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Chairperson
Public Accounts Committee
Room 371
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23 November 2016

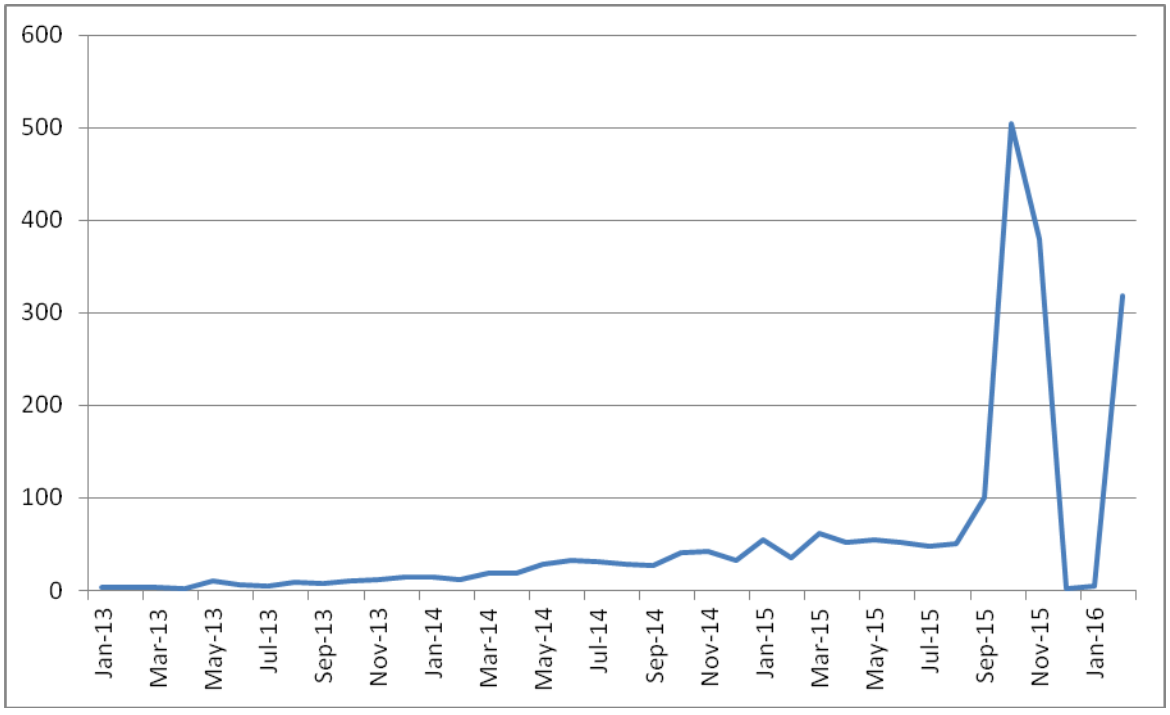
Dear Robin

Inquiry into Non-domestic Renewable Heat Incentive (RHI) Scheme

Thank you for your letter of 11 November 2016, requesting additional information in relation to the Non-domestic Renewable Heat Incentive (RHI) Scheme. The responses below have been provided in relation to each of your specific information requests.

1. An analysis of issues, including costs, which were generated following the spike in applications to the RHI Scheme.

The **graph below** provides an illustration of how monthly application numbers changed over time. **Annex A** provides a table of monthly application numbers.



Initially, the scheme grew slowly, with only 562 applications being received from the start of the scheme in November 2012, to the end of the 2014-15 financial year. From April 2015, application numbers remained steady at 50-60 per month until after the announcement on the proposed tariff changes on 8 September 2015. In that month 101 applications were received.

Almost as many applications were received during October and the first half of November 2015 as had been made in the previous 34 months. The spike in applications created three main pressures:

- increased costs once the applications had been successfully accredited;
- increased time and costs for accreditation of applications due to the increased volume; and
- increased audits required.

All applications received the same scrutiny by Ofgem since the launch of the scheme. Following the spike, the accreditation of the applications carried out by Ofgem was subject to an additional triage process to identify issues at an early stage.

To support the additional spike of applications, Ofgem and the Department signed a Change Request in February 2016, which included additional funding for staff and additional audits to be deployed in the remainder of 2015-16. Ofgem's operating costs increased from £165k in 2013/14 to £253k in 2015-16 reflecting this volume growth.

It is not possible to provide a definitive figure for the cost of the spike in applications as not all of the applications have been accredited. However, assuming the Department would have continued to receive 50 applications per month if tariff changes hadn't been announced, the estimated costs of the additional 835 applications received during September, October and November are £20.2m / year (or £405m over 20 years). This figure is based on 99kW boilers running for 43% of the time.

2. Confirmation or otherwise that it is common practice in the Department to appoint an SRO to a project/scheme and at what value is it considered that an SRO is required.

It is common practice for a Senior Responsible Owner (SRO) to be appointed to a project, programme or scheme. Examples of projects, programmes or schemes where an SRO has been appointed are the Training for Success / Apprenticeships NI re-procurement project (£258 million), the Gas to the West project (up to £32.5 million), the Northern Ireland Broadband Improvement Project (£19.6 million), the Superfast [broadband] Roll-Out Programme (£17.1 million), the Insolvency Service's IT replacement project (£1.5 million), the Essential Skills in Schools Project (£400K), the Apprenticeship and Youth Training Programme (£30 million over the next three years), the FE Means Success Programme (£20 million) and the REACH programme (£3 million over three years).

Although the Department has not set a specific value at which an SRO is required, staff are being reminded of the provisions of the Department of Finance Procurement Guidance Note (PGN) 01/09 (as amended) "Procedures and Principles of Best Practice in Programme / Project Management". This PGN defines the role of a Senior Responsible Owner (SRO) and sets out principles of good practice in project and programme management.

3. A clear explanation of what drove the spike in applications to the scheme.

The monthly application numbers indicate that the announcement of the proposed tiered tariffs on 8 September 2015 triggered the spike with an additional 985 applications received during the 10 weeks from the announcement until the tariff changes were made in November compared to the previous levels of 50 applications per month. Following the introduction of the tiered tariffs, monthly application numbers dropped to single figures until another spike was experienced prior to the scheme suspension in February 2016.

