Department of
Enterprise, Trade and Investment
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From: Trevor Cooper

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To: Michelle Scott
DFP

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NON-DOMESTIC RENEWABLE HEAT INCENTIVE (rHI) - APPROVALS

1. Thank you for meeting on 15 June to provide DETI an opportunity to update you on the Non-Domestic RHI. This letter highlights three challenges where we would value your assistance/views.

Background

2. The RHI is the Government's key mechanism for driving uptake of renewable heat to deliver the UK's contribution to the EU renewables target with the aspiration of generating 15% of energy from renewable sources by 2020. The Executive has decided that NI's contribution should be to achieve 4% renewable heat by 2015, as set out in the PfG, and 10% by 2020 as set out in the Strategic Energy Framework. This target contributes to the Executive's carbon reduction target of 35% reduction in GHG by 2025.

The non-domestic RHI scheme was introduced in NI in November 2012. A domestic RHI scheme was introduced in December 2014.

Ofgem is responsible for the administration of the Non-domestic RHI scheme on behalf of DETI, providing information to those thinking of applying for the RHI, renewing applications, receiving and examining meter data and making payments to participants. Ofgem is responsible for ensuring that the scheme is robust against fraud or error.

The scheme provides a 20 year payment to successful applicants to incentivise the move away from fossil fuels such as gas and, predominantly in NI, oil to renewables technologies such as solar, ground source heat pumps and biomass. Without subsidisation there would be no move away from fossil fuels as the sustainable technologies are more expensive. In NI the overwhelming majority of renewable heating installations supported under the RHI have been for biomass.

Approvals

3. The current basis for DFP approval for the non-domestic scheme was a business case which was agreed in April 2012. This included a commitment that any decision to continue the scheme beyond 2015 would require further/separate DFP approval. There was also a requirement to review the scheme starting in 2014.

4. Regrettably the necessary DFP approval for additional commitments under the Non-Domestic Scheme beyond 31 March 2015 has not been sought until now. The Department undertook work on a review of the Non-Domestic RHI with proposals being subject to public consultation in October 2013. Following this consultation, the Minister's focus was on implementation of the Domestic RHI Scheme and proposed actions on the Non-Domestic RHI were delayed to accommodate this.

5. When the position on approvals was realised in June 2014 [DN 2015?], an assessment was made to prevent ongoing, irregular funding. This concerns committed expenditure for new applications approved from 1 April. Committed expenditure (over 20 years) for applications approved prior to 1 April 2015 is covered by the Business Case approval. Unfortunately any room for manoeuvre is limited. The basis for the scheme is statutory and it is not possible to cease, suspend or otherwise delay applications. This has been confirmed (verbally) by DSO (we await written confirmation). This is logical given the unavoidable ongoing and continuous nature of the scheme which is designed to incentivise sustainable behaviour over decades. DETI has no choice but to incur this expenditure. To act otherwise would be to act unlawfully and invite challenge. Effecting legislative change requires affirmative resolution of the NI Assembly so will take at least three months to complete.

6. The Department is also, urgently taking forward work to provide supplementary information in support of the original business case that will provide a basis for renewed DFP approval and hence ~~seek to~~ regularise the position in relation to the Scheme expenditure (both RHI payments and administration costs) both prospectively and

retrospectively. This will include an assessment of the scheme's continuous and continuing provision of value for money in achieving the Executive's sustainable energy objectives.

Budgets

7. The second issue concerns budgets. RHI is paid out of general taxation from AME in accordance with an envelope set by HMT for 2012/15 for NI. This envelope was around £25m and DETI's main concern was underspend against this allocation. Only about half the funding was used in the period. This did not take full advantage of all the money made available to support the Executive's sustainability targets.

However, from late 2014 uptake for the non-domestic scheme has taken off and forecast expenditure in 2015/16 is estimated to be £23m – roughly double the previous forecast made in November 2014. This rapid increase is due to the NI poultry industry adopting biomass heating technologies for its hundreds of chicken houses. This increased uptake is welcome in delivering Executive targets, supporting the agrifood sector and providing environmental benefits. Nonetheless controls need to be considered (see below) to ensure that the scheme delivers the best value for money option and appropriate budgetary control.

On the latter point the funding via AME raises some questions:

- In light of the increase in scheme uptake, the previous 15/16 forecast of £11.64m (November 2014) is no longer appropriate and further funding is needed to meet unavoidable commitments – an increased AME in line forecast was recently submitted to inform the Chancellor's July Budget;

- [DN: are we sure we can stand over this and the next bullet point, given the Ministerial correspondence with DECC in the past. The "common law" of public expenditure management is that when any allocation comes under pressure, the budget holder has a responsibility to escalate the issue for resolution. In this case, we were told in a Ministerial letter that the amount available was the Barnett percentage of the DECC budget. Please consider and redraft as necessary to avoid any obvious riposte] There is lack of clarity about whether NI support is linked to spending by the Department of Energy and Climate Change (DECC) in GB, ~~. I~~in particular whether NI expenditure needs to stay with limits prescribed by a % relationship to GB spend;

- This impacts on a final question of whether there is an HMT budgetary limit for 15/16 which DETI should be observing [DN: as above – if there is an allocation, its there to be observed…].

We are in the process of writing formally to DECC, following verbal and email exchange at all levels to explore the position. From DECC's perspective, NI expenditure on RHI is nothing to do with them [DN so why write to them?]. They advise that AME expenditure for RHI should not be subject to any Barnett consequential type arrangement and that the matter should be pursued with HMT via DFP. Although we will continue to engage with DECC we would be grateful if you could also explore with HMT. Using the supplementary business case highlighted above and the controls mentioned below, we are working to demonstrate continuous value for money and implement more sophisticated budgetary controls.

Future Controls

8. The speed with which uptake of one particular technology (Biomass) has taken off has led us to consider measures to control future expenditure and maximise value for money. These measures include:

- The introduction of a tiered tariff for new biomass installations where the tariff significantly reduces after 1,314 hours of usage;
- Consideration of introducing a degression mechanism for tariffs for new renewable heating installations such that if scheme uptake exceeds triggers based on factors such as application numbers or budgetary estimates, there will be an automatic reduction in the tariff available; and
- Consideration of a straight tariff reduction for the most popular biomass tariff.

Together, these measures ~~will~~ would ensure more sensitive budgetary control in the short and long term; mitigate over-reliance on one technology; strengthen value for money ~~assessment~~ and continue to incentivise the growth in renewable heat to attain the Executive's 10% target.

Conclusion

9. This note sets out the actions we are taking to regularise the position on the non-domestic RHI. If there are further actions which you think should be taken I would be grateful to receive your views.

TREVOR COOPER

cc: