Action: Michael Woods to write to the Head of Energy Division regarding the change of audit plan and to copy his note to the Committee.

NON DOMESTIC RENEWABLE HEAT INCENTIVE (RHI) SCHEME

25. Stuart Wightman joined the meeting presented a paper outlining the history and current position in regard to the Non-Domestic RHI Scheme, including actions being taken to seek to secure appropriate approvals for expenditure in 2015-16 and beyond.

26. Stuart confirmed that officials in Energy Division have been working in conjunction with officials in DETI Finance Division and DFP to regularise matters. Approval for the Scheme has now been received covering the period from 29 October 2015 to 31 March 2016. Retrospective approval is currently being sought from DFP to cover the period from 1 April 2015 to 28 October 2015. Stuart confirmed that amendments to the Scheme involving tariff changes and the introduction of a cap on annual payments had been brought into effect in November 2015.

27. Trevor Cooper commented that there were lessons to be learnt in terms of the initial design of the scheme and the ongoing control of the scheme through regular reviews of tariffs. The Chairman asked if DETI’s equivalent department in Great Britain, the Department of Energy and Climate Change, had more flexibility in terms of its ability to quickly change tariffs. Stuart confirmed that GB has more flexibility through automatic digression, with tariffs being adjusted in response to changing costs. In response to a question from Claire Hughes, Stuart confirmed that the Scheme had been successful in terms of the achievement of targets for its uptake.

28. The Committee went on to discuss the operation of the Scheme. In response to a question from Claire Hughes, Stuart confirmed that OFGEM (which administers the GB Scheme) reviewed and checked applications on behalf of DETI. Anthony Harbinson considered it important to ensure that lessons are learnt from the issues which had arisen in the operation of the Scheme. He also underlined the importance of ensuring that if a similar issue were to arise in the future, it would be identified at an early stage and remedial action taken. Anthony reiterated the Committee’s view that the Scheme should be audited by Internal Audit Service at the earliest possible juncture.

29. The Chairman commented that he expected the internal audit process to identify any further issues with the Scheme. He considered that the Department is exposed until DFP approval for the period from 1 April 2015 to 28 October 2015 is received, and through entering into commitments over a 20 year period. Trevor Cooper informed the Committee that, following the Chancellor’s Autumn Statement, DFP has now confirmed that
expenditure under the Scheme may be subject to an absolute cap in terms of AME available in any given year. DFP is engaging with HM Treasury to seek clarification on the effect of the Autumn Statement in terms of funding. A response is awaited. Eugene stressed the importance of settling the budget position.

30. Stuart confirmed that an options paper would be put to the Minister in terms of the future operation of the Scheme.

31. The Chairman requested that a substantive paper outlining the latest position be provided to the next meeting of DAC.

Action: Energy Division to provide a paper regarding the current position on the Non-Domestic RHI scheme.

32. Stuart Wightman left the meeting at this stage.

33. Iain McFarlane outlined the current position in relation to the repayment of the loan provided to the. He informed the Committee that the 18 month business plan covering the period up to March 2017 has been received and is being reviewed by the Department in conjunction with its specialist insolvency advisers. Iain confirmed that a capital repayment of £14M was received in respect of the repayment due at the end of November which exceeded the scheduled £9m repayment by £5M.

34. Iain informed the Committee that work is ongoing regarding the year end accounts and that the Department has negotiated a reduction in supervisors’ fees, with a discount of 5% being achieved for February and March 2015 and a 10% discount being achieved from April 2015 onwards.

35. In response to a query from the Chairman in relation to the prospects of recovery of the loan in light of the state of the property market, Iain confirmed that the carrying value of the property assets in the accounts had been reviewed and this had resulted in their value being increased by £12M in the Accounts.

DETI REPORT TO THOSE CHARGED WITH GOVERNANCE (RTTCWG) 2014-15

36. Iain provided an update on the RTTCWG and confirmed that it contained four “priority two” issues. Two of the issues related to the Presbyterian Mutual Society, one related to Harland and Wolff, and one related to a CFER balance with Invest NI (this was also referred to in Invest NI’s
Thanks Keith
I take it this is a total cap i.e commitment to ongoing payments relating to prior installations are first call on this funding and then what is left can be used for further investment? In that circumstance this funding will be split between RAME and CAME – I take it that is what you expect and it is for us to provide the split when loading the next set of AME numbers to OSCAR. Our department will be talking to DECC on the operation of the revised scheme but I want to make sure that numbers are set before they embark upon a scheme that may fall outside of these parameters.
Thanks again
Pamela

Pamela Galloway
Central Expenditure Division
Room P1 New Building
Rathgael House
Bangor

Tel: 028 91858010
Internal: 68010
e-mail: pamela.galloway@dfpni.gov.uk

Please note any attachment with the suffix .tr5 is a TRIM reference which can only be accessed by DFP and OFMDFM

The RHI numbers for NI are

<table>
<thead>
<tr>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>GB</td>
<td>420</td>
<td>640</td>
<td>780</td>
<td>900</td>
<td>1010</td>
</tr>
<tr>
<td>NI</td>
<td>18.3</td>
<td>22.3</td>
<td>25.7</td>
<td>28.9</td>
<td></td>
</tr>
</tbody>
</table>

These are basically calculated using Barnett on the GB numbers.

I've not seen anything regarding conventional AME stuff announced at AS/SR.

Thanks

Keith Jarrett
Devolution Spending Control
Second Floor, Yellow Zone
Michelle

Please see attached letter from Trevor Cooper for your attention.

Thanks.

Laura McCoy

Personal Secretary
Department of Enterprise, Trade & Investment
Netherleigh
Massey Avenue
Belfast, BT4 2JP
Tel: 028 9052 9200 (ext: 29200)
TextRelay: 18001 028 9052 9200
Web: www.detini.gov.uk

NI Year of Food & Drink 2016

Please consider the environment - do you really need to print this e-mail?
7 December 2015

Dear Michelle

BUSINESS CASE ADDENDUM FOR THE NORTHERN IRELAND NON-DOMESTIC RENEWABLE HEAT INCENTIVE

1. I am writing in follow up to my letter of 27 October 2015 and the subsequent letter from Emer on 29 October 2015 setting out prospective RHI approval to 31 March 2015.

2. The legislative changes to the Non Domestic RHI scheme were approved by the Assembly on 17 November and came into operation on 18 November 2015. An increase in application activity was predicted in the run up to the scheme changes but the actual response far exceeded the expectation. The table below demonstrates how application numbers have increased from August 2015 up to the legislative changes on the 18 November 2015.

<table>
<thead>
<tr>
<th>Period</th>
<th>Application Numbers</th>
<th>Annual Cost</th>
<th>20 Year Cost</th>
</tr>
</thead>
<tbody>
<tr>
<td>Nov 2012 – March 2015 (Previous Commitments)</td>
<td>522</td>
<td>£12.3m</td>
<td>£246m</td>
</tr>
<tr>
<td>April 2015</td>
<td>85</td>
<td>£1.1m</td>
<td>£22m</td>
</tr>
<tr>
<td>May 2015</td>
<td>66</td>
<td>£1.4m</td>
<td>£28m</td>
</tr>
<tr>
<td>June 2015</td>
<td>49</td>
<td>£1.3m</td>
<td>£26m</td>
</tr>
<tr>
<td>July 2015</td>
<td>42</td>
<td>£0.9m</td>
<td>£18m</td>
</tr>
<tr>
<td>August 2015</td>
<td>55</td>
<td>£1.1m</td>
<td>£22m</td>
</tr>
<tr>
<td>September 2015</td>
<td>90</td>
<td>£2.14m</td>
<td>£42.8m</td>
</tr>
<tr>
<td>October 2015 (up to 28/10/15)</td>
<td>441</td>
<td>£9.8m</td>
<td>£196m</td>
</tr>
<tr>
<td>Total for Retrospective Period (1/4/15 – 28/10/15)</td>
<td>828</td>
<td>£17.74m</td>
<td>£355m</td>
</tr>
<tr>
<td>November 2015 (29/10/15 – 29/11/15)</td>
<td>452</td>
<td>£9.95m</td>
<td>£199m</td>
</tr>
<tr>
<td>December 2015 – March 2016 (forecast)</td>
<td>80</td>
<td>£1.92m</td>
<td>£38.4m</td>
</tr>
<tr>
<td>Total for Prospective Period (29/10/15 – 31/3/16)</td>
<td>532</td>
<td>£11.9m</td>
<td>£238m</td>
</tr>
<tr>
<td>Total Forecast Commitments to 31 March 2016</td>
<td>1882</td>
<td>£41.94m</td>
<td>£839m</td>
</tr>
</tbody>
</table>
3. Some 983 applications were received during the 2½ months leading up to the tariff changes on 18 November 2015. Processing and accreditation of these applications is likely to take many months given the numbers. There is nothing to suggest that all these applications won't be accredited. Ofgem's initial checks suggest the applications are in order. Accordingly the figures have been included for forecasting purposes.

