

BUSINESS CASE FOR PROPOSAL TO ENGAGE A CONSULTANT

Project Title: FOLLOW UP ANALYSIS ON THE NORTHERN IRELAND RENEWABLE HEAT INCENTIVE

Prepared By: PETER HUTCHINSON **Date:** 28 November 2011

Approved By: FIONA HEPPEL
Director of Energy Division

F. Hepper

Signed:

[Signature]

Date: 29th November 2011.

Section 1: NEED FOR THE ASSIGNMENT

Background – Purpose of the assignment

- 1.1 The paper has been prepared in line with the DFP guidance for the use of external consultants (22 December 2009).
- 1.2 The purpose of this assignment is to carry out further essential analysis on the potential design of a Renewable Heat Incentive¹ for Northern Ireland. For this assignment it is proposed that a contract is put in place via a Direct Award Contract with Cambridge Economic Policy Associates (CEPA) and AEA Technologies. A² previous assignment was carried out between February – June 2011 that designed a proposed RHI for Northern Ireland, and assessed the potential costs, risks and impact. This analysis was carried out by CEPA and AEA Technologies and supported the development of an appropriate NI RHI scheme. This current assignment is a follow up to that previous research and analysis.

Strategic/policy context

- 1.3 The development of the RHI is a key policy for DETI and will be a key driver in supporting the achievement of 10% renewable heat by 2020, the target set by the Executive through the Strategic Energy Framework (SEF). The Department of Energy and Climate Change (DECC) have now launched the RHI scheme in Great Britain, however Northern Ireland is not included in this scheme because of significant differences in the two heat markets. The launch of the GB scheme ahead of a Northern Ireland RHI will focus attention on the progress with the NI work.
- 1.4 The RHI is the main UK policy driver to satisfy obligations under the EU Renewable Energy Directive and to support the achievement of their renewable heat target of 12% by 2020, and as such Northern Ireland is expected to contribute to this target.
- 1.5 Previous research carried out by the Department has demonstrated that 10% renewable heat is possible by 2020 but only with significant support both in terms of financial incentives and policy measures. The most recent analysis carried out by CEPA and AEA helped to design a specific incentive scheme and assisted in developing a³ public consultation document on the issue.

¹ An RHI is an incentive scheme that will reward those who install eligible renewable heat technology with a set tariff to be paid over a number of years, the level of tariff and length of payment is determined by the size and type of technology involved. The tariffs are set in order to cover the capital, operating and other non-financial costs of installing such technologies.

² http://www.detini.gov.uk/economic_appraisal_into_the_northern_ireland_rhi_-_june_2011.pdf

³ http://www.detini.gov.uk/the_development_of_the_northern_ireland_renewable_heat_incentive.pdf

- 1.6 This consultation was carried out between 20 July 2011 and 3 October 2011 and received 76 responses.

What is the need for the assignment?

- 1.7 During the consultation a number of issues were raised that Energy Division now need to consider further before developing the final design option for the RHI. Some of these issues included;
- The proposed banding of the tariffs, each technology is banded so smaller installations receive a different incentive to larger installations, this is due to the different costs involved in these technologies. A number of consultees argued that the banding overly favored smaller, less-cost effective installations and should be revised.
 - Tariff levels and technology assumptions, a number of respondents were concerned that tariff levels were lower than GB equivalents; the reason for this is due to the fact that NI consumers will be switching from oil to renewable and therefore requiring less of an incentive than GB consumers switching from gas to renewables. There were also concerns raised about some technology assumptions and specifically recent increases in the cost of biomass. Energy Division wants to consider these issues and see how/if they affect the proposed tariffs.
 - Treatment of large industrial sites, it has been proposed that these sites are excluded from the RHI this is due to a number of factors (economics, technical capacity, biomass sustainability and potential impact on gas). Given the scale of these sites and their cost-effectiveness and State Aid issues, Energy Division needs to consider this issue again.
- 1.8 When these issues are all considered and final policy options agreed it will be necessary to carry out a final assessment of the scheme, this assessment would include the costs, the impact, the associated benefits and the displacement on other energy markets. This will be undertaken as part of this assignment.
- 1.9 As previously mentioned, the RHI is a key energy policy. In September 2010, the DETI Minister, made a ⁴statement committing to developing and implementing a Northern Ireland RHI, should it prove economically viable to do so.
- 1.10 In addition, following the Chancellor of the Exchequer's statement on the Spending Review in October 2010, that £860m of funding would be available for the RHI over the spending review period, the Chief Secretary to the Treasury informed the First and deputy First Minister that £25m of this (£2m/£4m/£7m/£12) would be available for a Northern Ireland RHI over the spending period.
- 1.11 The previous assignment has demonstrated that a Northern Ireland RHI has the potential to support the deployment of renewable heat and assist in reaching the Executive endorsed target of 10% renewable heat by 2020. It will also have positive impacts in terms of fuel security, carbon reductions and green jobs.