There are frequent spikes in applications to the GB RHI scheme prior to changes in tariffs through degression. However, the scale of the increase in October and November 2015 was unprecedented. As I explained at the start of the evidence session on 9 November, the Department had not recognised that the tariff structure up to November 2015 had created too generous an incentive, and hence we did not foresee that the announcement of the tariff changes would strongly incentivise all potential applicants to seek to qualify for the high tariff before it was reduced.

4. Clarification around the aspect of the level of inspections; is it 3% of applications or, as stated by OFGEM, is it the cost of inspection against the cost of the scheme.

The agreement was that the number of applications to be inspected by Ofgem in Northern Ireland was to be 3% of the number of inspections carried out in GB. Funding for administration is agreed annually between the Department and Ofgem. HM Treasury set out that overall funding for the NI scheme, based on the Barnett formula, to be around 3% of the GB scheme size. In line with this, the audit volume in Northern Ireland until 2015-16 was approximately 3% that of the audits in GB.

However, as the number of applications began to grow in Northern Ireland, it became clear that it would be necessary to review the audit rate. The Department and Ofgem agreed an increase in the number of audits in Northern Ireland in 2015-16 to reflect the increase in applications.

Based on the number of audits that could be deployed up to March 2016, this resulted in the 2015-16 audit volume in NI increasing to over 6% of the GB audit volume. A further increase was deployed in 2016-17 which will see forecast audit volumes increase to c. 25% of the GB audit volume.

5. Clarification that the OFGEM Feasibility Study specified that there was a potential risk from a tiered tariff.

The 2011 Ofgem Feasibility Study was written before decisions had been taken on the nature and form of the Northern Ireland scheme, and therefore it was not appropriate for there to have been comment or warnings in relation to tiering as that could only have come into focus at a later stage. The Study included the absence of cost controls as a possible risk factor – in the more general context of assessment of options for the Scheme, not specific application to the RHI as it took shape. Paragraph 6.9 stated: “At present there are no mechanisms in place to control costs of the scheme in the event that uptake is considerably higher than anticipated.” As I said in evidence, a tiered tariff in itself was not a cost control: it would have reduced the incentive, and removed the incentive for excessive use, but a tiered tariff would not have placed any ceiling on

applications or costs. Our records confirm that Ofgem drew attention to the risks from not having a tiered tariff in the spring of 2014. While Ofgem highlighted the absence of cost controls in the feasibility study, we do not have any evidence of any specific warning in relation to tiered tariff at any stage before 2014.

6. Figures for the payments suspended by OFGEM in light of the PWC report.

Following the PWC Report, Ofgem has temporarily suspended payments for 11 installations where there is evidence suggesting potential non-compliance with scheme regulations. Ofgem is now conducting investigations on each of these cases to determine any instances which fall short of the legal requirements for the scheme. This has led to the suspension of approximately £23k of payments to date.

7. Detail around the type of problems which arose during the random site inspections which didn't result in a penalty or action.

The Regulations set out powers to temporarily suspend payments for up to 6 months where there are reasonable grounds to suspect failure to comply with an ongoing obligation. The Regulations also allow suspension of payments for a year where there is failure to comply, and to permanently withhold payments where Ofgem is satisfied that there has been a material or repeated failure by a participant to comply with an ongoing obligation. Ofgem's site audits have identified both observations and potential non-compliances.

Observations include matters which Ofgem may highlight to participants but which do not constitute non-compliance with the regulations – for example, where the audit has identified health and safety concerns.

Potential non-compliances identified have included a number of key factors, which have prompted further investigation by Ofgem. These have been categorised as:

(i) potential discrepancies between application and situation on the ground:

- heat losses not properly accounted for
- accredited as non-single domestic but appears to be domestic
- schematic errors
- external pipework not declared
- nameplate different to that on application
- meter component installed incorrectly

(ii) potential breach of ongoing obligations:

- lack of fuel records
- wider range of fuels used than declared
- No notification of change to installation
- Wood drying to increase RHI payments

Ofgem has acted in line with the above approach in the cases identified through audits to date. Upon determining a non-compliance issue, Ofgem would consider whether it was appropriate to seek to partially or fully recover any payments made previously, in line with the powers set out in regulations and acting in line with principles of good administration.

8. Minutes of the meeting from the DETI Casework Committee that approved the Business Case and the names of the officials who sat on this committee.

Minutes of the meeting of the 9 March 2012 DETI Casework Committee that approved the initial Business Case are attached at **Annex B**.

Minutes of the meeting of the 21 October 2015 DETI Casework Committee that approved the subsequent Business Case are attached at **Annex C.**

The names of the officials who sat on the Casework Committees are contained in the minutes.

In line with established protocols, I would ask you to treat the information relating to the names and grades of DETI staff as "in confidence". It remains very important that their names are not used in public sessions or in any public comment by the Committee.

9. Copies of routine correspondence from the London Ministers to devolved administrations providing updates.

Copies of routine correspondence from London Ministers to Devolved Administrations have been provided at **Annex D**.

10. Carbon Trust Loans & EU De Minimis Regulations.

De Minimis aid is used to describe small amounts of state aid that do not require European Commission approval. The European Commission considers that public funding which complies with the de minimis regulation has a negligible impact on trade and competition, and does not require notification and approval.

The total de minimis aid which can be given to a single recipient is €200,000 (cash grant equivalent) over a 3-year fiscal period. This can be given for most purposes, including operating aid, and is not project-related.

Invest NI's Carbon Trust Loan Scheme has been in place since around 2003. It is a scheme to help businesses in Northern Ireland to invest in more energy efficient equipment through the provision of interest-free business loans. Businesses can currently borrow between £3,000 and £400,000 interest free to buy energy-saving equipment.

