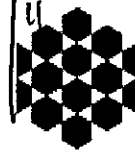


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○ Michael: for your approval.

Michael 5/1/11



Department of

**Enterprise, Trade
and Investment**

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**From: Fiona Hepper
Energy Division**

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Date: 30 December 2010

**To: 1. David Sterling [Content to approve 5/1/11]
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ASB/11 *10/1 Content*

DETI SUB 001/11

**BUSINESS CASE FOR THE APPOINTMENT OF CONSULTANTS TO
CARRY OUT AN ECONOMIC APPRAISAL OF A RENEWABLE HEAT
INCENTIVE (RHI) FOR NORTHERN IRELAND**

- Issue:** The submission seeks the mandatory internal approvals, ahead of an approach to DFP Supply, to appoint external consultants to carry out an economic appraisal of a Renewable Heat Incentive (RHI) for Northern Ireland.
- Timing:** Desk Immediate: As DFP approval is required and the appraisal completed to ensure spend in 2011/12 is achievable.
- Need for referral to the Executive:** The RHI scheme will be a DETI initiative and therefore will not require referral to the Executive. However the Executive will need to be consulted on a future Renewable Heat Strategy, which will be cross-cutting in nature. Issues regarding legislation may also require Executive approval.
- Presentational issues:** Not at this stage, however there is likely to be increased interest from MLAs, industry and media as this work progresses.
- FOI implications:** This submission is exempted under Section 35 of the Freedom of Information Act.
- Financial Implications:** This assignment will cost £ Sensitive commercial information redacted by the RHI Inquiry HMT has advised that funding of £25m will be available over the spending period for a Northern Ireland RHI scheme, should one be introduced.

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- Legislation Implications:** DETI does not hold primary powers for renewable heat. However, Energy Division officials are in contact with DECC colleagues in order to explore the possibility of amending the current Green Energy and Energy Security Bill to include renewable heat powers for Northern Ireland. I will write to you separately on this issue in January 2011.
- PSA/PFG Implications:** None at present, but it is likely that new PSA targets in relation to renewable heat will have to be developed.
- Statutory Equality Obligations:** None.
- Recommendation:** That the Departmental Accounting Officer and Minister consider and approve the business case for the appointment of consultants, at a cost of £2.5 million, to undertake a comprehensive economic appraisal of a RHI scheme for Northern Ireland. Once approval has been obtained, DFP Supply approval to incur the expenditure will be sought.

Background

My submission of 9 August 2010 (SUB 364/10) informed you of the completion of a study into the potential development of renewable heat in Northern Ireland and secured your approval to undertake an economic appraisal of a Renewable Heat Incentive (RHI) scheme for Northern Ireland.

Renewable Heat – Drivers and Potential

2. The key driver for developing the renewable heat market in Northern Ireland is the EU Renewable Energy Directive (RED), which sets challenging renewable energy targets for all EU Members States. The UK renewable energy target is 15% consumption from renewable sources by 2020, in order to support this target the Department of Energy and Climate Change (DECC) has adopted a target of 12% renewable heat by 2020. You will be aware that in order to achieve this target DECC intend to introduce a RHI in GB from June 2011. This will reward new renewable heat installations by a tariff depending on the size and type of technology installed.
3. The recent AECOM / Pöyry study into the potential development of renewable heat in Northern Ireland has indicated that the current level of renewable heat in Northern Ireland is 1.7%, with the vast majority of Northern Ireland's heating demand being met by imported fossil fuels. The

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study also demonstrated that the share of renewable heat could realistically be increased to 10% by 2020. However, significant Executive support in terms of policy levers and financial incentives would be required to make this a reality.

4. As a result of this study a target of 10% renewable heat by 2020 was officially adopted within the Strategic Energy Framework (SEF). DETI also committed to undertaking an economic appraisal of a specifically tailored RHI for Northern Ireland to ensure that the policy was both cost-effective and could be appropriately funded. Increasing the amount of renewable heat to 10% will not only contribute to the UK target, it has the potential to also support other energy policy goals in terms of increasing security of supply, reducing carbon emissions and creating opportunities for new green jobs in employment within the renewable heat supply chain.

Need for Consultants

5. DETI Energy Division now wishes to appoint external consultants to carry out an economic appraisal for a Northern Ireland RHI. This is a complex, one off task that requires the advice of specialist heat economists. DETI Economics Branch has confirmed that they do not have the skills necessary to undertake this work in-house.
6. The Chancellor of the Exchequer's statement on the Spending Review in October 2010 provided £860m of funding for the GB RHI over the spending review period. Following this, the Chief Secretary to the Treasury informed the First and deputy First Minister that £25m (£2m/£4m/£7m/£12) would be available for a Northern Ireland RHI. DETI now wishes to appoint a service provider to undertake an independent economic appraisal of a Northern Ireland specific renewable heat incentive.
7. This work is essential to ensure that the target adopted as part of the SEF is met in the most appropriate way. Previous research carried out has highlighted that the GB RHI, as it currently stands, could be ineffective in Northern Ireland as it does not take account of the specific elements of the heat market here and therefore to effectively incentivise the local market a Northern Ireland RHI should be developed.