What is the scope of the assignment, i.e. tasks anticipated to provide desired outcomes?

- 1.12 This assignment will help shape the final design of the Northern Ireland RHI and will ensure that issues or concerns that were raised during the consultation process are carefully considered and addressed, to help ensure the final scheme is fit for purpose.
- 1.13 The assignment will follow on the previous work carried out and will involve revisiting technology assumptions, considering alternative banding methods and assessing the impact

⁴ <http://www.northernireland.gov.uk/index/media-centre/news-departments/news-deti/news-deti-september-2010/news-deti-200910-foster-recoqnises-importance.htm>

of the final RHI scheme. This work is vital for the scheme to be implemented and money provided by HMT utilized in the most effective manner.

Timing of assignment – when is the information required and is there any possibility of deferring the assignment?

- 1.14 There is absolutely no possibility that this assignment could be delayed or deferred. It is of utmost importance that the final design of the RHI is agreed as soon as possible and any delay will impact on the delivery of the scheme, the achievement of the target and the utilization of available funding.
- 1.15 Without the final design option agreed arrangements on the administration aspects of the scheme cannot be finalized, it also impacts on the drafting and laying of the subordinate legislation that underpins the scheme. Finally, approval of the EU Commission will be required for this scheme to be launched and therefore they must be notified of the final tariffs, banding and technologies as soon as possible.
- 1.16 Delaying this assignment would have significant consequences for the delivery of the RHI scheme.

Description of previous similar consultancy assignments, including an analysis of past expenditures (corresponding evaluations must also be appended)

- 1.17 As previously mentioned, a similar assignment that considered the initial design of the RHI has been carried out by CEPA and AEA. This work was carried out between February 2011 – June 2011 at a cost of £ [REDACTED] (part financed by the European Regional Development Fund under the European Sustainable Competiveness Programme for Northern Ireland). The post project evaluation (PPE) for this project is attached at **Appendix I**. This work is a follow-up to this previous analysis.

Section 2: BENEFITS & THEIR TIMING

What are the projected outputs from the assignment?

- 2.1 The immediate output of this work would be a final design option for the Northern Ireland RHI that addresses issues raised by the consultation process. This work is required so the appropriate scheme can be finalised and implemented.

What are the expected benefits to be delivered from the assignment and give an indication of when they are likely to accrue?

- 2.2 The immediate benefit from this assignment will be an independent assessment and advice on the final design of the NI RHI. In addition there will be consideration of a range of complicated issues raised throughout the consultation and revision of technology assumptions used in the initial analysis. This approach will ensure that the final policy position is evidence based and fully costed, to allow final decisions to be taken. In turn, this will support the introduction of the NI RHI and the uptake of renewable heat technologies from 2012 onwards.
- 2.3 The long term benefit of undertaking this piece of work will be the development of the renewable heat industry in Northern Ireland. By increasing the uptake of renewable heat in Northern Ireland there are opportunities to reduce Northern Ireland's dependence on fossil fuels and therefore increasing fuel security and cutting carbon emissions. The development of the renewable heat industry also presents significant opportunities for 'green jobs' in the period 2012-2014 and beyond.

What are the implications of the assignment not going ahead?

