

**The Report of the  
Independent Public Inquiry  
into the Non-domestic  
Renewable Heat Incentive (RHI)  
Scheme**

**Volume 3 — Chapters 42–56  
&  
Appendices**



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**The Report of the Independent Public Inquiry into the  
Non-domestic Renewable Heat Incentive (RHI) Scheme**

**and**

**Department of Finance**

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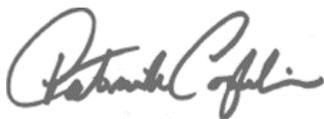
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**ISBN 978-1-912313-36-5**

**Printed in the United Kingdom by  
Digital Print Services  
of the Northern Ireland Department of Finance**

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## Chapter 42 – Audit investigations in 2016

42.1 After the suspension of the NI non-domestic RHI scheme, a number of steps were undertaken to find out more about the scheme and what had gone wrong with it. This was partly in response to the anonymous allegations provided to First Minister Foster in January 2016, which were passed to DETI and then passed to Internal Audit for investigation.

### The Comptroller and Auditor General's report

42.2 Before the DETI Internal Audit report was finalised, however, as noted in the introduction to this Report, Kieran Donnelly, the Comptroller and Auditor General for Northern Ireland published a report on the DfE Resource Accounts on 1 July 2016.<sup>2166</sup> Mr Donnelly's report confirmed the following basic conclusions (each of which have been dealt with in considerable detail already in this Report):

- Commitments under the scheme had exceeded the maximum amount that HM Treasury was prepared to fund. The excess funding would now have to be met from the NI block grant. Over the next five years, this addition to the NI block was estimated to be £140 million and significant costs would continue to be incurred until 2036.
- The Department failed to obtain required approvals from DFP for £11.9 million of expenditure over a seven-month period during 2015-16 (from the expiry of the original DFP approval on 30 April 2015 to the DFP grant of prospective approval only on 29 October 2015, discussed in chapter 33).
- The original design of the scheme did not introduce 'tiering' of payments as operated in GB where a reduced rate was applied after the equipment had been operated for 15% of hours in a year. Such tiering would have helped prevent potential abuse of the scheme by operating the equipment simply to increase the grant received.
- The scheme in GB also used 'degression', which allowed the amount of subsidy paid to change quarterly in response to changes in demand. From 2012 to 2016 the rates paid in GB fell by 50% while the rates in NI increased.
- Returns available to claimants under the scheme in NI appeared to be excessive and were guaranteed for the next 20 years.<sup>2167</sup>

42.3 Mr Donnelly also pointed out that since DFP had not approved the £11.9 million of expenditure in the seven-month period during 2015-16 such expenditure was irregular. Consequently, he qualified his opinion on the 2015-16 Department Resource Accounts as the expenditure had been incurred without conforming to the authorities which governed it.<sup>2168</sup>

42.4 A highly significant feature of the NIAO report was that it identified the existence of the perverse incentive, namely that as tariff levels were in excess of the cost of fuel, the subsidies available under RHI could incentivise scheme participants to waste heat simply to earn income under the scheme. Many witnesses, particularly those within the Civil Service, told the Inquiry that it was through the exposition of this issue by the NIAO that they first realised that, and how, the scheme provided such an incentive.

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2166 CAG-04049 to CAG-04068

2167 CAG-04050

2168 CAG-04052

42.5 On 12 May 2016, following Assembly elections, Simon Hamilton had been appointed Minister for the Economy, succeeding Minister Bell as the Minister in charge of the Department which had responsibility for RHI (now re-named the Department for the Economy). Publication of the NIAO report was followed by a press release from Minister Hamilton on 4 July 2016. In that press release Minister Hamilton said:

“The Audit Office’s findings in respect of the Renewable Heat Incentive scheme (RHI) are deeply shocking and catalogue multiple failings in the design and administration of this scheme. The potential ongoing costs of this scheme to Northern Ireland taxpayers are incredible and the accusations of fraud will be vigorously investigated.

Whether it is the absence of tiered tariffs or controls on costs, at various stages of the scheme there were serious systemic failings and opportunities were missed to remediate the situation by those directly responsible for administering the scheme.”<sup>2169</sup>

42.6 Minister Hamilton noted that he had held meetings with senior officials about the RHI scheme and that external consultants were being appointed to conduct on-the-spot and thorough inspections of installations to ensure that they met the spirit and letter of the scheme. Consideration was being given to options for controlling the costs of the scheme and “lessons must be learned for the future to ensure this type of situation never arises again.”<sup>2170</sup> In the event, the consultancy firm PwC was awarded the contract to conduct an independent review of the RHI scheme.

42.7 The publication of the NIAO report, however, and the consequential institution of an inquiry by the Assembly’s Public Accounts Committee, understandably resulted in a significant amount of concerned public attention.

## The DfE Internal Audit report

42.8 On 4 August 2016 an Internal Audit Service report was published by the DfE auditor, Michael Woods.<sup>2171</sup> The audit fieldwork for that report had been undertaken during the period December 2015 to April 2016.<sup>2172</sup> In expressing the overall audit opinion, he stated:

“Internal Audit considers that the system of risk management, control and governance established by management over the Non Domestic Renewable Heat Incentive Scheme is **Unacceptable**.”<sup>2173</sup> (Mr Woods’ emphasis)

42.9 He noted that the scheme had been formally closed to new applications from 29 February 2016, at which point a total of 2,128 applications had been received over the life of the scheme and that, if all applications (many of which were still awaiting accreditation decisions) were found to be valid, approved and funded, the potential annual liability for 2016-17 was estimated at £50 million. The funding available from HM Treasury, based on 3% of DECC’s projected budget (£640 million) was estimated at only £18.3 million. Mr Woods considered that the consequence of the shortfall between the scheme’s commitments and the available

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2169 POL-00127 to POL-00128

2170 POL-00128

2171 DFE-223638 to DFE-223682

2172 DFE-223640

2173 DFE-223653

- HMT funding meant that there was a potential shortfall of £140 million in the period 2016-17 to 2020-21 and that this could rise to approximately £450 million over the life of the scheme.<sup>2174</sup>
- 42.10 Internal Audit considered that the NI RHI scheme was inherently vulnerable to the risk of any sudden major increase in demand, which was further exacerbated by the limited nature of the funding. Its report concluded that the scheme should have adopted robust cost control measures and that it lacked an appropriate automatic response which would have allowed it to close to new applicants until such time as additional budget was secured.<sup>2175</sup>
- 42.11 Despite being advised by Energy Division that formal programme/project management structures had not been adopted due to the small number of staff involved, Internal Audit considered that adopting a recognised structured programme/project framework would have been beneficial.
- 42.12 It was also noted that, despite the commitment given to the Casework Committee in this regard, the establishment of a Budget Monitoring Committee (BMC) had not been effected. A programme oversight board would have provided a challenge role on delivery of outcomes for the programme, the programme plan, programme budget and programme risks. A programme oversight board might also have reached a different view of the risks potentially likely to arise from the decision to prioritise introduction of the domestic RHI scheme in 2014 without the cost control structure that had been proposed and consulted upon in respect of both schemes.<sup>2176</sup>
- 42.13 The internal auditor's report also commented adversely on: the absence of a clearly documented fraud risk strategy for the NI RHI scheme; the omission to prepare for and obtain DFP reapproval of the business case in 2015; the loss of key members of the team together with their organisational knowledge in late 2013/early 2014; the Department's over-reliance on Ofgem for the administration and control of the scheme without adequate oversight arrangements; the lack of the Department's own programme of independent on-site inspections; and the failure to carry out regular monitoring to ensure that initial assumptions around VFM remained valid.<sup>2177</sup>
- 42.14 The Inquiry notes that the category 'Unacceptable' is the lowest audit opinion/assurance level, indicating that the system of governance, risk management and control has failed or that there is a real and substantial risk that the system will fail and that urgent action is required to improve the adequacy and/or effectiveness of governance, risk management and control. Indeed, the auditor, Michael Woods, said in his oral evidence to the Inquiry that he had never reached a conclusion of 'Unacceptable' in any other audit and that his conclusion in the RHI audit was "the worst opinion" he had ever had to give.<sup>2178</sup>

## The RHI Task Force

- 42.15 In response to the difficulties with the scheme and its governance, which had been identified in both of the above reports, the RHI Taskforce was established by the Permanent Secretary of DfE in December 2016/January 2017 with the key aim of bringing the non-domestic RHI scheme back in line with policy, budget and governance requirements.<sup>2179</sup> In the summer of 2017 the Strategic Investment Board (SIB) was approached to support the work of the RHI Taskforce and

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2174 DFE-223653 to DFE-223654

2175 DFE-223657 to DFE-223658

2176 DFE-223660

2177 DFE-223664 to DFE-223680

2178 TRA-16070

2179 WIT-23911; WIT-00025

in July 2017, following approval by the Civil Service Commissioners, Richard Rodgers, a project director with experience of the commercial energy sector, was then appointed as Head of the Taskforce, with Stephen McMurray, who had been Taskforce Head prior to that point, remaining a member of the Taskforce in the post of Director.<sup>2180</sup>

- 42.16 The Taskforce is run as a formal project with governance utilising PRINCE2 methodology including a project board meeting every six weeks to take key policy decisions and an oversight board providing a wider external perspective.<sup>2181</sup> In addition, an NI RHI operational board meets monthly chaired by Ofgem, membership of which includes the Director, RHI Taskforce.<sup>2182</sup> A detailed written statement dealing with the structure and work of the Taskforce to date was provided to the Inquiry on 22 October 2018.<sup>2183</sup>

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2180 WIT-23910 to WIT-23911; WIT-00025

2181 WIT-23916 to WIT-23917

2182 WIT-23918

2183 WIT-23908 to WIT-23971

## Findings

- 223.** Like the NIAO report which was prompted by the irregularity of Departmental spend on the RHI scheme (arising from the lapse in DFP approval), the DfE Internal Audit report managed, within a relatively short period of time after the closure of the scheme, to identify a number of the significant failings and problems with the scheme and its administration, which are dealt with in further detail in this Report. It was an effective and helpful piece of work which the Inquiry hopes has already led to lessons being learned within DfE. It is unfortunate that Internal Audit's expertise was not brought to bear on the scheme in a more focused way earlier (an issue addressed in further detail later in this Report at chapter 55).



## Chapter 43 – New tariff proposals and the 2017 regulations

### Work on further plans to limit the RHI overspend

- 43.1 Despite the amendments to tariffs in November 2015 (including the introduction of tiering) and the closure of the scheme to new entrants in February 2016, expenditure was still well over the allocated budget and discussions continued throughout 2016 and into 2017 about further measures to bring spending within budget. These discussions were informed by the work of DfE’s Internal Audit Service and the NIAO which are discussed in the previous chapter of this Report.
- 43.2 At a meeting between DoF Supply and DfE officials on 17 October 2016, DfE officials indicated that they aimed to have a paper with their Minister by the end of October seeking his approval to consult on new draft regulations that would further amend the tariffs for the scheme.<sup>2184</sup> They also indicated that they intended to undertake a pre-consultation with major stakeholders prior to the main public consultation concerning the new draft regulations.<sup>2185</sup>
- 43.3 Upon being asked by DoF officials whether DfE was under a duty to consult, DfE officials stated that although there was no statutory duty to consult “strong advice from DSO” indicated that they should do so. However, they agreed to seek further legal advice as to whether consultation could be speeded up.<sup>2186</sup> DoF officials indicated that, as a consequence of the challenging nature of the cuts that would be announced, RHI would come under renewed scrutiny and DfE should explore every option available to reduce the overall cost of the scheme and take all actions as necessary moving forward.
- 43.4 At this stage DfE officials enquired as to whether it would be possible to go back to HMT for additional funding in the light of the high take-up of the scheme in Northern Ireland. DoF officials confirmed that this point had been raised with HMT following the Autumn Statement in 2015 but that HMT had confirmed the final position to be as set out in the January 2016 letter, namely that Northern Ireland would have to bear the cost of the overspend.<sup>2187</sup>
- 43.5 On 28 October 2016 Mr Wightman, who had been one of the officials present at the 17 October meeting, advanced a submission to Minister Hamilton and his SpAd, John Robinson.<sup>2188</sup> The submission related to the possible introduction of new controls with regard to the non-domestic RHI scheme in respect of which Mr Wightman advised that it was essential to bear down on future costs as soon as possible and that the aim was to launch a consultation in mid-November.<sup>2189</sup>
- 43.6 Minister Hamilton was reminded that the tariffs under the RHI scheme were subject to the ‘grandfathering principle’, meaning that “scheme participants would be guaranteed the tariff for the lifetime of the scheme.” This was to encourage investment by ensuring that scheme participants would receive the average rate of return of 12% over the 20 year lifetime of the technology, which had been the subject of the scheme’s EU State Aid approval. However,

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2184 DOF-09283 to DOF-09286

2185 DOF-09284

2186 DOF-09285

2187 DOF-09285 to DOF-09286

2188 DFE-137930 to DFE-137934

2189 DFE-137930

Mr Wightman now warned the Minister that many RHI participants who were in receipt of the medium biomass tariff prior to 18 November 2015 were set to receive much higher rates with the average rate of return for 99kW biomass boilers being likely to be between 49% and 109% depending on the initial capital outlay.<sup>2190</sup>

- 43.7 Details of the (then) recent PwC review of installations with regard to potential exploitation of the scheme were provided by Mr Wightman. He explained that the initial view from the European Commission was that any amendments to the tariff would be ‘notifiable’ (meaning that they required notification to be given to the Commission under EU State Aid rules) even if they involved tightening of the criteria for granting State Aid.<sup>2191</sup> He referred to the fact that DfE was developing cost control proposals aimed at bringing rates of return back within reasonable levels in line with the State Aid approval; but no detail regarding those proposals was provided. However, recognising that any reductions in the rate of subsidy were likely to be contentious, Mr Wightman sought approval to engage with two key industry players, the UFU and Moy Park, together with Biomass Energy Northern Ireland (BENI), a body which was heavily involved in the production, marketing and use of biomass, and CAFRE.<sup>2192</sup>
- 43.8 The Inquiry also notes that the submission recorded the view that it would be beneficial to speak to ‘Heatboss’, the energy efficiency company whose representative, Ms Janette O’Hagan, had previously met department officials and whose interactions with DETI at earlier junctures have been discussed in detail earlier in this Report.<sup>2193</sup>
- 43.9 Dr McCormick saw this submission for the first time on 26 October 2016 and did not see any difficulty with the main proposal to engage in pre-consultation with some key stakeholders. He focused primarily upon the hope and expectation that the views of the European Commission would provide a strong argument to reduce the flow of payments to pre-November 2015 scheme participants.<sup>2194</sup> Dr McCormick later changed this view, subsequent to a conversation with Ms Emma Little-Pengelly MLA at a lunch event in Titanic Belfast on 3 November 2016, when he was persuaded by Ms Little-Pengelly that the scheme was so riddled with difficulty that moving directly to closure, with compensation to scheme participants, but without consultation, would be a better approach.<sup>2195</sup>
- 43.10 There does not appear to have been a response from Minister Hamilton to the submission until a telephone call to Dr McCormick on or about 16 November 2016.<sup>2196</sup> Minister Hamilton said that there were weekly meetings with officials in which he asked for updates, although he accepted that he had not laid down a timetable for a paper.<sup>2197</sup> In contrast, Dr McCormick told the Inquiry that:

“Simon Hamilton made it clear to us that we should not be using issues meetings to nag him about submissions that had not been cleared.”<sup>2198</sup>

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2190 DFE-137931

2191 DFE-137932

2192 DFE-137933

2193 DFE-137933

2194 WIT-26443 to WIT-26444

2195 WIT-10531

2196 WIT-26444 – although Dr McCormick stated in this part of his witness statement that he believed the telephone call took place on 17 or 18 November 2016 it must in fact have taken place on or before 16 November as that was the date on which he withdrew the submission, as discussed later in this Report.

2197 TRA-16158 to TRA-16161

2198 WIT-26444

- 43.11 Minister Hamilton told the Inquiry that, given the need for urgent action, he had not been impressed with the proposals contained within the submission and, in particular, the suggestion that there should be yet further pre-consultations when no specific recommended cost controls or cost-limiting proposals had been suggested. Minister Hamilton felt that the submission was an unsatisfactory piece of work in that it did not fulfil his expectation of spelling out one or two solutions to solve the overspend problem and did not contain any specific preferred cost control, such as the buyout with compensation which had been discussed.<sup>2199</sup> The submission was duly withdrawn by an email from Dr McCormick, following his discussion with Minister Hamilton, on 16 November 2016.<sup>2200</sup>
- 43.12 On 6 December 2016 the BBC Spotlight programme on the non-domestic NI RHI scheme by Conor Spackman was broadcast. This is the programme which is referred to in the Introduction to this Report and which, amongst other matters, brought to light some of the email communication to the Department from Ms O’Hagan.
- 43.13 On the following day Dr McCormick visited Brussels for a meeting with the European Commission’s Directorate General for Competition (‘DG Comp’) regarding the possibility of DfE effecting a one-off ‘buyout’ of scheme members. According to Dr McCormick, the Commission preferred this closure option as the cleanest solution to the problem faced by DETI. They told him that:
- “If a compensation payment was calculated on a basis which would in effect be the equivalent of the applicant’s entitlement under UK law, there would be no State Aid issue and no State Aid notification would be required.”<sup>2201</sup>
- 43.14 DETI then sought formal advice from the Attorney General, which supported the choice of the closure option.
- 43.15 On the evening of 15 December 2016 the interview of Minister Bell by Stephen Nolan was broadcast by the BBC, adding to the public concerns generated by the Spackman investigation.<sup>2202</sup>
- 43.16 On the morning of 16 December 2016 DETI sent a paper to Mr Sterling at DoF setting out some of the cost control options for the NI RHI scheme.<sup>2203</sup> The purpose of the paper was to inform DoF, at a high level, of the merits of amending the scheme to achieve greater value for money.<sup>2204</sup> Three options were identified as potential solutions to the budgetary issues. These were:
- Option A: to place all medium biomass installations onto the post-November 2015 tariff (6.5p/kWh reducing to 1.5p/kWh after 1,314 hours and capped at 400,000kWh per annum);
  - Option B: to place all medium biomass installations onto a flat 1.5p/kWh tariff (capped at 400,000kWh per annum) and provide a single annual capital payment; and
  - Option C: a buyout of the capital expenditure by participants plus an uplift for a return on their investment.<sup>2205</sup>

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2199 TRA-16163 to TRA-16164

2200 DFE-302263

2201 WIT-10531

2202 DFE-228963 to DFE-228988

2203 DOF-43971 to DOF-43978

2204 DOF-43972

2205 DOF-43974

43.17 A table was provided illustrating the impact on the NI RHI scheme costs of adopting the various options.<sup>2206</sup> The conclusion noted that the results were very dependent on a small number of high-impact assumptions regarding actual and projected heat demand. Any small variation in the assumed demand would be likely to have a major impact on the projected cost of the scheme. The paper then stated:

“Indeed, it has become evident that the problems with the scheme’s budget appear to be related to an assumption in the original modelling relating to the assumed heat demand – the 17% load factor assumption. This assumption fed through to the tariffs offered under the scheme and the resulting budgetary difficulties.

Given the difficulty with forecasting costs and to reduce onerous task [sic] of examining individual boiler characteristics at this stage, the modelling has relied on various assumptions, which if changed could have a material effect on the results.

While recognising the dependence on these assumptions it is clear that option C is best in terms of NPC and by some margin. As a next step it would be helpful to conduct sensitivity analysis on the key assumptions used and the impact that has on option ranking.”<sup>2207</sup>

43.18 During the afternoon of the same day, 16 December 2016, Dr McCormick had a long telephone conversation with DoF officials as well as Minister Ó Muilleoir (who had become Minister responsible for the Department of Finance in May 2016 when Minister Hamilton assumed responsibility for DfE) and the DoF SpAd. Those DoF officials expressed a preference for an option that would continue to make use of the AME budget available from HMT i.e. that continued periodic payments rather than simply ending the scheme by means of a buyout.<sup>2208</sup>

43.19 The Inquiry notes in passing that it was in the evening on the same day, when according to a ‘Note for the Record’ produced by Dr McCormick for the purposes of the Inquiry, he and Mr Stewart took part in a telephone call with Mr Cairns who said that it had been Dr Crawford who had sought to influence a postponement of the RHI changes during 2015; and Dr McCormick confirmed that account of this telephone call in the course of his oral evidence.<sup>2209</sup>

43.20 Returning to DfE’s options paper, on 18 December Dr McCormick sent an email to Minister Hamilton explaining that his preference for option C was because it was the only option that brought to an end instantly all of the abuse of the scheme which may be ongoing; it was also the option with respect to which EU Commission confirmation had been agreed and the option that had stood up to the legal advice.<sup>2210</sup> He also sent an email to Mr Sterling expressing the opinion that any course of action other than option C would require a Ministerial Direction on the grounds of irregularity. He added that there was good reason to hope that HMT would agree to help in the circumstances.<sup>2211</sup>

43.21 Dr McCormick also emphasised the need to ensure that the public should not become aware of the proposal for scheme closure until the Department was ready to answer specific

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2206 DOF-43974

2207 DOF-43978

2208 WIT-10531

2209 IND-02100; TRA-15315 to TRA-15320

2210 WIT-10820

2211 WIT-10821

questions about any compensation scheme which might be put in place.<sup>2212</sup> On 18 December Minister Ó Muilleoir met Minister Hamilton at Belfast City Hall in the absence of officials to discuss the way forward.<sup>2213</sup> It seems that Minister Ó Muilleoir was very clear that all options needed to be considered but accepted that there should be no announcement in advance of HMT engagement.

- 43.22 According to Mr Sterling, there were close working relationships between officials at DfE and DoF which, in his view, helped the process of making provision for the future of the RHI scheme during the latter part of 2016. However, he believed that tension was increasingly evident at ministerial level within the Executive from around 16 December 2016 (after Minister Bell’s interview with Stephen Nolan) until the collapse of the institutions in January 2017. Mr Sterling considered that such tension was a factor which played in to the work which was being done by the two Departments at that time to address the cost overrun.<sup>2214</sup>
- 43.23 It seems clear from internal Sinn Féin emails which have been seen by the Inquiry that, by 16 December, the view was developing that, despite efforts by DoF over some 6 months, the DfE Minister Simon Hamilton was culpable for inaction since the problem with regard to RHI had become clear; and there was concern that the next line of questioning would be directed to DoF.<sup>2215</sup>

### First Minister Foster’s Assembly statement

- 43.24 On 19 December 2016 First Minister Foster made a statement to the Assembly (which she has accepted had not been cleared or approved by the deputy First Minister).<sup>2216</sup> She explained that she felt it was important to come before the House at the earliest possible opportunity since, for almost two weeks, there had been a “barrage of media coverage” of the RHI scheme including “wild claims and allegations, many of which have been based on spin rather than reality”.<sup>2217</sup> The First Minister conceded that there had been:
- “Shocking errors and failures in the RHI scheme and a catalogue of mistakes all of which coincided to create the perfect storm, resulting in the position in which we now find ourselves.”<sup>2218</sup>
- 43.25 During the course of her address the First Minister suggested that the “crucial mistake” in the RHI scheme was setting the tariff for the most commonly used boilers at a level higher than the market price of the relevant fuel, namely wood pellets.<sup>2219</sup>
- 43.26 Amongst other things, she offered a sincere apology to Janette O’Hagan and accepted that Ms O’Hagan had sent an email to her constituency office raising concerns about the way in which the scheme was being used.<sup>2220</sup> She also rejected the various allegations made by Minister Bell during the course of his interview with Mr Nolan.<sup>2221</sup> At the conclusion of her speech the

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2212 WIT-10822

2213 TRA-16300 to TRA-16302; POL-10305

2214 WIT-05226

2215 POL-10053 to POL-10064

2216 INQ-100218 to INQ-100226

2217 INQ-100218

2218 INQ-100218

2219 INQ-100219

2220 INQ-100220

2221 INQ-100221 to INQ-100223

First Minister maintained that she had been working hard to keep Northern Ireland moving forward and continued:

“That is why, rather than whipping up a media storm, I have actually been dealing with the problem along with my ministerial colleague, Simon Hamilton and the Finance Minister, working on a practical solution, because that is what responsible politicians do. That is what government is about.”<sup>2222</sup>

43.27 On the same day Minister Ó Muilleoir sent a text to Mr Sterling, his Permanent Secretary, drawing his attention to the fact that:

“Arlene says she has been working with me on a solution. Has she had any contact with the Department? She had none with me.”<sup>2223</sup>

43.28 Mr Sterling replied that there had been no such contact, to his knowledge, and that the only ministerial contact that he was aware of had been Minister Ó Muilleoir’s meetings with Minister Hamilton.<sup>2224</sup>

### Interaction between the DfE and DoF Ministers

43.29 It seems that at the meeting between Minister Ó Muilleoir and Minister Hamilton on 18 December there was a discussion about the options for closing down the RHI scheme. Minister Ó Muilleoir reported on his meeting and that DfE favoured a solution which would enable it to buy out users or have them continue at lower tariffs under which there would be costs to London and none to the Executive.<sup>2225</sup>

43.30 In his oral evidence to the Inquiry Minister Ó Muilleoir explained that his responsibility, as Minister for DoF, was to press DfE to come forward with a solution which his Department would then test with regard to value for money and protection of the public purse.<sup>2226</sup> In an email to a Sinn Féin official on 21 December, a few days after the meeting, Minister Ó Muilleoir added:

“That gives us a certain distance from the DUP attempts to say we are all in this together.”

The same email recorded in its final paragraph:

“The Dept of [sic] Economy leaked details of the solution options to the media which were carried today to give the impression that they are working towards a swift solution.”<sup>2227</sup>

43.31 Minister Ó Muilleoir emphasised to the Inquiry that the fact that the two Ministers had met in the City Hall confirmed that both were working to find a solution but, at this stage, he was advised by his own officials that none of the proposed solutions would work.<sup>2228</sup> When the Inquiry panel raised the apparent lack of a cooperative approach between the two ministers, Minister Ó Muilleoir said:

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2222 INQ-100223

2223 IND-06504

2224 IND-06504

2225 POL-10305

2226 TRA-16301 to TRA-16302

2227 POL-10305

2228 TRA-16302 to TRA-16303

“No. At this stage, you know, and with respect, at this stage, the DUP had become a by-word for less-than-appropriate behaviour in relation to RHI. The DUP is clearly managing its own internal problems around revelations, which are almost on a daily basis, around their advisers, so, with respect, I was making sure that we made them do their work, but I didn’t want them saying that ‘listen, its Sinn Féin holding this up.’”<sup>2229</sup>

- 43.32 In his oral evidence to the Inquiry Minister Hamilton stated that the buyout option (option C) had been favoured by Dr McCormick, whereas his own preference would have been for reduction of the tariffs.<sup>2230</sup> When asked by the panel whether the latter was a means of maximising the ongoing payments from HMT, which represented a business and economic benefit to Northern Ireland, Mr Hamilton accepted:

“It was a point that was being considered. How much weight that had over – I mean, it didn’t have more weight applied to it, in my mind and my thought process, than turning off the tap and stopping the flow.”<sup>2231</sup>

- 43.33 As referenced above in Minister Ó Muilleoir’s email of the same date, on 21 December 2016 the buyout option was leaked to the media and became the subject of a significant and adverse public reaction. As a consequence, that option was no longer pursued.<sup>2232</sup> The Inquiry was not able to make a determination from the evidence as to the identity of any individual or party responsible for the leaking, although it is clear that both Sinn Féin and the DUP were suspicious of each other.<sup>2233</sup> Minister Hamilton believed that it was leaked by Sinn Féin and in his oral evidence stated:

“There was [sic] other examples of briefings to media where a flavour of a meeting was given which wasn’t actually what happened in the meeting. So, I had a bit of [sic] a fear and a bit of a concern, and I thought that they were trying to undermine any solution, even though they were saying something different publicly. And the reason I thought that was because this was clearly an issue where the pressure was on the DUP – we were under immense pressure at that time – and that, if a solution was to come forward, Sinn Féin wanted to be in the middle of finding that solution and to be seen as the, sort of, saviours of the whole scenario, but, if it didn’t, well then the DUP were to blame.”<sup>2234</sup>

- 43.34 Minister Hamilton accepted that the fact that the option was leaked altered the course of departmental decision-making.<sup>2235</sup> As mentioned earlier, in his email dated 21 December 2016 Minister Ó Muilleoir had stated that “The Department of [sic] the Economy leaked details of the solution options to the media...”.<sup>2236</sup> However, in oral evidence he told the Inquiry that he did not know who leaked the document; but denied that it was anyone acting upon his behalf or with his knowledge.<sup>2237</sup>

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2229 TRA-16304

2230 TRA-16192 to TRA-16194

2231 TRA-16197 to TRA-16198

2232 WIT-26295 to WIT-26296

2233 TRA-16199

2234 TRA-16200

2235 TRA-16202

2236 POL-10305

2237 TRA-16302

43.35 On 4 January 2017 Minister Ó Muilleoir tweeted that he was “bemused at DUP ‘solution’ to RHI being trailed on media before any plan was shared with the Department of Finance.” He continued:

“I am alert to the dangers of allowing the person who was the architect of the RHI scheme – the DUP leader – to come up with a solution to this debacle. That is why I will ensure my officials rigorously test any plan which comes from the DUP. I will be guided solely by what is in the interests of the public purse. The DUP are in a hole and should stop digging.”

43.36 He closed this tweet by saying: “I will not be bounced into signing off on any new plans simply to save Arlene Foster’s skin.”<sup>2238</sup>

43.37 On the same date Minister Ó Muilleoir emailed Mr Ted Howell, who was a member of the Sinn Féin ard chomhairle (National Executive) and who had been brought out of retirement by the late Martin McGuinness, deputy First Minister, to chair a Sinn Féin ‘crisis committee’ to deal with the crisis engulfing the Stormont institutions and political process at that time.<sup>2239</sup> The email contained the following:

“DUP believe they now have a solution based on bringing all boiler owners back to a reduced payment which has been in place since November 15 2015 for those who applied to the scheme late. Problem is that Department of Finance told them last month that we believe that scheme is also badly designed and is already paying out almost twice as much as they intended. If they move all 3,000 boilers to the post-November 15 tariff and present that as a solution, you can see that they are only rearranging deckchairs on the Titanic.”<sup>2240</sup>

43.38 A further meeting between Minister Ó Muilleoir, Minister Hamilton and officials took place on 5 January 2017 when details of the DfE proposal were discussed, namely that as an interim measure all scheme participants would be moved onto the November 2015 tariffs as a stage 1 measure.<sup>2241</sup> On the following day, 6 January 2017, Minister Ó Muilleoir sent a formal email to Minister Hamilton in the following terms:

“Since taking up office my officials and I have repeatedly pressed the Department for Economy to produce a concrete plan to address the devastating financial impact of the RHI scheme. It is extremely disappointing that seven months on I have yet to receive such a plan.

Although you expect to provide me with a business case proposal in the coming days you indicated that this will only propose an ‘interim’ measure. Let me be clear; a piecemeal approach is not sufficient.

The handling of this scheme – from the stripping out of the cost controls contained in the equivalent British legislation, through to the failure to close the scheme promptly when the threat posed by the absence of cost controls materialised – has been characterised at least by incompetence and possibly by corruption.

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2238 POL-10432 to POL-10433

2239 TRA-16313 to TRA-16314

2240 POL-10431

2241 DOF-44619

In this context the only solution that is acceptable to me and to the wider public is a comprehensive one that deals with all elements of this disastrous scheme. It must be a robust solution that stacks up financially and protects the public purse. It must be legally sound and it must be future-proofed from further abuse.

As Finance Minister I will not allow the botched management of this scheme to be exacerbated by a botched solution. A stop-gap approach is a grave mistake. I urge you to bring forward a comprehensive plan.”<sup>2242</sup>

43.39 In a covering email to colleagues, including Mr Howell, Minister Ó Muilleoir indicated that the draft letter was to be made public and warned that the DUP would come back to defend their plan and accuse Sinn Féin of sabotaging it on political grounds. In the circumstances he advised that it was essential that Mr Brennan of DoF should be asked to update a ‘one-pager’ which he had produced highlighting potential shortcomings of Minister Hamilton’s approach.<sup>2243</sup>

43.40 On 9 January 2017 Martin McGuinness resigned as deputy First Minister and Mr Sterling noted that it was becoming increasingly clear that the devolved institutions were unlikely to be in operation again until well after the Assembly elections on 2 March 2017.<sup>2244</sup> In such circumstances there was only a limited window in which to legislate to reduce the cost overrun.

### The 2017 DfE business case

43.41 On 11 January 2017 the DfE business case for ‘addressing the deficiencies in the non-domestic RHI’ was submitted to DoF.<sup>2245</sup> The business case was signed off by Mr Stephen McMurray, then Head of the RHI Task Force, on behalf of the Departmental Accounting Officer. At section 2.7 of the business case there was a discussion of ‘Undesirable Behaviour’, as a result of which the Department had commissioned PwC to provide an opinion on the design of the scheme, the robustness of the controls in place to ensure that applicants met the scheme eligibility criteria and that participants continued to operate within the scheme guidelines, and to provide an opinion on whether there was evidence to support or refute a number of allegations received.<sup>2246</sup>

43.42 In the course of its work, PwC had identified two fundamental differences from the GB scheme, namely the absence of tiered tariffs to discourage heat waste and the lack of a suspension or degression mechanism to act as a cost control measure.<sup>2247</sup> In terms of value for money the business case recorded at paragraph 2.11:

“With the pre-November 2015 Medium Biomass Tariff Installations being on a path towards over-compensation to a significant degree, with the problems of such installations and the incentives for undesirable and/or abusive behaviours there are clearly significant VFM concerns with the continuance of the scheme, and its Grandfathered Tariffs, without any amendment to bring it back much more in line with the originally intended outcome of the scheme.”<sup>2248</sup>

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2242 DOF-44761 to DOF-44763

2243 POL-10440

2244 WIT-05233

2245 DOF-45052 to DOF-45083

2246 DOF-45057

2247 DOF-45057

2248 DOF-45058

43.43 As a consequence, it was noted that there was very clearly significant public concern about the non-domestic RHI scheme. The business case recognised that a comprehensive consultation approach would ensure that whatever actions were taken would be ones that would command clear public confidence and be as legally defensible as possible.<sup>2249</sup> The following available options were identified at paragraph 4.11:

- Option 1 – No action with the pre-November 2015 tariffs remaining at 6.5p/kWh for all heat output for the duration of the scheme;
- Option 2 – all recipients of the pre-November 2015 tariff for medium biomass boilers would be moved to the post-November 2015 tiered tariffs, with the 6.5p/kWh falling to 1.5p/kWh after the first 1,314 metered hours and overall payments capped at 4,032 hours per annum;
- Option 3 – all biomass boilers would receive a payment of 1.5p/kWh, with payments capped at 4,032 hours per annum after which no payment would be made for heat generated;
- Option 4 – the scheme and payments to medium biomass boilers would be suspended until a lasting solution was developed; and
- Option 5 – there would be an arbitrary reduction in tariffs, without any origin in the rate of return analysis, simply budget driven in order to increase the prospect of living within the projected AME budget.<sup>2250</sup>

43.44 The business case accepted that further work was needed to be undertaken to develop the options into concrete workable proposals including legal and State Aid issues, the impact on individual participants, setting appropriate tariff levels, the viability of operating administration and IT requirements, financial and budgetary implications and programmes of inspection.<sup>2251</sup> The business case considered Option 2 to represent the best-value, practical approach for 2017-18 with indications that such an approach would substantially manage costs back to the £22.3 million AME allocations in that year.<sup>2252</sup> Option 1 was not considered to be an affordable or viable option.<sup>2253</sup>

43.45 On 13 January 2017 the final version of the PwC Heat 1 Report was provided to DfE and, on 16 January 2017, the Assembly debate on the draft 2017 amendment regulations was adjourned until 23 January 2017.<sup>2254</sup>

43.46 On 19 January 2017 Mr Brennan, as Budget Director of the Public Spending Directorate of DoF, responded to a number of concerns that Minister Ó Muilleoir had raised with regard to the DfE business case.<sup>2255</sup> He began by pointing out that the business case presented was one that he would term “sub-optimal”, in that it did not present a solution that would result in an immediate and permanent cessation of a call upon the Executive’s DEL budget. Mr Brennan continued:

“However, in light of the legal advice that Option 2 is a robust defensible position and the need to have some further time to collate more usage data, I must

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2249 DOF-45062

2250 DOF-45062

2251 DOF-45158

2252 DOF-45162

2253 DOF-45160 to DOF-45161

2254 DFE-05530 to DFE-05612; INQ-100329 to INQ-100333

2255 DOF-50657 to DOF-50659

conclude that the proposed way forward is indeed the only practicable action that can be taken immediately to significantly reduce the current irregular expenditure. I take the view that in our current circumstances this is an essential first step in implementing a sustainable and permanent solution. However that solution will only work if DfE delivers on the commitments set out in the business case.”<sup>2256</sup>

43.47 Mr Brennan agreed with Minister Ó Muilleoir that the role of Ofgem and the planned inspection programme continued to be matters of concern; and he emphasised that the critical issue of successfully delivering on the business case objective was to expedite the inspection process of all installations. He also reassured the Minister that work was in hand to assist in putting in place a robust contract management regime.<sup>2257</sup> At paragraph 8 Mr Brennan noted:

“In relation to your wider concern about approving what might be deemed later to be a ‘botched’ plan, I can only say that this proposed way forward does:

- Immediately constrain tariff payments through the introduction of a tiered tariff and usage cap
- Offers [sic] a strong legal defence to challenge
- Puts [sic] in place an inspection and audit process that should drive down long term costs
- Offers [sic] best possibility of being State Aid compliant.”<sup>2258</sup>

### Economy Committee consideration of the draft 2017 regulations

43.48 On the same date, 19 January 2017, there was a meeting of the Assembly Economy Committee to discuss the draft 2017 regulations, which had been produced to give legal effect to Option 2 from paragraph 4.11 of the business case (discussed previously in this Report).<sup>2259</sup> Shane Murphy, DfE’s chief economist, explained to the Committee how the original scheme had been based upon the assumption of a 17% load factor with a return on investment at 12%. He said that about 15% of applicants were currently running their boilers at load factors of 15% or less and earning not more than a return of 12% or so. The remaining 85% of participants ranged from minor or marginal overcompensation up to earning multiple rates of return.

43.49 Mr Murphy estimated that about 70% of participants were outside the range (of acceptable rates of return) that had been specified to the European Commission.<sup>2260</sup> Mr Murphy pointed out that the objective of the recent DfE business case was to undertake a legally defensible course of action that, starting in the following year, could remove the perverse incentive to produce excessive heat.<sup>2261</sup>

43.50 Some work had been done on longer-term options but they did not appear yet to be sufficiently developed. Against that backdrop Mr Murphy advised the Committee that it was important to bear in mind that they were not yet at a stage where there was full assurance in legal

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2256 DOF-50657

2257 DOF-50658

2258 DOF-50658

2259 ETI-05339 to ETI-05354

2260 ETI-05342 to ETI-05343

2261 ETI-05344

terms, incentive terms or budgetary terms that a solution had been reached which could be maintained for 18 to 20 years.<sup>2262</sup>

- 43.51 Dr McCormick told the Committee that DfE had been examining a range of options, including closure. That option had been exposed publicly before Christmas and attracted a lot of criticism and concern about potential loss of future AME. He observed:

“We do not want to lose out. It is still beneficial to Northern Ireland to have the flow of that resource; it is our 3% share of what is going on for renewable heat across the water and its right to try to continue to make use of that.”<sup>2263</sup>

### Assembly approval of the 2017 regulations

- 43.52 On 23 January 2017 the Assembly debated the draft 2017 regulations.<sup>2264</sup> During the course of that debate considerable frustration was expressed at the lack of evidence provided to, and consultation with, the Assembly, while the Sinn Féin/DUP “Iron Curtain”, as Sinéad Bradley MLA described it, prevented other members of the Assembly from being privy to RHI developments.<sup>2265</sup>

- 43.53 At the conclusion of the debate, notwithstanding the absence of DoF approval of the business case, the Assembly resolved to approve the draft Renewable Heat Incentive Scheme (Amendment) Regulations (Northern Ireland) 2017.<sup>2266</sup> Those regulations amended the original Renewable Heat Incentive Scheme Regulations (Northern Ireland) 2012, as amended by the 2015 Amendment Regulations, with regulation 5(5) providing for the insertion of a new regulation 36(7B) that:

“The tariffs for installations accredited before 18 November 2015 and falling within the small or medium biomass tariffs set out in schedule 3A are the tariffs set out in the schedule adjusted by the percentage increase or decrease in the retail price index for 2016.”<sup>2267</sup>

- 43.54 The schedule specified that medium biomass boilers (20-199kW) would be subject to a first tier of 6.5p kWh reducing to 1.5p kWh after 1,314 hours with an annual cap of 400,000 kWh.<sup>2268</sup> The regulations provided that they should come into operation on 1 April 2017 or the day after the European Commission gave approval that the provision made by the regulations, to the extent that it constituted the granting of aid to which any of the provisions of Articles 107 or 108 of the Treaty on the Functioning of the European Union applied, was, or would be, compatible with the internal market, within the meaning of Article 107 of that Treaty, whichever was later.<sup>2269</sup>
- 43.55 The regulations were duly made on 24 January 2017.<sup>2270</sup> On that same date, Minister Ó Muilleoir made a statement to the Assembly establishing this Public Inquiry.

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2262 ETI-05344

2263 ETI-05346 to ETI-05347

2264 INQ-100382 to INQ-100432

2265 INQ-100382 to INQ-100383

2266 INQ-100432

2267 DFE-321783

2268 DFE-321784

2269 DFE-321782

2270 DFE-321782 to DFE-321785; DOF-18080 to DOF-18087

## Belated DoF approval of the DfE business case in relation to the 2017 regulations

43.56 Later that evening, 24 January 2017, Minister Ó Muilleoir sent an email to Ted Howell informing him of a meeting that he was to have with Minister Hamilton on the following day with regard to the business plan in respect of the interim solution for RHI.<sup>2271</sup> As noted previously, he had been in previous contact with Mr Howell by email with regard to Minister Foster’s statement to the Assembly and the delay in providing the DfE proposed solution.<sup>2272</sup> Minister Ó Muilleoir indicated that there was now no further reason to delay holding up the business plan and his email continued:

“I have concerns about the business plan for the inspections, which is separate to this business plan, but have received repeated assurances from my staff that it is coming to me and will be robust. I accept those assurances.

I also raised the issue of State Aid. However we have NO flexibility about the requirement that the solution not kick in until State Aid is approved as that was a condition of the Regulations the DUP passed on Monday night. It may be that turns out to be a mistake if Europe holds up State Aid permission but for now, it is out of our hands.

Would you be content if I were to sign off the business plan on Wednesday afternoon? It remains a flawed plan, but it is the only show in town with a strong chance of saving £27 million to the public purse.”<sup>2273</sup>

43.57 It was put to Minister Ó Muilleoir by Inquiry Counsel that in this email he was asking Mr Howell whether he was content that he, a Minister who was democratically responsible to the Assembly and the Northern Ireland electorate, should comply with the advice that he had received from departmental officials.<sup>2274</sup> Minister Ó Muilleoir rejected such a suggestion, emphasising that the decision was his alone and stating:

“I’m telling Ted Howell that my decision has now been made. We have probed this. We have exhausted it. I have come to the conclusion that, while there are still risks inherent in it, risk to the public purse, risks to my reputation, risks to Sinn Féin if we signed off on a botched solution which was challenged and which would turn out in three weeks’ time to dissemble. And I’m telling him, as someone who is heading up a crisis committee dealing now with the collapse of government and all that that entails, that this is what is going to happen.”<sup>2275</sup>

43.58 He added that he was giving Mr Howell his place as the head of a “crisis committee” and letting him know the proposed way forward in case, for reasons unknown to Minister Ó Muilleoir, it may have implications for the peace process.<sup>2276</sup> When asked how that could be reconciled with the wording “would you be content if I were to sign off the business plan on Wednesday afternoon?” Minister Ó Muilleoir maintained that he was asking Mr Howell about the “timing” rather than whether he wished the business plan to be signed off. He further explained:

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2271 POL-10501

2272 POL-10440 to POL-10445

2273 POL-10501

2274 TRA-16332

2275 TRA-16333

2276 TRA-16333

“This is a political world, and we cannot divorce what was happening from the collapse of the Executive, from all the things that are happening outside the confines of Clare House.<sup>2277</sup> It was my decision, but I think it was appropriate and prudent to say to the Sinn Féin chair of the crisis committee this is when it was going to happen.”<sup>2278</sup>

- 43.59 In the interests of fairness, the Inquiry has reminded itself of the evidence given by Sir Malcolm McKibbin about the history of “advisers” being given passes to Stormont Castle and his acceptance of the fact that they could equally have operated from Party HQ,<sup>2279</sup> further detail of which is considered at chapter 54 of this Report.
- 43.60 Special Advisers are recognised as having a legitimate and valuable function in government. They are paid as civil servants from public funds but they are expected to form a trusted relationship with the Minister to whom they are allocated. They are not subject to the civil service duty of impartiality and they may liaise between Ministers and party members and officials in order to offer advice on party political policy from a standpoint that is more politically aware and committed than would be available from the professional civil service. They occupy influential positions and, accordingly, the Northern Ireland Assembly has enacted legislation to clearly define their status and provide a mandatory code to govern their activities in order to ensure that there is clarity about their tasks and limitations. If Ministers are to seek approval for decisions from advisers who neither hold electoral office nor are subject to the Special Advisers legislation and code, the Inquiry considers that they should only do so in accordance with transparent and accountable procedures.
- 43.61 On 25 January 2017 DoF granted approval of the DfE business case and on 16 March the approval of State Aid was received from the Commission. On 1 April 2017 therefore the 2017 amendment regulations came into operation.
- 43.62 The RHI Taskforce has confirmed that the tiered tariff introduced for all participants by the 2017 regulations has reduced the potential for gaming by the production of unnecessary heat.<sup>2280</sup> In his most recent report on DfE’s 2018-19 Resource<sup>2281</sup> the Comptroller and Auditor General reports that the heat produced under the NI RHI scheme has now reduced by 44% from 684GWh in 2016-17 to 383GWh in 2018-19; and that payments have almost halved from £42 million to £21.1 million in the same period.

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2277 Clare House is where DoF and Minister Ó Muilleoir were based.

2278 TRA-16333 to TRA-16334

2279 TRA-16723 to TRA-16727

2280 WIT-23920

2281 INQ-115003 to INQ-115010

## Findings

224. The Inquiry emphasises that it heard no detailed personal evidence about Mr Howell or his role in the Sinn Féin Party other than that he was the chair of the Sinn Féin “crisis committee”. He did not hold accountable elected office. The Inquiry finds that the wording of the 24 January email was not limited to approving the timing but also encompassed seeking Mr Howell’s consent to the proposed course of action by an Executive Minister.<sup>2282</sup> The Inquiry is conscious that the evidence that it received from Minister Ó Muilleoir was received in the course of an Inquiry instituted in order to restore public confidence in the workings of Government. Transparency and accountability are key elements in maintaining such confidence.
225. Ultimately, the Renewable Heat Incentive Scheme (Amendment) Regulations (NI) 2017 came into force on 1 April 2017. However, the Inquiry finds that the heightened degree of suspicion, lack of co-operation and lack of trust between the political parties with respective responsibility for DfE and DoF during the period from late 2016 to early 2017 did not facilitate the particular and pressing need for the achievement of a timely solution of the RHI problem in the public interest.
226. In this context, the Inquiry notes the wording of the ministerial pledge of office contained in the Belfast Agreement and referred to in sections 16, 18 and 19 of the Northern Ireland Act 1998 “...to serve all the people of Northern Ireland equally...” and “to promote the interests of the whole community represented in the Northern Ireland Assembly towards the goal of a shared future.”<sup>2283</sup>

2282 POL-10502

2283 WIT-04072



## Chapter 44 – Anonymous provision of emails showing disclosures about RHI changes in 2015

- 44.1 Meanwhile, whilst seeking to introduce changes to the RHI scheme which would reduce its overspend and during the height of public and political controversy in relation to the RHI scheme, on 5 January 2017, during a period in which he was engaged in giving evidence to the PAC, Dr McCormick received hard copies of a number of emails in an envelope postmarked 23 December 2016. These documents were sent anonymously and included evidence of disclosures made to commercial stakeholders by Mr Wightman and Mr Hughes regarding possible changes to the RHI scheme in 2015. One was dated 1 July 2015, **before** (the Inquiry's emphasis) the 8 July submission was sent to Minister Bell setting out the proposals to amend the scheme; the second, dated 23 July, confirmed that stakeholders had been briefed about further emerging proposals, including October as the proposed date for implementation of the proposed amendments. The emails were exchanges between the stakeholders passing on the information that they had received from the officials in question.<sup>2284</sup> Copies of the two emails, as well as being posted to Dr McCormick, were also sent to the Economy Committee Chairman, Conor Murphy MLA, on the same date (23 December 2016).<sup>2285</sup>
- 44.2 Dr McCormick wrote to the PAC to give notice that he had received copies of the emails and he referred them to the PwC representatives carrying out a fact-finding process that he initiated in response to evidence which emerged in preparation for his appearance before the PAC in autumn of 2016.<sup>2286</sup> During a subsequent PAC hearing on 18 January 2017 Dr McCormick, as a consequence of what he had been told by Mr Cairns, named Dr Crawford as the SpAd who had sought to delay the introduction of tariffs in 2015.<sup>2287</sup>
- 44.3 On 19 January 2017, the day after Dr McCormick spoke at the PAC, copies of the emails were also sent anonymously to Sam McBride at the *Newsletter* and Kathleen Carragher, Head of BBC News.<sup>2288</sup> Dr McCormick appreciated that the evidence contained in the emails was serious, since neither he nor Mr Stewart had authorised the degree or the extent of disclosure which they revealed. He was referred by the Inquiry to the Code permitting officials to engage informally with potential or actual stakeholders but he told the Inquiry that he was satisfied that, in the context in question, the disclosure clearly overstepped the line.<sup>2289</sup> Dr McCormick emailed Minister Hamilton with regard to receipt of the emails pointing out that one, dated 1 July 2015, indicated the inference drawn by the person briefed by officials was that applicants should move quickly to ensure they secured access to the favourable tariff that was then in force.<sup>2290</sup>
- 44.4 In a written statement of evidence John Robinson, the SpAd to Minister Hamilton, said that he had received copies of the emails from Dr Crawford on 16 December 2016. He said that when they discussed the documents some days later Dr Crawford's primary point was that

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2284 WIT-10601 to WIT-10604; WIT-26310; TRA-16683 to TRA-16684

2285 WIT-22047

2286 TRA-16685

2287 TRA-16686

2288 TRA-16685; WIT-22046 to WIT-22047

2289 TRA-16687 to TRA-16688

2290 IND-32926 to IND-32927

the documents proved that the industry was being given advanced briefing by civil servants rather than political sources. Mr Robinson said that he was encouraged by both Mr Bullick and Dr Crawford to share the emails with the media, although the latter did not want the original source of the material, i.e. himself, to be disclosed. According to Mr Robinson, Minister Hamilton primarily wanted the material to be shared with the departmental investigation; but he also recognised the benefit of challenging the ‘media narrative’ then being portrayed against the Democratic Unionist Party.<sup>2291</sup>

44.5 The Inquiry’s Senior Counsel asked Minister Hamilton, in the course of his oral evidence to the Inquiry, about the disclosure of these emails, which might have shifted the focus from Dr Crawford back onto departmental officials. Minister Hamilton accepted that the disclosures were “not unhelpful” to Dr Crawford and he stated that he had become aware of them through his SpAd, Mr Robinson.<sup>2292</sup> Minister Hamilton referred to the argument that DUP SpAds had caused the spike during the summer of 2015 by making disclosures and he expressed the view that the emails, “if not completely refuting that, cast a significant shadow of doubt on the accusations.”<sup>2293</sup>

44.6 He told the Inquiry that Mr Robinson had sent the emails anonymously to Dr McCormick and to a journalist. Minister Hamilton conceded that he had agreed with Mr Robinson to make the disclosures.<sup>2294</sup> It was put to Minister Hamilton by the Inquiry that what he had done was to use a cloak of anonymity in order to take the pressure off a SpAd.<sup>2295</sup> He conceded in the course of further questioning by the panel:

“But you’re right: it is not my proudest moment. It is one of many things that I regret around this period. It was – the only thing I offer in mitigation – and it is not a wonderful thing to offer in mitigation – is the atmosphere that we found ourselves in. It was an incredibly difficult time.”<sup>2296</sup>

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2291 WIT-22040 to WIT-22041

2292 TRA-16217 to TRA-16218

2293 TRA-16218

2294 TRA-16217 to TRA-16221

2295 TRA-16222

2296 TRA-16223

## Findings

**227. Andrew Crawford, John Robinson and Richard Bullick were employed as civil servants, albeit specialised civil servants, and they were paid as civil servants from public funds. Irrespective of the pressures to which Minister Hamilton and his party were being subjected at the material time, the Inquiry finds it unacceptable that emails relating to the conduct of, albeit not to or from, junior civil servants were leaked to the media by a political party. This disclosure of emails was intended to relieve, to some degree, the pressure on one form of civil servant, a SpAd, by making public the identities and actions of more junior civil servants. While, in some respects, Mr Robinson, Mr Bullick and Dr Crawford were all participants in this action, it was a quite extraordinary and unacceptable step for an Executive Minister to also acquiesce.**



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## Chapter 45 – Ofgem as the NI RHI scheme administrator

- 45.1 In chapter 15 of this Report the Inquiry examined the creation of the relationship between DETI and the Gas and Electricity Markets Authority (GEMA – Ofgem for the purpose of this Report) in respect of the administration of the NI RHI scheme. Ofgem continues to be the administrator of the NI RHI scheme, albeit the scheme is now closed to new applications. In this, and the next chapters, the Inquiry examines some particular issues and problems that arose during Ofgem’s administration of the NI RHI scheme.
- 45.2 Ofgem’s principal role and mainstream activity was as regulator of GB gas and electricity markets, but it had also established an internal division, E-Serve, to respond to a demand to administer payments for government-backed energy schemes, such as the NI RHI scheme. During the course of the Inquiry a substantial amount of evidence was received and considered which related to issues concerning the nature of the relationship between DETI (latterly DfE) and its appointed scheme administrator, Ofgem E-Serve.
- 45.3 As discussed elsewhere in this Report, the relationship between DETI and Ofgem was set out in the ‘Arrangements’ finally agreed between them in December 2012. Reaching agreement had proved difficult and unresolved issues continued to cause problems as the scheme developed. These issues are summarised and analysed below, with particular regard to the benefits that Ofgem, in its December 2011 Feasibility Study, had indicated that DETI could expect to receive by engaging and relying upon Ofgem as the scheme administrator.

### Ofgem’s provision of scheme information to DETI – data sharing

- 45.4 The issue of the sharing of information, or data sharing, proved particularly problematic for a long period of the RHI relationship between DETI and Ofgem E-Serve.
- 45.5 Ofgem provided DETI with weekly spreadsheets and monthly reports which contained information about the NI RHI scheme. Ofgem also produced internal summary reports in a more accessible format, but these were for internal use and were not shared with DETI.<sup>2297</sup> On one occasion, in 2013, Ofgem produced a brief annual report that it did share with DETI, but this was not repeated in future years.
- 45.6 None of the material that was provided to DETI included information about the identities, precise location/address or industry sector of the RHI scheme applicants, although some limited postcode information was included in the 2013 annual report. DETI quickly became aware of this data-sharing problem when, in January 2013, after the first application to the NI RHI scheme had been received, it asked Ofgem for the name of the applicant but was told that this information could not be provided until the applicant had signed a privacy document.<sup>2298</sup>
- 45.7 As a consequence, Ms Hepper of DETI wrote to Keith Avis, then RHI Project Manager at Ofgem, on 17 January 2013 pointing out that the 2012 NI RHI regulations clearly stated that:

“...all applications for accreditation must be made in writing to the Department where the Department is defined as DETI.”<sup>2299</sup>

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2297 OFG-60504

2298 DFE-86970

2299 DFE-86975

- 45.8 She went on to point out that there was no mention of Ofgem in the regulations and that since the application was to be made to DETI, that is where the legal power and responsibility in relation to the application resided, and that Ofgem was carrying out the work on DETI's behalf, so there should be no issue in providing DETI with any information provided by an applicant.
- 45.9 Ms Hepper then made it clear that, if the Arrangements between DETI and Ofgem were at any stage terminated, Ofgem would immediately be obliged to provide DETI with the very information that it would not share while the Arrangements were in place.<sup>2300</sup>
- 45.10 Mr Harnack of Ofgem agreed on 29 May 2013 during a meeting at DETI that:
- “Ofgem was willing to share information and data as long as the requests are reasonable and have a purpose.”<sup>2301</sup>
- 45.11 Nevertheless, email exchanges between Ms Hepper and Mr Harnack of Ofgem in July 2013, and between Ms Hepper and Ms Clifton of Ofgem in January 2014, revealed differences relating to the sharing of information.<sup>2302</sup> In particular, requests were made for the names and postcodes of applicants and the standard industrial classification of businesses.
- 45.12 In respect of the July 2013 request, the purposes for which the information was requested included the need to co-ordinate the NI RHI scheme with the spending initiatives of other NI Departments to ensure no double funding and the need to monitor take-up in relation to other projects such as gas extension. On both occasions it was made clear that the information was also required to brief the DETI Minister properly. Ms Hepper pointed out that the view of DETI's solicitors was that, as the specific public authority with statutory responsibility for the NI RHI scheme, DETI had a legitimate interest and, as such, there should be no difficulty in disclosing the data for a “legitimate purpose”.<sup>2303</sup> On these and other occasions, it appears to the Inquiry that DETI had perfectly reasonable grounds to request the information, but that these were not necessarily communicated clearly to Ofgem, exacerbating the situation.
- 45.13 This was explored in oral evidence with Ms Hepper of DETI.<sup>2304</sup> Ms Hepper told the Inquiry that the information that she had sought in July 2013 would have been useful for the then anticipated first review of the scheme in 2014, although she had not specified that as a reason in her request to Ofgem.<sup>2305</sup> She also indicated that a legitimate reason for DETI to seek the information was to brief the Minister properly when visiting various NI companies in her role as Enterprise, Trade and Investment Minister.<sup>2306</sup>
- 45.14 In the course of his oral evidence Ofgem Chief Executive, Dr Dermot Nolan, referred to DETI seeking information needed for the Minister to make a speech and Ofgem raising doubts about such a purpose in terms of data protection. He continued:

“Then a process took place with Ofgem – which took too long, and I think much of that lies with Ofgem....I think there were genuine concerns about what DETI did want it for; data protection concerns are not trivial. But it took too long to put the DSP [the Data Sharing Protocol of February 2015] in place.”<sup>2307</sup>

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2300 DFE-86975

2301 DFE-86998

2302 OFG-148029 to OFG-148035

2303 OFG-148029

2304 TRA-05287 to TRA-05292

2305 TRA-05285 to TRA-05286

2306 TRA-05286

2307 TRA-14873

- 45.15 Dr Nolan also told the Inquiry that the agreement about data sharing could have been completed more quickly but his sense was that, for quite a while, Ofgem had no idea, or no clear idea, as to why the information was wanted by DETI.<sup>2308</sup>
- 45.16 Various initiatives to resolve the issue continued but it was not until 10 February 2015 that a Data Sharing Protocol between DETI and Ofgem was finally signed by both parties with implementation from March 2015, more than two years after scheme launch.
- 45.17 During his oral evidence to the Inquiry, Marcus Porter, the Ofgem lawyer who had advised Ofgem’s RHI team on the approach to data sharing, was questioned about this, although without examining whether Ofgem’s interpretation was right or wrong. In his evidence he stated that:

“No. I mean, I think that joined-up government demands that, if, in the course of our administration of the scheme, something arises that looks as if it’s gonna [sic] cause a problem, whether it’s tiering or anything else – something we perceive to be significant – then, yes, we should pass it on.”

And later:

“I think it’s part and parcel of our obligation as a government Department administering a scheme in conjunction with another government Department to be on the alert for issues arising, problems that may have long-term implications and, at the very least, considering whether they should be raised with the other Department, and almost certainly I would have thought doing so, but it’s rather difficult in the abstract.”<sup>2309</sup>

- 45.18 It was pointed out to Mr Porter that his views on Ofgem’s obligation as a public body were not in line with how matters played out in practice.<sup>2310</sup>
- 45.19 This evidence also appeared to be in stark contrast to Mr Porter’s original view set out in an internal email on 17 January 2013 when briefing his colleagues in the following terms:

“Thus we are not obliged to *volunteer* any information to DETI under the Arrangements but rather only to provide it as and when they *reasonably request* it under the provisions referred to above [Mr Porter’s emphasis]. Moreover, I would strongly advise against choosing to volunteer such information as it is doubtful that we have the necessary legal powers to do so.”<sup>2311</sup>

- 45.20 As indicated above, Mr Porter accepted in evidence to the Inquiry that there was an obligation on Ofgem to be alert for issues arising on the NI RHI scheme, including problems that may have long-term implications, and to communicate these to DETI. The Inquiry considers this was particularly so with issues like multiple boilers where DETI was significantly hampered without the information that Ofgem possessed and was withholding.<sup>2312</sup>

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2308 TRA-14877

2309 TRA-06347 to TRA-06349

2310 TRA-06349 to TRA-06350

2311 OFG-215501. Any claim for legal privilege in the text of the document OFG-215501 quoted in this report, or any claim for legal privilege in the copy document from which the quote is taken (and which is published by the Inquiry along with this Report), is waived by Ofgem purely for the purposes of the Inquiry, but not otherwise. In addition, it is not intended that any confidentiality or legal privilege in any other related material is waived as a result of the limited waiver in respect of the subject material.

2312 TRA 06348 to TRA-06349

## Findings

- 228.** Ofgem had access to information and analysis that it did not share with DETI, e.g. its weekly internal NI RHI reports. The Inquiry notes that those weekly internal reports were in a much more accessible and understandable format than the spreadsheets with the raw data that were in fact supplied by Ofgem, and may have helped DETI to identify issues that it would otherwise not have picked up, for example low numbers of audits and high non-compliance rates. There was no good reason for the failure to share this information.
- 229.** Ofgem only once produced a very brief annual RHI report, in 2013. This was the only potential indicator DETI received before 2015 hinting at geographical groupings of boilers, but not to a level of detail that was useful in clearly identifying a multiple boiler issue. It is not clear to the Inquiry why this report failed to issue in future years.
- 230.** Ofgem, together with DETI, failed to agree a data sharing protocol until relatively late in the lifetime of the NI RHI scheme – the protocol did not become effective until March 2015. The Inquiry agrees with Dr Nolan that agreement of the data sharing protocol should not have taken so long.
- 231.** A consequence of the lack of a data sharing protocol meant that Ofgem in effect withheld information that DETI requested. Ofgem did not comply with requests for names, postcodes and standard industry codes until March 2015.
- 232.** There were disagreements about ownership of the scheme data – DETI made the point that, should the Arrangements have been terminated at any time, the data would automatically have been transferred to it, so it did not make sense that Ofgem restricted access prior to termination. Under these circumstances, Ofgem’s approach appears to the Inquiry to have been counter-intuitive and unnecessarily obstructive.
- 233.** It is clear to the Inquiry that the limited information provided by Ofgem materially impacted on DETI’s ability to monitor the scheme and identify adverse trends like multiple boilers. Whether or not DETI would have done anything with this information does not bear on the Inquiry’s finding that this was a major failure by Ofgem.
- 234.** The Inquiry finds it was justifiable for DETI to ask for information from Ofgem to meet an objective of promoting the NI RHI scheme, given that renewable heat targets were part of the Northern Ireland Executive Programme for Government 2011-15. In the circumstances it was not justifiable for Ofgem to refuse such requests.

## The auditing of installations accredited to the NI RHI scheme

- 45.21 One of the functions Ofgem performed, on both the GB RHI and the NI RHI schemes, was the auditing of RHI installations to ensure compliance with the relevant regulations. Ofgem subcontracted the carrying out of the physical audits to Ricardo/AEA, a specialist engineering and environmental consultancy. In November 2013, arising from the audits it had conducted on the GB RHI scheme, Ricardo/AEA made a presentation to the Ofgem RHI team on RHI Auditing. That presentation covered trends that Ricardo/AEA had discovered during audits including the use of multiple boilers and wasted heat.
- 45.22 The presentation indicated that the audits conducted had revealed unintended developments on the RHI scheme which represented a “significant financial cost to the programme in terms of payments.”<sup>2313</sup> Photographic evidence of the types of issues were displayed as part of the presentation. It also made recommendations about changes that should be made to deal with the issues. It does not appear that the November 2013 Ricardo presentation to the Ofgem RHI team on RHI Auditing was ever supplied to DETI or discussed with DETI officials.<sup>2314</sup>
- 45.23 In March 2014 Ofgem’s subcontractors, Ricardo/AEA, performed five audits on accredited installations in Northern Ireland. Ricardo/AEA caveated its work by pointing out to Ofgem that a sample selection of five sites was very small, so it was “difficult to comment on whether these findings are representative of the installations installed under the Northern Ireland programme.”<sup>2315</sup> It is not clear whether such a difficulty was passed on to or discussed with DETI. Gareth John, who took up post as head of RHI operations within Ofgem E-Serve in January 2014, told the Inquiry that he was unaware whether that Ricardo summary had been provided to or discussed with DETI. He could not see any good reason why it should not have been shared but observed: “In hindsight, potentially. It just, you know, wasn’t practice.”<sup>2316</sup> When pressed by Inquiry Counsel as to why such reports would not have been provided to DETI, which owned the scheme, Mr John replied:
- “I don’t know. Potentially, you know, they could’ve been. It was something that I picked up from a process point of view; I inherited. It was not something that changed until much further down the line.”<sup>2317</sup>
- 45.24 Robert Reid of Ofgem engaged in an email exchange with Ms Clifton on 16 October 2013 referring to the small intended audit sample of five installations and asking whether DETI was satisfied with that number given that it was unlikely to identify any possible trends in non-compliance. On 28 October Ms Clifton replied, stating that:
- “They [DETI] are happy that they will get a good sample from 5 seeing as they have only had 30 accredited, so they are really looking for early warning signs and then an understanding of what that looks like against the GB non-compliances and whether there is the [sic] similar pattern emerging.”<sup>2318</sup>
- 45.25 Across the first three full financial years of the NI non-domestic RHI scheme, beginning with the financial year 2013-14, 31 audits were performed out of 2,120 applications received,

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2313 OFG-87882

2314 OFG-87866 to OFG-87887

2315 OFG-94268

2316 TRA-08981

2317 TRA-08981

2318 OFG-24124

an overall percentage of 1.46%. The number of audits carried out in each of those financial years in percentage terms, when compared to the number of applications received, was 4.20% in 2013-14, 2.76% in 2014-15 and 0.89% in 2015-16<sup>2319</sup> – a diminishing sequence never approaching a sample size of 7.5%.

- 45.26 Ofgem did offer to do additional audits from time to time, provided DETI bore the cost. However, those offers were not linked to explanations of the audit strategy being adopted by Ofgem, nor to any warnings that the percentage number of audits being conducted did not reach the sample size Ofgem had set for itself for the RHI schemes. Ofgem also did not provide any advice as to the sample size from which a satisfactory level of confidence might be drawn. When additional funds were provided for the 2015-16 year, Ofgem did carry out additional audits.

### Ofgem's audit strategy for installations on the RHI schemes

- 45.27 The relationship between DETI and Ofgem with regard to external auditing of Ofgem's administration of the NI RHI scheme is dealt with in detail later in this Report, with particular reference to the evidence of Ms Dolan, DETI's Head of Internal Audit at the time when the scheme was set up. This part of the Report is concerned with the Ofgem strategy in respect of the actual site audit of installations for which applications were made to the NI RHI scheme.
- 45.28 Ofgem commissioned advice from Deloitte, its external auditor, as to the most appropriate methodology for audit sampling in relation to the non-domestic RHI scheme in GB. Deloitte recommended the Monetary Unit Sampling (MUS) method as providing a direct linkage between the financial value of payments and sample size – this was to be determined by the confidence level and level of materiality required.
- 45.29 Ofgem operated a site audit sample size of 7.5% of applications per annum to the GB RHI scheme. Dr Ward told the Inquiry that the figure of 7.5% was an Ofgem figure arrived at "... with reference to experience on some of the other E-Serve schemes at the time" and an "understanding of the likely sort of risk factors associated with the scheme".<sup>2320</sup> Dr Ward had not been personally involved in the early stages of the GB RHI audit programme but he told the Inquiry that his understanding, from the documents he had read, was that the amount of funding and resources available for the audit programme had been based on a "nominal sort of 7.5% of applications".<sup>2321</sup>
- 45.30 The 'Ofgem E-Serve Non Domestic Renewable Heat Incentive Audit Strategy'<sup>2322</sup> of 20 February 2014, a document which was supposed to apply to both the GB and NI RHI schemes, but which was not provided to DETI, recorded that Ofgem had correlated with Deloitte's recommended sample size as much as possible but that numbers and types of installations had not matched the original forecast. It recognised that modification of approach was required but, in the interim, Ofgem planned to maintain its site audit sample size at 7.5% for new applications in the GB scheme for 2014-15.
- 45.31 Prior to the production of the above audit strategy, on 16 December 2013, Ofgem's Robert Reid gave a presentation to suppliers in which he stated that 7.5% of new applications received each

2319 WIT-95078; TRA-10479

2320 TRA-10460 to TRA-10461

2321 TRA-10460

2322 OFG-97828 to OFG-97835

year was the sample size Ofgem had adopted.<sup>2323</sup> This clearly shows that, prior to 2014-15, Ofgem was operating a site audit sample size of 7.5% on the GB RHI scheme.

45.32 The approach was designed to provide Ofgem with a level of confidence of 86% that no more than a relatively small amount of money was being wasted on the scheme. However, there does not seem to have been any suggestion that 7.5% of applications automatically represented a statistically significant sample from which reliable conclusions about all the applications might be drawn.<sup>2324</sup> Indeed, Dr Ward told the Inquiry that, in the early years, after consultation with Deloitte, it was the budget that determined the number of audits that needed to be done. In his oral evidence to the Inquiry Dr Ward said:

“Ofgem cut its cloth in terms of the confidence level to fit the available funding to a degree.”<sup>2325</sup>

To make best use of resources and to be cost effective Ofgem decided that the audit sample would consist of both targeted and randomly selected installations.

45.33 In its December 2011 Feasibility Study for the development and implementation of the NI RHI, whilst asserting that the broad principles of the GB RHI audit strategy should be applied to the NI RHI, Ofgem recognised, in paragraph 5.26, that: “To determine the approach most suited to the NI RHI it will be necessary to undertake a separate risk assessment during the development phase.”<sup>2326</sup> However, the Inquiry found no evidence that Ofgem carried out such an assessment or gave any specific thought to whether the 7.5% approach operated for the GB RHI scheme was appropriate for the NI RHI scheme, a scheme that was distinct and had different risk factors.

45.34 In the course of replying to a number of questions from Ms McCutcheon, just after the launch of the NI RHI scheme, Mr Avis of Ofgem stated in an email of 3 December 2012:

“I should say that the number of audits carried out for NIRHI will be dictated by the percentage of scheme costs that DETI is paying, and hence by the value of tariff payments made in NI as a portion of total RHI payments. In other words, if DETI were paying for 3% of total scheme costs then that would mean that 3% of tariff payments were being made to NI installations, so for both of these reasons it would be appropriate to ensure that 3% of audits were conducted on NI based installations.”<sup>2327</sup>

45.35 There was no assessment by Ofgem of the actual audit requirements with regard to the NI RHI scheme. In any case, it appears to the Inquiry that setting the number of NI RHI audits as a percentage of GB RHI audits could never have guaranteed even a fixed number, let alone guaranteed a statistically significant sample of NI RHI applications.

45.36 Nonetheless, almost by default (arising from the read across methodology that was adopted), this became the approach that applied to the NI RHI scheme as well. The effect of the Ofgem approach was that:

- in GB there was an intended sample size of 7.5% of all applications per annum to be audited.

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2323 OFG-27107 to OFG-27109

2324 OFG-97828 to OFG-97835

2325 TRA-09142

2326 OFG-126037

2327 DFE-86713

- based on population share, Northern Ireland would be paying about 3% of the costs of RHI audits conducted on behalf of Ofgem; therefore
- if 3% of the number of GB applications were audited in Northern Ireland, this would be equivalent to 7.5% of NI applications.

However, that would only hold good for as long as the number of Northern Ireland RHI applications constituted 3% of the number of GB RHI applications.

45.37 Dr Ward told the Inquiry that he understood the problem with this to be that the number of audits for which funding in Northern Ireland was available was too small for the audits to be statistically significant, but he understood that this had been agreed between Ofgem and DETI at the point when the NI RHI scheme was established.<sup>2328</sup>

45.38 Dr Ward also agreed that it was not possible to draw statistically significant results from the Northern Ireland sample, but it is not clear whether that was ever discussed in detail with DETI officials.<sup>2329</sup> However, as mentioned previously, internal Ofgem emails passing between Mr Reid and Ms Clifton during October 2013 suggest, in the context of an Ofgem concern that a sample of five installations was unlikely to identify any trends, that DETI was content with that sample size at a time when it had only 30 accredited installations.<sup>2330</sup>

45.39 It seems that neither Ofgem nor DETI actively monitored whether the assumption of 3% of GB RHI audits (in order to produce a 7.5% audit of NI RHI applications per annum), regardless of whether it was an appropriate basis upon which to calculate the number of audits appropriate for the NI RHI scheme, was occurring in practice. This work, which was primarily the responsibility of Ofgem, was not carried out. Consequently, no steps were taken to assess the significance for the NI RHI scheme and its audit strategy of the fact that Northern Ireland RHI applications were beginning to track ahead of the 3% of GB assumption.

45.40 During 2015 Ofgem did work with external experts on further developing its RHI audit strategy, but at no time did it involve DETI. Ofgem did not even provide DETI with a copy of the applicable audit strategy for the NI RHI scheme until 2016, after the NI RHI scheme had closed.

45.41 This was despite what was set out in the Arrangements at clause 3.2(e) which provided that Ofgem would:

“Take all reasonable steps to ensure that wherever possible it will facilitate the ability of DETI to operate effectively in relation to the Regulations. This may mean providing briefing or attending meetings with industry, providing resources are available to do this. GEMA [Ofgem] will communicate with DETI on matters of common interest and common concern as appropriate.”<sup>2331</sup>

45.42 Clause 5.2 of the Arrangements is also relevant in this regard, which stated:

“Where either Party becomes aware of any actual or proposed amendments to or re-enactments of the Regulations or the Guidance, or that there is a need to effect such amendments or re-enactments, it will be responsible for informing the other Party as soon as reasonably practicable.”

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2328 TRA-09140

2329 TRA-09140

2330 OFG-24124; OFG-24139 to OFG-24140

2331 OFG-18385

- 45.43 On 5 January 2017 Ofgem conducted an internal workshop on lessons learned from the NI RHI scheme. One of the ideas to be given further consideration as a consequence was: “Clearer audit strategy built on external expertise in statistical sampling to determine right level of checks.”<sup>2332</sup>

## Site audits of RHI installations and the site audit reports

- 45.44 According to Mr Wightman’s written evidence to the Inquiry, DETI did not receive any copies of audits or details from Ofgem, during his time in DETI, of the number of audits being conducted until after a teleconference between the two organisations in September 2015.<sup>2333</sup> That teleconference was followed by an email from Mr Hughes on 15 September about the issue, and it seems that Mr Wightman then formally wrote to Dr Ward on 19 October 2015 indicating that DETI had been wrongly of the impression that more site visits were being undertaken, probably in the order of one in ten for new installations.<sup>2334</sup> Mr Wightman told the Inquiry that, despite repeated requests, no copies of audit reports were sent to DETI until 2 September 2016, when reports compiled by Ricardo in 2013-14, 2014-15 and 2015-16 were received. Dr Ward provided written evidence to the Inquiry stating that:

“Prior to 2015, we did not routinely share the results of audit findings with the Department. In response to a request in 2015 to share information on audit findings, I shared a summary of audit findings from the NI RHI programme to date [479]. More recently, Ofgem has been proactive in seeking to share audit findings and lessons learned. We now routinely share the completed audit reports for all site inspections, as part of our normal processes.”<sup>2335</sup>

- 45.45 The Inquiry found it difficult to understand the omission on the part of Ofgem to provide copies of audit findings to DETI until September 2016, almost four years after the initiation of the NI RHI scheme. It is particularly hard to reconcile such an omission with the Annex to the 2012 Arrangements between DETI and Ofgem which provided as follows:

“Ofgem shall notify DETI immediately in writing if any financial irregularity in relation to the NI RHI is suspected, and indicate the steps being taken in response. Irregularity means any fraud, theft or other impropriety, mismanagement, or use of funds for purposes other than that approved.

Ofgem will communicate with DETI regarding the Terms of Reference for the audit activity undertaken by Deloitte/AEA, and endeavour to ensure that any DETI concerns regarding the NI RHI are adequately addressed. Upon completion of the audits, Ofgem will share the outcomes where they relate to the NI RHI.

While being consistent with the obligations set out in the arrangements, including the requirement to comply with any legal obligations, Ofgem will provide any records, information, or explanations which may reasonably be required to enable DETI to follow scheme payments, including but not limited to information relating to accredited installations, calculation of payments and transfer of funds from Ofgem to the installer. If DETI has any issue requiring further consideration, Ofgem will

2332 OFG-131064 to OFG-131067

2333 WIT-17762

2334 WIT-17773; WIT-17693

2335 WIT-114147

provide DETI, or the Northern Ireland Audit Office, with access rights relating to the payments made to accredited installations.”<sup>2336</sup>

- 45.46 Dr Ward accepted that the Arrangements imposed a clear obligation upon Ofgem to share with DETI any relevant information arising from audits of NI RHI installations.<sup>2337</sup> Given the accepted omission by Ofgem to provide copies of the audit findings to DETI, it is not easy to identify the partnership element between public bodies with regard to protecting public expenditure in such circumstances. As noted earlier in this Report, clauses 3.2(i) and 5.2 of the Arrangements placed a clear obligation upon Ofgem to provide information to DETI to enable it to carry out its duties in a proper manner, including the need to effect amendments to the regulations.
- 45.47 The Inquiry notes that the names, postcodes or types of business of owners of accredited installations would not have been included until the data sharing protocol was agreed. If Ofgem had provided the audit reports to DETI when it should have done, within a short time of Ofgem receiving each audit report, it is likely that steps to ensure effective data sharing would have been expedited. Otherwise DETI would have been receiving heavily redacted documents. Dr Ward also accepted that Ofgem should have communicated any themes relevant to the NI RHI scheme arising from either GB or NI RHI audits.<sup>2338</sup> The Ricardo/AEA November 2013 presentation was a prime example of material that should have been communicated to DETI, filled as it was with evidence of the utilisation of multiple boilers and examples of wasted heat.
- 45.48 It is also the view of the Inquiry that DETI officials had a responsibility to ensure that there was compliance with the terms of the Arrangements. DETI must accept some responsibility for not identifying and raising the failure to comply with the terms of the Arrangements relating to auditing at a relatively early stage, instead of waiting until problems started to arise.

### Enhanced audits and inspections on the NI RHI scheme

- 45.49 After the emergence of the problems with the NI RHI scheme from 2015 and into 2016, and due to widespread public and political concerns as well as an anonymous allegation of widespread fraud and abuse of the scheme,<sup>2339</sup> DETI made a commitment to an increased number and intensity of audits.
- 45.50 In February 2016, just as the scheme was closing, DETI sought to commission additional audits and inspections from Ofgem/Deloitte. On 11 July 2016, five months later, the Permanent Secretary at DfE (the successor to DETI from May 2016), Dr McCormick, wrote to Ofgem expressing his frustration about constraints being imposed by Ofgem:

“Ofgem colleagues have now advised us that there are constraints around what will be provided in terms of providing an independent view on the potential for recipients to take advantage of the scheme and the extent to which they are taking advantage of the scheme at present; expressing an opinion over the allegations of abuse; and providing an independent view which can be provided to NIAO and PAC as evidence. There is a strong concern here, not only from my perspective as Accounting Officer, but also from the Minister, that it is essential that we can secure a clear assessment of the allegations and an approach to investigation

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2336 OFG-18391

2337 TRA-09125

2338 TRA-10573 to TRA-10574

2339 DFE-10408 to DFE-10410

that is proportionate and fit for purpose. I would ask you to note my concern that we have not been able to secure a satisfactory approach through the established arrangements, which is not a point I make lightly. The fact that OFGEM has not been able to commit to a process that would provide the clarity of opinion I have been seeking as Accounting Officer has had the effect of delaying the start of on-site inspections, and while it is still possible that the allegations we received were overstated, it is now increasingly likely that we will face criticism from the PAC here that we have for too long allowed potential abuse to be continued.”<sup>2340</sup>

- 45.51 The Inquiry considers that it was significant that Dr McCormick felt it necessary to express a strong concern, both for his part as Accounting Officer, and that of the Minister, that it was essential to secure a clear assessment of the allegations and an approach to investigation that was proportionate and fit for purpose. He also expressed his concern that it had not been possible to secure a satisfactory approach with Ofgem through the Arrangements agreement.
- 45.52 The Inquiry notes that in response to this correspondence Mr Poulton, the then Managing Director of Ofgem E-Serve, indicated on 4 August 2016 that, from the start, Ofgem had indicated that it was only able to support an approach whereby any report produced was not publishable, and must only focus on findings in line with the regulations as drafted rather than commenting upon policy matters.<sup>2341</sup>
- 45.53 DfE subsequently commissioned PwC to carry out site inspections in August/September 2016, which found widespread exploitation of the scheme. Commercial, poultry and farm sites were included. Section 5.24 of the subsequent PwC report set out the overall site inspection outcomes. The initial 51 sites visited by the end of August 2016 were categorised as follows:
- 23% of the installations inspected showed participants to be generating heat for an eligible purpose but not one which met the original policy intentions of the scheme;
  - 13.5% of the installations inspected showed participants to be generating heat for an eligible purpose but using heat in a way that was not efficient;
  - 7.9% of the installations inspected showed participants to be generating heat which might be for an ineligible purpose and, therefore, one which might be in breach of the scheme.
- 45.54 The corresponding percentages for the installations at the 29 site inspections completed at the beginning of September were 47.9%, 6.5% and 5.3%.<sup>2342</sup> After the results of these inspections became apparent, Ofgem’s then Managing Director, Mr Poulton, expressed his concern internally to Dr Ward that PwC had found things Ofgem “didn’t know about on site and in our activities.”<sup>2343</sup>
- 45.55 In accordance with a subsequent commitment made by then DfE Minister Hamilton to carry out a programme of 100% inspections, DfE contracted directly with Ricardo in August 2017. After the introduction of this enhanced audit approach by DfE, the NIAO Report on the review of DfE Accounts for 2018-19 stated that:

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2340 DFE-340867 to DFE-340868

2341 DFE-342097

2342 DFE-05571

2343 OFG-43090

“Of the 231 site visits that had been completed, the Department has told me that it is working its way through its assessment of them and that this assessment can take several months. At this stage its experience has been that around 80 per cent of cases it looks at have potentially serious compliance issues, mainly in relation to past over production of heat. Of these the Department expects that it will be able to resolve most cases through discussion and other actions short of revocation although it estimates that around 10 per cent will enter the Department’s revocation process with potential clawback of grant already paid.”<sup>2344</sup>

## Findings

235. Having recognised, in its December 2011 Feasibility Study, the need to undertake a separate risk assessment to determine the audit strategy most suited to the NI RHI scheme, Ofgem should have carried out an area specific assessment of what the auditing requirements were for the NI RHI scheme in order to meet the level of confidence it considered was necessary to ensure it was achieving an acceptable level of error/waste on the scheme. That assessment should have taken into account the differences between the NI RHI scheme and the GB RHI scheme.
236. Not having carried out an individual assessment, Ofgem should have properly, and in writing, explained to DETI the approach it was taking to the auditing of applications on the NI RHI scheme, on what the approach was based, and what its limitations and weaknesses were. DETI would then have at least been informed of the limited nature of the auditing being carried out.
237. Ofgem should have provided DETI with a copy of the RHI Audit Strategy that applied to the NI RHI scheme from or before the commencement of the NI RHI scheme.
238. Ofgem should have provided DETI with a copy of the November 2013 audit themes presentation Ofgem received from Ricardo/AEA. This should have been provided to DETI shortly after the presentation was delivered to Ofgem. This presentation alone, from a time when there was only a small number of accreditations on the NI RHI scheme, would have alerted DETI to the extent of potential abuse that could occur on the scheme, in effect confirming some of the concerns expressed in the Ofgem November 2011 legal review. The Inquiry notes that the Ricardo/AEA presentation went as far as making recommendations as to solutions for the problems it encountered.
239. Ofgem should have provided DETI with copies of the audit reports from the inspections carried on the NI RHI scheme, at least as soon as each report was finalised.
240. Ofgem should also have provided DETI with any relevant findings and themes that emerged from audits conducted on the GB RHI scheme, and which could have a bearing on the operation of the NI RHI scheme.
241. It was a major failing that Ofgem did not provide DETI with copies of the audits it did carry out in Northern Ireland or with relevant findings from audits in GB.
242. Ofgem set the sample size for audits in the NI RHI scheme by reference to the 3% contribution it was assumed DETI would make to Ofgem in respect of the total cost of both the GB and NI RHI Schemes. Even if the number of audits of NI RHI installations in any year had reached 7.5% of the number of applications in that year (7.5% being Ofgem's intended sample size for the GB RHI scheme, which was indirectly relevant to Northern Ireland because of the assumption that NI RHI applications would constitute approximately 3% of GB RHI applications), it is doubtful whether that would have been sufficient to provide statistically significant results. In any event, Ofgem never audited 7.5% of NI RHI applications and in this regard Dr Ward accepted that the audit figures were as follows: 4.2% of applications in 2013-14, 2.8% in 2014-15 and 0.9% in 2015-16.<sup>2345</sup> Ofgem should have been clearer with DETI about the differences

between the approach it adopted to audits in GB and the approach it adopted in Northern Ireland. Whilst the Inquiry recognises that on occasions Ofgem did indicate to DETI that further audits could be carried out if more money was available, Ofgem did not go on to explain to DETI why it might have been advisable to increase the number of audits or consider moving to a sampling method similar to that used in GB.

243. The Inquiry also notes that in order to understand properly the difficulties with RHI-supported installations and manage the scheme on an ongoing basis, in addition to Ofgem's audits, DfE have subsequently had to employ third party contractors to carry out an additional independent inspection programme.

## Chapter 46 – The effectiveness of Ofgem’s warnings

46.1 During the development and early implementation of the regulations, Ofgem commented on the drafts provided by DETI, see also earlier chapter 14 of this Report. The following section considers how effectively Ofgem communicated issues that it identified regarding the interpretation of the regulations as well as if, and how, it followed up to ensure that serious warnings it had given were heeded.

### Legal review and interim cost controls

46.2 Ofgem produced a very detailed analysis of the legal risks embodied in the draft NI RHI regulations drawing on issues it had already identified and communicated to DECC following its review of the GB RHI regulations. This was given to DETI on 4 November 2011. The document was produced by Faye Nicholls, then an Ofgem lawyer. The Inquiry has referred to this document as the ‘Ofgem November 2011 Legal Review’.<sup>2346</sup> It included suggested remedies to potential defects in the NI RHI scheme, for instance the need for a clear definition of ‘heating system’.

46.3 DETI did not take the steps that might have been expected with regard to the Ofgem November 2011 Legal Review – it was not shared for some months with those whom DETI Energy Division had tasked to work upon the draft regulations. Mr Bissett from Arthur Cox, DETI’s external legal advisers on the regulations, did not receive it until four months later in March 2012.<sup>2347</sup> Nicola Wheeler from the Departmental Solicitors Office, who was charged with providing internal legal advice to DETI on the regulations, told the Inquiry that the November 2011 Legal Review was never given to her.<sup>2348</sup>

46.4 Similarly, there is very little evidence of any meaningful follow-up by Ofgem with DETI on the issues raised. Five months after the provision of the November 2011 Legal Review, in April 2012, Ofgem lawyer Marcus Porter did ask internally whether DETI had taken on board the numerous comments previously made by Faye Nicholls.<sup>2349</sup> However, at an internal Ofgem meeting also attended by Mr Porter on 22 May 2012, it was still unclear to the participants whether DETI had even been sent a copy of it – Mr Avis took an action to check with his colleague, Catherine McArthur.<sup>2350</sup> Having received confirmation that DETI had received the November 2011 Legal Review, Mr Avis then flagged to Ms McCutcheon of DETI that Ofgem had offered these comments to DETI and Ms McCutcheon agreed to look back through the detail that Ofgem had sent.<sup>2351</sup>

46.5 When Mr Hutchinson of DETI sent through the amended regulations to Ofgem on 13 June 2012 he wrote a covering note with a general reference to the November 2011 Legal Review:

“Your legal team have previously seen a copy of these regulations and made comments. As discussed with Catherine previously, these regs largely reflect the GB RHI regs however are amended to cover specific issues with the proposed NI scheme, namely the tariffs and banding. We are aware that DECC intend to

2346 OFG-205301 to OFG-205350

2347 TRA-02885 to TRA-02886

2348 TRA-02822

2349 OFG-205446

2350 OFG-03281

2351 OFG-03311 to OFG-03312

make legislative changes to the GB RHI in the near future however it would be our preference to closely follow their existing regs and then make necessary amendments in the future once DECC’s legislative programme is clearer.”<sup>2352</sup>

46.6 In advance of their teleconference on 26 June 2012, Ofgem sent DETI back a copy of this more recent draft of the regulations marked with Mr Porter’s comments and proposed amendments.<sup>2353</sup> Although these did reflect the potential inclusion of DECC’s interim costs controls and some reflections on State Aid issues, the Inquiry notes that none of the comments or changes Mr Porter made related back to the critical points Ofgem had raised in the November 2011 Legal Review, like the need for a definition of ‘heating system’.<sup>2354</sup>

46.7 In the Ofgem internal minutes of the teleconference with DETI on 3 July 2012 issues relating to regulation 23 and State Aid are recorded together with an action for:

“Ofgem Legal to send a note to DETI spelling out our concerns with Regulation 23 as soon as possible.”<sup>2355</sup>

46.8 The Inquiry notes that this issue appears to have been important enough to minute and to write to DETI about, but again no reference is made to any of the issues from the November 2011 Legal Review.

46.9 Mr Hutchinson stated to the Inquiry that in the year following the Legal Review, and in the run up to the launch of the NI RHI scheme, there were no issues at all where Ofgem came back to him, as the person responsible for the regulations, to say that some form of an amendment or addition or change was needed.<sup>2356</sup>

46.10 Evidence to the Inquiry indicates that the effectiveness of Mr Porter’s approach to warnings was questioned both externally and internally. Mr Hutchinson said in oral evidence, regarding the 26 June 2012 teleconference, that the point about the wisdom of proceeding with RHI regulations broadly the same as/mirroring those in GB just as those in GB were about to change was made by Mr Porter:

“... to be fair to Mr Porter, I think he did make that point clear, but I think, you know, that was from a legal opinion, and then I think the administrative side of Ofgem, maybe, saw our viewpoint.”<sup>2357</sup>

46.11 Ms Hepper reflected a similar view in her oral evidence when asked if she meant that Mr Hull and Mr Harnack of Ofgem were not agreeing with their own legal department and were happy for both DECC and DETI to go ahead and ignore the warnings that Ofgem’s legal department was giving. She stated:

“...certainly that was the message we were getting that, you know, DECC went ahead with their regulations. Ofgem were obviously – must’ve been – content with that.”<sup>2358</sup>

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2352 OFG-03398

2353 OFG-03444 to OFG-03487

2354 OFG-205444

2355 OFG-17094

2356 TRA-04883

2357 TRA-02206

2358 TRA-02649

46.12 Despite several attempts to raise internally within Ofgem the issue of DETI following DECC’s example and proceeding with flaws in the regulations and progressing without cost controls, Mr Porter’s views and concerns of the risks this posed to Ofgem were not escalated to the GEMA Board as he wished. The ineffectiveness of this approach is perhaps reflected by Ofgem’s closing submission to the Inquiry which stated:

“...the repeated, somewhat scattergun, attempts by MP [Marcus Porter] to escalate issues through various avenues has caused Ofgem to consider whether there is a separate learning point for Ofgem.”<sup>2359</sup>

46.13 Dermot Nolan, Ofgem Chief Executive, told the Inquiry with reference to the risks that Ofgem identified at the start:

“But Ofgem did not monitor them. And I suppose you could say did not tell DETI it’d be monitoring them. I accept that too, although I think, fundamentally, Ofgem should have monitored them and should have kept them up.”<sup>2360</sup>

46.14 The Inquiry noted that there was no mention of the need for cost control in the Ofgem Northern Ireland Summary 2013.<sup>2361</sup>

### Concerns about lack of tiering

46.15 In July 2012 Ofgem was involved internally in an exercise to identify any differences between the GB and the then draft NI RHI regulations. During that process Oliver More, an Ofgem E-Serve official with biomass expertise, was asked to consider the draft NI RHI regulations from a biomass perspective. His comments, emailed internally on 20 July 2012, included the following statement about tiering:

“The tiered tariff has proved a good way of reducing the incentive to waste heat in the scheme (i.e. once they have generated beyond the tier threshold, their fuel costs will often be higher than the RHI payments so boilers are only run if heat has a real value). So taking it out increases the likelihood of abuse and heat wastage.”<sup>2362</sup>

46.16 Despite this point being made to Ofgem officials on both the operations and legal sides, the warning about the consequences of omitting to include tiering was not conveyed by Ofgem to DETI.

46.17 Mr More’s view was then incorporated into a legal comparison document by William Elliott, a lawyer on secondment in the Ofgem legal department. The relevant section read:

“Under the existing GB Regulations, the existence of a tiered tariff for biomass minimises the incentive for participants to engage in gaming/intentional heat wastage, ensuring that boilers are only run if the produced [sic] is itself of value. This benefit will therefore be lost under the NI scheme.”<sup>2363</sup>

46.18 Mr Porter saw the email from Mr More and reviewed the document from Mr Elliott. In common with other sections judged by him to be examples of where “administrative impact was

2359 SUB-01029

2360 TRA-14860

2361 DFE-331065 to DFE-331067

2362 OFG-161309 to OFG-161312

2363 WIT-104878

discussed”, he deleted this warning from the document and the concern was never shared with DETI.<sup>2364</sup> This was justified by Mr Porter in oral evidence to the Inquiry on the basis that Ofgem thought DETI would have given due thought to the question and his assumption was that DETI knew what it was doing.<sup>2365</sup>

46.19 Mr Porter also removed the warning from Mr Elliot’s legal comparison because he thought that it “was more in the nature of a comment” in a document that was trying to identify differences between the two sets of regulations. The Inquiry finds his approach at this time quite inconsistent with his previous dogged insistence that the absence of cost controls needed to be “hammered home”.

46.20 During his oral evidence to the Inquiry Dr Nolan agreed that a warning ought to have been given and that the unwillingness to go back to DETI was only “somewhat understandable”.<sup>2366</sup> It was another example of a communication failure.

46.21 To be fair to Mr Porter, who regularly raised issues of risk, the document in question from which the words were deleted was internal and not one that was to be sent to DETI. In addition, a number of other Ofgem personnel had received the same warning from Oliver More, including Lindsay Goater, Sophie Jubb, Keith Avis and Luis Castro. In the teleconference of 26 June 2012 DETI had told Ofgem that the NI RHI regulations would replicate the GB RHI regulations, “although possibly with differences in the tariff structure”<sup>2367</sup> an observation which, in its closing submission, Ofgem has said must have been a reference to tiering. However, the Inquiry notes it might instead, or as well, have been a reference to banding.

46.22 Either way, Ofgem took no steps to find out and did not pass on the subsequent warning. Mr Porter agreed in oral evidence to the Inquiry that it would have been a good idea to raise Mr More’s warning that tiering of tariffs minimised the incentive for gaming during the teleconference but his assumption was that DETI had thought about it. He added that:

“Had I thought it was significant at the time, I would probably have said something ...  
But I don’t think I was looking at it in that way at the time because, as I say, my assumption was that DETI knew what they were doing.”<sup>2368</sup>

The clear inference is that the warning was not specifically raised.

46.23 While the Inquiry acknowledges all of the points made by Ofgem in its closing submission, nonetheless the Inquiry agrees with the ultimate position taken by Dr Nolan, the Ofgem Chief Executive, that the warning about the absence of tiering, which was an absence that increased the “likelihood of abuse and heat wastage”<sup>2369</sup> in the NI RHI scheme should have been given by Ofgem to DETI.

### Additional warnings about cost controls

46.24 The Inquiry acknowledges that the Ofgem Legal Review of 4 November 2011 laid out a range of warnings about weaknesses in the draft NI RHI regulations (many were in common with weaknesses in the GB RHI, which was much further advanced). Ofgem gave a strong warning

2364 WIT-104878; TRA-06323 to TRA-06326

2365 TRA-06325

2366 TRA-16364

2367 OFG-22571

2368 TRA-06324 to TRA-06325

2369 OFG-161312

- regarding the need to define a ‘heating system’ stating “DETI should add a defined term to ensure clarity” and “it is not acceptable for this to be clarified in guidance.”
- 46.25 As indicated earlier in this Report, the Inquiry accepts that, in June 2012, Ofgem did highlight the risks of proceeding without the interim cost controls that DECC had by that point adopted. However, Ofgem accepted DETI’s assurance that such controls would be introduced at a later stage. On behalf of Ofgem, Dr Nolan conceded in oral evidence that Ofgem ought to have monitored this but did not do so.<sup>2370</sup>
- 46.26 In further evidence to the Inquiry, some Ofgem witnesses stated that they had continued to warn DETI about the need for cost controls. In particular, Mr John and Mr Poulton said this happened at two face-to-face meetings in Belfast in April and October 2014. The Inquiry received detailed written closing submissions from Ofgem’s representatives on this aspect of the evidence in support of the recollection of the Ofgem officials.<sup>2371</sup>
- 46.27 The first of these two meetings took place on 16 April 2014 and was attended by Mr Poulton, Mr John and Ms Clifton from Ofgem and Mr Hutchinson, Ms McCutcheon and Mr Mills from DETI. Mr Poulton told the Inquiry that he had prepared in advance of the meeting to talk about cost control.<sup>2372</sup> He stated that they may also have talked about tiering, but his main recollection was the discussion on degeneration versus other mechanisms. He recalled “quite a focused discussion around cost controls”.<sup>2373</sup> Mr John told the Inquiry that his recollection was that there was a discussion about degeneration at both meetings.<sup>2374</sup> However Mr John qualified that evidence by explaining that, in that discussion, Ofgem was simply “laying out the stall in terms of, operationally, what we could do for them” and he accepted that was very different from the warnings that Ofgem had expressed earlier in the context of what was being done in GB,<sup>2375</sup> referring to legal challenge and the need to mirror the GB scheme, as in the November 2011 Legal Review and the June 2012 warning about interim cost control.
- 46.28 The only contemporary documentation relating to the meeting of 16 April that was shown to the Inquiry was the detailed note made by DETI.<sup>2376</sup> Despite his assertion that he had prepared in advance to discuss the topic and that a focused discussion had taken place, there is no reference in that note to Mr Poulton raising the subject of cost control. The note begins with a list of the main areas of proposed discussion, as suggested by Ms Clifton, and the subject of cost control was not one of the proposed discussion topics then. The document does not contain any reference to tiering of tariffs.
- 46.29 Further, an email sent by Mr John to other Ofgem staff five days after the meeting, listing action points arising from the meeting, did not mention either topic.<sup>2377</sup> An email sent by Ms Clifton to Ofgem colleagues the day after the meeting made no mention of either cost control or tiering of tariffs.<sup>2378</sup>

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2370 TRA-14860

2371 SUB-01071 to SUB-01083

2372 TRA-09716 to TRA-09717

2373 TRA-09720 to TRA-09721

2374 TRA-08908

2375 TRA-08931

2376 WIT-08736

2377 OFG-89927

2378 TRA-06669

- 46.30 The second meeting, on 13 October 2014, was attended by Dr Ward, Ms Clifton, Mr John and Mr Poulton of Ofgem and Mr Wightman, Mr Hughes and Mr Mills from DETI. Dr Ward told the Inquiry he remembered the Ofgem representatives saying that Ofgem could readily introduce changes such as degression and tiering. According to Dr Ward, it was not a primary part of the discussion, but it definitely did form part of the meeting.<sup>2379</sup>
- 46.31 No minute or record appears to have been made of the October meeting although an internal briefing note, by way of preparation, was sent by Mr Wightman to Mr Mills on 10 October.<sup>2380</sup> That note contained a summary of key issues to be discussed, which focused upon Ofgem’s administration charges, Carbon Trust loans and the provision of a data sharing protocol, without any reference to cost control or tiering of tariffs.
- 46.32 Mr Hughes described it as the “annual meeting” and he did not recall any discussion at all about tariffs in the meeting.<sup>2381</sup> He told the Inquiry “I’m not saying Edmund didn’t raise it: he may have done so, but, I mean, I don’t recall it”.<sup>2382</sup> When he was later asked further questions by Inquiry Counsel, Mr Hughes said of the October meeting:
- “I’m absolutely certain that meeting did not deal with cost controls...I’m absolutely certain that cost controls weren’t discussed in that meeting. I have no recollection of that at all. And I would have remembered.”<sup>2383</sup>
- 46.33 Mr Mills commented upon this issue at a number of points in his first witness statement to the Inquiry at paragraphs 17, 76 and 85-89.<sup>2384</sup> He had no recollection of the need for cost controls being highlighted by Ofgem. In his written evidence to the Inquiry Mr Wightman confirmed that the focus of the October meeting had been to agree a change control for Ofgem’s administration costs and he emphasised that, during all his contacts, Ofgem had never once raised concerns over the level of payments that recipients were receiving.<sup>2385</sup> Mr Wightman also had no recollection of the issue of cost controls being discussed at that meeting.<sup>2386</sup>

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2379 TRA-06669

2380 WIT-14868 to WIT-14870

2381 TRA-05898

2382 TRA-05898

2383 TRA-08565

2384 WIT-14522; WIT-14536; WIT-14539 to WIT-14540

2385 WIT-17056

2386 PWC-04674 to PWC-04675; WIT-17056

## Findings

244. The Inquiry is satisfied that when Ofgem’s Oliver More explained to colleagues in July 2012 that tiering had the known benefit of reducing the incentive to waste heat, and that the effect of the NI RHI scheme not having tiering increased the likelihood of abuse and heat wastage, an appropriate warning should have been passed by Ofgem to DETI. Identifying the problem/risk of the absence of tiering increased the obligation upon Ofgem to ensure that any associated increased risk was properly considered by DETI. In fact, the Ofgem Fraud Prevention Strategy, discussed elsewhere in this Report, purporting to apply to both GB and NI RHI schemes, asserted that the NI RHI scheme had tiering when it did not.
245. As discussed earlier, Ofgem provided a legal review of the draft regulations to DETI on 4 November 2011 where it laid out a range of warnings about weaknesses in the draft NI RHI regulations (many were in common with weaknesses said to be in the GB RHI regulations, which were much further advanced). Ofgem gave, for instance, a strong warning regarding the need to define a ‘heating system’, stating “DETI should add a defined term to ensure clarity” and “it is not acceptable for this to be clarified in guidance.”<sup>2387</sup>
246. However, the Inquiry has seen no evidence of serious attempts in 2012 by Ofgem to follow up on the issues from the November 2011 legal review. Given the strength with which the warnings were drafted in November 2011, the Inquiry finds that Ofgem should have followed up the omission of DETI to heed these warnings, at a minimum writing formally to flag this to senior management in DETI.
247. The Inquiry has already found that, in June 2012, Ofgem did warn DETI officials about the need for cost controls in the NI RHI scheme. However, the Inquiry finds that the recollection of Ofgem officials that additional detailed/focused discussions of the need for cost controls in the meetings with DETI during 2014 was not supported by the evidence.
248. In its closing submissions to the Inquiry, Ofgem accepted that “Ofgem should have communicated with DETI again once the risks of which it had warned had clearly materialised.”<sup>2388</sup> The Inquiry considers this lapse to have been a major failing.

2387 OFG-205444

2388 SUB-01038



## Chapter 47 – Other factors influencing Ofgem’s approach to the NI RHI

47.1 Although the role E-Serve was to carry out for Ofgem was not a regulatory activity and, in any case, Ofgem did not have a regulatory function in Northern Ireland, it appeared to the Inquiry that E-Serve acted according to the practices and culture of a regulator. This played out in a number of ways which adversely impacted on the relationship with DETI and which are summarised and analysed in this chapter.

### E-Serve’s expansion strategy

47.2 DECC’s Delivery Review in 2010-11 had confirmed that E-Serve, the service delivery arm of Ofgem, was to remain as part of Ofgem under the governance of the Gas and Electricity Market Authority (GEMA). E-Serve’s Managing Director at that time, Paul McIntyre, was considering the potential impacts and opportunities from this and, in a paper for the July 2011 Board meeting, sought guidance from the GEMA Board on expansion options that would allow E-Serve to bid for new work, including from Departments other than DECC.<sup>2389</sup> In a separate presentation Ofgem indicated that among the potential new areas for work under consideration was the Northern Ireland Renewable Heat Incentive.<sup>2390</sup>

47.3 The paper was considered by the GEMA Board at its July 2011 meeting and the Board agreed that a set of criteria should be established to govern its choices in expanding E-Serve’s role.<sup>2391</sup> The paper to the Board had set out the need for independence in exercising any statutory functions it administered<sup>2392</sup> and this became one of the evaluation criteria adopted, e.g. when specifically considering the administration of the NI RHI scheme.<sup>2393</sup>

### Independence

47.4 The Inquiry heard evidence from a number of witnesses that raised a question of whether, and how, Ofgem’s insistence on ‘independence’ adversely impacted on its attitude to DETI and the carrying out of its functions in the NI RHI scheme.

47.5 With regard to the development of the relationship between DETI and Ofgem in summer 2012, Ofgem’s senior lawyer, Ruth Lancaster, raised serious concerns in regard to the relationship with DETI:

“...about importing services agreement terminology into the agreement lest it compromise the Authority’s actual and perceived independence.”<sup>2394</sup>

47.6 This was repeated in an email from another Ofgem lawyer on 17 July 2012:

“The decision to prepare a non-legally binding form of the administration arrangements arose from Ruth Lancaster’s concern that the administration arrangements should avoid contractual language lest the agreements be construed

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2389 OFG-215097 to OFG-215103

2390 OFG-215105 to OFG-215124

2391 OFG-215130

2392 OFG-215103

2393 OFG-17373

2394 OFG-205568

as a private law Administration Services Agreement...and compromise the Authority’s independence.”<sup>2395</sup>

47.7 This concern about independence was not limited to interactions with DETI. In the same 17 July 2012 email it is stated with regard to service standards that:

“DECC’s advances were rejected by the Authority on the basis that such performance setting would compromise the Authority’s independence.”

47.8 In August 2012 Mr Cook, the then Managing Director of E-Serve, sought the views of the “independence team” of senior Ofgem managers on “independence work”.<sup>2396</sup> This was part of consideration of a draft E-Serve paper on independence (in respect of its relationship with DECC), which appears to have been submitted in final form to the GEMA Board in December 2012.<sup>2397</sup> On one of the key topics, KPIs (Key Performance Indicators), Mr Cook stated his belief in an email of 15 August 2012 that E-Serve should:

“...be willing to embrace performance measures...so long as we lead the development of the KPIs (and these are not imposed upon us)...these should not be in any MOU (Memorandum of Understanding), because they would be ‘cast in stone’ and imply a greater role for DECC than is appropriate.”<sup>2398</sup>

47.9 Although it was not written specifically with regard to DETI, this August 2012 email showed the background to some of the difficulties that emerged during 2012 when Ofgem and DETI were trying to agree the form and nature of their relationship in respect of the NI RHI scheme. This can be seen first in the letter sent by Bob Hull, then Ofgem Commercial Managing Director, to Ms Hepper on 31 October 2012, enclosing a copy of the draft Arrangements, in which he stated:

“Within the framework for independence set out in our statutory duties...we have set out our proposed internal performance measures and targets in the attached document.”<sup>2399</sup>

47.10 A similar point was made in a further Ofgem letter sent to DETI by Mr Hull in December 2012 regarding the Arrangements for the NI RHI scheme:

“In respect of KPIs I know that Matthew has highlighted that there is a legal requirement on us to operate independently of Government. Our duty is to be accountable to the public and as such we consult publicly on KPIs through our Corporate Plan process and report on our performance in our annual report.”<sup>2400</sup>

47.11 Thus Ofgem made it clear to DETI that these measures would be open to public consultation and that, as with other stakeholders, DETI could respond to the consultation process. The Inquiry notes that on this issue DETI effectively had been relegated to being a mere stakeholder in its own scheme for which it was providing the funding.

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2395 OFG-205601

2396 OFG-215302

2397 OFG-215426

2398 OFG-215302

2399 OFG-81442 to OFG-81443

2400 WIT-16189

- 47.12 In its closing submission Ofgem emphasised that, ultimately, it cannot be dictated to in the exercise of its functions where its legal interpretations differ from those of DETI and that this had led to revised Arrangements under which DETI was able to give notice that it wished to exercise any of the functions conferred on Ofgem, in particular with regard to inspection and enforcement.<sup>2401</sup>
- 47.13 Mr Harnack of Ofgem told the Inquiry that the need for independence may have been a factor in why the joint project board with DETI was not set up. Whether or not this was correct, the Inquiry considers that for a senior manager in Ofgem to even countenance this, in the context of acting as a scheme administrator and not as a regulator, was a reflection of the culture within Ofgem around the question of independence.
- 47.14 Ms Hepper from DETI referred to this in her oral evidence:
- “Ofgem held the view that they should not be in a position of ‘reporting’ on performance to another government body.”<sup>2402</sup>
- “...there was this overarching issue of independence which they did guard quite jealously.”<sup>2403</sup>
- 47.15 These examples illustrate a lack of consideration being given by Ofgem to the fact that DETI was only seeking an organisation to carry out non-regulatory administration activities which could have been done by any properly experienced commercial entity. Moreover, Ofgem was not the statutory regulator in Northern Ireland.

### Attitude towards DETI

- 47.16 The Inquiry saw some evidence that Ofgem officials were dismissive of DETI and that DETI’s requirements were not considered important. Looking back at the experience of developing the Arrangements in February 2013, Mr Harnack referred to DETI as “such small fry ... not worth the hassle”, although he explained in oral evidence this reference was to the low take-up in NI.<sup>2404</sup>
- 47.17 According to an internal Ofgem email from Richard Kayan relating to a meeting on 1 August 2012, the Environmental Programme Board minutes of a month earlier had classified the NI RHI scheme as “relatively low priority”.<sup>2405</sup>
- 47.18 The Ofgem E-Serve Senior Management Team (SMT) did not categorise the NI RHI scheme as a major project so (from January 2012) there was no need for the Senior Responsible Officer (SRO) of the project to report to the SMT, only for the project manager to comment to the Operations Committee. On this basis Mr Harnack decided not to review the NI RHI scheme because it was not going to SMT.<sup>2406</sup> The Inquiry notes that the GB RHI scheme was classified as a major project in Mr Harnack’s area of responsibility.

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2401 SUB-01138

2402 TRA-05246

2403 TRA-05249

2404 OFG-12531

2405 OFG-126516

2406 OFG-03076 to OFG-03077

- 47.19 In August 2012 Paul Heigl, one of the managers with responsibility for the NI RHI scheme, sent an email to colleagues asking:
- “...which reports they would **not** like to offer to NI to save on time and resources... but enough information so that ad hoc requests don’t become restrictive.”<sup>2407</sup>
- 47.20 In 2012 the Chair of the GEMA Board expressed doubts about whether E Serve should support the NI RHI scheme. In response Mr Cook, the Managing Director at the time, expressed his view that the NI RHI scheme was a small project and unlikely to add significantly to their workload or the problems they were experiencing.<sup>2408</sup>
- 47.21 As discussed in other chapters of this Report, this attitude was then reflected in practice where DETI, if at all, was considered at best as an afterthought when it came to circulating documents that contained useful and even essential information (e.g. the Fraud Prevention Strategy and audit reports). The Inquiry saw documents which referred only to the requirements of DECC and the need to inform DECC about matters. A clear indication of the divergent approach to communications from Ofgem to DECC and DETI is given in the summary analysis of communications produced by the Inquiry and utilised during its oral hearings.<sup>2409</sup>
- 47.22 When asked about why DETI was not considered or included, Ofgem witnesses<sup>2410</sup> stated that (apart from where there had been data protection concerns) there was no good reason for DETI not to receive the documents or for DETI not to be considered in important documents, such as the Fraud Prevention Strategy (discussed later in this Report).
- 47.23 Dr Ward confirmed to the Inquiry in oral evidence that DETI had not been informed about or provided with a copy of the AECOM report and the discussion about the definition of ‘heating system’ (a subject covered later in this Report). When asked by Inquiry Counsel whether DETI should have been provided with a copy of the report, he said “I think that would’ve been a very reasonable course of action to take”, adding that the report had been produced some months prior to the NI RHI scheme coming into being.<sup>2411</sup> At another point in his oral evidence Dr Ward, when asked about the failure to furnish a copy of the AECOM report to DETI, said:
- “I wasn’t responsible for the relationship with DETI at that time. My reading, though, is that this fell into the, rightly or wrongly, fell into the category of documents that Ofgem was using to inform its own approach, and there was no wider discussion or engagement from DETI on the details of the scheme.”<sup>2412</sup>
- 47.24 He agreed that the report was an example of material which would currently be routinely passed to DETI and that he could not see any “clear reason” why that had not occurred.<sup>2413</sup>
- 47.25 Mr John confirmed that the Ofgem Fraud Prevention Strategy, with its accompanying risk registers, which had been in existence when he became head of the Ofgem RHI team, had not been provided to DETI. He was unable to think of any good reason why DETI should not have been supplied with detail of the Fraud Prevention Strategy until it was annexed to the NI RHI Phase 2 Feasibility Study in July 2015.<sup>2414</sup>

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2407 OFG-04628

2408 OFG-03402

2409 INQ-100980 to INQ-100989

2410 TRA-08959 to TRA-08960; TRA-10530 to TRA-10531

2411 TRA-09078 to TRA-09079

2412 TRA-10530

2413 TRA-10530 to TRA-10531

2414 TRA-08959 to TRA-08960

47.26 As discussed in other chapters of this Report, there has been evidence of a lack of clarity and understanding of the allocation of roles and responsibilities between Ofgem and DETI. Ms Hepper was expecting Ofgem to provide a service to DETI, and her successor, Mr Mills, was led to believe when he took over the role that, because of Ofgem’s involvement, the scheme would effectively run itself. He accepted that, in terms of administration, DETI relied on Ofgem, stating:

“In terms of administration, I think there’s an assertion in the DFE statement that we relied on Ofgem too much on things like monitoring, and that is, I think, that’s a fair criticism. We had experienced administrator [sic] who ran both the domestic and the non-domestic schemes in England, so we relied on that....We needed 20 people, at least, working on this area, not two.”<sup>2415</sup>

47.27 Ofgem submitted to the Inquiry in its closing submission that:

- Ofgem found DETI a less engaged partner when compared to DECC and mistakenly thought that DETI officials were in regular contact with DECC.<sup>2416</sup>
- Ofgem did not consider whether DETI was sufficiently competent and resourced to manage its role in the scheme and was unaware of the lack of resource, knowledge and understanding amongst DETI officials.<sup>2417</sup> However the Inquiry notes the internal Ofgem review dated 6 February 2013 in which it was stated at paragraph 5.8: “However, the team also noted that they felt at times that the DETI team was very small for the size of the project and that they were inexperienced.”<sup>2418</sup>
- Ofgem assumed without carrying out any checks that DETI had the levels of governance and policy understanding needed.<sup>2419</sup>

47.28 The Inquiry was told in November 2018 that Ofgem had, presumably arising from its experience with the NI RHI scheme, decided to carry out due diligence checks on the ability of a partner to govern, policy-manage or resource future schemes.<sup>2420</sup> Ofgem had not carried out any due diligence checks to ascertain whether DETI was a competent Government Department for the purpose of designing and implementing the NI RHI scheme. It had only assumed that to be the case.

47.29 In Ofgem’s closing submission it said that: “Upon arrival at Ofgem, Dr Nolan noted that there [sic] work of E-Serve had expanded significantly, but was less on his ‘radar’ than the regulatory functions of Ofgem.”<sup>2421</sup>

### **Budget issues within Ofgem in respect of administering the NI RHI scheme**

47.30 The Inquiry saw evidence that a lack of available budget and/or a concern to avoid GB consumers having to cross-subsidise activity in NI led to tension within Ofgem, and between Ofgem and DETI, and to Ofgem not carrying out some work or delaying it.

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2415 TRA-10999

2416 SUB-01099 at 357

2417 SUB-01008 at 14

2418 OFG-83204

2419 SUB-01008 at 15

2420 SUB-01008 at 16

2421 SUB-01143

- 47.31 In January 2012, Faye Nicholls the Ofgem lawyer who had authored the November 2011 Legal Review, warned colleagues in the Ofgem policy team that budget constraints would continue to impinge on the extent of legal support that they would receive on the GB and NI RHI schemes. She went on to point out that the Ofgem legal team might not be able to address some matters due to resource constraints and that management of, and decision-making in relation to, the resulting legal risks rested with the policy team.<sup>2422</sup>
- 47.32 In October 2012 there were internal discussions in Ofgem as to whether the allocation proposed for the legal budget was insufficient. Ruth Lancaster, a senior lawyer in Ofgem, made it very clear to Keith Avis, the NI RHI project manager at the time, that limiting the budget was a decision that he made at his own and Ofgem’s risk. She made clear that there was no money left beyond October.<sup>2423</sup> Also in October 2012, Bob Hull, then Ofgem Managing Director, refused to sign off the Arrangements to formally commence Ofgem administering the NI RHI scheme, which was about to go live, following representations from Ofgem Legal.
- 47.33 As discussed earlier in this chapter, the approach to the number of audits was restricted by the budget to such a low level that meaningful or statistically significant conclusions could not be drawn about what was happening with the RHI scheme in Northern Ireland.

## Value for money

- 47.34 As a Government body with both regulatory and administrative functions, the Inquiry considers that Ofgem would have been familiar with the obligation on the part of Government Departments to ensure value for money with regard to the expenditure of public funds. In such circumstances, having regard to their relationship, Ofgem should have drawn DETI’s attention to potential failures to achieve value for money of which it was aware. The Inquiry notes the following:
- (i) When DETI notified Ofgem that they intended to mirror the GB RHI scheme apart from the tariffs, Marcus Porter of Ofgem Legal raised the concern that the known deficiencies in the regulations could lead to legal and reputational risk for Ofgem<sup>2424</sup> – no mention was made of the potential costs and failure to achieve value for money.
  - (ii) In the Ofgem RHI fraud prevention risk registers there were further examples where the legal or reputational challenge to Ofgem was the only, or the top, risk identified. Value for money was mentioned far less frequently.
  - (iii) Ofgem adopted an interpretation of the regulations which had the consequence of permitted gaming and led to significantly higher costs than were envisaged in the original policy intent (dealt with later in this Report). Ofgem did not inform DETI that the approach it was taking would have, or was having, that effect.
  - (iv) With regard to the issues raised by the application to the NI RHI scheme of Stephen Brimstone (dealt with later in this Report) Ofgem staff described their “nagging concerns” that the approach being taken by Ofgem may not be in the interest of the public purse<sup>2425</sup> and that: “there is a difference between slavishly following the rules and doing the right thing by the public purse.”<sup>2426</sup>

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2422 OFG-205431

2423 OFG-22783

2424 OFG-205456

2425 OFG-200296 to OFG-200297

2426 OFG-217279

- (v) One of Mr John’s initial reactions to hearing about the problems with the NI RHI scheme was to worry about whether Ofgem would get paid,<sup>2427</sup> not about the waste of public money.

47.35 Dr Nolan stated in oral evidence that Ofgem makes decisions on accreditation on a statutory rather than on a value for money basis and suggested to counter this that value for money should itself be put on a statutory basis if Ofgem were to take it into equal consideration.<sup>2428</sup> The Inquiry notes in contrast that in public documents Ofgem has stated “the value for money issue...is absolutely foremost in our thoughts”<sup>2429</sup> and that “We work to promote value for money...”<sup>2430</sup>

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2427 OFG-61743

2428 TRA-16436

2429 TRA-16472

2430 WIT-285275

## Findings

249. The Inquiry finds that the relationship between DETI and Ofgem was adversely affected by Ofgem’s failure to distinguish sufficiently between its roles as regulator and administrator.
250. The Inquiry considers that the treatment of DETI fell well below the level of care and attention provided to DECC. This is evidenced by, among other things, the approach to documentation and communication, where DETI was considered, if at all, as an afterthought: full consideration was not given to identifying its distinctive needs, which could have included the different tariffs and counterfactual fuel; other differences between the GB and NI schemes which may have given rise to additional risks; and DETI’s resource and capability. The Inquiry recognises that the primary responsibility for ensuring that DETI was adequately resourced with officials who had relevant expertise lay upon the NI Executive.
251. The Inquiry notes that Ofgem in its closing submissions has said that it will, in future, clearly spell out at a senior level to its public sector partners where it is having to cut corners it would not wish to because of budgetary pressure.<sup>2431</sup> The Inquiry finds that this should always have been common practice.
252. The Inquiry finds that Ofgem did not have sufficient regard, overall, for the value for money of the NI RHI scheme.
253. Ofgem’s internal discussions about the tension between seeking to ensure value for money and what the legislation in fact required were not communicated to DETI as they should have been.

2431 SUB-01145

## Communication

- 47.36 Throughout the evidence provided to the Inquiry the issue of poor communication between Ofgem and DETI was raised many times and, in the main, Ofgem has recognised its failings in this regard.
- 47.37 By way of example, the Inquiry refers to an article in the edition of *Farmer’s Weekly* for 29 May 2013 about a GB poultry farmer who installed 11 undersized boilers.<sup>2432</sup> The pellets cost 3.8p/kWh versus 5.5p/kWh when the sheds were heated by gas, bringing a saving of 2p/kWh, regardless of RHI payment. The farmer in question, when referring to the RHI subsidy that he also received, was quoted as saying: “When I get paid 8.6p/kWh I’m quids in.”<sup>2433</sup>
- 47.38 The article was seen and considered by Ofgem. It was included in an Ofgem ‘Difficult Decisions’ log with a note to confirm that planned site inspections would explore and elaborate on whether undersizing was occurring, and that DECC had been informed and had a submission with their Minister for consideration of the policy implications.<sup>2434</sup>
- 47.39 When asked about the article in oral evidence, Dr Nolan accepted that the tenor of such information should have been communicated to DETI as it reflected a risk identified in the November 2011 Legal Review, adding “I suppose I go back to the general point that Ofgem did not communicate issues in relation to gaming and they should have.”<sup>2435</sup>
- 47.40 The Inquiry agrees with the remarks of Dr Nolan on information sharing, when he observed in his written evidence to the Inquiry that:
- “In my opinion the open exchange of information, opinions, experience, intelligence and potential solutions as between Ofgem and the Government Departments for which it delivered schemes and programmes is essential for any or all of: the effective delivery of schemes and programmes, achieving best value for money, making the schemes and programmes more effective in meeting policy objectives and/or ensuring that they take account of all prevailing circumstances.”<sup>2436</sup>
- 47.41 Dr Nolan added that, from the evidence in the case of the NI RHI scheme, the level of information sharing between both Ofgem and DETI “**could have been better.**”<sup>2437</sup> (the Inquiry’s emphasis)
- 47.42 The Inquiry also agrees with Ofgem lawyer, Mr Porter, who told the Inquiry (as previously noted):
- “I think it’s part and parcel of our obligation as a government Department administering a scheme in conjunction with another government Department to be on the alert for issues arising, problems that may have long-term implications and, at the very least, considering whether they should be raised with the other Department, and almost certainly I would have thought doing so, but it’s rather difficult in the abstract.”<sup>2438</sup>

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2432 INQ-100759

2433 INQ-100762

2434 OFG-126980

2435 TRA-14901 to TRA-14902

2436 WIT-95269

2437 WIT-95269

2438 TRA-06349

- 47.43 The Inquiry heard evidence from Ms Clifton that DETI had to ask Ofgem for any information DETI believed it needed, and also Dr Ward’s position, summarised as Ofgem would communicate if prompted. That should not have been the case.
- 47.44 It was put to Dr Nolan that “there was a lot of introspection and internal sharing of information, but not a lot of it reaching people who could have done something with it in NI”.<sup>2439</sup> The Inquiry accepts Dr Nolan’s response that Ofgem’s failures in communication are “sobering”.<sup>2440</sup>

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2439 TRA-14943  
2440 TRA-14943

## Findings

254. Ofgem did not communicate effectively with DETI.
255. A better governance structure would have prompted Ofgem to communicate more frequently with DETI. Without appropriate governance arrangements in place, as was the case with DECC, there was little to bridge the risk of things falling through a policy/administration gap and leaving a “them and us” mentality.
256. Ofgem mistakenly believed that DETI was receiving more advice from DECC than was actually the case. However, that does not explain Ofgem’s own failure to properly communicate with DETI.
257. Ofgem had an obligation under clause 3.2(a) of the Arrangements to share with DETI the information DETI needed to enable it to carry out certain retained functions, in particular its statutory reporting function – it did not.
258. In all the circumstances where Ofgem held information relating to the NI RHI scheme that was not available to DETI, but nevertheless relevant to the NI RHI, Ofgem had a heightened responsibility to share such information. This was particularly so with regard to postcode data.
259. In accordance with the Arrangements and as a matter of principle, where a trend emerged that suggested the guidance or the regulations needed to be reconsidered, there was an onus on Ofgem to communicate this to DETI. For example, it failed to share important information when risks it had earlier warned about materialised in practice from GB as well as NI – in particular with regard to multiple boilers. It also failed to share audit findings about both the NI and GB schemes with DETI. Even audit reports specific to NI were not shared until after the scheme had closed.