4. The current 2015/16 AME budget is £22.8m which was based on monthly non domestic application numbers up to August 2015 and a forecast of increased application numbers in September and October. However, with almost 1,000 applications received during the 2½ months leading up to the changes, we are now forecasting Non Domestic RHI expenditure to be £30m in 2015/16. Even if there were no new offers of support beyond 2015/16, Non Domestic RHI scheme expenditure is forecast to be £42m in 2016/17 (as shown above) and for the subsequent years going forward. Any further offers in 2016/17 would increase this further.

5. If there were no new offers of support under the Domestic RHI beyond 2015/16, annual expenditure under this scheme is forecast to be £2.2m from 2016/17 onwards pushing total RHI expenditure to £44.2m.

6. Application numbers have dropped dramatically as expected after the introduction of the scheme changes with only 1 application received since the 18 November 2015. It is expected that numbers will remain low going forward. However, it is likely that any decision to close or restrict either of the RHI schemes from April 2016 could trigger another spike in demand and committed expenditure.

Yours sincerely

[Trevor Cooper's signature]

TREVOR COOPER
Head of Finance Division

cc Eugene Rooney
Chris Stewart
John Mills
Bernie Brankin
Iain McFarlane
Stuart Wightman
From: Rooney, Eugene
To: Cooper, Trevor
Cc: McCormick, Andrew (DETI); Stewart, Chris (DETI); Mills, John (DETI); Brankin, Bernie; Wightman, Stuart; McFarlane, Iain
Subject: RE: Treasury Position on RHI
Date: 07 December 2015 17:49:14

Trevor
We discussed. We need to offer DFP urgently lines to take on the RHI funding position for their meeting with Treasury. You have requested to attend the meeting with Treasury.

At the Audit Committee last week Stuart advised that DECC was being contacted to establish the RHI position for GB following the Spending Review. We need to have urgent confirmation of the DECC position in terms of funding methodology agreed for the coming years and the policy position being pursued.
I am trying to have a word with Mike or Joanne.
Eugene

From: Cooper, Trevor
Sent: 07 December 2015 17:06
To: Rooney, Eugene
Cc: McCormick, Andrew (DETI); Stewart, Chris (DETI); Mills, John (DETI); Brankin, Bernie; Wightman, Stuart; McFarlane, Iain
Subject: Treasury Position on RHI
Importance: High

Eugene
Further to our earlier conversation on RHI, DFP has now informed me that they expect to receive Chief Secretary letter tomorrow which will amongst other issues cover RHI.
As regards budget for RHI they anticipate that NI will receive notification of a capped AME amount of £18.3M in 2016-17, £22.3M in 2017-18, £25.7M in 2018-19 and £28.9M in 2019-20. Any difference between actual spend in any of these years and the capped AME amount would in terms of the position presented fall as a call on NI Block Resource DEL.
Michelle is participating in a meeting with Treasury tomorrow pm to see if the position can be changed in any way. She is going to discuss further tomorrow arguments that may be deployed. As things stand Energy colleagues are currently forecasting spend under both schemes would total £44.2M in 2016-17 (assuming steps taken immediately around closure of both schemes, and numbers do not take account of any further spike in demand that may result from announcements that each of the Domestic and Non-Domestic Schemes will be closed). Should the Treasury position on funding not change this would leave an inescapable resource pressure of at least £25.9M from commitments on RHI in 2016-17.
Trevor
8.

a. Prior to the RHI scheme I do not recollect any other funding proposal with a similar AME limit and associated DEL penalty.

b. Such a scheme doesn't carry greater risk if the relevant Accounting Officer (in this case DETI) adheres to the terms of the approved business case. From an accountability perspective a pound of AME money should carry the same degree of Value for Money concern as a pound of DEL.

c. I do not recollect any similar such funding arrangement. The spending profile and recording of that spend is as determined by HMT. In this case the UK Spending Review Settlement Letter, 2010, approved a four year profile to March 2015 and the DETI approval to spend was time-limited to that point.

d. All relevant public expenditure documentation during this period (Managing Public Money NI, HMT Consolidated Budget Guidance, HMT Statement of Funding Policy for the Devolved Administration) was made available to DETI (and all other Departments).

9.

a. HMT did not impose a Spending Review limit for the Scheme in 2015-16. Indeed, in discussions with HMT officials in autumn 2015 there was an explicit reference to the fact that there was no 2015-16 Scheme limit because there was no UK Spending Review in place.

b. There was no Scheme spending limit in place for 2015-16 as there was no HMT Spending Review in place. Because of the UK electoral cycle HMT was preparing for a new UK Spending Review to take effect from April 2016.

c. There was no Scheme spending limit for 2015-16. Effectively HMT gave a commitment to cover actual Scheme costs that materialised for that year only. As HMT clarified (in a meeting in December 2015) how 2015-16 funding would be provided this information was relayed to DETI by the Supply team (detailed in DFP / DOF Corporate Submission). The Spending Review Settlement Letter received in January 2016 then set the Scheme funding limits for 2016-17 year and thereafter.
Dear Peter and Martin,

SPENDING ROUND 2013 SETTLEMENT – NORTHERN IRELAND EXECUTIVE

This letter records the Spending Round 2013 settlement for the Northern Ireland Executive for the financial year 2015-16. It sets out both the budgetary settlement and any additional aspects which may be of interest.

Resources and investment for 2015-16

2. This settlement provides the Northern Ireland Executive with a Total Departmental Expenditure Limit (TDEL) of £10,682 million in 2015-16.

3. Your Resource Departmental Expenditure Limit (RDEL) (excluding depreciation) will be £9,622 million in 2015-16, equivalent to a real terms reduction of 1.5 per cent on your 2014-15 baseline. The impact on the Northern Ireland Executive of the overall reduction in the UK RDEL envelope of 2.6 per cent has been mitigated in part by the ongoing protections afforded to health and the schools budget in this Spending Round.

4. Your fiscal Capital Departmental Expenditure Limit (CDEL) in 2015-16 will be £956 million. In addition you have been allocated £104 million of financial
transactions. This provides you with an overall CDEL limit of £1,060 million. This represents a real terms growth of 24.8 per cent on your 2014-15 baseline and a real terms growth of 1.5 per cent on your 2014-15 control total.

5. The settlement has been determined in accordance with the Barnett Formula, using the comparability factors set out in the Statement of Funding Policy together with the latest midyear estimates of population (mid 2010).

6. The following elements were determined outside the Barnett formula:

- Following work by the Police Service of Northern Ireland and the Northern Ireland Office to determine the PSNI national security requirement for 2015-16, I have agreed to provide £31 million in 2015-16. This is made up of £29.5 million resource and £1.5 million capital. This funding will be added to your settlement for 2015-16, ring-fenced for that purpose. This element of your settlement is a one off and will thus not be baselined in future spending rounds. I understand that you will continue to discuss the PSNI’s funding requirements as part of your ongoing liaison with NI departments.

- Following our correspondence in April 2013 on the block grant adjustments necessitated by the devolution of Air Passenger Duty on long haul flights from Northern Ireland to the Northern Ireland Assembly, I have applied a reduction of £2.3 million to your block grant adjustment for 2015-16.

- The spending review has announced some policies which impact on AME in 15-16. These have been certified by the OBR, but not included in the forecast. As such we will reflect the Barnett consequential impacts of these measures on Northern Ireland AME at Autumn Statement 2013. We do not anticipate that there will be any impact on the DEL settlement for
Northern Ireland. Where the principle of parity applies we will expect the Northern Ireland Assembly to legislate to implement similar reforms.

- In the SR we announced the intention to help local authorities in England freeze their council tax in 2014-15 and 2015-16, by providing a 2 year grant in 2014-15 and a 1 year grant in 2015-16. In year 1 of each scheme, the Treasury will fund this from the Reserve at Supplementary Estimates once the final costs are known, for the second year of the 2014-15 scheme, the grant will be transferred at Main Estimates. You will receive appropriate Barnett consequentials. The intention is that these grants will not be baselined for future spending reviews. As part of this, the council tax freeze grant afforded to Local Government in England in 2013-14 (£181million) has been baselined. Your 2015-16 settlement will include Barnett consequentials of £1.1 million.

9. The Northern Ireland Executive’s Annually Managed Expenditure (AME) budget for 2015-16 remains in line with the latest Office for Budget Responsibility forecast provided by you for Budget 2013.

10. Full details on 2015-16 control totals and growth rates are set out in Annex A.

11. While there is currently no intention to reopen this settlement, the Treasury retains the right to do so should it be necessary to meet the Government’s deficit reduction plans.

Other aspects of this settlement

- As agreed in discussion with the Prime Minister on the Northern Ireland economic pact, your capital borrowing limit under the Reinvestment and Reform Initiative will be temporarily extended by £50 million in 2014-15 and 2015-16. Given the earlier agreement to re-profile your limit given a
delay in your proposed A5 investment this means your RRI limit will be £300 million in 2014-15 and £250 million in 2015-16. The additional borrowing is only available for the Executive to use in respect of shared housing and education projects and will be subject to ongoing Treasury oversight and approval.

