for example, could have been a place to identify some of the key risks of the scheme. However, the nearest reference in it to the risk of something going wrong in respect of RHI was “Failure to develop a coherent heat policy for NI.”<sup>3037</sup> Mr Sterling accepted that there should have been more specific recording of RHI risks on the Energy Division risk register: “Given the novelty of the scheme and the fact that it was an incentive based scheme, there should have been a risk on the divisional risk register...”.<sup>3038</sup> He also accepted that the process did not work on this occasion and that it

3031 TRA-12046 to TRA-12050; TRA-12057

3032 TRA-12058 to TRA-12059

3033 WIT-13520

3034 WIT-13519

3035 TRA-12058

3036 TRA-06146

3037 DFE-399110

3038 TRA-06805

did not do what was intended, although his view was that this was less to do with the design of the risk system and tended more towards those whose responsibility it was to identify and escalate the risk.<sup>3039</sup>

- 55.48 Referring to the escalation of risks within the Department, Mr Sterling told the Inquiry that “no particular risks were flagged to me in regard to the RHI during the period from when it was set up until I left in 2014.”<sup>3040</sup> He said that risk was taken seriously in the Department during his time as Permanent Secretary.<sup>3041</sup> Referring to minutes of Departmental Board meetings between 2012 and 2014 he told the Inquiry that, at “pretty much every meeting there was a discussion about risk and ... new corporate risks were brought forward. As we saw the risks being managed, they then were relegated down to departmental risks again.”<sup>3042</sup>
- 55.49 As it happens, Ms Hepper attended the Departmental Board on 25 April 2012. This was part of a routine arrangement whereby heads of division were invited on occasions to the Board. Mr Sterling told the Inquiry he thought that such attendances by heads of division were “a good control...a good opportunity for the board to challenge heads of division over the extent to which they were managing risk and their assessment of risk in their particular area.”<sup>3043</sup>
- 55.50 Ms Hepper presented a paper to the Board with an overview of Energy Division risks rated as either high impact/high likelihood or medium impact/high likelihood at quarter end 31 March 2012.<sup>3044</sup> The RHI scheme was referenced briefly in her paper in the context of a concern about possible future failure to meet the target of 10% renewable heat by 2020. The paper stated: “high take up of the Renewable Heat Incentive will be needed to help attain the target – and at this early stage this is an unknown.”<sup>3045</sup> Of course, at that time, the RHI scheme was still in development and had not been launched. The practice of inviting divisional heads to attend the departmental board in order to explore and discuss divisional risks seems a laudable one. That said, it was not intended to be, nor could it have been, a replacement for the other risk reporting mechanisms discussed above.
- 55.51 By way of an example, any one of these reporting mechanisms – the Operating Plan, the six-monthly assurance statement process or the divisional and corporate risk register system – could have been a channel in 2013 to flag up CEPA’s assessment at that time that the Department was unlikely to meet the 2011-15 Programme for Government target of 10% renewable heat by 2020. Mr Sterling told the Inquiry that he could not recall being specifically alerted to the CEPA assessment. The Programme for Government progress reports submitted by DETI in late 2013 and early 2014 also did not reflect the concerns raised by CEPA, notwithstanding the fact (which the Inquiry notes) that meeting the 10% target had been at the core of the original justification for the NI RHI scheme.<sup>3046</sup>
- 55.52 Mr Sterling was asked in oral evidence whether, in so far as things did go wrong with the RHI scheme in its early stages, it was because the Department’s systems and procedures were deficient or because the systems were good systems but were not used or applied properly, or

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3039 TRA-06146

3040 TRA-06107 to TRA-06108

3041 TRA-06145

3042 TRA-06145

3043 TRA-06146

3044 DFE-181165 to DFE-181168

3045 DFE-181166

3046 TRA-06103 to TRA-06104; DFE-417681; DFE-417690 to DFE-417691

whether it was a mix of both. Mr Sterling replied, “I think my analysis would be it was probably a mix of both.”<sup>3047</sup>

55.53 Mr Stewart was also asked about a range of issues with the RHI scheme that did not come to his attention through these systems. He said:

“...I think all of the permanent secretaries and all of the deputy secretaries who have given evidence to you have stressed that our role is of [sic] designers and overseers of systems rather than day-to-day managers. The corollary of that is, where the system isn’t good enough, then that’s a responsibility that I have to accept. Yes, I might’ve have been alerted to look at that [referring to data sharing issues and the absence of a joint DETI/OFGEM project board] by people escalating unresolved issues to me, and, if that didn’t happen, then, yes, that’s a mistake, and it’s something that should’ve happened. Equally, I have to accept, and the Audit Office has made this criticism, that I could’ve been proactive and could’ve been more curious and could’ve looked systematically across policy group to see whether we had the correct systems in place and were correctly being operated [sic] and I didn’t do so.”<sup>3048</sup>

## Internal Audit

### Internal Audit and the RHI 2011-14

55.54 As mentioned above, systems of internal control in Northern Ireland’s Government are intended to pick up problems early and to assure senior managers and the Permanent Secretary that activity is being managed in the Department according to the agreed rules and practices. Yet such systems can themselves contain weaknesses, either by design or in the way they are used. A Department’s Internal Audit function exists primarily to help overcome these weaknesses.