Any business in Northern Ireland can apply for a loan - Incorporated businesses trading for at least 12 months and non-incorporated businesses trading for at least 36 months (this will include charities, friendly societies, clubs and the like).

The scheme provides £1,000 of loan for every 1.5 tonnes CO2 saved per annum for a project. Each project is technically assessed on its potential to deliver energy savings. Carbon Trust also carry out a credit check. The loan scheme is funded by Invest NI and managed by the Carbon Trust. A Carbon Trust Loan is considered a De Minimis grant.

In 2013, Ofgem refused an RHI application because the business had previously received a 0% Carbon Trust loan towards the installation costs of a boiler. However,

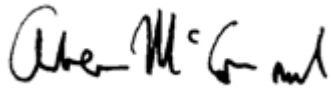
legal advice provided to the Department in December 2013 was that applicants could avail of both schemes provided the total support received (loan interest saved and RHI payments) over 3 years did not breach the EU De Minimis threshold. While RHI grant does not fall under the De Minimis Regulations, any further government funded grant regardless of its classification, would breach the De Minimis threshold applicable to the Carbon Trust Loan. However, if the facility existed for applicants to pay back the Carbon Trust Loan, applicants would not be in breach of the De Minimis threshold and could be eligible for the RHI Scheme.

Unlike the GB legislation, Northern Ireland legislation did not facilitate the payback of loans / grants. An amendment was made via the Domestic Renewable Heat Incentive Scheme (Northern Ireland) 2014 in December 2014 to enable these applicants to pay their loan back and become eligible for the RHI Scheme.

In October 2014, it was agreed that Ofgem would refer all such cases to the Department for adjudication. To date, the Department has considered 35 cases of which 32 were approved. Receipt of both schemes is compatible provided the support is within the EU De Minimis threshold.

I confirm that I will make myself available to attend further evidence sessions that may be convened by the Committee. I hope the above information is helpful.

Yours sincerely



ANDREW McCORMICK
Permanent Secretary

cc TOA

Annex A

Monthly Application Numbers

Month	Application Numbers	Total Application Numbers
Jan-13	3	3
Feb-13	3	6
Mar-13	3	9
Apr-13	2	11
May-13	10	21
Jun-13	6	27
Jul-13	5	32
Aug-13	9	41
Sep-13	8	49
Oct-13	10	59
Nov-13	11	70
Dec-13	15	85
Jan-14	14	99
Feb-14	11	110
Mar-14	18	128
Apr-14	18	146
May-14	28	174
Jun-14	33	207
Jul-14	31	238
Aug-14	28	266
Sep-14	27	293
Oct-14	41	334
Nov-14	42	376
Dec-14	33	409
Jan-15	54	463
Feb-15	35	498
Mar-15	62	560
Apr-15	52	612
May-15	55	667
Jun-15	52	719
Jul-15	48	767
Aug-15	51	818
Sep-15	101	919
Oct-15	505	1424
Nov-15	379	1803
Dec-15	2	1805
Jan-16	5	1810
Feb-16	318	2128

Annex B

Renewable Heat Incentive Scheme Case Work Committee

Friday 9th March 2012 @ 2.00pm
DETI Headquarters, Netherleigh House

Present:

Casework Committee panel:	Trevor Cooper (Chair) Philip Angus Shane Murphy
Energy Division:	Fiona Hepper Joanne McCutcheon Peter Hutchinson Susan Stewart (note taker)
Economics - Analytical Services Unit:	Sam Connolly

Documentation provided:

1. Synopsis of Renewable Heat Incentive Scheme Project
2. Assessment of the Potential Development of Renewable Heat in Northern Ireland -AECOM Pöyry
3. Full Economic Appraisal – CEPA/AEA June 2011
4. CEPA/AEA additional analysis
5. Ofgem Feasibility Study
6. Risk Register
7. State Aid application / Addendum to application
8. DFP – Strategic Outline Case & DFP response
9. Economists comments

Issues addressed

1. Background
2. Policy Context
3. Options
4. Additionality
5. Budgetary management solutions
6. Governance / Ofgem management arrangements
7. Funding issues arising from Ofgem and internal resources
8. State Aid
9. Risk management
10. Conclusion and Agreed Actions

1. Background

TC asked for a brief overview of the proposed project.

FH advised that the work on the Renewable Heat Incentive (RHI) came as a result of the Renewable Energy Directive (RED), published in June 2009, which requires the UK to ensure that 15% of its energy consumption comes from renewable sources by 2020. In September 2010, the Northern Ireland Executive endorsed a target of 10% renewable heat in NI by 2020 (against a baseline of 1.7% in 2010). This target is included in the Strategic Energy Framework (SEF) and an interim target of 4% by 2015 is included in the Programme for Government (PfG).

FH explained that the NI RHI was largely based on the GB RHI which provides a continuous income scheme of 20 years (the lifetime of the technology) for those who generate renewable heat. The main differences between the NI and GB schemes is that the NI tariffs are set against an oil counterfactual whereas the GB tariffs have been set against a natural gas counterfactual; this results in lower tariffs being required in Northern Ireland. The reason for this is that the NI heat market is dominated by oil (over 75%) with an emerging gas market (17%), in GB gas is the market leader (70%) with oil a secondary heating source (10%).

FH also explained that the introduction of the RHI would be through a phased approach. The scheme will firstly be open to the non-domestic sector and include the most well-established renewable heating technologies. The domestic sector would then be introduced in phase 2; this phase might also include additional technologies. In the interim, domestic householders will be able to apply for *Renewable Heat Premium Payments* to assist in the capital cost of installations. Those who do avail of the RHPP will still be able to get a RHI but for a lesser period i.e. 18 years instead of the full 20 years as the RHPP represents two years of RHI payments.

FH also advised that another major component of the RHI would be the administration of the scheme. Her Majesty's Treasury (HMT) has provided DETI with funding of £25m over the next four years for the development of the renewable heat market. However HMT has advised that this funding is only to be used for the RHI itself and not the administration of the scheme. Therefore the costs of administration will have to be paid by the DETI. The Department of Energy and Climate Change (DECC) in GB has paid Ofgem (the GB energy regulator) over £5m for the development of the system, of which IT systems are a large part; it expects to pay around £10m over the next 4 years for the administration of the system. By contracting with Ofgem and utilising systems and processes already in place, DETI can expect significant savings whilst enjoying the benefits of the Ofgem administration systems.