- The budgetary flexibilities afforded to DOJ in 2010 Spending Review in the form of unlimited carryovers of underspends will be withdrawn with effect from 2015-16 and DOJ underspends will be subject to the normal Budget Exchange arrangements for Devolved Administrations. To be clear, the last year of unlimited carryforward of DOJ underspends will be from 2013-14 into 2014-15.

- The Coastal Communities Fund will continue in 2015-16 as a UK wide fund. As before, the funding in Scotland will be equal to 50% of the revenues generated by the Crown Estate’s marine assets in Scotland. The funding arrangements in Scotland will continue those agreed during the current Spending review period, with funding drawn down from the Reserve at the Supplementary Estimates and added to the Scottish Government’s allocations to only be used for the Coastal Communities Fund. The size of the fund is subject to periodic review as with all Government spending. We will review the proportion of revenue that the size of the Fund is based on at each Spending Review. We will also review the size of the Fund should revenue rise or fall significantly in any given year.

- The Spending Round announces that the Government will, for the first time, introduce a cap on the country’s welfare spending. The cap will improve spending control, support fiscal consolidation and ensure the welfare system remains affordable. This cap will apply to UK social
security and tax credits spending. Under the parity principle, NIE will be required to deliver the AME savings consequentials of any DWP policy reforms introduced under this framework. Any future changes to the DEL/AME budgeting framework for DWP will apply to NIE in the same way. Further details on the implementation of this reform will be announced by Budget 2014.

12. I am copying this letter to the Prime Minister, Deputy Prime Minister, Chancellor, the Secretary of State for Northern Ireland, and the Northern Ireland Minister for Finance and Personnel.

Best wishes

DANNY ALEXANDER
Annex A: details of the Northern Ireland Executive Spending Round 2013 budgetary settlement

13. This section sets out in full the details of the Northern Ireland Executive’s Spending Round 2013 budgetary settlement.

14. The budgets set out here are to be administered in accordance with the Treasury’s Consolidated Budgeting Guidance except where specific derogations have been agreed. Any future changes to the budgeting guidance will apply to this settlement.

15. Consistent with the Consolidated Budgeting Guidance, departments are encouraged not to allocate their DEL fully against their programmes at the start of a financial year but to hold some provision back to deal with unforeseen pressures that emerge subsequently, including from any known contingent liabilities.

16. Access to the Reserve will be considered only for large, genuinely unforeseeable and unavoidable contingencies, and then only as a last resort after your ability to absorb such new pressures within your settlement has been fully taken into account. New priorities must be funded within this settlement through reprioritisation and further efficiencies.

Northern Ireland Executive control totals

17. Table 1 sets out your agreed control totals in 2015-16. All figures are in £million and include VAT. These control totals are set inclusive of all tax liabilities arising from your department’s activities. The Treasury will not entertain bids for funding to meet unanticipated costs.
### Table 1: Northern Ireland Executive control totals: RDEL and CDEL (£million)

<table>
<thead>
<tr>
<th></th>
<th>14-15 baseline</th>
<th>15-16 control total</th>
<th>Real terms change (%)</th>
</tr>
</thead>
<tbody>
<tr>
<td>RDEL</td>
<td>10,071</td>
<td>10,167</td>
<td>-0.8%</td>
</tr>
<tr>
<td>o/w non-ringfenced</td>
<td>9,597</td>
<td>9,622</td>
<td>-1.5%</td>
</tr>
<tr>
<td>o/w depreciation ringfence</td>
<td>373</td>
<td>404</td>
<td>6.3%</td>
</tr>
<tr>
<td>o/w student loans ringfence</td>
<td>100</td>
<td>141</td>
<td>37.9%</td>
</tr>
<tr>
<td>CDEL</td>
<td>835</td>
<td>1,060</td>
<td>24.8%</td>
</tr>
<tr>
<td>o/w financial transactions</td>
<td>0</td>
<td>104</td>
<td>n/a</td>
</tr>
<tr>
<td>Existing RRI Borrowing</td>
<td>250</td>
<td>200</td>
<td>n/a</td>
</tr>
<tr>
<td>Additional RRI Borrowing</td>
<td>50</td>
<td>50</td>
<td>n/a</td>
</tr>
</tbody>
</table>
Andrew – you asked if there was any update on RHI yesterday.

HMT has now confirmed that the CST Settlement Letter will state that the NI DEL will have to take the hit on the excess RHI payments over the £18m cap which equates to our population share. Apparently DECC has never factored the additional NI energy output (over the 3% population limit) into the national target!

So Jon D wasn’t able to exert pressure by saying that the UK would lose over 5% of its contribution towards the renewable target because DECC never counted it in the first place. The CST letter will say that they won’t retrospectively seek to clawback in 2015-16 but the NI DEL will have to take the strain from 2016-17 on.

In light of this we will now have to issue a letter to DETI to advise them to take corrective action immediately

M
(a) I became more involved in the RHI issue in Autumn 2015. As advised in my first statement to the Inquiry,

“...in discussions with HMT officials in autumn 2015 there was an explicit reference to the fact that there was no 2015-16 Scheme limit because there was no UK Spending Review in place.” WIT 43219 refers.

(b) On 8 December 2015 I chaired a meeting with HMT. A number of issues were discussed at the meeting including RHI. Michelle Scott from Supply attended that meeting at my request. As advised in my first statement to the Inquiry, HMT clarified how 2015-16 funding would be provided. This information was relayed to DETI by the Supply team, WIT 43219 refers.

(c) I am also aware that there was further engagement with HMT after this meeting as to the funding model for RHI going forward. Given the passage of time I do not recall the exact sequence or detail of this engagement but I do recall that it was in advance of the HMT Settlement Letter, which was received on 13th January 2016.

(d) On 18 December 2015, a HMT official (Jon Donaghy) advised me by telephone that, having discussed the issue with other relevant HMT officials, no additional monies would be available for NI RHI Scheme over and above the population share, 3%, of the DECC RHI Budget, and that contrary to previous advice given to DFP from DETI, DECC had never factored in the increased contribution from NI to the wider UK target on renewables’.

(e) During this period I had many engagements with Andrew Crawford on a wide range of finance issues. In that context I have no recollection of any specific RHI engagement with him during this time or him issuing instructions to me. The documents provided to me by the Inquiry show that I updated David Sterling and the SpAd of the RHI position, DOF 02272 demonstrates that Andrew Crawford specifically asked for an “update on RHI yesterday” . It is likely that I kept both Andrew Crawford and the DFP Permanent Secretary informed pursuant to any request, but also voluntarily, as Supply officials were keeping me informed on DETI AME forecasts for 2015-16 and beyond which had increased significantly.
and it was not clear if sufficient monies would be made available from 2016-17 onwards through the AME funding model to meet these pressures.

(f) My approach to the DFP Permanent Secretary and SpAd was in line with the established way of working between myself as Budget Director, my direct line manager and the DFP SpAd.

(g) In and around this time, 18 December 2015, evidence with which I have been presented shows that I appear to have provided Andrew Crawford with a copy of Supply’s draft letter to DETI, (declining its request for retrospective approval for installations under the RHI Scheme from April to November 2015)(DOF 04722/3). I have no distinct recollection of this action but I presume that I did so because the action of declining retrospective approval was a step of considerable importance and one about which the Minister of my Department, the DFP Minister, should be alerted. This letter was subsequently issued without amendment to DETI on 21 December 2015, (DFE 152933/36).

**January 2016**

From the email you sent to Andrew Crawford on 18 December 2015 (DOF-02272) it appears that you had a general understanding of the position which HMT was going to adopt in relation to RHI funding in the 2015 Spending Review settlement for Northern Ireland. As a result, in that communication you indicated that DETI would need to be advised to take corrective action immediately.

On 12 January 2016 Ms Foster became First Minister of Northern Ireland, and was replaced as DFP Minister by Mervyn Storey. Andrew Crawford continued as the DFP Special Adviser.

On 13 January 2016 the Chief Secretary to the Treasury provided the NI Executive with the 2015 Spending Review settlement letter for Northern Ireland (DOF-42007 to DOF-42012), which dealt with RHI funding at paragraph 13 (on DOF-42009).
Trevor

Please see attached correspondence.

Many thanks

Emer

Emer Morelli
Supply
DFP
Tel: 02891858128 (Ext:68128)
21 December 2015

Dear Trevor

NON-DOMESTIC RENEWABLE HEAT INCENTIVE- ADDENDUM

Thank you for your letter of 7 December regarding the retrospective element of the Non-domestic Renewable Heat Incentive (RHI).

As you are aware, the DFP approval for the non-domestic RHI scheme expired on 31 March 2015. Therefore, the addendum submitted to DFP in October 2015 sought both prospective approval for the amended scheme going forward and retrospective approval for the operation of scheme during the first seven months of 2015-16.

DETI requested urgent DFP consideration of the addendum given the intention to introduce legislative changes in early November. Therefore, DFP focused on the prospective element of addendum with the intention of returning to the retrospective request in due course.

Retrospective Approval

DFP will only grant retrospective approval within very limited circumstances. MPMNI states that DFP may consider granting retrospective approval if it is satisfied that:

(a) it would have granted approval had it been approached properly in the first place; and
(b) the Department is taking steps to ensure that there is no recurrence.

DFP approval for the non-domestic RHI scheme was only granted until 31 March 2015 to reflect the period for which HMT funding had been secured. DFP should have been approached well in advance of this date, at which time both affordability and value for money would have been considered. At that stage there would also have been an opportunity for an open dialogue between the departments on the outcome of DETI’s 2013 consultation and the subsequent decision by DETI not to introduce annual cost control measures.

DFP was not afforded the opportunity to review or influence the policy decisions being taken at that time, and I cannot conclude that we would have been content with the decision not to amend the scheme. Therefore, the first condition has not been satisfied and retrospective approval cannot be granted.

In the absence of DFP approval for this expenditure all commitments entered into between 1 April 2015 and 28 October 2015 will result in irregular expenditure. You have quantified this expenditure at £17.74m in 2015-16, and £355m across the 20 year life of the non-domestic RHI agreements.

This level of annual expenditure is around £10m per annum higher than the costs reported in the October addendum. Looking at the detail of this cost escalation, your letter indicates that 441 applications were received in October alone, almost double the amount of applications received in the first twenty months of the scheme. This clearly warrants further investigation to test both the origin and authenticity of the additional applications, and I welcome your commitment to bring forward the audit of the scheme. I would be grateful if you could keep Supply informed of the outcome of this audit and any implications for the projected scheme costs.

Supply will now write to the Audit Office to notify them of our decision in relation to this retrospective approval request. DETI’s management of this scheme has raised a number of concerns, both in relation to adherence to DFP approval and DETI’s operation of tariff based schemes. It will be important to establish how irregular expenditure of this magnitude was incurred and what process can be put in place to ensure there is no reoccurrence of this situation.

**Affordability**

While the level of irregular expenditure reported is a considerable concern for DFP, these concerns are dwarfed by the very immediate and long term budgetary implications.

As you are aware, HMT has provided a RHI AME profile for the SR period which is significantly lower than the level of expenditure now committed to. DFP has engaged with HMT on this profile and highlighted the specific local issues which have resulted in the higher spend levels. However, while HMT are still considering
the funding issue, we must be aware that a possible, and indeed probable, outcome is that the NI Executive will have to fund all costs above the AME profile from the Executive’s DEL allocation. I should therefore be grateful if you would advise as a matter of urgency, on the options available to DETI for the future operation of this scheme in the context of a considerably more constrained DETI/DfE budget.

It would be useful to discuss the affordability concerns in more detail. My office will be in contact to arrange a suitable time to discuss both the budgetary and value for money implications of the operation of the non-domestic RHI scheme.

Yours sincerely

EMER MORELLI

cc Mike Brennan
Eugene Rooney
Michelle Scott
Noel McNally
We discussed the TOR for Internal Audit - this letter reinforces my reasons for needing a direct approach to establishing how this went so badly wrong, and what lessons we need to learn in relation to internal governance.

We will need to discuss further with Finance and Energy colleagues.

Many thanks.

-----Original Message-----
From: Stewart, Chris (DETI)
Sent: 21 December 2015 14:02
To: Mills, John (DETI)
Cc: McCormick, Andrew (DETI); McIlwrath, Linda
Subject: FW: HP TRIM DFP Document : DF1/15/948906 : Supply - DETI - RHI retrospective

John

For advice please.

C

-----Original Message-----
From: Rooney, Eugene
Sent: 21 December 2015 13:56
To: McCormick, Andrew (DETI); Stewart, Chris (DETI)
Cc: Hill, Janice
Subject: FW: HP TRIM DFP Document : DF1/15/948906 : Supply - DETI - RHI retrospective

-----Original Message-----
From: Morelli, Emer
Sent: 21 December 2015 13:43
To: Cooper, Trevor
Cc: Brennan, Mike; Scott, Michelle; Rooney, Eugene; McNally, Noel
Subject: HP TRIM DFP Document : DF1/15/948906 : Supply - DETI - RHI retrospective

Trevor

Please see attached correspondence.

Many thanks

Emer

Emer Morelli
Supply
DFP
Tel: 02891858128 (Ext:68128)
Dear Mervyn,

SPENDING REVIEW AND AUTUMN STATEMENT 2015 – NORTHERN IRELAND EXECUTIVE

Congratulations on your appointment as Minister for Finance and Personnel. I look forward to working closely with you and continuing the open and constructive relationship that Arlene and I have enjoyed. I would be very happy to have an early meeting, and if you have any plans to be in London please do contact my office.

2. This letter records the settlement for the Northern Ireland Executive following the outcome of the combined Spending Review and Autumn Statement which the Chancellor delivered on 25 November 2015.

3. I am also grateful for the constructive nature of the engagement with the Treasury by your predecessor and your officials in advance of the Chancellor’s announcements.

Resource DEL, capital DEL and financial transactions capital DEL allocations

4. The Barnett Formula was applied to changes in UK Government departmental allocations in the usual way, reflecting the updated comparability factors, which were shared in advance, and the latest mid-year estimates of population. The outcomes of these calculations on the Northern Ireland Executive’s allocations for Resource DEL, Capital DEL and within CDEL ring-fenced financial transactions are set out in Annex A.

5. You will have noted that RDEL allocations have been set for 4 years, through to 2019-20. In order to provide some additional security for longer-term planning for investment, CDEL allocations have been set for one additional year.

Block grant adjustment – Long-Haul Air Passenger Duty (APD)

6. As agreed between the previous Chief Secretary and the then-Minister for Finance and Personnel Sammy Wilson, it is necessary to adjust the Executive’s block grant to adjust for the impact of the devolution of long-haul Air Passenger Duty (APD).
7. The following table sets out the RDEL block grant adjustment over the SR period, based on forecast growth rates for UK long-haul passengers. The 2015-16 figure does not reflect the adjustment made for this financial year, but instead sets a new baseline for the Spending Review period.

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<td>0.319</td>
<td>0.329</td>
<td>0.338</td>
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<tr>
<td>Reduced rate adjustment</td>
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<td>1.847</td>
<td>1.896</td>
<td>1.945</td>
<td>1.997</td>
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<td>2.166</td>
<td>2.224</td>
<td>2.283</td>
<td>2.343</td>
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Corporation Tax

8. As set out in the ‘Fresh Start’ agreement, the UK Government remains committed to the devolution of corporation tax rate-setting powers if the Northern Ireland parties meet their commitments in the Stormont House Agreement. This includes demonstrating that the Executive’s finances are on a sustainable footing for the long-term.

9. There are two further areas that we need to progress so that we are in a position to proceed if these commitments are met. I am pleased that on the first of these, a Memorandum of Understanding has been agreed that will allow HMRC to start work to update IT systems. I am content for officials to take forward further discussions on the second area on arrangements for a block grant adjustment to deal with the direct and behavioural effects of devolution, over coming months.

Temporary accommodation management fee

10. The existing fee paid to local authorities in Great Britain for the costs associated with managing temporary accommodation is due to end in April 2017. Currently an AME cost managed by the Department for Work and Pensions in Great Britain, the Executive has in the past received AME cover sufficient to cover the costs generated in Northern Ireland.

11. In England, from 2017-18 funding will be provided to the Department for Communities and Local Government through DEL. The Barnett formula has been applied to the overall DCLG settlement in the usual way. Decisions on the mechanisms and levels of funding to support the relevant bodies in Northern Ireland for their responsibilities in similar areas are now for the Executive to take from within available resources.

Coastal Communities Fund

12. The Coastal Communities Fund will continue to be funded annually from the Reserve. For allocations in 2017-18 and beyond, the annual allocation for Northern Ireland will be set at 33
per cent of the gross marine revenues of the Crown Estate in Northern Ireland two years previously.

Renewable Heat Incentive (RHI)

13. As in the previous Spending Review period, AME cover based on a population-proportionate share of the budget which has been set for the Renewable Heat Incentive in Great Britain will continue to be made available to the Northern Ireland Executive. The level of cover available is therefore £18.3, £22.3, £25.7 and £28.9 million from 2016-17 to 2019-20. Any spending on RHI above this level will need to be funded from the Executive’s DEL budgets or other sources of income.

Ring-fenced PSNI Additional Security Funding

14. The PSNI bid for Additional Security Funding for this Spending Review period has been met in full. Ring-fenced sums of £32.24, £34.26, £33.71 and £31.14 million will be added to the NI Executive block grant from 2016-17 to 2019-20, to be used specifically for the purposes set out in the PSNI bid. This funding is made available on the understanding that the commitments entered into in relation to police funding to be provided from the Executive’s overall block grant in both the Stormont House and the Fresh Start agreements are honoured.

National Cyber Security Programme

15. The National Cyber Security Programme will support cyber security across the UK, according to the objectives set out in the National Cyber Security Strategy, to be revised in 2016. Where the devolved administrations are responsible for the delivery of specific cyber objectives, they will be able to bid to the Cabinet Office for programme funding for transformational projects to effect significant improvements to the UK’s cyber security. The National Cyber Security Programme will not fund routine or ‘business as usual’ cyber security activity which would otherwise be funded from within existing devolved administration budgets. Further details will be set out by the Cabinet Office in due course.

Apprenticeship Levy

16. I am pleased that our officials are engaging on the Apprenticeship Levy, as they work to ensure that Northern Ireland, Scotland and Wales all receive their fair share of the levy. As I have previously highlighted, we have no intention to undermine your flexibility over skills and apprenticeship policy within your responsibilities, and we aim to develop a system which as far as possible complements your policies. It remains a priority to ensure the Levy will have transparent and fair funding flows for employers right across the UK.
Changes to Housing Benefit and Interactions with rents in the Social Rented Sector

17. Following the Summer Budget, I set out that the devolved administrations would be expected to identify proportionate savings in relation to Housing Benefit to those which will be delivered from the down-rating in rents in the Social Rented Sector in England. The Spending Review and Autumn Statement introduced further reforms to Housing Benefit. It is clear from the discussions officials have had to date that there are complex interactions between the AME costs of Housing Benefit, and the role of the devolved administrations in relation to general housing policy. I cannot accept that it is fair to taxpayers across the UK to permit costs generated by Housing Benefit in Northern Ireland to continue to rise, as a direct result of policy decisions on rents in the social rented sector taken by Northern Ireland Executive Ministers, a position I trust you will understand. Officials should continue to explore these issues in order to provide further advice on the options available to move forward.

Donations to women’s charities

18. Your predecessor wrote to me on 27 November regarding the Chancellor’s Spending Review announcement of a fund for women’s health and support charities. Details of the bidding process will be set out in due course, and we will follow this up with you in the New Year.

Spectrum charges

19. The Northern Ireland Executive is the holder of electromagnetic spectrum, for which it has to pay an annual charge. This is to ensure that publically held spectrum is used efficiently. The RDEL charge on the Executive will be £188,632. This fee should be paid to Ofcom. Where the Executive clears spectrum for full release or enters into sharing arrangements that have the effect of freeing up high-value bandwidth for productive civil use, charges for that spectrum will be abated accordingly.

Finance Ministers' Quadrilateral meeting

20. I recognise the value of the Finance Ministers' Quadrilateral (FMQ) meeting to discuss financial issues of mutual interest, alongside the bilateral conversations that I have recently been prioritising. I therefore suggest that an FMQ meeting takes place alongside the forthcoming Joint Ministerial Committee (Plenary) meeting.

Setting the Executive’s 2016-17 Budget – accessing ring-fenced funding and borrowing

21. Our officials have had useful initial discussions on the process for constructing the Executive’s 2016-17 budget. However, I was disappointed that the Executive decided to agree a budget for next year and put the substance of this budget into the public domain without clear agreement from the Treasury. As the Secretary of State set out in her letter of 17 December,
the Government's clear expectation was that further discussions would take place before this happened.

22. Whilst I understand the compressed timescales within which you are working, I trust that engagement will continue at each stage of the budgetary process. I expect to be provided the opportunity to give consent to the proposed budgetary treatment of each element of Stormont House or Fresh Start agreement support before it is presented to the Assembly, to ensure that the capacity for misunderstanding is minimised.

23. We must avoid a repeat of the Executive's decision to adopt a draft budget for 2015-16 which implied spending which exceeded the established control totals set by the Treasury. We must also be clear that where proposals in the Fresh Start and Stormont House Agreements state that Government agreement is required, then this could involve an active role in ensuring any proposals meet our expectations.

24. I am copying this letter to the Prime Minister, the Chancellor, and the Secretary of State for Northern Ireland.

Yours ever,

GREG HANDS
Annex A

Table 1 sets out the Northern Ireland Executive’s Barnett-formula determined DEL outcomes from Spending Review 2015, covering the years 2016-17 to 2020-21.

All figures are in £million and include VAT. These control totals are set inclusive of all tax liabilities arising from your department’s activities.

These figures exclude any additions arising from the Stormont House Agreement or previous / subsequent individual arrangements. Officials will be liaising separately to ensure that an understanding of the working control totals which should be used to inform the NI Executive’s 2016-17 draft Budget is reached.

Table 1: Northern Ireland Executive SR outcomes: RDEL and CDEL (£million)

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<tbody>
<tr>
<td>Resource DEL (excl Depreciation)</td>
<td>9,661</td>
<td>9,777</td>
<td>9,855</td>
<td>9,861</td>
<td>9,885</td>
<td>***</td>
</tr>
<tr>
<td>Capital DEL</td>
<td>1,062</td>
<td>1,123</td>
<td>1,137</td>
<td>1,150</td>
<td>1,192</td>
<td>1,239</td>
</tr>
<tr>
<td>o/w CDEL in PSGI</td>
<td>957</td>
<td>1,010</td>
<td>1,036</td>
<td>1,073</td>
<td>1,126</td>
<td>1,185</td>
</tr>
<tr>
<td>o/w Financial Transactions Capital</td>
<td>104</td>
<td>114</td>
<td>101</td>
<td>76</td>
<td>66</td>
<td>54</td>
</tr>
</tbody>
</table>

*** Resource DEL budgets were only set for the years to 2019-20 at SR15.
to address the other questions which Emer has asked.”

And then if we have a look at DFE-153056. Dr McCormick is in America at this stage, but these communications make their way to him. And you’ll see his initial response, which is that he’s just spoken to Dr Malcolm McKibbin, head of the Civil Service. He says:

“Issue is where it is, and nothing more Chris or I can do to shift it.

Unthinkable this is delayed any further.”

Again, without taking the panel back into a lot of the evidence that they’ve heard, Dr McCormick’s concern at this stage is that his Minister has approved a submission on the 22nd of January and that’s been sucked in to be considered by Timothy Johnston and others.

So, we can see DFP at this stage is pushing strongly for extreme urgency. It’s come on to your desk; you’re sending that message clearly to DETI, and Dr McCormick, I think, is displaying some frustration that, at that stage, he feels there’s nothing more that they can do, and we’ll see some further communications to that effect.

Mr Sterling: I think I would, in fairness, I would have been engaged on this earlier than that late stage in January.

Mr Scoffield QC: That was the first question I was going to ask you: can you remember —

Mr Sterling: But not in a documentary basis.

Mr Scoffield QC: OK. So can you remember when it was first brought to you and why?

Mr Sterling: [Short pause.] There would’ve been regular discussions within the Department of Finance in that period running through December into January. Obviously, we had the Chief Secretary’s letter on — I think it was the 13th of January — and that probably was the sort of final nail in the coffin when — [Cough], excuse me — when it come to any thought that there might be any additional funding. Sorry, excuse me. But I’m fairly sure I would’ve had telephone discussions with probably Andrew McCormick and perhaps others
Dr MacLean: One of the things through the evidence that appeared around the time that that Treasury decision came, which I think was December —

The Chairman: ’15.

Dr MacLean: — 2015.

Mr Stewart: Yes.

Dr MacLean: It looked like what you were saying at the time was, “Oh my God, this is DEL. Now it’s really serious”. And, what we were trying to understand was, in terms of spending public money or managing public money, it shouldn’t matter whether it’s DEL or AME; an overspend is something which is serious full stop. And we were just trying to understand why that suddenly got everybody’s attention and got action going and whether that was characteristic of either a more general treatment of AME versus DEL or a symptom of the misunderstanding of the RHI funding.

Mr Stewart: I would hope to reassure you on that point. I can absolutely understand the panel’s concern that it looks as if we only started to get worried about overspend if it had to come out of a DEL budget. That wasn’t the case. An overspend of the extent that manifested itself was a very serious matter for which we were always going to be, rightly, seriously criticised. But, whilst it was capable of being borne on the broad back of AME and some DEL, then it was at least feasible to do that. Once it reached the point where it had to be borne entirely from DEL, it’s not that it suddenly started to matter, it suddenly became completely unaffordable.

Dame Una O’Brien: That’s because you would’ve had to take it off money committed to other programmes.

Mr Stewart: Yes.

Dame Una O’Brien: So, it was more the displacement effect than —.

Mr Stewart: It’s the displacement, and, I have to say, the day that that realisation dawned
on us was a day of complete dismay, because we realised that the net effect of that was a huge opportunity cost to the Northern Ireland Executive. That money was going to have to be found from other programmes. That’s not to say that a huge overspend from AME is something that can be wished away or thought of as having no consequence. You’re absolutely right: that was taxpayers’ money. It’s our fundamental duty to spend taxpayers’ money in the way that Parliament and the Assembly require us to do.

If the overspend had come from AME, that would’ve been a very serious issue for which we would’ve been rightly criticised. Coming from DEL, it was an even more serious issue or an issue with even more serious consequences.