55.55 DETI had a small Internal Audit team that ranged across the Department undertaking work against an audit strategy and an annual plan, both agreed with the Permanent Secretary and with DETI’s Audit Committee. The first detailed Internal Audit report into the non-domestic NI RHI scheme was completed in May 2016.<sup>3049</sup> This was almost five years after Ms Hepper first informed Internal Audit in August 2011 about the NI RHI scheme as part of a wider discussion on the work of Energy Division’s teams.<sup>3050</sup> The Inquiry sought to understand why this important part of DETI’s governance system did not focus on RHI sooner, particularly given the novel nature of the scheme.

55.56 Michael Woods, head of Internal Audit in DETI from August 2014 (DFE from May 2016), gave the Inquiry his definition of Internal Audit, quoting directly from ‘Public Sector Internal Audit Standards’, a publication issued by a number of public sector audit standard-setters in the UK (including DoF in Northern Ireland) in collaboration with the Chartered Institute of Internal Auditors:

“Internal auditing is an independent, objective assurance and consulting activity designed to add value and improve an organisation’s operations. It helps an organisation accomplish its objectives by bringing a systematic, disciplined

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3047 TRA-06105

3048 TRA-11565

3049 DFE-138104 to DFE-138148

3050 WIT-19438 to WIT-19439

approach to evaluate and improve the effectiveness of risk management, control and governance processes.”<sup>3051</sup>

- 55.57 He explained that, in practice, there were two approaches used by Internal Audit: a ‘systems audit review’ to look at the controls and operational environment in any given area to see that they are effective; and an ‘investigation’, which would start with an allegation or proposition where the aim would be to see if it is true or not.<sup>3052</sup> Ms Dolan, Mr Woods’ predecessor, who served as head of DETI Internal Audit between June 2010 and August 2014, also referred to the provision of ‘advice and guidance’ and to the ability of Internal Audit to undertake consultancy services at the request of management.<sup>3053</sup>
- 55.58 As well as delivering reports on specific issues or on business areas of the Department, the further significance of Internal Audit’s work within DETI lay in its responsibility to provide an ‘opinion’ at the end of the financial reporting year on the effectiveness and overall adequacy of the systems of governance, risk management and control. Ms Dolan explained that this ‘opinion’ was independent and objective: “...in support of the accounting officer’s ability to sign off the annual statement on internal control or, it subsequently became, the governance statement.”<sup>3054</sup> These statements appeared in the published annual accounts of DETI and thus formed part of the Department’s overall accountability to the Northern Ireland Assembly and to the public.
- 55.59 Both Mr Woods and Ms Dolan emphasised three core features of the status of their role within the Department: their independence; the fact that they reported to and worked closely with the Permanent Secretary and an independent chair of the Department’s Audit Committee (‘DAC’); and their ease of access to the Accounting Officer, i.e. the Permanent Secretary, to discuss the Internal Audit plan and raise any issues. Neither witness encountered any difficulties with the status of Internal Audit during their time in post.<sup>3055</sup>
- 55.60 Mr Thomson, referring in a statement to his time as head of Policy Group in DETI up to the summer of 2014, told the Inquiry:
- “Each year, Internal Audit would spend some time reviewing governance arrangements throughout the department, ensuring proper systems were in place to facilitate reporting and the provision of assurances. I do not recall any significant concerns arising from these which would have called into question the reporting and assurance processes.”<sup>3056</sup>
- 55.61 Ms Dolan explained that towards the start of her tenure she considered DETI to be “risk mature”,<sup>3057</sup> meaning that she understood risk management to be embedded throughout the Department. This assessment was made in 2011 when Ms Dolan was developing the Audit Strategy for DETI for 2011-12 to 2014-15 and is set out on page 4 of the DETI Audit Strategy,<sup>3058</sup> which was presented to the Departmental Audit Committee in October 2011.

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3051 WIT-23123 to WIT-23162

3052 TRA-15981 to TRA-15982

3053 TRA-08697

3054 TRA-08697

3055 TRA-16028; TRA-15986 to TRA-15988; WIT-19416 to WIT-19417; WIT-19420

3056 WIT-13520

3057 TRA-08711 to TRA-08712

3058 DFE-260838

55.62 In written representations to the Inquiry, Ms Dolan emphasised that the Government Internal Audit Standards applicable at the time required the Audit Strategy to take into account the risk maturity of the organisation. The Strategy was based on management’s assessment of risk. In practice, this meant that Ms Dolan relied on each business area accurately completing risk registers and escalating risk; and where that was not done she expected management to convey risks to her and the Internal Audit team outside the formal risk management and assurance reporting processes.<sup>3059</sup> The Audit Strategy was also approved by the Permanent Secretary as Accounting Officer and endorsed by the Audit Committee.

55.63 On being questioned as to how Internal Audit could know about a set of risks if, for example, a project risk register had not been updated after its initial creation (as was effectively the case for RHI), Ms Dolan told the Inquiry:

“In terms of knowing that there was a risk in a particular project that hadn’t made its way onto the risk register, we would only know that when we would go in and do an audit of that business area and, potentially, we would identify that risk.”<sup>3060</sup>

55.64 In practice, although there were several occasions up to the summer of 2014 when the Internal Audit team and process touched on the RHI scheme, the first reference to the RHI scheme in an annual statement was in DETI’s resource accounts for 2014-15, published on 3 July 2015,<sup>3061</sup> by which time the governance statement included a reference to the fact that the Department was “currently working to address governance and financial requirement issues arising with the scheme” (a reference considered earlier in this chapter, and earlier in this Report).<sup>3062</sup>

55.65 No systems audit of Renewable Heat Branch business and no divisional review of the energy policy area took place during Ms Dolan’s tenure as head of Internal Audit.