SM clarified that the approvals being sought were for the RHI scheme, the RHPP scheme and the costs for administering these schemes. TC confirmed that it would be essential to address all the costs that arose from any policy proposal including administration consequentials.

FH added that by growing the renewable heat market there are significant opportunities for Northern Ireland to reduce our dependence on imported fossil fuels and increase NI's fuel security and diversity of supply, this in turn will reduce carbon emissions.

2. Policy Context

TC asked what would happen if the NI target of 10% renewable heat generation by 2020 was not met, given the target set under the RED. TC also asked if DECC was comfortable with the target set for NI.

FH advised that Northern Ireland, whilst not an EU Member State, is expected to contribute to the UK target of 15% renewable energy by 2020. To support this target, DETI has set targets of 40% renewable electricity and 10% renewable heat by 2020. If the UK as a whole fails to achieve its target of 15%, then it would be expected that the EU Commission would impose infraction fines at Member State level. It would then be up to Whitehall to pro-rata fines depending on how each of the regions had contributed to the target. It is therefore important that Northern Ireland demonstrates a significant increase in renewable heat levels by 2020. DECC is content with targets set by DETI for Northern Ireland.

FH added that renewable heat technologies are currently unable to compete with existing fossil fuel alternatives, given the often higher capital costs and also the lack of understanding and awareness amongst consumers of what are often seen as innovative technologies. There is a need to consider the implementation of both policy instruments and financial incentives as there is a risk of market failure and of Northern Ireland not achieving the targets set. Financial incentives have already been successful within the Northern Ireland Renewable Electricity market. Since the introduction of the Northern Ireland Renewables Obligation (NIRO) in 2005, the level of electricity generated from renewable sources has increased from 3% to over 12%.

SM confirmed that he was content that there were legal and statutory obligations to be met.
PA asked if NI is not on course to meet its target, is there room to negotiate with DECC on the NI target? FH advised that GB would probably look at how the other regions were progressing with their targets. However, if NI did alter its target, this would affect the amount of funding from HMT. As with the NI Renewables Obligation (NIRO), the Department has sought to counteract the possibility of not meeting targets by including periodic reviews of the RHI scheme; the first review is scheduled for 2014. However, the Department has also included an option to hold emergency reviews, if the need arises.

PH added that a RHI roadmap will also be developed, with other NI Departments, and that the Renewable Heat Strategy Group would facilitate this.

TC confirmed that the policy development and implementation had been thorough and robust and showed that there was a definite need to implement a renewable heat scheme in Northern Ireland in line with EC and National obligations and in particular given the provision of GB funding for the policy (although not for the administration thereof).

3. Options

SM asked why the challenge fund was not taken forward as the preferred option, as evidence in the consultant's report showed it to be a viable alternative.

PH advised that the report by CEPA and AEA Technology examined a number of options to incentivise the renewable heat market. The two main type of options included capital grant/challenge fund options, which would provide a one off payment to consumers, and renewable heat incentive options that provide a long term, 20 year, stream of payments to consumers to make up the difference in the whole-life cost of a renewable heating system compared to an oil based heating system.

The June 2011 economic appraisal recognised that each approach had its own merits but it was not unequivocal in its overall conclusion. In addition, since then, the feasibility study report compiled by Ofgem has provided further information on the cost of administering a RHI scheme. Whilst the June 2011 analysis suggested that a challenge fund option could produce the most renewable heat at the lowest cost, Energy Division was conscious of a number of other key factors that needed to be taken account of in the final policy decision. These factors have been very influential in the conclusion, by Energy Division, to proceed with the RHI option. They include the following:

- ***Affordability of Administration***
  In terms of administration, the costs of running a Challenge Fund were considered to be prohibitive, especially in comparison to potential costs of administering the NI RHI. Previous experience of running *Reconnect* demonstrated administration costs of £1.48m for a grant scheme worth £10.5m (14%). The *Reconnect* scheme was for domestic customers only, and on a 'first-come-first-served' basis. A challenge fund, dealing with commercial applications and involving complex evaluation metrics, could be expected to be at least as, if not more, costly than the *Reconnect* scheme, equating to potentially £3.5m over the first 4 years. **This would not be available within DETI budget.**

  The RHI option, whilst requiring complex administration arrangements, can be implemented at a fraction of the cost through building on existing systems already in place for the GB RHI. The expected costs of the RHI scheme have been assessed and project development costs of £386k and running costs of £710k over the first 4 years. These administration costs are much more affordable in comparison to the Challenge Fund option.

- ***Challenge Fund Assumptions***
  Under the Challenge Fund options it is assumed that only the most cost effective systems are incentivised given that applications are ranked via a set of evaluation criteria. On reflection, it has been considered that this assumption is much too idealistic, in that it relies on cost effective applications being made in the first instance. If, however, applicants unduly focus on less efficient technologies then the scheme will be skewed towards these less efficient

systems. The experience learned from *Reconnect* was that in a capital grant scheme applicants will focus on technologies that are most affordable, not the most appropriate or efficient. Under *Reconnect* the most popular technology, the one installed most often (50% of the time), was solar thermal. Within this analysis solar thermal is shown to be the most costly and least efficient renewable heating technology. If this experienced was repeated, in a RH grant scheme, the target would be missed, funding would be skewed towards the most costly and inefficient systems and the appraisal's NPC would undoubtedly be wide of the mark.

The RHI operates a technology neutral approach in that the same methodology is used to determine each tariff and a specific tariff set for each technology. This, in theory, results in each technology being as attractive as each other and therefore consumers are free to select the most appropriate application. As the tariff factors the whole life cost of the technology (capex, opex, fuel and non-financial hassle costs) consumers are expected to select the most efficient system. This in turn supports the achievement of the renewable heat targets, as well as helping to build overall capacity within the renewable heating industry as it should support a wider range of technologies, helping this market to grow further than might be expected under a challenge fund.

- ***Ability to meet targets over set timescales***
  The RHI scheme provides the most certainty in terms of achieving the targets of 4% and 10% renewable heat by 2015 and 2020 respectively, as set out in the Programme for Government. This is because an RHI will deliver more heat earlier than a challenge fund as the initial annual payments to consumers will be smaller compared to capital grants, thus enabling more installations to be facilitated within each budgetary period. Whilst the Challenge Fund could also meet the targets, and potentially deliver more renewable heat, it is likely that this would be at a later date. As designed currently the RHI will achieve around 11% renewable heat by 2020.

- ***Risk***
  It has been considered that the RHI presents a lower level of risk than the potential Challenge Fund. This is largely due to the fact that incentives will be paid on actual heat output. RHI payments will only be made on metered heat output with installers paid for the amount of heat generated. This ensures that installations are kept in working order and used therefore meeting the renewable heat targets.

  As the Challenge Fund would be contributing to the capital costs of the installation (rather than the whole life costs under the RHI) a risk would develop that, after a short time, installations would stop generating renewable heat. This could be because the renewable heat fuel is no longer affordable, that a fossil fuel alternative (such as gas) become available or more attractive, that the site is no longer in business etc. In these circumstances clawback arrangements would need to be initiated, which could be costly and complicated, and the target would be hindered. As the RHI only rewards actual heat output there is less risk and less impact if sites stop generating renewable heat.

Also, in terms of risk, an RHI delivers earlier against the target. In the event that corrective action were required then the RHI option would identify this need earlier and also allow more time, scope and budgetary flexibility for action to be taken to put the scheme back on track.

- ***Consistency with GB***
  Whilst energy is a devolved matter Energy Division is mindful that a high number of commercial operators wishing to avail of support for renewable heat in Northern Ireland will operate jointly in GB. Whilst it is wholly appropriate for a specific incentive mechanism to be developed in Northern Ireland given the variances in the two energy markets, Energy Division is conscious that consistency in approach with GB would be beneficial to those availing of support in both Northern Ireland and GB. Therefore a specific NI RHI, whilst addressing the NI heat market, would be a more consistent approach with GB and will assist policy development options in the future.

- ***Example of the NIRO***
  The NIRO was launched in Northern Ireland in 2005 to support the development of renewable electricity installations. Similar to the RHI, the NIRO offers no up-front capital support for installations but instead offers 20 years of payments over the lifetime of the technology with payments determined by actual energy output. This example has proved successful with installers and has led to an increase of renewable electricity levels from 3% to over 12% currently. This experience increases confidence in a RHI scheme to generate investment in renewable heat. On the other hand the potential uptake under the Challenge Fund option would be subject to greater unknowns.

On the basis of the information presented above, the Casework Committee accepted that the RHI was the most appropriate method of incentivisation for the Northern Ireland renewable heat market.

TC asked how the tariffs had been designed and whether Energy Division felt that the various tariffs and types of technologies were appropriate.

PH advised that the tariffs vary depending on the type and size of technology to ensure that financial support is targeted for the specific installation and so over-compensation is avoided. Tariffs are paid for 20 years (the lifetime of the technology) and are 'grandfathered'. This provides certainty for an investor by setting a guaranteed support level for projects for their lifetime in a scheme, regardless of future reviews. The tariffs will be amended on a yearly basis, for existing installers and new schemes, to reflect the rate of inflation (RPI).

PH further explained that the tariff setting methodology has three general principles:

- Renewable installations are divided depending on the type of technology and size of installation;
- Within each banding a reference technology is chosen to develop a consistent tariff across technologies and scales; and

- The net costs (difference between capital and operating costs of fossil fuel counterfactual and renewable alternative) are calculated and a tariff determined.

In order to generate the appropriate tariff, the difference is determined in the costs between the renewable technology and the fossil fuel counterfactual and this figure is divided by annual heat output to arrive at the appropriate tariff. For most of the tariffs a discount rate of 12% is applied, this is consistent with the GB approach in designing the GB RHI and other renewable energy schemes, for 'domestic' tariffs a discount rate of 16% is assumed, again this is consistent with GB. The solar thermal tariff is set differently, in-line with GB, as to set the tariff in the same way would result in a tariff vastly higher than the other incentives given the cost of solar thermal and could lead to a large amount of the funding being skewed to the least efficient technology.

PH explained that the scheme would be open for new installations until 31 March 2020 and therefore the final payments would be made in 2040. The length of payment is set as the lifetime of the technology. The first review of the scheme would begin in 2014, with proposed changes implemented in 2015. In addition to this, phase 2 of the scheme would begin in April 2013 and involve the introduction of the domestic sector and consideration of tariffs for additional technologies (bioliquids, air-source-heat-pumps, deep geothermal etc).

PA asked what factors have been taken account of when scheduling a review of the RHI scheme.

FH explained that the NI RHI will have scheduled reviews built-in to the scheme to allow DETI to ensure that the scheme remains fit for purpose and value for money for the duration. The scope of these reviews will include analysis of tariffs (either to be reduced or increased), the appropriateness of technologies (remove existing technologies or add new innovative ones) and the assessment of effectiveness and success.

PH added that it may be that the tariff levels are not sufficient to encourage uptake or that they are too generous (very unlikely) and hence uptake is such that there is insufficient budget. This is a main risk of the RHI and to help counteract this risk, Ofgem will provide regular management reports which will enable uptake to be carefully monitored and forecast expenditure. The RHI will be reviewed in 2014 (and at regular intervals thereafter) and tariff levels may be adjusted, for new installations, if appropriate.