The Chairman: Taking that view that you’ve just said, and emphasising the seriousness of the AME overspend, makes it more and more difficult to understand why, without any clear decision by anyone, the interim cost controls were dropped. Surely they were supposed to control your budget.

Mr Stewart: Yes.

Dr MacLean: I think, Mr Stewart, in your evidence you — in your statement, you go further and suggest that the whole structure of the scheme right from the very beginning should have been designed with this in mind, is that correct?

Mr Stewart: Well, if you go right upstream, I wouldn’t have gone for this type of scheme at all; I would have gone for the competitive grant option —

Dr MacLean: Yes.

The Chairman: Well, I think everybody —.

Mr Stewart: — which I think would’ve been much easier to understand and control.

Dr MacLean: And consistent with the funding — with the funding risk —

Mr Stewart: Yes.

Dr MacLean: — in a way that the demands-driven scheme never could be.
Mr Scoffield QC: At this stage — now we’re only talking about closure in principle rather than the mechanism for delivering that — did you discern any resistance on the part of either the special adviser or the Minister to the proposition that the scheme now needs to be closed?

Mr Stewart: No, I don’t. And I think this is one of the contrasts between this period and the summer of 2015. Having said that, I think it would’ve been a brave man or woman who would’ve opposed the rationale that we needed to close.

Mr Scoffield QC: Chair, I want to move on now to a further submission of the 19th of January. There’s a couple of minutes left before lunch, just in case there’s any questions arising from what we’ve covered already.

Dame Una O’Brien: I’ve got a question. Just going to that meeting on the 11th of January 2016, I hear what you say that there was no resistance from the Minister or the special adviser but can you give us a bit more information about, well, what was their reaction to this being put in front of them? Having gone through weeks and weeks of stress and debate and trying to arrive at an agreement about what should be done in the autumn, to be presented in this, what was their reaction? What did they say?

Mr Stewart: I think the reaction was very much one of dismay, like that of officials. I don’t recall significant anger, as it were, or any apportioning of blame at that stage. I think we were all a bit shell-shocked just at the situation that we’d found ourselves in. But there wasn’t resistance, and I think there was a recognition on both the Minister’s part and Timothy’s part as well that this really was now a very, very serious situation. It was a catastrophe.

Dame Una O’Brien: Uh-huh. And what action were they requiring of you and the permanent secretary, being faced with this? I mean, obviously agreeing to its closure, but can you give us a bit more flavour of, further to their reaction, what more were they asking
Treasury would not meet costs above the Barnett consequential levels of the DECC budget.

173. However, the legislation meant we could not stop spending and we already faced problem getting a tiered tariff agreed. Also, Bernie’s position appeared to be a personal view rather than a definitive Departmental position.

174. To my recollection, shortly afterwards additional budget was provided to meet our increased expenditure. I asked that definitive confirmation be provided and this was forthcoming. Thus, extra budget was provided (and the same thing happened later in the year) just as you would expect with an AME budget.

175. We were relieved to see our budgetary needs met but not complacent as implied by the Departmental Statement. The fact that the budget appeared to be treated as “traditional” AME did not slacken our efforts to introduce the tiered tariff.

176. The documentation from the 2015 Autumn statement appeared to confirm the status of the RHI budget as AME. However, the end of this strand of the RHI was confirmation (21 December 2015) that Treasury had said that monies above the DECC RHI Barnett consequential budget ceiling would need to be met from the NI Block. At that point I knew we had to close the scheme as soon as possible. I drafted a submission by the end of December 2015 and advice was submitted in January inviting the Minister to close the scheme (see Departmental Annexes 124 and 125).

177. Thereafter events proceeded rapidly through Ministers to the Finance Minister, the Executive, the Departmental Committee and the Assembly. The basic issue was really the balance of legal and financial risk – effecting swift closure versus giving reasonable warning. The exceptional budgetary circumstances justified actions (foreshortened warning period, no consultation, no Committee procedure) which would not have been justified at earlier periods.
Mr Scoffield QC: OK so, come the end of January, energy division’s role is giving effect to often shifting instructions as to timescale, but the key decision-making at that stage is happening, from your perspective, elsewhere and outside your immediate purview.

Mr Mills: Oh, yes, at the highest political levels, and between the head of the Civil Service and the head of — and the current head of the Civil Service, then head of the Department of Finance and Personnel, were becoming involved.

Mr Scoffield QC: I want to look, then, principally in your evidence at what happens in December and, maybe more so, in January 2016. And the key submission, I think, which recommends closure of the scheme comes to the Minister on the 31st of December 2015. But I just wanted to ask you about the timing of that submission. I think we know that you begin drafting that submission on or about the 23rd of December 2015.

Mr Mills: Chris Stewart says to me, or sent me a note, on the 21st saying, “the game’s up; we have to pay for this”. And we start drafting it on the 21st. And, by the 23rd, I think I send out a draft and then, by the 31st, various comments have been received and the submission goes up to the Minister on the 31st.

Mr Scoffield QC: Just to give the panel some context for that: in Mr Mills’ first statement, at paragraph 176, he says that it was the 21st of December when you knew that you “had to close the scheme as soon as possible.” And I think “the game’s up” email is at DFE-10325. That particular phrase is not used. But if we go to 10325, we see there that Chris Stewart says that:

“Andrew” —

that’s Andrew McCormick has advised him that —

“David Stirling has confirmed the HMT stance on RHI – expenditure over and above the Barnett share will have to be found from within NI resource DEL. DFP is very concerned, and will ask us formally for proposals to close/suspend the schemes as soon as possible.”
So then he asks you, in the first instance:

“for a quick note ... setting out the options and critical path”.

So it was on that date that, really, the course was set that a recommendation to close would be made to the Minister.

A question I wanted to ask you just about that is: how come it took so long to get to that position? And I say that partly because the November spending review had obviously happened about a month before but, even before that, if we just look very briefly at DFE-10251. This is an email from Stuart Wightman on the 13th of November. Now, this is, really, explaining what was happening in terms of the spike. And we see, just at the bottom of the screen there, he’s talking about the surge in applications. Now, he’s sending this to Mr Stewart, so he’s almost going above your head, as it were, copying in a number of the top management team. And if we just go to the bold text, he says:

“I feel that in light of this situation regardless of what impact the amendment regulations might bring there is no choice now but to move to close both RHI schemes”.

Now, he’s talking about closing them from the 31st of March 2016 but, mid-November, he’s saying, “We’ve no option but to close”. So, I just wonder if you can explain for the panel why it took until the 21st of December for Mr Stewart to say to you, in your words, “The game’s up”.

Mr Mills: Uh, well, I mean, we wouldn’t have — I think Stuart’s responding to the spike there and the realisation of how much the money’s — how much money is now involved. I think we were probably waiting to see what the outcome of the spending review was to see what the actual — to see what the real impact was. Um, and also I think it may still have been an open question, then, whether the scheme was going to be closed down across the UK. Um, so, uh, I think the thought would have been, then, that it was premature to move, uh, before the spending review outcome, which was 25 November.
Mr Scofield QC: After the 25 November spending review —.

Mr Mills: Um, after 25, uh, November spending review, um, there is another email which, I think, shows that there is an acceptance in principle that it may be, um — that we may be, uh, are agreed on closure, but on something like the 8th of December there seems to be —. Because if we — if we accept that, um — that we have to close, it is also accepting that — the DEL consequence, I think, by that stage. And there is a last-ditch attempt by DFP to, um — to engage with Treasury to argue for the money for Northern Ireland, and that’s about the 7th of December, and we provide arguments for then —

Mr Scofield QC: So it was a —

Mr Mills: — for that meeting.

Mr Scofield QC: — hope against hope, really, that HMT would change its position?

Mr Mills: Yes, I guess so.

Mr Scofield QC: And it’s 21st of December that the final word comes back that that’s just not going to happen, and that’s when things shift into a different gear?

Mr Mills: Yes.

Mr Scofield QC: Now, I just want to have a look briefly at the submission of the 31st of December, and we find that at DFE-287880.

Dr MacLean: Just while we’re waiting for that. So, on the 21st of — was it the 21st of December — there’s confirmation of what ultimately the original letter from Jon Parker had indicated was going to happen? That you had the full DEL consequence of the of the overspend? That’s ultimately what’s happened on that day, is that correct?

Mr Mills: Well, I’d always interpreted the Parker email as the 5% penalty, but if you — if you take the view that the —.

Dr MacLean: Take the entirety of the material which you’ve now seen. It does rather seem that the character of the funding is absolutely fundamental to how the Department —
not just the Department, the whole Executive — was thinking —

Mr Mills: Yes.

Dr MacLean: — at that time. So, as long as it was AME — as long as there was somebody else paying for it — it was fine, but then, my God, the real consequences suddenly become clear on the 21st, and then, as you say, everything completely changes. That rather does suggest that the character — the nature of the funding has that fundamental impact on how people treat it and how decisions are made.