55.66 The likelihood of a systems audit happening was reduced by the method used at the time to select audit topics. Ms Dolan told the Inquiry that, with the agreement of the Permanent Secretary and the Chair of the Departmental Audit Committee, Internal Audit prioritised ‘thematic reviews’ to test the degree to which project management and risk management were being applied across the Department. This focus was influenced by a desire on the part of both Ms Dolan and the Permanent Secretary to improve the way projects and risks were managed in the Department:

“I think the previous plans in the Department would’ve been very much branch-by-branch reviews, where I adopted a more thematic approach. So, I tried to do more horizontal reviews to give the accounting officer an assurance over a particular risk across the organisation rather than doing a number of individual branch, deep-dive reviews. So, that was different.”<sup>3063</sup>

55.67 Thematic reviews of project management were conducted for three successive years, and in the third such review, 2013-14, even though the RHI scheme was included in the field work in January/February 2014, no problems were picked up. Ms Dolan in her oral evidence agreed that, although a focus of this work was on payments, the absence of formal project management structures for the NI RHI scheme should have been picked up by this review and

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3059 TRA-08718

3060 TRA-08717

3061 DFE-04640 to DFE-04745

3062 DFE-04691

3063 TRA-08719

the reason this did not happen was most likely because the auditor at the time took the view “that Ofgem were responsible for monitoring and the programme management arrangements weren’t considered any further”; in effect, that Ofgem were managing the project and had it covered. No professional scepticism was applied to pursue the issue any further.<sup>3064</sup>

- 55.68 As mentioned earlier, when meeting Ms Dolan in August 2011 about Energy Division branches in general, Ms Hepper had mentioned the nascent RHI scheme. A follow-up meeting took place shortly afterwards between an Internal Audit team member and Mr Hutchinson, and a similar meeting subsequently took place between an Internal Audit team member and both Ms McCutcheon and Mr Hutchinson where a number of topics were discussed, including the administrative agreement and operating and development costs for Ofgem.<sup>3065</sup>
- 55.69 In November/December 2012, Renewable Heat Branch officials were back in touch with Internal Audit to seek advice and guidance on the issue of audit access to Ofgem’s delivery of the scheme. Ms Dolan told the Inquiry that their “starting point was full audit access should be built into the agreement” but “it soon became apparent, I think, that full audit access was not an option and that, therefore, a workaround was required.”<sup>3066</sup> She explained that if DETI’s own Internal Audit could not provide assurance then Ofgem’s Internal Audit would have to do so, but DETI should be able to feed into the scope of Ofgem’s audit reviews and see the outcomes of those reviews and take any follow-up action necessary.<sup>3067</sup>
- 55.70 Although she commented on the draft of the Arrangements between DETI and Ofgem as far as it related to audit, Ms Dolan told the Inquiry that she never saw the final version that contained some textual amendments put forward by Ofgem to the original DETI draft dealing with the audit activity undertaken by Deloitte/AEA for Ofgem, including the removal of the word “consult” with DETI and substitution of the word “communicate”.<sup>3068</sup> More significantly, she also said that she was not aware that DETI was never subsequently asked by Ofgem to contribute to the terms of reference of any audit review of Ofgem’s administration of RHI, nor was it shown the outcomes of any such reviews, let alone the reports. Asked if this left a gap in the audit coverage of Ofgem Ms Dolan said: “Yes. It left a gap in the monitoring arrangements by the business area in the Department.”<sup>3069</sup>
- 55.71 In the DETI Audit Strategy agreed by the Permanent Secretary and the Departmental Audit Committee, Ms Dolan had highlighted a number of risk factors that would be considered in audit planning for the period 2011-14. One of those was the use of external delivery organisations (known as ‘EDOs’) to deliver part of DETI’s business.<sup>3070</sup> The strategy stated:

“The use of EDOs poses a risk to the Department that funds may not be used for the purposes intended and therefore it is fundamental that adequate oversight arrangements are in place including the monitoring of governance and accountability of EDOs. As a result, Internal Audit coverage of sponsor control arrangements and governance and controls reviews of EDOs are built into the DETI (and other) strategies annually.”<sup>3071</sup>