- 2.4 If this assignment did not go ahead then the scheme, as currently designed, would have to go ahead without further analysis and without a technical consideration of new issues raised during the consultation. This, in turn, might affect the effectiveness of the scheme and lead to criticism on the Department. It is also a possibility that, as currently shaped, the scheme would not receive State Aid approval (given the treatment of large industrial sites).
- 2.5 In the long term it would be likely that the 10% target would be missed and funding from HMT not used in the most effective way.
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Section 3: ASSESSMENT OF ALTERNATIVES OPTIONS

- 3.1 As required, a number of alternative options to external consultancy have been considered;

i) Option 1 – Do nothing

Doing nothing would result in the Department continuing in the development of the RHI without further analysis and without a detailed technical consideration of new issues raised following engagement with stakeholders. This could result in an ineffective and costly option being employed and therefore would have a detrimental impact on the Northern Ireland renewable heat market.

ii) Option 2 – Complete the analysis in-house

The necessary resources and technical expertise do not currently exist in-house in either Energy Division or the Economics Division as specialist heat economist input is required.

iii) Option 3 – Partial completion of assignment using in-house resources

The necessary resources and technical expertise to develop appropriate support mechanisms for renewable heat and to advise on the potential cost / benefit do not currently exist in-house. In-house economists will be utilised in during this assignment, however they do not have the necessary technical experience in renewable heat to undertake this task fully.

iv) Option 4 – Short/Medium term secondment of industry experts

Whilst the secondment of industry experts would provide the necessary technical expertise the resources do not exist within energy division to either manage this secondment on a day-to-day basis or to house the seconded experts.

v) Option 5 – Use of External consultants

This is our preferred approach. This will ensure the appropriate level of expertise is available for this project and that it can be completed in a timely and cost-effective manner. This approach would also ensure that the assessment is independent and the conclusions based on economic analysis and evidence. It is also proposed that CEPA and AEA are re-appointed to continue with the work they have already undertaken in previous analysis; this will ensure the project is carried out in a timely manner and at lower cost, given the expertise and knowledge already built up through initial study.

SECTION 4: EXPECTED DELIVERABLES

Please provide details on the deliverables expected from consultancy. If available, a copy of the draft terms of reference for the proposed consultancy should be attached.

- 4.1 CEPA and AEA will be tasked with considering a range of issues that were raised directly by the consultation and have an impact on previous assumptions, modeling and tariffs developed. These issues include;
- considering updated costs on Northern Ireland biomass and the associated impacts;
 - designing additional banding levels to support medium and large scale commercial applications;
 - assess the need to support large industrial sites and an associated tariff if required;
 - analyze the impact of the final policy in terms of renewable heat delivered, costs and unintended impacts (i.e. displacement of gas).
- 4.2 A project proposal document is attached at **Annex A**.

Section 5: SKILLS TRANSFER***Outline the potential for skills transfer***

- 5.1 This piece of work requires a combination of both economic and energy, specifically renewable heat, expertise to understand the current heat market and technologies in terms of supply and demand and to assess the effectiveness and cost of the various support measures that will be considered. In addition, it requires expertise developed over the previous analysis work as many of the considerations or revisions relate to previous assumptions that require further checking and potential updating.
- 5.2 The expertise for this assignment will be required to analyse the current heat market and provide the evidence base for the final design of the Northern Ireland RHI.

What arrangements have been put into place to facilitate the transfer of skills from the consultants to departmental staff to the extent that this is a benefit of the consultancy?

- 5.3 Though the project will be brief there may be some opportunity for skills transfer to Departmental staff, specifically in relation to energy economics and the cost/benefit of the various options considered.

When is it anticipated that knowledge and skills delivered by the consultancy will be transferred to internal staff?

- 5.4 Knowledge and skills delivered by the consultancy will be transferred to internal staff throughout the project through meetings and discussions about the elements of the project. The final analysis will assist in in-house knowledge and support the final design of the RHI to be considered by the DETI Minister.

What are the implications of skills transfer for future consultancy support?