Mr Mills: Yes, fair enough. I think that’s — that’s undeniable. I think that — I think what I would contend with personally is that, “It was AME and you didn’t care”. So, from July, we — 2015 — we do get all the money, and we are still trying to get tiering in to control that. Of course we didn’t. The spike then escalates the magnitude of the problem — doubles it again, nearly, um, which is, I’m sure, why — what Stuart’s reacting to in his emails. But I — the fundamental point you make is, um, that, um, when we — when it was known there was a full DEL consequence, yes, the system reacted in that way. But I suppose you could say, in 2015, there was a risk that it was that. By December, that risk was a reality. So, you’re reacting to the fact that you don’t have — you need 20 million that you didn’t budget for, or however much, in the Northern Ireland Executive’s budget.

Dame Una O’Brien: A risk that wasn’t really, perhaps, fully spelt out in that 8th of July submission?

Mr Mills: Uh, or there was not clarity until December, given that the — um, the, um —. I can only speak from my understanding, which was that there was a 5% penalty. We got that money. We got the AME money in, um, July. Dr MacLean’s quite right: when it was known that there was — it was gonna have a DEL impact, the system moved to close down the scheme.

Mr Scoffield QC: I think the submission that we see — I’m not gonna take you through it
John

Andrew advises me that David Stirling has confirmed the HMT stance on RHI – expenditure over and above the Barnett share will have to be found from within NI resource DEL. DFP is very concerned, and will ask us formally for proposals to close/suspend the schemes as soon as possible.

May I ask you, in advance of a formal submission to the Minister, for a quick note to Andrew and me, setting out the options and critical path for suspension/closure. May I also ask you and Stuart to consider the consequences for the Energywise project, assuming that resource will have to prioritised towards RHI.

Chris
Mr Scoffield QC: OK so, come the end of January, energy division’s role is giving effect to often shifting instructions as to timescale, but the key decision-making at that stage is happening, from your perspective, elsewhere and outside your immediate purview.

Mr Mills: Oh, yes, at the highest political levels, and between the head of the Civil Service and the head of — and the current head of the Civil Service, then head of the Department of Finance and Personnel, were becoming involved.

Mr Scoffield QC: I want to look, then, principally in your evidence at what happens in December and, maybe more so, in January 2016. And the key submission, I think, which recommends closure of the scheme comes to the Minister on the 31st of December 2015. But I just wanted to ask you about the timing of that submission. I think we know that you begin drafting that submission on or about the 23rd of December 2015.

Mr Mills: Chris Stewart says to me, or sent me a note, on the 21st saying, “the game’s up; we have to pay for this”. And we start drafting it on the 21st. And, by the 23rd, I think I send out a draft and then, by the 31st, various comments have been received and the submission goes up to the Minister on the 31st.

Mr Scoffield QC: Just to give the panel some context for that: in Mr Mills’ first statement, at paragraph 176, he says that it was the 21st of December when you knew that you “had to close the scheme as soon as possible.” And I think “the game’s up” email is at DFE-10325. That particular phrase is not used. But if we go to 10325, we see there that Chris Stewart says that:

“Andrew” —

that’s Andrew McCormick has advised him that —

“David Stirling has confirmed the HMT stance on RHI – expenditure over and above the Barnett share will have to be found from within NI resource DEL. DFP is very concerned, and will ask us formally for proposals to close/suspend the schemes as soon as possible.”
Private Office

Please see attached *desk immediate* submission from John Mills for the Minister’s attention.

Regards,

Laura McCoy
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NI Year of Food & Drink 2016

Please consider the environment - do you really need to print this e-mail?
From: John Mills

Date: 31 December 2015

To: 1. Timothy Cairns
    2. Jonathan Bell MLA

Copy Distribution List below

FUTURE OF RENEWABLE HEAT INCENTIVE

Issue: Future of Northern Ireland Renewable Heat Incentive (RHI)

Timing: A decision is needed immediately to pursue the necessary legislative changes to minimise overspending on the existing scheme.

Executive Committee Referral: Yes. Paragraph 2.4 of the Ministerial Code requires referral of matters that have implications for the PfG (10% target not being reached if scheme closed) or are “significant or controversial” which this would be. It might also be considered cross cutting.

PFG Implications: The PfG targets for renewable heat are 4% by 2015 and 10% by 2020.

Presentational Issues: Likely to attract criticism given the scale of the unapproved expenditure

FOI Implications: Not discloseable on grounds of policy development.

Financial Implications: Treasury has indicated that the cost overrun may need to be covered from the Executive’s Resource DEL which, if confirmed, would imply a substantial opportunity cost to DETI or other NI Block services.

Legislation Implications: Any changes to the scheme require, at least, affirmative resolution regulations.

Statutory Equality Obligations: Equality screening suggests the proposed Regulations do not have a significant impact.

Recommendation: That you:
- agree to close (or suspend) both RHI schemes as soon as possible;
- agree to procure additional audit checks for the Non Domestic RHI scheme.
BACKGROUND

1. The Non-domestic RHI scheme was introduced in November 2012. The Domestic RHI scheme in December 2014. Both schemes provide payments for people to move from conventional heating (mainly oil) to sustainable heating such as wood pellets (biomass). In light of unprecedented applications over the last 2 months for the Non Domestic Scheme, the outcome of the Government's Spending Review, and consideration by DFP and HMT of developments in respect of the non-domestic scheme here, an urgent decision is now needed on the future of the NI RHI schemes.

SCHEME PERFORMANCE

2. Successful domestic RHI applicants receive an upfront payment of up to £3,500 (depending on the technology) along with 7 annual tariff payments based on the heat requirements of the property. Annual payments are typically around £1,200 but are capped at a maximum of £2,500. Uptake of the Domestic RHI scheme has increased steadily (c.700 applications since the scheme was introduced).

3. The Non Domestic RHI scheme on the other hand involves 20 years of annual tariff payments based on the metered heat usage of the business. Tariffs are dependent on the type and size of technology. To date, average annual payments of been around £24,000. The Non Domestic scheme therefore involves larger and longer financial commitments than the domestic scheme.

4. After a slow start during the first two years, non-domestic scheme uptake increased steadily during 2015. During the Autumn of 2015 there was a surge in applications. This increase relates to one particular technology – biomass and has been attributed to one particular industry’s wholesale uptake of the scheme. This is the poultry industry’s use of RHI for chicken sheds. Uptake of the non domestic scheme and an estimate of indicative expenditure is summarised in the table below.

<table>
<thead>
<tr>
<th>Period</th>
<th>Application Numbers</th>
<th>Annual Cost</th>
<th>20 Year Cost</th>
</tr>
</thead>
<tbody>
<tr>
<td>Nov 2012 – March 2015 (Previous Commitments)</td>
<td>522</td>
<td>£12.3m</td>
<td>£246m</td>
</tr>
<tr>
<td>April 2015</td>
<td>85</td>
<td>£1.1m</td>
<td>£22m</td>
</tr>
<tr>
<td>May 2015</td>
<td>66</td>
<td>£1.4m</td>
<td>£28m</td>
</tr>
<tr>
<td>June 2015</td>
<td>49</td>
<td>£1.3m</td>
<td>£26m</td>
</tr>
<tr>
<td>July 2015</td>
<td>42</td>
<td>£0.9m</td>
<td>£18m</td>
</tr>
<tr>
<td>August 2015</td>
<td>55</td>
<td>£1.1m</td>
<td>£22m</td>
</tr>
<tr>
<td>September 2015</td>
<td>90</td>
<td>£2.14m</td>
<td>£42.8m</td>
</tr>
<tr>
<td>October 2015 (up to 28/10/15)</td>
<td>441</td>
<td>£9.8m</td>
<td>£196m</td>
</tr>
<tr>
<td>Total for Retrospective Period (1/4/15 – 28/10/15)</td>
<td>828</td>
<td>£17.74m</td>
<td>£355m</td>
</tr>
<tr>
<td>November 2015 (29/10/15 – 29/11/15)</td>
<td>452</td>
<td>£9.95m</td>
<td>£199m</td>
</tr>
<tr>
<td>December 2015 – March 2016 (forecast)</td>
<td>80</td>
<td>£1.92m</td>
<td>£38.4m</td>
</tr>
<tr>
<td>Total for Prospective Period (29/10/15 – 31/3/16)</td>
<td>532</td>
<td>£11.9m</td>
<td>£238m</td>
</tr>
<tr>
<td>Total Forecast Commitments to 31 March 2016</td>
<td>1882</td>
<td>£41.94m</td>
<td>£839m</td>
</tr>
</tbody>
</table>
5. The sustained increase in applications during March and April was the catalyst for the legislative changes you recently took through the Assembly to, inter-alia, introduce a tiered tariff (reducing after 1,314 hours) and an annual cap (at 400,000 KWh) on RHI payments for biomass. However, in the run up to these legislative changes, scheme uptake has rocketed with a further 900 applications received in 6 weeks. An increase in applications had been forecast as businesses try to beat the deadline, but not at the numbers we received.