3064 TRA-08776; TRA-08779; TRA-08782

3065 WIT-19438 to WIT-19440

3066 TRA-08747

3067 TRA-08749

3068 TRA-08752 to TRA-08753

3069 TRA-08756

3070 DFE-260833 to DFE-260884

3071 DFE-260845

- 55.72 Ms Dolan explained that, in using an EDO, a Department “relinquishes part of the control that it has around funds” and the reasons such inspections of EDOs had been introduced went back to issues raised by the NIAO in 2003.<sup>3072</sup> An EDO inspection had two parts: first, there would be an audit of the EDO itself and the arrangements between DETI and the EDO; and, second, audit of the oversight arrangements within DETI, referred to as the ‘sponsor control arrangements’.<sup>3073</sup>
- 55.73 Ofgem was initially classified as an EDO. Accordingly, its administration of the RHI scheme and the sponsor arrangements within Renewable Heat Branch were candidates for an audit in the 2013-14 audit plan, but the Inquiry heard that no such audit took place during the life of the scheme. Ms Dolan explained that, initially, the audit was deferred to 2014-15 for several reasons, including that the scheme had only recently commenced and, mindful that audit work on EDOs was to be sub-contracted, given that only one EDO (Ofgem) had been put forward, there was a case for deferral on the grounds there would be more work to tender in the following year.<sup>3074</sup>
- 55.74 Ms Dolan also told the Inquiry that she thought at the time that the audit approach might not be suitable for Ofgem as a non-ministerial Government Department and that she was aware of discussions about using a different audit approach in circumstances where public sector bodies took on delivery of DETI’s policies. In this alternative approach the Accounting Officer of that delivery body would be asked to sign an assurance about governance arrangements, although this was not something that was introduced while she was in post.<sup>3075</sup>
- 55.75 The Inquiry notes that there clearly was a plan of sorts by DETI to introduce this type of arrangement with Ofgem, as such an intent was noted in section 8 of the Energy Division’s ‘Checklist for 6 monthly assurance statement on internal control’ dated September 2014 and April 2015.<sup>3076</sup> Both documents stated “Annual assurance statement to be provided by Ofgem for administration of the non-domestic RHI scheme.” However, the Inquiry saw no evidence that this was followed through during the life of the scheme.
- 55.76 In her statement to the Inquiry Ms Dolan explained that in March 2014 she wrote to the Permanent Secretary requesting a meeting about the audit plan for 2014-15 and that in the email, amongst other things, she proposed cancelling the EDO review “as we have been advised by management that DETI currently has no EDOs”. On 28 May 2014, the audit plan for 2014-15 was agreed by the Departmental Audit Committee and the EDO review was cancelled.<sup>3077</sup> The minutes do not record any detail of discussion of the audit plan.<sup>3078</sup>
- 55.77 Ms Dolan could not explain to the Inquiry how the ‘carry forward’ of the review of Ofgem was lost. She told the Inquiry it was management’s responsibility to identify EDOs and she thought that the audit would have taken place in 2014-15 if Ofgem had still been considered an EDO, “but as to why Ofgem’s not identified as an EDO, I can’t answer that question.”<sup>3079</sup> The Inquiry considers this was a lost opportunity to audit Ofgem’s role administering the RHI scheme and to review the Renewable Heat Branch’s sponsorship of Ofgem.

3072 TRA-08798 to TRA-08799

3073 TRA-08799

3074 TRA-08801 to TRA-08802

3075 TRA-08801 to TRA-08804

3076 DFE-388318; DFE-388384

3077 WIT-19445

3078 DFE-394024 to DFE-394026

3079 TRA-08806 to TRA-08810

### Internal Audit and the RHI 2014-16

- 55.78 As noted above, Michael Woods succeeded Ms Dolan as DETI’s Head of Internal Audit in the summer of 2014. During his oral evidence he told the Inquiry that in respect of the RHI scheme at that point “there was no information in terms of the audit strategy, nor the audit plan, nor in the departmental risk register.”<sup>3080</sup> Unaware of the RHI at the start, but taking a look across the Department as a whole, he undertook an audit needs assessment to identify key risks. This exercise was needed anyway as the audit strategy had run its three-year course and a plan was required for 2015-16.<sup>3081</sup>
- 55.79 Mr Woods used, but did not rely on, the risk assessments that had worked their way into the corporate risk register. However, he also told the Inquiry that it can be problematic for an Internal Audit strategy to place too much reliance on risk registers that are drawn up by management.<sup>3082</sup> He therefore sought to triangulate information from the risk registers with other information from DETI Finance and from discussions with officials.<sup>3083</sup>
- 55.80 By early January 2015 Mr Woods had concluded that the RHI scheme should be subject to an audit for three reasons: it relied on an external delivery organisation; the projected size of the budget in 2015-16; and the fact that the scheme had been in place since 2012 and had yet to be subject to a systems audit.<sup>3084</sup> But he also said to the Inquiry: “I was told nothing about any problems with the scheme.”<sup>3085</sup> The audit plan, including the proposal for an audit of the non-domestic RHI scheme to commence in early 2016, was approved by Dr McCormick, the Permanent Secretary, on 21 April 2015 and by the Departmental Audit Committee at its meeting on 1 June 2015, a meeting attended by Dr McCormick, Mr Cooper and Mr Rooney.<sup>3086</sup>
- 55.81 The Inquiry asked Mr Woods whether he thought the audit of the RHI should have been done earlier. Mr Woods agreed it should have been brought forward to the summer of 2015 and that information available to others in the Department at that time, had it been conveyed to him, would have caused him to ask searching questions.<sup>3087</sup> He said that, “If the response to those questions had’ve been say, less than perfect, I probably would’ve had sufficient concern to bring the audit forward.”<sup>3088</sup>
- 55.82 In his oral evidence referring to the system of Internal Audit, Dr McCormick indicated that the Head of Internal Audit’s direct access to him was another means of assurance to him as Permanent Secretary and Accounting Officer. However, in the case of the non-domestic RHI scheme, he said that this “didn’t help because there was no transmission of a concern or risk to him [Mr Woods], so, therefore, it wasn’t picked up.”<sup>3089</sup> He went on to say that, in this regard, “Something wasn’t getting through...” and that “there’s a lot more that could have been done.”<sup>3090</sup>