Objectives of the Assignment

8. This assignment will refine the need for a RHI in Northern Ireland, will outline the objectives for introducing such a scheme, advise on possible structures of a RHI and assess the cost/benefit. The assignment will also involve considering a range of methods for developing the heat market, either through the RHI structure or other means. This will ensure that the most cost-effective method of developing renewable heat is implemented.
9. The key objectives of this assignment are to;

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- Identify the strategic context within which this policy sits, specifically identifying the particular EU, UK and NI policy that is relevant.
- Determine the need for Government intervention in the renewable heat industry in Northern Ireland.
- Outline the objectives of Government's support of the renewable heat industry and the associated benefits.
- Identify a full list of potential options for future delivery of a Northern Ireland Renewable Heat Incentive.
- Provide a detailed analysis of the economic cost/benefit of implementing a renewable heat incentive in domestic, non-domestic and the large industrial sector in NI.
- Identify and quantify the monetary costs and benefits for each option.
- Assess and identify the potential risks in delivery in a future support scheme.
- Outline the non-monetary costs and benefits of delivering a RHI support scheme and increasing renewable heat levels to 10% by 2020.
- Calculate net present values and assess uncertainty.
- Make recommendations, based on the evidence gathered and the economic analysis carried out, on the most cost effective structure of a Northern Ireland RHI to increase the level of renewable heat to 10%.

10. The terms of reference, drafted with input from DETI Economics Branch, is appended to the full Business Case attached at **Annex 1**.

Tender Process

11. The initial cost of this piece of work was estimated to be between £40-50k, which would be in line with costs of a standard economic appraisal. Therefore, following my approval, Sustainable Energy Branch engaged with Central Procurement Directorate (CPD) and began a competitive tender process for this work. Four service providers submitted bids for this work, these bids were as follows;

- AECOM Ltd, partnering with Pöyry Energy Consulting Sensitive commercial information redacted by the RHI Inquiry
- Cambridge Economic Policy Associates (CEPA); partnering with AEA Sensitive commercial information redacted by the RHI Inquiry
- Europe Economics, partnering with Cyril Sweett and Scott Wilson Sensitive commercial information redacted by the RHI Inquiry
- Element Energy, partnering with Cambridge Econometrics Sensitive commercial information redacted by the RHI Inquiry

12. Only one of the proposed service providers was within the expected price range. The higher than expected prices is due to the very specialised technical nature of this economic appraisal. On Friday, 10th December 2010, Alison Clydesdale, Peter Hutchinson (both Sustainable Energy

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Branch) and Sam Connolly (Economics Branch) met to evaluate the tenders. Following an assessment of each of the applications based on methodology, resource allocation and contract management, the markings were as follows;

- i) Cambridge Economic Policy Associates (CEPA), partnering with AEA, Sensitive commercial information redacted by the RHI Inquiry
- ii) Europe Economics, partnering with Cyril Sweett and Scott Wilson, Sensitive commercial information redacted by the RHI Inquiry
- iii) Element Energy, partnering with Cambridge Econometrics, Sensitive commercial information redacted by the RHI Inquiry
- iv) AECOM Ltd, partnering with Pöyry Energy Consulting, Sensitive commercial information redacted by the RHI Inquiry

Cost and Timing

13. As the expected cost of this piece of work is higher than anticipated, and above the threshold which I can approve, I am now seeking your approval to proceed with this project. Providing you are content I will then seek approval from DFP Supply. The price quoted by CEPA for this work is valid until 28th February 2010.

14. This project will be part-financed (50%) by the European Regional Development Fund under the European Sustainable Competitiveness Programme for Northern Ireland. The remaining £ Sensitive commercial information redacted by the RHI Inquiry will be provided from the existing Energy Division budget. EU programmes has confirmed that a further £21k of activity can be accommodated in the Programme under Priority 3. In addition Finance Branch has confirmed they are content and that an internal reallocation between EU Receipts and EU Expenditure will be required as part of February Monitoring.

14. It is essential that this project goes ahead as soon as possible. DECC intend to have the RHI in place in GB from June 2011 and the continued absence of firm policy proposals for Northern Ireland is causing uncertainty in the market place. This work will advise on the appropriate next steps and inform a consultation process on the design and implementation of Northern Ireland incentive scheme; this will ensure that domestic consumers and businesses have the confidence to begin investing. Further to this, HMT has allocated £2m of funding for a Northern Ireland RHI in 2011/2012. To ensure this money is utilised this economic appraisal must go ahead.

Recommendation

15. The Department does not have the relevant technical expertise to carry out an in-depth economic analysis of an incentive method for renewable heat. Whilst this project will be managed by Sustainable Energy Branch, with input from Economics Branch, it is necessary to appoint an external consultant to take this work forward and advise on the appropriate incentive scheme for Northern Ireland.

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16.I therefore recommend that the Departmental Accounting Officer and Minister:

- i) approve the attached business case for the appointment of consultants at £^{ensitive commercial} and ^{information redacted by the RHI Inquiry}
- ii) note the approval will subsequently be sought from DFP Supply to incur the expenditure.

17.I am happy to discuss.

(signed)

**FIONA HEPPER
ENERGY DIVISION
(Ext 29215)**

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Subject: DETI SUB 001/11: Business Case for the appointment of Consultants to carry out an Economic Appraisal of a Renewable Heat Incentive (RHI) for Northern Ireland
Date: 11 January 2011 10:07:06
Attachments: [SUB 001 Minister cleared 10.01.11.pdf](#)

Fiona

The Minister has read your submission of 30 December and she is content with the recommendation outlined. Please proceed.

Michael Duffy

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