## Ofgem and Edward Fyfe

- 47.45 During the course of its work the Inquiry became aware of a serious allegation made against Ofgem by a former employee relating to Ofgem’s administration of the RHI schemes and the alleged destruction of relevant evidence. The Inquiry considered that the allegation should be investigated by it.
- 47.46 Edward Fyfe is a former employee of Ofgem, engaged primarily in work relating to the GB domestic RHI scheme, who initially came to the attention of the Inquiry through documents provided to the Inquiry by Sinn Féin on 9 May 2017. These documents included an email from Mr Fyfe to Sinn Féin dated 20 January 2017<sup>2441</sup> in which he stated that he felt there were “on-going moves to ‘cleanse and wipe clean all’ the damning evidence relating to Ofgem’s mismanagement of the RHI.”<sup>2442</sup>
- 47.47 Having become aware of Mr Fyfe and his allegations concerning Ofgem, the Inquiry took a number of steps, including the following:
- Serving a detailed Section 21 Notice on Mr Fyfe on 31 May 2017, (No. 249 of 2017),<sup>2443</sup> to which he replied on 31 August 2017 with a witness statement.<sup>2444</sup>
  - Seeking from Mr Fyfe, ultimately through a further Section 21 Notice (No. 539 of 2017),<sup>2445</sup> documentary evidence in support of his allegations, to some of which evidence he had referred in his 31 August witness statement.
  - Obtaining from Mr Fyfe, on 13 February 2018, various documents. These related primarily to the GB domestic RHI scheme<sup>2446</sup> but included an extract from an email from Mr Fyfe to Public Concern at Work (now known, and hereinafter referred to as, ‘Protect’) dated 3 February 2017<sup>2447</sup> in which he claimed that Ofgem employees were “wiping clean and sanitising information ahead of the meeting on NI on 24/02/2017.”
  - Persistently seeking from Mr Fyfe, from August 2018 onwards, a full copy of his email to Protect. To date, this has not been provided.
  - Seeking from Protect, on 5 March 2019, a copy of the said email. This request was declined on 20 May 2019 on the ground that Protect’s ‘advice line’ is subject to legal advice privilege.
  - Seeking, during December 2018 and January 2019, detailed responses to Mr Fyfe’s allegations from the following other Ofgem employees:
    - o Edmund Ward (WIT-280863-280908);
    - o Chris Poulton (WIT-282970-282984);
    - o Gareth John (WIT-284013-284077);
    - o Teri Clifton (WIT-285306-286325);

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2441 POL-10095 to POL-10097; WIT-99018 to WIT-99020

2442 WIT-99018

2443 WIT-99001 to WIT-99007

2444 WIT-99008 to WIT-99020

2445 IND-79988 to IND-79999

2446 IND-80000 to IND-80060

2447 IND-80033

- o Alison Smith (WIT-286501-286539).

In summary, each of the above persons provided detailed witness statements in which they robustly denied Mr Fyfe’s allegations and provided detailed responses to the issues raised in his witness statement.

- Offering Mr Fyfe several opportunities to consider, and respond to, the statements from his five former colleagues. These offers took into account Mr Fyfe’s personal difficulties and included the following:
    - o Repeated offers to send him copies of all of the statements, none of which were accepted.
    - o An offer to meet with the Inquiry Solicitor so that he could receive a verbal précis of the Ofgem responses. Although Mr Fyfe accepted this offer, he twice failed (without any prior notice) to attend such meetings (14 and 20 March 2019).
    - o An offer to meet the cost of a lawyer in Scotland (where Mr Fyfe is based) being engaged to act on his behalf in order to consider the Ofgem responses, consult with Mr Fyfe regarding same, and to submit any further evidence he wished to submit in response. This offer, like the offers to send him the Ofgem statements, was not accepted.
  - Considering Mr Fyfe’s allegations when analysing the voluminous evidence provided by Ofgem to the Inquiry. In this particular regard the Inquiry notes that:
    - o It served 77 Section 21 Notices seeking witness statements and 50 Section 21 Notices seeking documents upon more than 50 Ofgem witnesses;
    - o Ofgem and its witnesses have provided the Inquiry with almost 200,000 pages of disclosure as well as almost 6,000 pages of witness statements;
    - o Nine Ofgem witnesses were called before the Inquiry to give oral evidence across approximately 12 hearing days.
- 47.48 The Inquiry’s engagement with Mr Fyfe has been protracted and sometimes difficult, not least because of personal difficulties experienced by him. In response to these difficulties the Inquiry has made several adjustments to accommodate Mr Fyfe including, as mentioned above, the offer of face-to-face meetings with the Inquiry Solicitor and the offer of limited legal representation at the expense of the Inquiry.
- 47.49 The Inquiry’s engagement with Mr Fyfe has also been hampered by reason of his request, expressed repeatedly from 16 October 2018 onwards, that the Inquiry delete all documents provided by him. The Inquiry refused to accede to this request, leading to a formal complaint being made by Mr Fyfe on 17 April 2019 which, following full consideration of the matter, was rejected by the Inquiry Chairman on 15 May 2019.

## Findings

**260. Ultimately, having taken all of the steps set out above and, in particular, having considered the evidence of Mr Fyfe, Dr Ward, Mr Poulton, Mr John, Ms Clifton and Ms Smith, as well as the manner in which Ofgem has engaged with the Inquiry providing, as it has done, voluminous documentary evidence, some of which is unhelpful to Ofgem, the Inquiry does not accept that Mr Fyfe’s claim that Ofgem was involved in the destruction or withholding of relevant material is supported by the evidence.**

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## Chapter 48 – Ofgem’s interpretation of the regulations

48.1 In this chapter the Inquiry examines four particular issues that arose on the NI RHI scheme as a result of Ofgem’s interpretation of the NI RHI regulations: multiple boilers, wasted heat, installations heating domestic properties on the non-domestic RHI scheme, and a particular matter relating to alternative financial support that produced a State Aid issue. Ofgem has maintained that it was its responsibility to interpret the NI RHI regulations, having been appointed the scheme administrator by DETI. Questions of legal interpretation are matters for Courts. It is therefore not the job of the Inquiry to substitute its own interpretations for those adopted by Ofgem. Rather, the Inquiry, in this chapter, having explained the issue, examines Ofgem’s handling of the matters that arose from the interpretations it adopted.

### Multiple boilers

48.2 Multiple boilers emerged as a significant theme during the course of the Inquiry, particularly in circumstances in which the efficient use of heat indicated installation of a boiler(s) above 99kW in capacity which qualified for lower subsidy than a boiler(s) below that capacity. As demonstrated in several of the Invest NI technical consultancy reports considered earlier in this Report, by altering the design and operation of their renewable heat installations, users could maximise their income by targeting the highest available tariffs. The following sections analyse how this became a major contributory factor to subsidy payments under the NI RHI scheme being much higher than had been originally intended, with the result that many scheme members were overcompensated, and causing much greater overall spending on the scheme than might otherwise have been the case.

### The policy intent

48.3 Similar to the approach adopted by DECC in GB, a clear intention to prevent exploitation through multiple installations was set out publicly by DETI in the July 2011 consultation document for the NI RHI scheme. Paragraphs 3.6, 3.9 and 3.26 of that document said:

“The proposed RHI is not designed as a reward but as an incentive to increase the uptake. The non-domestic market presents the greatest opportunity for large-scale deployment of renewable heat, this will provide a high level of renewable heat at a cost-effective rate.

In order to prevent situations where a number of smaller installations are installed to provide heat for one heat source in order to avail of higher tariff levels, installations will be defined as one or multiple technologies connected to the same heating system. ***Where multiple installations of the same technology are installed to serve a single heating system the combined capacity will be considered for the eligible tariff.***<sup>2448</sup> (the Inquiry’s emphasis)

48.4 The tariff structure was clearly banded to provide higher levels of support for smaller installations, with the level of subsidy dropping rapidly as installations increased in size to a point, as shown below, that there was no support for installations above 1MW in capacity for biomass boilers (2012 tariff levels):

>1MW	0 p/kWh
100 – 999kW	1.5 p/kWh
20 – 99kW	5.9 p/kWh
0 – 19kW	6.2 p/kWh

48.5 Taken together, this indicated a recognition by DETI that larger users benefit from economies of scale and, compared to smaller users, need lower tariffs, or indeed no support at all. DETI also saw that the approach could lower the cost of the RHI scheme and was clearly aware that there was a risk to this if larger users exploited higher tariffs by installing multiple, smaller units – something that it wanted to prevent.

48.6 DETI, as DECC had done, endeavoured to reflect this in the 2012 NI RHI regulations, where as well as setting out the banded tariffs, specific references to multiple installations were made in regulation 14, which stated that a plant does not meet the eligibility criteria if the plant is comprised of more than one plant (regulation 14(1)), but went on to state that where two or more plants use the same source of energy and technology, and form part of the same heating system, those plants are then to be considered as a single plant and consequently would meet the eligibility criteria (regulation 14(2)).<sup>2449</sup> Thus, multiple plants that were part of the same heating system had to be treated as one plant to be eligible for accreditation, and their individual capacities combined to ascertain the tariff to which the deemed single installation was entitled. With the benefit of hindsight the Inquiry accepts that this was not an easy regulation to interpret and would have benefited from more focused attention, both legal and technical.

#### Ofgem’s interpretation of ‘heating system’

48.7 For the Northern Ireland Renewables Obligation (NIRO), which Ofgem was already administering on behalf of DETI, Ofgem had adopted an approach to multiple generating stations whereby the total installed capacity was used to determine the appropriate banding and payment level (e.g. Appendix 1, paras 1.8-1.15 of Renewables Obligation: Guidance for Generators, 1 May 2013).<sup>2450</sup>

48.8 In accordance with DECC/DETI’s RHI policy intent as well as the NIRO, various parts of Ofgem initially pursued an aggregated capacity approach to multiple RHI installations. For example, in February 2011 in advice to DECC, Ofgem suggested the following definition:

“An RHI installation is one or multiple units of the same heating technology where one or more of the following apply: they are located on the same premises; they are connected to a common heating system; they share engineering features, such as common civil works, pipes, etc.”<sup>2451</sup>

2449 LEG-00001 to LEG-00035

2450 INQ-15970 to INQ-16085

2451 OFG-265637 to OFG-265639

- 48.9 Further, in Ofgem’s RHI Fraud Prevention Risk Register from March 2011 it was stated that the tariff would be set on the basis of total installed capacity.<sup>2452</sup> This approach persisted until at least September 2012 where the same entry was still in the risk register.<sup>2453</sup>
- 48.10 The November 2011 Legal Review provided by Ofgem to DETI contained a number of relevant recommendations:
- Addressing the draft regulation 2, which set out the NI RHI scheme definitions, Ofgem indicated that it had a considerable number of concerns about the definitions in the GB RHI regulations (or the omission of such definitions), which were set to be replicated in the NI RHI regulations. It said it was “critical” that these concerns were addressed as, without clear definitions, Ofgem would not be able to advise appropriately and would be unable to administer the scheme without serious risk of legal challenge.<sup>2454</sup> At the same point it suggested that the regulation 14 ‘heating system’ term may require definition, and referred to specific comment on regulation 14.
  - DETI should redraft regulation 14 (to do with plants comprised of more than one plant) to make the policy intent in this area clearer.<sup>2455</sup>
  - ‘Heating system’ should be defined, as this concept was said to be a key determinant of whether multiple plants should be treated as a single installation, something which fed through into the calculation of payments. Ofgem also noted that it was not acceptable for it to be left to be clarified in the guidance document.<sup>2456</sup>
  - In a section in the Legal Review headed “Potential Perverse Outcomes” Ofgem suggested that some participants may install additional pipework and multiple, smaller units in order to meet the eligibility criteria or tariff thresholds.<sup>2457</sup> Ofgem then suggested that DETI consider “tightening” the definition and imposing a requirement that where the systems serve the same end use, they should be regarded as part of the same system.<sup>2458</sup>
- 48.11 The above statements demonstrate an awareness, at least within some parts of Ofgem, in 2011 of the policy intent to prevent exploitation of higher tariffs through multiple installations or manipulation of the capacity. They also show an awareness and concern about the potential for abuse and that weaknesses in the definitions may lead to legal challenge of decisions.
- 48.12 However, as discussed elsewhere in this Report, DETI did not make any changes to the regulations and Ofgem made no further serious representations to DETI on this topic, instead developing and implementing its own interpretation of the term “heating system” and approach to multiple boilers.
- 48.13 Ofgem could provide no evidence to the Inquiry of any formal process followed by it to develop and evaluate its interpretation of the definition of ‘heating system’ contained in regulation 14. A working interpretation evolved – paragraphs 42 and 43 of Ofgem’s first witness statement to the Inquiry of 29 March 2019 state:

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2452 OFG-134852

2453 OFG-134921

2454 WIT-01247

2455 WIT-01241

2456 WIT-01252

2457 WIT-01243 to WIT-01244

2458 WIT-01243 to WIT-01244

“Ofgem’s interpretation of ‘heating system’ was identified during the development of the GB RHI Regulations...”<sup>2459</sup>

“Ofgem’s interpretation focussed upon the presence of a hydraulic connection when assessing the extent of a ‘heating system’.”<sup>2460</sup>

48.14 In 2012 a number of Ofgem staff indicated some uncertainty about the clarity and consistency of its approach to this definition and the appropriate response to be adopted to multiple boiler installations:

- In April 2012 Pharoah Le Feuvre, an assistant manager in the RHI team in Ofgem, discussing a multiple installation question, stated:

“Yes they form part of the same heating system. Although it appears there is not [sic] set definition for this.”<sup>2461</sup>

- In May 2012 Ofgem wrote to AECOM with a request for technical consultancy on this and other issues and stated:

“Currently, a number of operational decisions involve the definition of a ‘heating system’. At present we do not have a consistent approach in dealing with applications where this definition comes into question.”<sup>2462</sup>

- In a response in June 2012 AECOM summarised their understanding of Ofgem’s concern that this term was ambiguous and was being interpreted inconsistently.<sup>2463</sup>
- The risk register for the RHI Fraud Prevention Strategy still contained reference to total installed capacity in September 2012.<sup>2464</sup> However earlier in 2012 Ofgem had adopted its working definition of ‘heating system’ which had the effect of altering the accumulation approach that had been recorded in the Ofgem risk and fraud documentation referred to above. It did not tell DETI of the working definition it had adopted, nor any of the potentially unwanted consequences that could flow from it (some of which had been the subject of warnings in the Ofgem 2011 Legal Review, albeit in the context of the absence of any definition of ‘heating system’).

48.15 As RHI Senior Technical Manager from early 2013, Dr Ward was a key figure in Ofgem with regard to technical questions in respect of the GB and NI RHI schemes. In his written evidence to the Inquiry he confirmed that his role included making final decisions on RHI scheme applications, including those for the NI RHI scheme.<sup>2465</sup> In his oral evidence to the Inquiry he related how Ofgem approached its interpretation of the meaning of heating system:

“...in the absence of a definition of heating system in the regulations, we have ultimately adopted what...a heating engineer or a man on the street might consider...constitutes a heating system. ...what would a plumber say? Where

2459 WIT-95410

2460 WIT-95411

2461 OFG-218493. Any claim for legal privilege in the text of the document OFG-218493 quoted in this report, or any claim for legal privilege in the copy document from which the quote is taken (and which is published by the Inquiry along with this Report), is waived by Ofgem purely for the purposes of the Inquiry, but not otherwise. In addition, it is not intended that any confidentiality or legal privilege in any other related material is waived as a result of the limited waiver in respect of the subject material.

2462 OFG-260460

2463 WIT-114584

2464 OFG-134921

2465 WIT-114045

is the heating systems? [sic] Well, it’s whatever pipework is connected to that boiler. That’s what forms part of the heating system. So this concept of physical connection or hydraulic connection is one which...forms the...core of Ofgem’s... interpretation of the regulations.”<sup>2466</sup>

48.16 The Inquiry notes that Dr Ward used both the concept of hydraulic and physical connection in the context of Ofgem’s working definition of heating system, but the approach applied in practice related only to hydraulic connection.

48.17 It appears that the approach being taken was not regarded as satisfactory by Ricardo/AEA, the company carrying out the RHI installation audits for Ofgem. As referred to previously, in November 2013, in Ricardo/AEA’s audit themes presentation to Ofgem, it explained what it described as “a number of unintended developments”<sup>2467</sup> that it had encountered in respect of multiple installations under the GB RHI scheme. Ricardo/AEA stated that what it found represented a “significant financial cost to the programme in terms of RHI payments”. It then went on to recommend that:

“- The definition of site boundary should be changed. Multiple installations on one site/property should be regarded as a single RHI installation. Applicant retains flexibility of multiple or individual boiler, total capacity of boilers sets tariff payment levels.

- Defining site boundary would negate the need to define a heating system in further detail, i.e. to amend regulations for hydraulically separated systems in Hereford case. This would be regarded as one installation as it is on the same site.”

48.18 The Inquiry notes that the Ricardo/AEA 2013 recommendation was actually how DECC’s original draft GB RHI regulations from 2011 had approached this issue, and that it was on Ofgem’s advice that the use of “site” was changed. The Inquiry did not see any evidence as to what Ofgem did in response to Ricardo/AEA’s recommendation. There is no evidence DETI was informed about it, nor about why Ricardo/AEA had made such a recommendation.

48.19 The Inquiry also saw evidence of emerging concern and uncertainty within Ofgem itself about the working definition as evidence of exploitation mounted. During the latter part of 2014, some staff within Ofgem tried to put forward an interpretation of ‘heating system’ to deal with the exploitation of which they were now aware. The approach put forward was, in effect, the same approach indicated in the earlier 2012 Ofgem risk and fraud documentation described above. For example:

- In April 2014, in an internal Ofgem email exchange about the definition of a heating system, Atika Ashraf stated:

“Ofgem currently have an informal definition of a heating system. This is not detailed in our guidance but means when accrediting an installation it is the hydraulic heating system which defines the boundary of the installation.”<sup>2468</sup>

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2466 TRA-09006 to TRA-09007

2467 OFG-87882

2468 OFG-260163

- In October 2014 a “layman’s type guide...based on the RO interpretation” was suggested in an internal Ofgem email exchange between Joseph Grice and Dr Ward.<sup>2469</sup> This went on to say that:

“If heat generating equipment is located on the same premises and provides space heating to the same volume of space or water then we would deem this to be one plant, even if the systems are not hydraulically linked.”<sup>2470</sup>
- Later in October 2014 a paper was prepared by Ofgem’s Valerio Pelizzi on the subject of the “Definition of one Heating System”.<sup>2471</sup> This outlined the issues and recorded that:

“Basically they [participants] split the existing heating system into two different hydraulically separated systems, even if these two applications are related to the “same” eligible use, i.e. both the heating systems feed the same poultry shed; this behaviour is allowed because it is not against the current Regulations .... Those behaviours seem to be a clear example of gaming the scheme, made to increase the periodic support payments but the legal team stopped us to chase those participants because we have no [sic] enough power to investigate and stop those requests and there is no specific Regulation that can support us against them.”<sup>2472</sup>
- In November 2014 the inconsistency between the new recommendations and the existing approach was discussed in an internal email exchange between Katy Read, senior policy manager at Ofgem from 2014,<sup>2473</sup> and Dr Ward. On 10 November Dr Ward wrote:

“An eligible biomass boiler feeding a water/air direct heat exchanger. This supplies a space which also has a wet heating system fed from a second independent biomass boiler. One plant-both systems feed a common space.”