TC asked why each accredited technology was guaranteed payment for 20 years and how can we ensure that the renewable heat technology was being utilised. PH advised that tariffs are paid for 20 years as this is the lifetime of the technology. Currently, the RHI only applies to the non-domestic sector therefore all renewable heat installations will be required to be accompanied with a heat meter that will determine actual heat output. Heat meters are already common in many commercial

applications and therefore should not be a barrier to uptake. Meters will allow for accurate readings to be taken of actual heat usage and appropriate payments made. They will also ensure accurate statistics are maintained throughout the lifetime of the scheme.

SM sought clarification on the fact that the scheme appeared to be backdated to September 2010. PH explained that applicants who had technologies installed on or after that date would be able to avail of the RHI scheme but the payment would not be backdated to that date.
It was confirmed to TC and SM that no retrospective payments would be given out under the NI RHI and RHPP schemes.

On the basis of the evidence presented, the panel accepted that of the options presented the proposed RHI scheme was the most appropriate option to implement in NI.

ACTION

- The business case to DFP (and the Minister) should explicitly address the reasons why the RHI is favoured over the Challenge Fund option.

4. Value for Money / Additionality / Displacement

FH advised that without Government subvention for renewable heat installations, the target of 10% renewable heat by 2020 would not be met. This would impact on the UK's delivery of 15% renewable energy set under the RED. FH also said that it was important that the scheme was not over-subsidising the renewable heat sector; the consultant's work ensured that there was a balance created in terms of the technologies to be incentivised and the tariffs to be given.

The DETI Economist has reviewed the approach taken by the consultants and is content that the proposed scheme represents the best value for money.

In terms of displacement, the main area where displacement might occur, as a result of the RHI, will be in the established heating markets. Displacement is likely to be greatest in the oil market given the fact that tariffs are set against an oil counterfactual (and therefore provide oil customers with a greater incentive). However, this displacement is necessary to ensure a more diverse heating market and reduced carbon emissions. Displacement of natural gas is likely to be much more limited. In terms of job displacement, the RHI is expected to create new jobs, given the need for installers and suppliers. However, these jobs will, to a certain extent, be displacing existing jobs in the fossil fuel market.

TC enquired whether it would also be beneficial to switch natural gas customers to renewable heat as well as oil consumers.

FH stated that the Department was not excluding gas customers from switching and that they could avail of the RHI. However, the Department had based the NI RHI on an oil counterfactual because oil was the predominant fuel source in NI. Oil is also a

greater polluter (through carbon emissions) than natural gas. Gas customers are also relatively new and it would be wasteful for consumers to switch whilst their boilers which were reasonably new whereas a large proportion of oil boilers had reached the end of their life.

5. Budgetary management solutions

TC asked what commitment there was from HMT that payments made up to 2015 would be met for 20 years and how would the Department manage the payments based on the current budgets.

FH highlighted the financial commitment made by HMT in the GB RHI and the subsequent funding made available to DETI for the Northern Ireland scheme. FH also advised that HMT had informed DETI that any commitments made under this initial budget would be met by HMT for the lifetime of the scheme i.e. meeting the 20 year payment commitment. The RHI is a flagship policy for DECC and whilst budgets have only been set until 2015/2016 it is expected that further monies will be made available in the next budget period. This is demonstrated by the GB scheme being open to 2020 and in documentation provided by DECC to the EU Commission suggesting expected subsidies of £2.2bn in 2020.

In terms of managing payments, PH explained that there would be monthly draw downs to maintain and manage the financial aspect of the RHI to ensure that the budget would not go into overspend on any particular year. PH further advised that Ofgem has significant experience in financial profiles and budget handling as it has also worked on the GB Renewable Obligation, the NIRO and the GB RHI.

FH added that a monitoring committee would also be established in respect of the budget and the Department would receive monthly reports from Ofgem on the applications, accreditations and spend budget for the NI scheme.

TC asked how often the meters would be read for non-domestic customers. PH advised that meters would be read on a quarterly basis. The amount paid will be based on metered heat output and the tariff for the type of technology installed. This would also allow the Department and Ofgem to calculate annual forecasts for the RHI budget. If necessary the scheme could be closed to new applicants mid-year if applications were higher than expected and budgets risked being overspent.

FH confirmed that Energy Division would return to the casework committee within the next year to seek approval for the implementation phase 2 of the NI RHI.

ACTION

- Energy Division to seek casework committee approval in advance of Phase 2 of the RHI scheme.

6. Governance / Ofgem management arrangements

TC asked what controls would be in place for the project management aspect of the contract with Ofgem. JMC advised that discussions had taken place with CPD and

Ofgem. TC asked for assurance that any contract would include detail on performance targets, remedies, safeguards in place for under-performance, and breakpoints. PA enquired if the Department would have a separate contract or be part of the DECC contract in place with Ofgem. JMC confirmed it would be a separate contract.

PA asked if we had aright of audit entry included in the contract. FH assured that this would be put in place.

TC stated that IAS should be consulted in relation to the proposed management arrangements (in particular in regard to validation of amounts due and controls over payments as appropriate), and assurances that any contract would give DETI/NIAO etc appropriate inspection/monitoring/audit rights. FH stated that IAS had not yet been consulted but this would be done.

TC stated that when seeking approval for any contract, Accounting Officer approval should also be sought on the basis of the appointment of an external delivery/management organisation.

FH confirmed that a request for approval of a Direct Award Contract would be submitted to the Permanent Secretary, David Sterling along with a Third Party Organisational delivery award.

SM asked if the Utility Regulator was to be involved in the management of the RHI scheme.
FH explained that the Utility Regulator was to have no role in the scheme; it was felt that it was more appropriate to deal directly with Ofgem to ensure that all of the Department's corporate and governance requirements were put in place.

ACTIONS

- Energy Division to obtain the respective approvals from DAO and Minister for the appointment of Ofgem through a Direct Award Contract (if confirmed as appropriate by CPD) and Third Party Organisation Delivery Award.
- Energy Division to engage with Internal Audit regarding Ofgem management arrangements and, in particular on the requirement for External Delivery Organisation (EDO) audit inspections to be carried out on Ofgem as administrators of the scheme.
- Energy Division to confirm Casework Committee that any contract with Ofgem for administration of the RHI scheme would have performance targets, remedies, safeguards in place for under-performance, and breakpoints.