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3080 TRA-15995

3081 TRA-15996

3082 TRA-15990 to TRA-15991

3083 TRA-15991 to TRA-15992

3084 TRA-16002 to TRA-16004

3085 TRA-16004

3086 DFE-390825 to DFE-390839; TRA-16010; DFE-279551 to DFE-279564

3087 TRA-16023 to TRA-16024; TRA-16035; TRA-16043

3088 TRA-16035

3089 TRA-12050

3090 TRA-12050

55.83 Mr Cooper stated in written evidence to the Inquiry that, in a senior management meeting on 29 May 2015, he had identified control issues with the scheme during an exchange of views with Mr Mills.<sup>3091</sup> Mr Woods had not been present at that meeting. As mentioned earlier, Mr Woods, Mr Cooper, Dr McCormick and Mr Rooney were, however, amongst those who attended a meeting of the Departmental Audit Committee on 1 June 2015. The minutes of that meeting do not record Mr Cooper (or anyone else) raising any issue as to control with regard to the RHI scheme.<sup>3092</sup> The only reference to RHI in the minutes referred to approvals for 2015-16 commitments and budget pressures due to high levels of forecast demand.<sup>3093</sup> Mr Woods told the Inquiry he could not recall anyone saying anything about control issues:

“...if somebody had said, ‘This is a result of lack of controls’, that’d have been totally different. I would’ve gone, ‘Well, hold on a second. There’s no point getting more budget if we don’t fix the hole in the roof’. That wasn’t what I understood and it wasn’t what I was told.”<sup>3094</sup>

He told the Inquiry that he probably would have insisted on bringing the audit forwards had he been told that the scheme lacked controls.<sup>3095</sup>

55.84 Nor does it appear that Mr Woods was informed that, on 3 June, Mr Cooper had told the Chair of the DAC, David Beck, and another independent member, Claire Hughes, about the absence of a tiered tariff as compared with the GB RHI scheme, that the scheme was over its AME budget, with potential for a 5% penalty, and his belief that demand was being driven by the poultry sector.<sup>3096</sup>

55.85 As discussed previously in this Report, on 17 June 2015, in a further RHI meeting involving senior officials, Mr Cooper mentioned overcompensation and possible breach of State Aid as issues with the RHI scheme. Mr Cooper did not convey these concerns to Mr Woods, who would not have been present at the meeting.<sup>3097</sup> According to Mr Cooper’s written evidence, he and Shane Murphy considered that the best approach could be to do a quick review of the whole scheme, including a detailed review of the tariffs payable under each technology. This idea was put forward at the meeting on 17 June 2015 by Mr Murphy, but was discounted. Mr Cooper’s view was that this was on the basis that the Permanent Secretary wanted amendments made as quickly as possible and that any changes beyond the introduction of tiering would take a long time to do.<sup>3098</sup> This suggestion for a quick review also does not appear to have been conveyed to Mr Woods nor, according to the minutes of the DAC, was it raised at its meeting of 24 June.<sup>3099</sup>

55.86 As alluded to in the previous paragraph, the DAC met for a second time in the same month on 24 June 2015 (their earlier meeting having been on 1 June). The minutes of the meeting of 24 June show that Mr Cooper was recorded as saying that financial and governance issues had emerged with the RHI scheme and that DETI was currently engaging with DFP on reapproval

3091 WIT-19055 to WIT-19056

3092 DFE-395329 to DFE-395342

3093 DFE-395336

3094 TRA-16027

3095 TRA-16028 to TRA-16034

3096 WIT-18553 to WIT-18554

3097 TRA-16024 to TRA-16038

3098 WIT-18544

3099 DFE-394720 to DFE-394725

and the budget for 2015-16.<sup>3100</sup> At the end of September, when the DAC met again, Mr Cooper updated the meeting, recording that the issue with RHI was a budget and an approval one.<sup>3101</sup> Mr Woods was present at all of these DAC meetings but, as the minutes suggest, his recollection is that none of the wider concerns that Mr Cooper has told the Inquiry he was expressing elsewhere were mentioned. Mr Cooper accepted that if Mr Woods was saying that was what occurred, and those matters were not mentioned, it was difficult for him (Mr Cooper) to contradict him.<sup>3102</sup> Mr Woods told the Inquiry that he believed such concerns should have been raised.<sup>3103</sup> When he was asked why this did not happen, Mr Woods said:

“The only thing I can think about is that people were so fixated on a solution that any information contrary...to that solution was ignored...So, the conception was it’s a budgetary problem, we’ll solve a budgetary problem. I think if we’d stepped outside the problem and said ‘Exactly why is this happening?’, then perhaps we would’ve understood it better and then, therefore, the solution could’ve been better.”<sup>3104</sup>

55.87 In one of his written statements of evidence to the Inquiry Mr Cooper stated that, following the unprecedented spike in applications to the non-domestic RHI scheme in October 2015, “the potential for abuse of the scheme came into focus.”<sup>3105</sup> He said that in mid-November he discussed the spike with Mr Woods and asked Mr Wightman to clarify the position.<sup>3106</sup> On 18 November Mr Cooper forwarded to Mr Woods an email that he had received from Mr Wightman on the previous day. That email, under the heading “Future Changes”, contained the following:

“It is worth highlighting that Michael’s team are to audit the Non Domestic RHI Scheme in the New Year which provides an opportunity to review Ofgem’s current system of checks.