6. The increase in applications means that over 167MW of renewable heating capacity has now been installed under the non domestic scheme. This equates to between 6.7% - 8.3% of total installed capacity under the GB non domestic scheme. It is estimated that over 6% of NI's total heating needs are now provided through renewable technologies. The PfG target of 4% renewable heat by 2015 has been exceeded and we're well on our way to achieving the Executive's 2020 target of 10%. However, this success comes at a price. Total expenditure for both RHI schemes in 2015/16 is now forecast to exceed £30m. Even if no new applications are received in 2016/17 (i.e. both schemes are suspended/closed on 31/3/16), forecast RHI expenditure in 2016/17 is expected to be around £42m.

**DFP APPROVAL**

7. When the non-domestic scheme was established in 2012, DETI sought and obtained approval of a business case from DFP and one of the conditions was for re-approval in March 2015. Unfortunately the need for this approval was overlooked. DETI had no choice but to keep making the payments because the RHI scheme is set out in statutory Regulations and there are no grounds for DETI to cease making payments to properly made applications.

8. DFP approval was subsequently sought for retrospective and future operation. Prospective approval has now been received from DFP for scheme expenditure from 29 October 2015 through to 31 March 2016 on certain conditions which include, tariff changes (done), a review and a further approval from March 2016. Retrospective approval from 1 April 2015 to 30 September 2015 has, as of 21 December, been declined, because we cannot meet the test that had we sought approval at the time it was required, DFP would have been able to approve.

**AFFORDABILITY**

9. The affordability of RHI going forward obviously depends on the budget available. The RHI schemes (non-domestic and domestic) are paid out of AME. To quote the HMT Autumn Statement of 2015, “the UK government provides funding for certain programmes which are devolved....if they are not only demand-led but also may be volatile in a way that could not adequately be controlled by the devolved administration”. It goes on to give assurance that devolved administrations do not have to find off setting savings for increases but

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1 The NI Renewable Heat Incentive is listed as a NI Executive AME Programme at Table E3 of the HMT Statement of Funding Policy – funding the Scottish Parliament, National Assembly for Wales and NI Assembly – November 2015.
warns that they may have to fund schemes that are more generous than elsewhere in the UK.

10. However, when the scheme was first introduced in 2012, HMT confirmed that RHI spending would not be treated as standard AME, where the Exchequer takes on all risks. Instead, there is a risk-sharing arrangement whereby, should RHI spending in one year exceed the allocated budget, NI would need to repay this in future years. This could be achieved through scheme changes. However, the rules provided that a small proportion of any required future savings (likely to be of the order of 5%) would have to be funded directed by NI through DEL.

11. Also, unlike traditional AME, the initial 4 year (2011/12-2014/15) NI allocation of £25m was based on a Barnett formula of c.3% of the DECC budget (£838m). HMT confirmed that any 20 year commitments entered into during this period would be honoured. This arrangement was rolled forward in 2015/6 though the AME 2015/16 budget has since been raised to £23m in light of increased demand.

12. If RHI funding was “pure” AME there would be no impact on NI DEL (of course, we would still need to take action due to the sharp increase in costs). If the Barnett formula + 5% penalties approach was carried forward the effect on NI DEL would be relatively small – generally less than £1m p.a. over the 2016/17–20/21 period (this assumes scheme closure in March 2016).

CHANGE IN HMT POLICY

13. However, the effect of the Chancellor’s Autumn Statement was to reduce the NI RHI budget and, on 21 December, DFP advised that HMT’s likely position will be that NI will have to cover the full costs (not 5%) of any overspends. This creates significant budgetary pressures for the next 5 years with additional average annual costs of around £15m even if there are no new applications after the end of this financial year.

14. Discussions between DFP and HMT are ongoing but we must proceed on the basis that the major overspend that has now arisen will not be covered by HMT.

OPTIONS

15. The combination of lack of HMT funding and DFP approval together with DETI’s ongoing, legal obligation to keep making RHI payments means there is very little scope for action other than to close/suspend the scheme as quickly as possible. However, the options are:

- **Do nothing (i.e. keep the RHI scheme open).** This would help reach the Executive target of 10% renewable heat by 2020, help reduce greenhouse gas emissions, contribute to the UK’s renewables obligations and support the local renewables industry (at a time when other support, in the form of NIRO, is being withdrawn). It is assumed that anything above the HMT proposals

\[2\] Costs in the first year (i.e. 2016/17) would be higher and gradually diminish as time went on. This is because, if the scheme was closed to new applications, its costs would remain static while the allowed HMT budget would rise thus reducing the estimated NI scheme overspend from around £23m in 2016/17 to around £7m by 2020/21.\]
would have to be funded from DEL. The shortfall from 2016/17 - 2020/21 is estimated to be around £165m (roughly £30m pa). However, experience has taught us that the scheme is extremely difficult to predict and there would be a risk that actual expenditure could be higher. Finally, we simply do not have funding for existing commitments over the HMT figures, let alone any extra. Following this course would require Executive agreement – which is unlikely given existing overspend and the DEL impact.

- **Continue domestic scheme only.** The funding problems have arisen in respect of the non-domestic RHI, principally as a result of the increase in installation under one tariff (biomass) for one industry (poultry). The domestic scheme is much more evenly distributed in terms of technologies and has been steadier in terms of growth. It could be asked why the domestic scheme should suffer as a result of events on the non-domestic side. Separating out the two schemes to close the non-domestic and leave open the domestic might cost a total of £105m over the five years 2016/17-2020/21 (something like £20m pa). Keeping open the domestic scheme may help mitigate an adverse industry reaction. However, HMT do not distinguish between the two schemes so keeping open the domestic scheme adds costs to existing non-domestic overspend. In addition, there is a risk that the domestic scheme would prove unpredictable. If non-domestic markets were no longer available, supplier efforts could be targeted on the domestic market resulting in a spike in applications.

- **Close (or suspend) both schemes as soon as possible.** Given the funding situation arising from HMT’s proposals (and DFP conditions for approval of the non-domestic scheme to March 2016) there seems little choice but to bring potential increases in scheme costs to as swift an end as possible. If both schemes are closed to new applications by April 2016 the costs might be around £75m over the five years (around £15m p.a.). However, opposition from the industry (including legal action) can be anticipated. There is also the risk of increasing costs in the short term by setting a deadline which suppliers then attempt to achieve. The latter risk could be avoided by giving no notice of scheme closure. On the other hand such action would increase risk of legal challenge – particularly from those who have invested in installation only to find they cannot get the anticipated RHI payments (RHI installations have shorter lead times than NIRO projects – typically 6 weeks). It may be possible to keep some options open by suspending rather than finally closing the schemes, though we would not recommend doing so if that would lead to any delay. We are seeking legal advice on the issues around closure and will advise further on this and the suspension option as soon as possible. Inevitably there would be some public warning, even if there was no notice, as the policy and legislation would have to be progressed through the Committee and Assembly (and the Executive prior to that).

**CONCLUSION**

16. To minimise further overspending and to meet the conditions of DFP’s approval, we now have no choice but to close both the non-domestic and domestic schemes as soon as possible. This may seem drastic but, as the RHI payments are for 20 years, the funding risk is very serious indeed. Separate advice on handling will be submitted once you agree the policy approach.
NEED FOR ADDITIONAL AUDITING OF NON DOMESTIC RHI SCHEME

17. There have been recent anecdotal claims that applicants are abusing the NI Non Domestic RHI Scheme. This issue was recently raised at the DETI Audit Committee. Although we currently have no evidence to support these claims, it is recommended that additional audits are completed for the NI Non Domestic RHI scheme.

18. The Non Domestic RHI scheme administered on DETI’s behalf by Ofgem (the GB gas and electricity regulator) which also administers the GB domestic and non domestic schemes. Ofgem’s administration costs for the NI scheme are based on 3% of the GB scheme costs. Ofgem complete an annual programme of audits for the GB and NI schemes which includes desk based analysis and on-site checks. In 2015/16, Ofgem will be competing 200 detailed site audits for the GB Scheme. This translates into 6 site audits for the NI scheme.

19. In light of the increased number of applicants and recent claims of scheme abuse, we are arranging for additional audits to be completed by Ofgem this year. However each audit will cost around £1,000. This is because Ofgem have to procure an external assurance provider to travel to NI to conduct the audits. In the longer term, it would be more cost effective to procure a separate local assurance provider. A Business Case will therefore be prepared for an additional audit programme from 2016/17 to complement Ofgem’s current systems of assurance and control. This might cost in the region of £100K.

Recommendation

20. That you:

- Agree to close (or suspend) both RHI schemes as soon as possible; and
- Agree to procure additional audit checks for the Non Domestic RHI scheme.

JOHN MILLS
Energy Division
Ext. 29215

cc: Andrew McCormick
    Chris Stewart
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    Stuart Wightman
    Trevor Cooper
    Rob Robson
    Ian McCrea MLA APS
    Sean Kerr
    Press Office