7. Funding issues arising from Ofgem and internal resources

TC asked how the Ofgem feasibility study had been financed and was advised that it had been paid from Energy Division's consultancy budget. FH added that Energy Division would be putting in a bid for the budget to cover Ofgem's development and operating costs. For the NI RHI, estimates are - £386k capital spend to develop the

system and then a further £136k operational spend in the first year. TC stated that the costs of any scheme would need careful consideration and as noted above, TMT approval would need to be sought.

PA enquired whether there is the possibility of developing and operating the RHI system in-house. FH explained that there were neither the skills, expertise nor resources within DETI or the wider NI Civil Service to currently undertake the administration of the NI RHI.

SM expressed concerns over the 100% contingency budget for the development of the IT systems. JMC advised that this contingency was for the development phase and would only be required for a short period of time. Energy Division had sought clarification on the Ofgem proposal for £1m legal budget. Ofgem has accepted that DETI already has a separate legal contract in place to cover DETI's legal responsibilities and it was not anticipated that the existing budget would be exceeded. TC asked if there had been much experience of legal claims. FH confirmed that there had been one recent incident under the NIRO but the matter was concluded satisfactorily without any legal involvement.

ACTION

- Energy Division to send a paper to the Top Management Team seeking approval for the ongoing administration costs for Ofgem to operate and maintain the NI RHI system.

8. State Aid

TC enquired about the current status of the state aid application.

FH advised that in December 2011, the Department sent a detailed submission to the Commission, outlining the NI RHI proposals. This submission took on board lessons learned from the GB application that was approved in November 2011. An addendum to the December application was submitted in February 2012 advising on proposed changes as a result of further economic analysis carried out by external consultants.

TC was advised that as and when the tariffs are amended or revised, the Department would have to reapply for State Aid approval.

9. Risk management

PH provided a brief overview of the risks and uncertainties in implementing a renewable heat incentive in Northern Ireland: These are:

- Incorrect subsidy level - subsidy levels proposed for the RHI are either too high or too low. This risk will be managed through regular, planned, reviews of subsidy levels.

- Risk of harm to other sectors - an increase in renewable heat may lead to a reduction in the demand for conventional heating (oil, gas, coal and electric

heating). At a high level, the short term harm to any sector should be relatively small, especially given the current scale of the oil market. However if the uptake of renewable heat impacted disproportionately on the gas sector this could have negative consequences for the extension of the gas network.

- Risk of failure of renewable heat supply - supplies of renewable fuel (i.e. biomass, biogas and bioliquids) may be disrupted. In addition, new skills will be required if installations can be made. DETI will work with colleagues in DARD and DEL to mitigate against this.

- Risks of low take-up – This could be a result of tariffs or other possible barriers include planning restrictions, a lack of awareness, and negative perceptions of the reliability and/ or cost of renewable heat. The Department has budget cover to deliver messages about renewable heat to homes and businesses.

- Risk of failure to implement targets set by EU Renewable Energy Directive - the RED is the key driver for the work undertaken by the Department on renewable heat. The requirement to meet the very challenging 12% renewable energy target falls at Member State level, not at Devolved Administration (DA) level. Each DA is expected to contribute as much as possible to the overall UK target and the Department has undertaken to introduce a renewable heat scheme in Northern Ireland in order to mitigate this risk.

- Risk of insufficient budget for administration or future payments - there may be the possibility of a higher than expected uptake leading to a requirement to manage the annual budget and higher administration costs. This will be mitigated by liaison with Ofgem to assess uptake levels and expected spend against profiled budget. The Department has also been liaising with the DECC finance team regarding future financing and with HMT relating to the budget for existing commitments.

- Risk of failure to receive State Aid approval - the EU Commission may refuse to approve the NI RHI scheme. The Department took on board the lessons learned from the GB state aid application. This is a low risk; it would be more likely that the scheme would be amended.

- Risk of instances of fraud - instances of fraud could include duplicate applications, unusual meter readings (too high for expected output), lack of information being provided to the administrator and using unregistered installers. The Department has put in place measures to counteract instances of fraud and where there are instances of suspected fraud, the participant will be investigated and payments will be stopped.

- Risk of failure in administration of RHI - there is the potential for delays in dealing with applications, accreditations and payments for the NI RHI scheme which would lead to stakeholders complaining about application process. This could be as a result of difficulties in IT systems or a lack of

communication between Ofgem and the Department. The Department will establish a joint project team with Ofgem as the scheme is implemented.

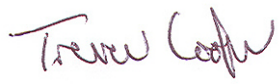
10. Conclusion and Agreed Actions

The Casework Committee confirmed that they were content to approve the RHI and the RHPP schemes to proceed to DFP conditional on completion of the following agreed actions:

- Energy Division to obtain the respective approvals from DAO and Minister for the appointment of Ofgem through a Direct Award Contract (if confirmed as appropriate by CPD) and Third Party Organisation Delivery Award;
- Energy Division to confirm Casework Committee that any contract with Ofgem for administration of the RHI scheme would have performance targets, remedies, safeguards in place for under-performance, and breakpoints;
- Energy Division to engage with Internal Audit regarding Ofgem management arrangements and, in particular on the requirement for External Delivery Organisation (EDO) audit inspections to be carried out on Ofgem as administrators of the scheme;
- Energy Division to send a paper to the Top Management Team seeking approval for the ongoing administration costs for Ofgem to operate and maintain the NI RHI system;
- Energy Division to seek casework committee approval in advance of Phase 2 of the RHI scheme;
- The business case to DFP (and the Minister) should explicitly address the reasons why the RHI is favoured over the Challenge Fund option; and
- Energy Division to send submissions concurrently to DFP and Minister seeking approval for the RHI scheme.