We also hope to legislate to introduce an annual cap on maximum heat for existing installations although this will be very contentious and will require public consultation. This will help minimise the risk of boilers being run just to generate RHI income.”<sup>3107</sup>

55.88 At the DAC meeting on 2 December 2015 it was agreed, arising from the views expressed by Mr Woods, that although the audit of the domestic RHI had commenced, it would be halted and the audit of the non-domestic RHI would commence urgently in light of the issues that had arisen.<sup>3108</sup>

55.89 When asked whether a systems audit of the RHI could have been done much earlier, for example at the start of the scheme or even before it went live, Mr Woods agreed it was possible and was something that should have been done with the RHI scheme and had been done with some other projects or schemes. He gave the example of Internal Audit’s work on testing the adequacy of design of the ‘Gas to the West’ project, work that had included: advising for about

3100 DFE-394723

3101 DFE-394846 to DFE-394856 at DFE-394848

3102 TRA-15962

3103 TRA-16041 to TRA-16043

3104 TRA-16048

3105 WIT-18547

3106 WIT-18547

3107 WIT-18830 to WIT-18831

3108 DFE-289104 to DFE-289114

a year and a half; reviewing the letter of offer; testing the robustness of the business case; and how it was proposed to control the scheme.<sup>3109</sup>

- 55.90 In the event, the first full engagement of Internal Audit with the non-domestic RHI scheme took place in early 2016 and the audit report was completed and submitted to management in DETI on 19 May 2016.<sup>3110</sup> The report concluded that “the system of risk management, control and governance established by management over the ... Scheme is unacceptable.”<sup>3111</sup> Mr Woods described it to the Inquiry as the worst opinion he had ever had to give in over 500 systems audits.<sup>3112</sup>

### Janette O’Hagan emails and Internal Audit

- 55.91 Janette O’Hagan’s interactions with DETI have been dealt with in detail in chapter 23 of this Report, but her interventions also have some significance in the context of the role of Internal Audit, in particular a possible role for it in investigating issues such as those raised by Ms O’Hagan.
- 55.92 In relation to the email communication from Ms O’Hagan that arrived in DETI in October 2013, Ms Dolan told the Inquiry that Internal Audit and senior managers should have been made aware:

“I think some of the concerns were around misuse of the scheme and the scheme not necessarily being used for the purposes intended. And to me that’s indication that there’s an irregularity, and the DETI guidance at the time, the fraud response plan, and also the internal audit charter would’ve highlighted that any suspicions of irregularity should be reported immediately to the head of internal audit.”<sup>3113</sup>

She also considered that, whether or not officials believed the allegations, they should still have forwarded them on.<sup>3114</sup>

- 55.93 Mr Woods told the Inquiry that he first became aware of Ms O’Hagan’s emails in September 2016. He was particularly critical of the fact that these emails were not drawn to his attention during the work on the Internal Audit review in early 2016. But he also believed they should have been shown to him in 2015 when he was working on the audit plan and at the very least, given DETI’s anti-fraud policy, Internal Audit should have been consulted when the emails were received.<sup>3115</sup>

### Quality of policy advice to Ministers

- 55.94 As appears throughout this Report, the Inquiry has examined in depth the quality of advice provided to Ministers in DETI that formed the basis on which Minister Foster and subsequently Minister Bell took decisions in relation to the NI RHI scheme. The Inquiry has also examined advice used in support of other decision-making processes, such as that presented to the DETI Casework Committees and in the business cases presented to DFP for approval. In the course of that examination, shortcomings, omissions and errors in the advice have been identified and are set out in detail in previous chapters of this Report. A number are noted below:

3109 TRA-16015; see also TRA-16009 to TRA-16010

3110 WIT-23200 to WIT-23244

3111 WIT-23215

3112 TRA-16069 to TRA-16071

3113 TRA-08813

3114 TRA-08816

3115 TRA-16082 to TRA-16083; TRA-16022

- The submission to Minister Foster of 8 June 2011<sup>3116</sup> contained a potentially misleading statement regarding the NI RHI option, namely, that it offered “... the highest potential renewable heat output at the best value.”<sup>3117</sup>
- In turn, the potentially misleading assertion, first contained in the 8 June 2011 submission, that “the NI RHI produced the most heat at the best value” was repeated on a number of occasions, without the qualification that this was restricted to a comparison with the GB RHI scheme. Examples include regulatory impact assessments and SL1 letters, both of which invited a ministerial signature.
- The submission to Minister Foster of 5 July 2011 failed to highlight the very significant changes that had been made in the CEPA final report of June 2011 since the earlier draft of that report of 31 May 2011, upon which the submission of 8 June had been based.
- The submission to Minister Foster of March 2012 contained the erroneous statement that tiering of the tariff was not included in the NI RHI scheme because in each instance the subsidy rate was lower than the incremental fuel cost.
- The submission to Minister Foster of March 2012 also omitted to inform the Minister that the lifetime subsidy costs of the scheme had risen from £334 million to £445 million between CEPA’s final report of June 2011 and its Addendum of February 2012.
- Incomplete and/or inaccurate information was provided to the Casework Committee in March 2012 on the full lifetime costs of the different schemes. The evidence base for comparing the administration costs of a Challenge Fund and the NI RHI scheme was not well founded.
- A variety of ministerial submissions, although perhaps most notably the submission to Minister Bell of 8 July 2015, failed to make clear the unusual nature of the funding for the NI RHI scheme and the potential DEL consequences of overspend.
- The submission to Minister Bell of 8 July 2015 also inaccurately proposed tiering as the chief mitigation to contain the overall NI RHI budget.
- In the same 8 July 2015 submission, the earlier Phase 2 proposals and 2013 consultation were represented as constituting compliance with the 2012 DFP condition for review of the non-domestic RHI scheme. This was incorrect and misleading.
- The October 2015 Business Case Addendum contained numerous errors and omissions. In particular, there was an inadequate evidence base for the claim that the scheme represented “continuous and continuing value for money.”