- 5.5 Due to the highly technical nature of renewable heat, specifically the economics surrounding the various technologies, the skills transfer involved in the project will not mean that future consultancy won't be required. However, the transfer of skills, knowledge and understanding during this assignment will ensure that this work can be developed further in-house and that

any future consultancy will be monitored and quality assured by knowledgeable and experienced staff.

Section 6: PROPOSED DIVISION OF WORK

What in-house support will be given to the consultants e.g. technical/specialist inputs, accommodation, photocopying and typing services etc?

- 6.1 The external consultants will be required to provide the delivery of specific objectives as described in the project proposal.
- 6.2 In-house staff will be used to manage the delivery of the project, assisting consultants with queries if appropriate and providing the consultants with full and supporting background documentation to give contextual awareness of renewable heat in Northern Ireland, specifically this will be to provide an update on issues and concerns raised by stakeholders. It is estimated that 2-3 meetings will be held with G7, DP and DP Economist throughout the project (via teleconference).

Provide indicative estimates of the number of consultancy days by consultancy grade.

- 6.3 The assignment is estimated to take up to 30 consultancy days as follows:-
- Principal Economist – 4 to 6
 - Junior Economist – 6 to 8
 - Senior Technical Advisor – 2 to 4
 - Junior Technical Consultant – 10 to 12

Provide indicative estimates of the expected number of in-house staff days by staff grade.

- 6.4 The assignment is estimated to take up to 8 in-house staff days, estimated at 4 days at DP, 2 days at G7 and 2 days at Deputy Economist.
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Section 7: EXPECTED COSTS OF THE ASSIGNMENT***External Consultancy Costs***

- 7.1 It is expected that this follow up work will cost in the region of £20,000. Budget is available from the Energy Division Budget.

In-House Costs

- 7.2 The in-house cost of 3 meetings, reading time and project management (detailed at para 6.4) for a G7, DP and Deputy Economist is in the region of £2500
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Section 8: PROJECT MANAGEMENT / PERFORMANCE REVIEW ARRANGEMENTS

What are the proposed project management arrangements, including details of monitoring officers, draft reports, Steering Groups etc?

- 8.1 The project will be managed by Sustainable Energy Branch with the successful consultants expected to liaise closely with the Head of Branch and Deputy Principal on a regular basis. A Deputy Economist will also provide support throughout the project, specifically quality assuring the work of the consultants.

Proposed arrangements for on-going monitoring of consultancy performance and expected deliverables. The project managers should ensure that appropriate mechanisms are in place for influencing performance at interim stages.

- 8.2 Regular teleconferences will take place throughout the project with the consultants expected to provide regular update reports as required. An updated economic model and an accompanying draft report will be required by 16 January 2012.

Identify person/persons responsible for managing/delivering skills transfer.

- 8.3 The progress of the assignment will be monitored closely by the Deputy Principal to ensure that the project is completed on time and within budget.

What are the performance review arrangements for the assignment, e.g. the quality assurance employed from Departmental specialists?

- 8.4 Payment will only be on completion of satisfactory analysis and a recommendation paper, which has been approved by dept economists.

Skills transfer should be pro-actively managed and monitored like any other consultancy benefit.

- 8.5 There will be a number of teleconferences held throughout the assignment to assist in project management and skills transfer. Consultants will also be expected to explain the analysis carried out and the evidence gathered so skills and knowledge will be transferred.

Section 9: IMPLEMENTATION AND EVALUATION PLAN

How will the results of the consultancy be implemented?

- 9.1 The results of this consultancy will be to provide an evidence base on the final scheme of the Northern Ireland RHI and assess the potential impact, benefits and costs of this final policy position. This information will be used to advise the Minister in advance of a final policy decision in respect of a RHI rollout.

Proposed arrangements for evaluating the outputs delivered by the consultancy assignment. This should include information on who is the responsible officer for ensuring the evaluation takes place and also information on when it is proposed to carry out the evaluation. Whilst ideally the evaluation should be independent of the project promoters, in most instances, evaluations should be carried out by internal resources, i.e. in-house staff or internal consultancy.

- 9.2 Following the completion of this assignment a Post Project Evaluation on the work of the consultants will be carried out by Energy Division, to be completed within 6 months of the satisfactory conclusion of the project.