11. Approval of Note

Signed:



Trevor Cooper,
Panel Chairman

Date: 30 Mar. 12

Annex C

MINUTES OF DETI CASEWORK MEETING
RENEWABLE HEAT INCENTIVE (RHI) SCHEME
21 October 2015

COMMITTEE:	Eugene Rooney	(Chairperson, DETI)
	Trevor Cooper	(Head of Finance, DETI)
	Shane Murphy	(Head of ASU, DETI)
PROJECT TEAM:	John Mills	(Head of Energy Division,DETI)
	Stuart Wightman	(Energy Division, DETI)
	Alan Smith	(Energy Division, DETI)
	Seamus Hughes	(Energy Division, DETI)
DFP :	Emer Morelli	(DFP)
	Angela Millar	(DFP)
	Michelle Scott	(DFP)
	Noel McNally	(DFP)
SECRETARIAT:	Lee-Anne Hutchinson	(ACB - DETI)

Introduction

1. ER welcomed everyone to the DETI casework meeting to discuss the RHI scheme. ER explained that the aim of the meeting was to discuss the issues which needed to be resolved urgently for the RHI scheme given the imminent proposed legislative changes.

2. It was confirmed by all attendees that there were no conflicts of interests to declare.

Background

3. ER asked what was the current position regarding the legislation on the RHI scheme. JM said that a notice had been issued two months earlier to say the legislation changes would be made in early November. He confirmed that it is currently with the legal advisors and it will go to the Assembly in November 2015. JM confirmed the Minister has cleared the policy and the Committee have cleared the SL1. He confirmed that the last legal issues are being scoped and are on track. JM explained that the main change in the legislation relates to the change introducing a tiered tariff and an annual cap on the hours.

4. EM asked if the proposals required consultation. SW said that a consultation had taken place in 2013. He said that the final policy was in line with legal advice. ER felt that DFP approval needed to be in place before the legislation could be laid.

5. ER asked if DECC views had been sought on the proposed changes. JM said they hadn't but they had been dealing with OFGEM and they had numerous discussions with them on the practicalities. ER asked if there had been any concerns raised. JM confirmed there had been issues but they had been worked through.

6. ER noted that much of the take-up in technology related to biomass and questioned whether England has similar issues. JM said that the vast majority in GB is biomass with 90% in the non-domestic market with the domestic market being more balanced. He confirmed they did have similar issues.

7. EM asked were Energy Division relying on the 2013 consultation. JM confirmed that the current legislative proposals are being considered as the out workings of the 2013 consultation and that no additional public consultation would be carried out. He explained that energy Officials have ensured that key representatives from the industry were informed of the published final proposals.

8. TC asked if Energy Division had held discussions with the industry. SW confirmed they held discussions with suppliers and installers. He said they had spoken to some clients after the notice had been issued.

9. MS enquired about the trigger points that were not implemented in 2013 and should they not have been included. JM said that it was a Ministerial decision to look at the domestic scheme rather than pushing through the trigger points on non-domestic which would have significantly delayed the implementation of the domestic scheme.

10. SW confirmed that there had not been enough resources to do both and that it had taken to December 2014 to introduce the domestic scheme.

11. ER asked if any other industry, than poultry, in England used biomass. SW said that it wasn't just the poultry industry there but other agriculture industries, and hotels.

12. MS asked what triggered the cost control measures that were implemented in England in 2012. SW was unsure and confirmed they would check to identify the trigger. He assured the panel the NI scheme had received limited application numbers in 2012/13.

Action Point: Energy to identify the trigger of the cost controls in England in 2012.

13. NMcN asked about the tariff digression and if the band widths were to be widened how had this been taken into account. SM said this would reduce any quirks in the incentive to install sub optional sized equipment. NMcN asked how this change would be fed into the forecast. SW said the forecast has the higher expenditure amount included for the 199 KW boiler. SW said the forecasts incorporated this increase.

14. EM asked if the tariff change is the most effective way to control the scheme at this time. SW confirmed this to be the case pending the further review and proposals for next year.

15. MS enquired if any more discussions had been held with DECC as the Spending Review will be concluded in November. JM said that there had been nothing as yet.

16. JM indicated DETI would be happy if approval has a caveat and Energy Division can report to DFP after November.

17. JM said that it was a Ministerial agreement that the legislative changes be taken forward as a priority.

18. TC asked DFP if a multiyear position would be received from Treasury in November. MS said they were unsure how much information would be provided by Treasury as in previous years they hadn't provided much information. DFP may need to get further advice from Treasury.

19. ER asked if the renewable targets were being reported against PFG and JM confirmed they were.

20. ER asked about the reference to security of supply in the business case addendum. SW confirmed it was in relation to availability of biomass fuel but agreed to remove this from the business case.

21. ER asked about the contract with OFGEM. SW confirmed that Ofgem are appointed by DETI under powers in the Energy Act 2011 and that an Administrative Agreement was in place with Ofgem. SH said that it is an indefinite agreement but that it can be stopped in 60 days. ER said the approval sought around administration of the scheme should be clarified.

22. TC clarified that the information included in the casework on the Domestic Scheme was for purposes of looking at affordability of both schemes going

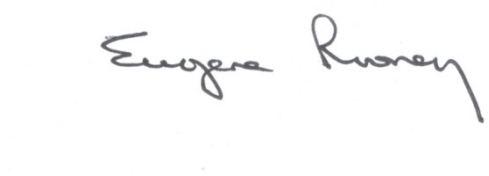
forward, not around any approval for the Domestic Scheme as this was already in place.

Conclusion and recommendation

23. ER summarised the position that DETI had been examining the options for managing the scheme in the short term pending a full review and in light of a rapid acceleration in demand for biomass technology in recent months. The DETI Casework Committee had concluded that, at this time, the proposed changes set out in the business case seemed to be the best way of approaching the Non-Domestic Scheme in the short term.

24. ER noted that DFP approval is required before the legislation could be laid and the Minister needs to be informed.

25. MS said that DFP required more time to review the business case and provide comments. She asked that DETI provide DFP with the reasons why the scheme went outside the previous approval period and what is in place to prevent it happening again.



EUGENE ROONEY

10 MARCH 2016