55.95 Mr Sterling explained that one of his three roles as Permanent Secretary was to be the principal adviser to the departmental Minister but explained that this responsibility was discharged through a system of management within the Department:

“Although I am the Minister’s principal advisor with ultimate responsibility for all advice provided by the Department, I discharge that responsibility by ensuring that processes and internal controls are in place for officials to provide advice on my behalf. On any given issue I will seek to ensure that it is clear to the Minister that there is lead official [sic] who will be responsible for providing advice on the

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3116 WIT-00739 to WIT-00749

3117 WIT-00744

relevant issue. The lead official will normally be the head of the relevant division and almost always a member of the Senior Civil Service (SCS) ie an assistant secretary or above. The lead official will normally be supported by an appropriate team including specialist advice if this is considered necessary. It is then the role of the lead official to take responsibility for the advice provided to the Minister. This does not diminish my ultimate personal responsibility...”.<sup>3118</sup>

55.96 Dr McCormick also accepted that it was his responsibility as Permanent Secretary to ensure that the advice which went to the Minister was fair, accurate and comprehensive, although it is not and never has been a Permanent Secretary’s role to deal with the detailed technical aspects.<sup>3119</sup>

55.97 Mr Sterling, when asked about the ‘processes and internal controls’ on which he relied to ensure objective and reliable advice was given to the Minister, explained “it would largely be about people” and about the “element of supervision” provided by the official at grade 5 level “so what goes to the Minister is fit for purpose.”<sup>3120</sup> He made the general point:

“I would generally have had confidence in the teams working across the Department that they would have produced quality advice or, if there was an issue of particular concern, they would’ve known to come to me. And that was borne out of the fact that, as I say, we worked pretty closely together, we had a Minister that we knew, Minister and adviser that we knew very well. These things didn’t need, sort of, a great deal of formality to them.”<sup>3121</sup>

55.98 He described the team responsible for the NI RHI as:

“...a group of people who were competent in many ways but not specialist in their areas – well, that would be characteristic of many teams that we have, not just in what was then DETI and now DFE but across the Northern Ireland Civil Service.”<sup>3122</sup>

55.99 The team though, he acknowledged, was under pressure, had resource issues and did not have sufficient capacity or competence on the technical aspects of the scheme; that was why on several occasions they had obtained his and the Minister’s approval to use consultants (respectively AECOM/Pöyry and CEPA). Looking back, Mr Sterling observed that while the team at the time felt they were managing the consultants well, the experience of the NI RHI scheme had led him to reflect that “there is probably a case for having had that additional expertise to allow the team to properly manage the consultants.”<sup>3123</sup>

55.100 Mr Sterling cited two further processes on which he relied: the establishment in 2010 of the Analytical Support Unit, which has been referred to previously in this Report. The ASU comprised economists and statisticians, as a source of ‘specialist advice’ for those preparing submissions; and ‘an element of feedback’ from the Minister.<sup>3124</sup> He told the Inquiry “I took comfort from the fact that a departmental economist had looked at the scheme with a view to

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3118 WIT-04018 to WIT-04019

3119 TRA-12021 to TRA-12022

3120 TRA-06077 to TRA-06078

3121 TRA-06141

3122 TRA-06083

3123 TRA-06105

3124 TRA-06078

determining whether it was going to provide value for money.”<sup>3125</sup> He had noted the evidence given to the Inquiry by the economist Mr Connolly however, and said he would still like to understand why Mr Connolly had not felt able at the time to raise his concerns.<sup>3126</sup>

55.101 On the question of feedback from Minister Foster on submissions from Energy Division, Mr Sterling said “I think the view I would have got from the Minister and Special Adviser is: the advice we get is thorough, comprehensive, perhaps too long,” and although there would have been requests from time to time to make submissions a little shorter, Mr Sterling did not consider this to have been a major issue.<sup>3127</sup> He added:

“But I would just say, generally, the quality of submissions coming from energy division would have been regarded as probably the best in the Department.”<sup>3128</sup>

55.102 Mr Sterling considered that the broad system that applied in DETI would have been no different from that of all the Departments where he had previously worked and he believed the approach to providing advice to Ministers “is pretty consistent” across all Departments.<sup>3129</sup> When asked for his overall view of that system he said it was “generally sound”.<sup>3130</sup> In further representations to the Inquiry however, Mr Sterling made clear that he considered that there were shortcomings in some of the advice received by the Minister about RHI and accepted that the system failed to operate in order to prevent such shortcomings. He emphasised that, while believing the control system was generally sound, the application of the control system for ensuring that the Minister received good advice about RHI was deficient.

55.103 One aspect of the system of provision of advice to the Minister which the Inquiry noted was that ministerial submissions were routinely copied to a wide range of officials, often including the Permanent Secretary. It was not anticipated that the Permanent Secretary would read all of the submissions crossing his desk, and certainly not in any detail, other than those formally requiring the Permanent Secretary’s sign-off;<sup>3131</sup> and Mr Sterling firmly disavowed any suggestion that the authors of such submissions would have taken any reassurance from the fact that he had been copied into a submission. He said that:

“...nobody who was regularly submitting submissions to the Minister could have reasonably concluded that I was going to check their homework; that was not the purpose of me being copied in.”<sup>3132</sup>

55.104 There was a provision within the Private Office Guidance in force within DETI which suggested that some submissions did require to be ‘pre-cleared’ with the Permanent Secretary, in terms to the effect that:

“The Permanent Secretary must have been consulted on policy proposals which have major resource implications, raise Accounting Officer issues, or have Machinery of Government implications before a submission is sent to the Minister.”

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3125 TRA-06105

3126 TRA-06105 to TRA-06106

3127 TRA-06078 to TRA-06079

3128 TRA-06079

3129 TRA-06080

3130 TRA-06080

3131 TRA-06131 to TRA-06132; TRA-06135

3132 TRA-06135

55.105 Mr Sterling’s evidence was that there was no formal guidance given to civil servants as to when these thresholds would be met. Rather, the process was more informal: he would have been aware of sensitive issues through ongoing communication; and more junior civil servants within the Department “would just have known what were the issues where it would be sensible to take my mind.”<sup>3133</sup> Mr Sterling’s “general point” in this regard was that he:

“Would generally have had confidence in the teams working across the Departments that they would have produced quality advice or, if there was an issue of particular concern, they would’ve known to come to me.”<sup>3134</sup>

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3133 TRA-06140 to TRA-06141

3134 TRA-06141

## Findings

313. DETI's internal governance systems failed over four years as a conduit to deliver important information to senior management about the flaws and mounting risks of the NI RHI scheme. The systems were not fit for purpose where RHI was concerned. Responsibility for this must rest with DETI/DfE's successive Permanent Secretaries/Accounting Officers: Mr Sterling and Dr McCormick.
314. When, in the summer of 2015, mounting concerns about the scheme's finances were expressed in stark terms by Mr Mills and Mr Stewart using the assurance statement system, the governance statement signed by the Permanent Secretary and given to the Departmental Audit Committee was comparatively muted. The Inquiry recognises the concern about stimulating a spike but that should not have inhibited officials from ensuring that full and accurate facts were internally communicated, particularly to the DAC and the Head of Internal Audit.
315. To the extent that the failure of DETI's internal governance systems in respect of the non-domestic RHI scheme was caused or contributed to by reluctance on the part of officials to report potential problems to line managers, in particular where those officials were attempting to address the problems in question, the Inquiry finds that such reluctance reinforces the importance of the application of relevant principles of project and programme management to such schemes. The Inquiry finds that the proper application of such principles would have decreased the likelihood of potential problems going unreported through the formal governance and assurance systems.
316. It was unfortunate that the management information available to Ms Dolan, Head of Internal Audit, and her team, when preparing the DETI Audit Strategy, led to the assessment that DETI was a "risk mature" organisation. It meant in practice that between 2010 and 2014 the Internal Audit Service applied too little independent judgment and was overly reliant on information from individual branches and divisions in deciding what to include in its audits. Opportunities to scrutinise the RHI scheme as part of a project management audit and as part of an audit of external delivery organisations did not materialise, but the responsibility for decisions about the Audit Plan that led to these shortcomings must be shared with the Permanent Secretary.
317. The initial good intentions of the internal auditor, Ms Dolan, that 'full audit access' for DETI should be built into the Arrangements with Ofgem did not materialise and the agreement offered a lesser form of words. Unfortunately, Ms Dolan did not see the final wording of the Arrangements which were agreed between Ofgem and the relevant business area within DETI. In the event, DETI did not even gain access to any of the audit reports delivered by Ofgem's own auditors, nor was DETI consulted on the audit terms of reference. The implications of the Arrangements might have come to light had DETI's Internal Audit reviewed Renewable Heat Branch's use of Ofgem and Ofgem's management of the scheme. The deferral in 2013-14 and then the cancellation in 2014-15 of this audit was a significant missed opportunity to

highlight problems with implementation. The limited audit access to Ofgem provided for in the Arrangements was a further reason to seek to ensure an External Delivery Organisation audit of the arrangements with Ofgem. Responsibility for this missed opportunity must again be shared with the Permanent Secretary.

318. When in January 2015 the need became clear for the RHI scheme to be the subject of an internal audit, it took 12 months for the audit to commence. The audit of the non-domestic RHI scheme was scheduled for early 2016 and this plan was signed off by the Permanent Secretary in April 2015 and by the DAC in early June 2015. Once problems with the scheme's funding and approval came to light from early June 2015 however, it would have been open to the Permanent Secretary, or to the Senior Finance Director (Mr Rooney), or to the Director of Finance (Mr Cooper), and/or Mr Stewart at any point to have asked for the audit to be brought forward and, given what they each knew, this is what should have happened. The Inquiry cannot know what difference this would have made for certain, but given what was eventually revealed in the Internal Audit report of May 2016 it is at least possible that an earlier report might have led to better decision making in the autumn of 2015 or the beginning of 2016.
319. Whilst Mr Sterling told the Inquiry that the system for ensuring a good quality of advice to Ministers was generally sound, the Inquiry agrees with him that this was not the case as far as the RHI scheme was concerned. Indeed, the evidence suggests that further investigation could usefully be undertaken as to the reliability of this system in other areas. In relation to RHI, a range of factors discussed throughout this Report – including (although not limited to) lack of technical expertise, imprecise drafting, pressure of time and resources, and failure effectively to retain or pass on corporate knowledge – resulted in numerous mistakes and omissions being made in policy advice provided by officials. These were of significant importance and, having been made in ministerial submissions, were often repeated in later submissions or other documents used to transmit or explain decisions, thus compounding the errors. The Inquiry also finds that when, in 2015, problems with the scheme became apparent, the quality of advice to the then Minister was sub-optimal and aspects of it were unclear and inaccurate. In light of these matters, the Inquiry concludes that the system for ensuring the quality of such advice, such as it was in DETI/DfE, was not adequate.