48.20 Ms Read responded by observing that it seemed to go against what Ofgem had been saying about “...two different combustion units via separate pipework NOT making it one plant,” and it was decided to “stick with the previous line for now.”<sup>2474</sup>

- The Ofgem note prepared for a teleconference call with DETI officials on 27 January 2015 included, with reference to regulation 14 (1) of the GB RHI regulations:

“On the GB scheme Ofgem allows applicants to apply separately for installations which are hydraulically separate from each other, even if they generate heat for the same heat use (e.g. heat the same building/premises). This risks applicants abusing the system by deliberately installing two or more smaller boilers which are hydraulically separate, instead of installing a larger boiler which would potentially be more efficient but would be accredited on a lower tariff.”<sup>2475</sup>

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2469 OFG-260760

2470 OFG-260762

2471 OFG-260761 to OFG-260766

2472 OFG-260764

2473 OFG-260790 to OFG-260792

2474 OFG-260789

2475 OFG-31160

- 48.21 In the course of making a note of the contents of the call Mr Hughes of DETI recorded “‘More than one boiler’, working definition needed.”<sup>2476</sup>
- 48.22 Even in 2019, there still appeared to be open questions about what is meant by the term ‘heating system’. In its written statement to the Inquiry of 29 March 2019, Ofgem stated that the NI RHI regulations which it had to interpret were not internally consistent in terms of the interaction between a heat generating installation and a heating system. Due to the inconsistencies throughout the regulations as to whether a heat generating installation was part of, or discrete from, a heating system, Ofgem’s interpretation of ‘heating system’ had to be capable of accommodating both approaches.<sup>2477</sup>

### Definitions in guidance

- 48.23 Despite the Ofgem warning against clarifying the term in guidance, the formal ‘NI RHI Guidance Document, Volume 1: Eligibility and How to Apply from November 2012’, produced by Ofgem for the NI RHI scheme,<sup>2478</sup> provided direction regarding multiple plant.
- 48.24 This guidance appeared to be focused upon administration issues, such as how many applications to make. For instance, in the section of the guidance entitled “How to apply when you have multiple plants” the document states at paragraph 2.27:

“Applicants should apply only once for each installation for which they wish to claim NIRHI support. If you have multiple plants, then you need to know whether these need to be applied for separately or if they should be considered together as a single installation.”<sup>2479</sup>

- 48.25 And further at paragraph 2.28:

“As provided in the Regulations, an installation can consist only of one plant unless two or more plants making up an installation meet the following criteria:

- o the component plant meets the eligibility criteria
- o the plants use the same source of energy and technology (e.g. ground source heat pump)
- o the plants form part of a common heating system, and
- o none of the plants has already been accredited as an NIRHI installation.

In these cases, two or more component plants will be regarded as a single plant for NIRHI purposes if, in addition, the eligibility criteria referred to in the Regulations are also satisfied and you should make one application for that single plant.”<sup>2480</sup>

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2476 IND-04414

2477 WIT-95410

2478 INQ-30020 to INQ-30182

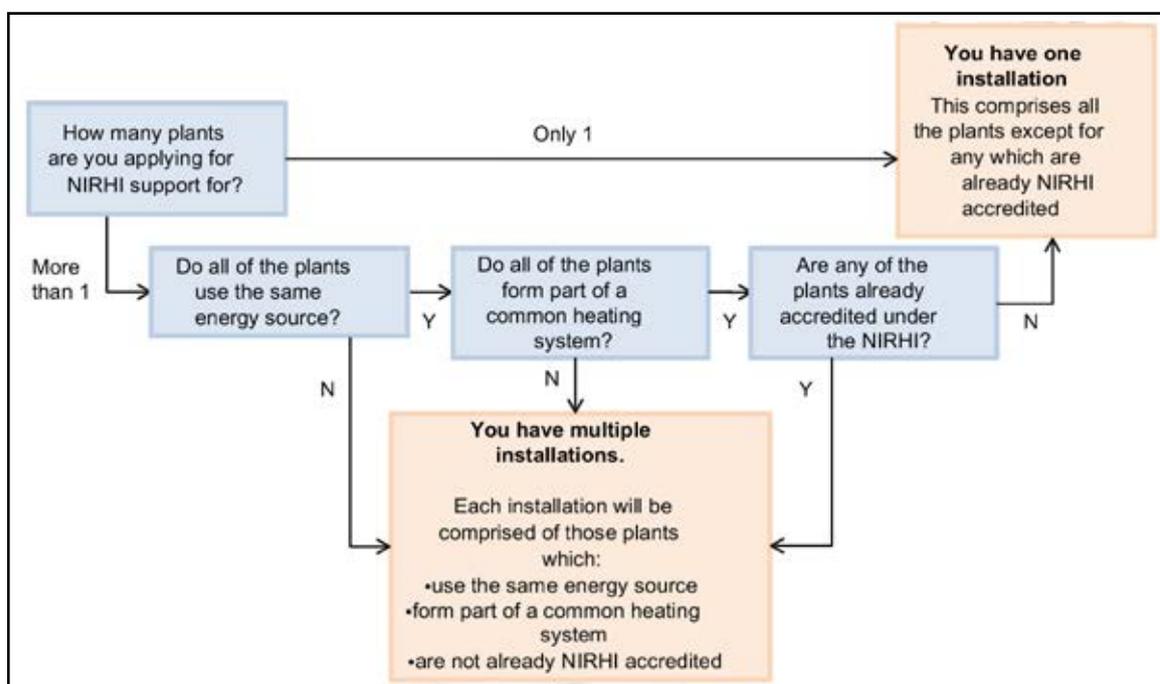
2479 INQ-30036

2480 INQ-30036

48.26 An explanatory flowchart, set out in Figure 3 of the guidance, is also included:

**Figure 5 – NI RHI Guidance Document on Multiple Plant Application**

Figure 3: Do I need to submit a single application for NIRHI support or multiple applications?



48.27 In paragraph 2.32 there is a reference to the combined installation capacity, but in relation to eligibility criteria like metering arrangements.<sup>2481</sup>

48.28 The Inquiry concludes from this that the guidance is primarily concerned with how many applications were needed. There is no mention of how the tariff for multiple installations would be determined.

### Ofgem’s consideration of its interpretation

48.29 Ofgem stated in written evidence to the Inquiry that:

“In this context, the interpretation of what ‘a plant’ means in paragraph (1) [of regulation 14] is key. To date it has been interpreted by Ofgem as meaning an installation which is the subject of an application for accreditation.”<sup>2482</sup>

48.30 This suggests that whatever the application happened to cover was the basis used by Ofgem in determining the eligibility of the application. It appears to the Inquiry that Ofgem therefore only considered regulation 14 when it received a specific application with explicit reference to multiple units.<sup>2483</sup>

48.31 In April 2012 an internal Ofgem email exchange took place between Marcus Porter, Lindsay Goater and Pharoah Le Feuvre in which consideration was given to the interpretation of

2481 INQ-30037

2482 WIT-95415

2483 WIT-95414 to WIT-95417

regulation 14 in the context of an application for a multiple plant installation to be included in the GB RHI scheme.<sup>2484</sup> In this exchange the primary concerns appeared again to be administrative.

48.32 Ofgem lawyer Marcus Porter suggested that if there was a problem with a single application for multiple plant:

“Following considerable discussion of the matter last Autumn (including with DECC) it was concluded that it should still be permissible in this situation to make separate applications for accreditation in respect of the individual component plants.”<sup>2485</sup>

48.33 In the given example, concerned with three component heating plants, Lindsay Goater, an Ofgem E-Serve RHI manager, stated:

“There are several administrative hurdles to the treatment of them as 3 HPs, which I appreciate do not allow any violation of the law! They will have the same address, which the IT system does not allow, and we have 3 times the work, almost (1 lot of thinking!).”<sup>2486</sup>

48.34 He went on to suggest that if the individual plants were to receive a higher tariff than the combined one “a further implication *could* be over-compensation” (Mr Goater’s emphasis). He thought that this was “arguably not the policy intent” and that “**Reg. 14 is there in fact to group such plants.**”<sup>2487</sup> (Mr Goater’s emphasis)

48.35 Marcus Porter responded that:

“This is a really difficult situation and it makes plain that Reg. 14 arguably does not achieve DECC’s declared intention for it (to prevent the gaming of the tariff structure) or at any rate doesn’t do so in clear terms.”

48.36 Marcus Porter accepted that the objective of DECC was to try to avoid gaming of the tariff structure but he repeated that if, due to the application of both the requirements of regulation 14, a single application made up of other plants failed, then separate applications would be necessary and that might, in some cases, result in a higher tariff being payable. He added:

“This does not seem in keeping with the apparent policy objective and for this reason DECC may wish to review the provision at the earliest opportunity with a view to amending it in a suitable fashion.”<sup>2488</sup>

48.37 The Inquiry notes that no consideration was given to informing DETI, at a time some six months prior to the coming into force of the NI RHI regulations, of the fact Ofgem was dealing with a concrete example on the GB RHI scheme which provided evidence as to why there was a crucial need to consider properly and resolve the multiple plant issue.

48.38 As discussed above, in May 2012, Ofgem consulted AECOM on a technical definition of ‘heating system’. However, this was in relation to issues of metering regarding regulations 16 and 17

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2484 OFG-218489 to OFG-218493. Any claim for legal privilege in the text of the document OFG-218489 to OFG-218493 quoted in this report, or any claim for legal privilege in the copy document from which the quote is taken (and which is published by the Inquiry along with this Report), is waived by Ofgem purely for the purposes of the Inquiry, but not otherwise. In addition, it is not intended that any confidentiality or legal privilege in any other related material is waived as a result of the limited waiver in respect of the subject material.

2485 OFG-218492 (See footnote 2484)

2486 OFG-218490 (See footnote 2484)

2487 OFG-218490 (See footnote 2484)

2488 OFG-218489 (See footnote 2484)

and not accreditation or tariff determination under regulation 14.<sup>2489</sup> The definition of a heating system that emerged from this process was:

- The heating system comprises all heat sources, equipment, distribution systems and heat uses necessary for the safe and controlled generation and delivery of heat from the heat sources to the heat uses.
- Heating plants/installations, heat uses or heat distribution are considered part of the same heating system whenever there is a physical connection linking them to the system.<sup>2490</sup>

48.39 The Inquiry notes that Ofgem’s approach, based only on whether there was “hydraulic” connection rather than “physical” connection, had the effect of allowing many more boilers to accredit as single installations than would have been the case under the AECOM definition, had it been adopted. However, Ofgem has not produced any material to the Inquiry to establish that any technical or legal consideration was given internally to the AECOM report<sup>2491</sup> when it was received, nor any material to show how its working definition came to be adopted. Of even greater import in the present context was the fact that this process, and the definition that resulted from it, was being conducted by Ofgem without any recourse to DETI. Indeed, DETI was not provided with the AECOM report about ‘heating system’ until this Inquiry was conducting its investigations.

48.40 Ofgem could not provide evidence that any alternative technical or legal consideration had been given to its own interpretation and application of regulation 14 in connection with heating systems until July 2017, a year and a half after the NI RHI scheme had been closed to new applicants.<sup>2492</sup>

## Evidence of problems with multiple boilers

48.41 The Inquiry considered many examples of the problems caused by multiple boiler accreditations which Ofgem’s November 2011 Legal Review had foretold for the NI RHI scheme. This included the November 2013 presentation from Ricardo/AEA, Ofgem’s audit sub-contractor, from its experience of audits of the GB RHI scheme.<sup>2493</sup> In its presentation Ricardo/AEA highlighted:

- Hydraulically separate multiple boilers are heating the same space.<sup>2494</sup>
- Systems are designed to maximise RHI benefits that would not have been designed this way without the RHI.<sup>2495</sup>
- Multiple installations represent a significant financial cost to the programme.<sup>2496</sup>
- Multiple installations on one site should be regarded as a single installation.<sup>2497</sup>

48.42 As mentioned previously in this Report, Ofgem did not provide DETI with that presentation, or even a summary of the issues arising from it. However, the problem was not just being brought

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2489 WIT-95402

2490 WIT-114584 to WIT-114596

2491 WIT-95409

2492 WIT-95415

2493 OFG-87862 to OFG-87887

2494 OFG-87874

2495 OFG-87882

2496 OFG-87882

2497 OFG-87882

to Ofgem’s attention through the GB RHI scheme. In an email to Dr Ward dated 15 August 2013 Alastair Nicol, a consultant working for Invest NI (and whose concerns about the operation of the NI RHI scheme were expressed in his reports for Invest NI and its client businesses, which have been dealt with earlier in this Report), stated:

“I seek urgent advice on the interpretation of the RHI as applied in Northern Ireland. We work for a quasi-Governmental Organisation in Northern Ireland and in one particular project they are adamant a multiple boiler solution may be used to maximise RHI benefits. This is at odds with my reading and understanding but perhaps you or Jacqui could consider and clarify. The situation is probably best summarised by the three cases below - I’ve exaggerated the values to illustrate the case clearly. The question is one of aggregation. Would you be kind enough to advise.”<sup>2498</sup>

48.43 Details of the three cases were provided. This communication seems to have generated an internal discussion in Ofgem, with Dr Ward then confirming to Mr Nichol that what was proposed was acceptable.

48.44 In February 2014, after attending an industry event in GB, Jacqueline Balian of Ofgem, who was then in charge of RHI operations, told DECC that:

“However, one thing that you need to be aware of is the amount of noise about the multiple...boiler issue. Many of those present mentioned it, one saying ‘I know quite a few people in our local farming community who are saying they’re giving up sheep and just raking in the money from the RHI.’ Others saying that they are being asked all the time about putting in multiple installations and that reasons for fitting multi biomass boilers are being sought far and wide. One or two ask if this can possibly be right and saying that they don’t agree with it but all their clients are asking for it. Others asking how long they have before the loophole is closed...”<sup>2499</sup>

48.45 In July 2014 a director of an English private company involved in the sale of heating systems had emailed Ofgem saying that:

“I am growing increasingly frustrated by the obvious oversizing of boilers we hear about on a regular basis, with 199kW boilers apparently being installed by some Companies as though there is no other size of boiler available...

1 – As a taxpayer I object to seeing tax revenues wasted

2 – It is incredibly frustrating to see an excellent incentive scheme which is designed to help reduce greenhouse gases being misused and consumers actively encouraged to generate heat that serves no useful purpose purely in order to generate RHI income

3 – Every £ of the RHI budget that is wasted in this way is a £ less to be spent on genuine installations, and means we hit depression far faster than we would otherwise.”<sup>2500</sup>

48.46 In November 2014 feedback from an agricultural conference in Scotland, which was again attended by Ms Balian, included information that returns were so high that farmers were

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2498 OFG-164264 to OFG-164266

2499 OFG-260635

2500 OFG-260645

planning installations without an existing or planned heat requirement. Another farmer had sold his herd of cows in order to prepare his sheds for RHI installations without having decided what the heat produced would be used for, and farmers were generating heat for drying until they had used up their tier one allowance when the boiler would be turned off and other technologies that appeared very energy inefficient were turned on.<sup>2501</sup>

48.47 In order to illustrate the scale of the problem the Inquiry has included a real-life example. The picture below<sup>2502</sup> is of eight 199kW boilers installed in a single building. It was sent to Ofgem by DECC in December 2014. DECC had received it from a private sector energy company. It was described by DECC as providing “an interesting case study from the poultry sector” in GB.<sup>2503</sup>

48.48 To the Inquiry, and no doubt to most people, it looks like a single energy centre or single heating system. The reader might reasonably have assumed that the accumulated output value of the eight boilers would be used to determine the RHI tariff to which the owner was entitled. Instead, the pipework had been configured without hydraulic connection between the various boilers in order to facilitate accreditation on the GB RHI scheme as eight individual installations. Each accredited boiler attracts the higher tariff, as compared to the tariff to which the owner would have been entitled had the boilers been treated as one single heating system.

**Figure 6 – A Multiple Boiler Installation**



2501 OFG-261209

2502 OFG-260198

2503 OFG-260197

- 48.49 Ofgem’s approach, as with this example, was to accept a series of separate applications and accredit each individual boiler rather than accumulating their capacity. The result was, and is, that each individual boiler was able to access the highest tariff, requiring approximately four times the subsidy than would have been payable if the tariff had been based on accumulated capacity (whether or not such a system ought to merit any tariff from public funds is another matter). For example, the total capacity of the plant in the illustration was 1,592kW, in excess of the 1,000kW banding threshold. In GB, on an accumulated basis, this would only have received a subsidy of 2.25p/kWh, rather than 9.92p/kWh on the basis of individual boilers (at 2019-20 tariff rates).
- 48.50 It is not within the Inquiry’s terms of reference to make findings in relation to the GB non-domestic RHI scheme or Ofgem’s management of that scheme. However, it is apparent from the evidence that, as far back as 2012, information was available within Ofgem on the use of multiple boilers in the GB RHI scheme that suggested that the risks identified in Ofgem’s earlier warnings to DETI were materialising. In addition, by 2014 that information was reinforced by what some Ofgem staff were hearing at conferences and by the emergence of individual case studies. It is clear that during 2014 Ofgem had received emails from industry relating to instances of oversizing and wasting heat for higher payments.<sup>2504</sup> None of this material was shared with DETI, thus depriving it of an opportunity to act sooner to clamp down on exploitation of the NI RHI scheme by multiple boiler usage.
- 48.51 As mentioned previously, Ms Katy Read was a senior policy manager with Ofgem. According to Dr Ward she was responsible for Ofgem’s engagement on regulation changes and how such changes would be administered.<sup>2505</sup> When she was enrolled as a part-time student at Birkbeck College, University of London, she conducted a number of interviews with installers in preparation for a paper entitled ‘The Non-Domestic Renewable Heat Incentive; The Roles and Perspectives of Installers’.<sup>2506</sup> She presented that paper as an academic dissertation for her MSc in Climate Change Management in September 2014. The interviews with installers had been conducted in the spring of 2014. The majority of interviewees (12 in total) brought up the practice of oversizing biomass boilers in order for customers to earn a higher GB RHI income. In her subsequent paper of January 2015, ‘Gaming – Wasting Heat’,<sup>2507</sup> Ms Read noted that there had been a general view that projects were being “designed around the RHI to maximise their revenue essentially rather than it being designed to meet the demand on the site”.<sup>2508</sup>
- 48.52 Valerio Pelizzi, another member of the Ofgem team, produced a paper in December 2014 entitled ‘Gaming Multiple Heating Systems’<sup>2509</sup> in which the risk of overcompensation on the GB RHI scheme, by running boilers up to the 1,314 working hours at full capacity for Tier 1 and then switching to another boiler, was recognised. The examples of a poultry shed and grain drying were analysed in order to illustrate the potential for excessive payments. Later in the same paper Mr Pelizzi estimated the potential financial overpayment of permitting separate applications in respect of 436 poultry sheds to be in the region of £92 million over 20 years

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2504 OFG-260772

2505 TRA-09097

2506 WIT-114709 to WIT-114784

2507 WIT-114696 to WIT-114708

2508 WIT-114703

2509 OFG-260805 to OFG-260807; WIT-114693

under the GB scheme. As noted previously, Mr Pelizzi had provided a summary document in October 2014 which recorded that:

“If heat generating equipment is located on the same premises and provides space heating to the same volume of space or water then we would deem this to be one plant even if the systems are not hydraulically linked. Any equipment which meets the criteria set out in regulation 14 and shares common primary or secondary pipework would be deemed as one plant.”<sup>2510</sup>

48.53 Ms Read’s paper entitled ‘Gaming – Wasting Heat’, was circulated internally to Ofgem staff, including Dr Ward, on 6 January 2015. It related to different forms of gaming thought to be occurring in the non-domestic GB RHI scheme. According to Dr Ward the core of Ms Read’s January 2015 paper was drawn from the earlier December 2014 paper from Mr Pelizzi. Mr Pelizzi’s work was referred to at page 5 of Ms Read’s paper for further analysis of the cost implications of multiple smaller boilers on separate heating systems.<sup>2511</sup>

48.54 Ms Read’s 2015 paper was to be furnished to DECC and commenced with the following background:

“OFGEM are aware of scenarios where participants may be gaming the non-domestic RHI by wasting heat in order to increase their RHI payments. Some of these have been discussed with our legal team and with DECC on previous occasions, but without a clear view on how to proceed with dealing with these issues. Since the scale of these issues is likely to increase over time and external attention appears to be growing, the associated risks are becoming more significant.”<sup>2512</sup>

48.55 Examples of wasting heat included designing the installation in such a way that RHI payments were maximised either by the installation of an incorrectly sized boiler/boilers or a heat use created because of the existence of the RHI payments or simply wasting heat following accreditation to the RHI, through actions such as designing particularly inefficient processes, venting more than necessary, opening doors and windows etc. In the context of the GB RHI scheme, upon which the analysis was based, the paper recorded:

“Heating systems may be split up in order to have multiple smaller boilers on separate heating systems instead of one large boiler, in order to meet the heat demand of the site... If so, this presents bad value to the tax payer. It may also mean that the overall efficiency is lower, reducing the amount of carbon savings. The separate analysis of split heating systems with 199kW boilers shows that the wasted heat could be worth around £211,469.00 over the lifetime of the scheme per accreditation. We think there are roughly 60 examples of this so far for poultry sheds alone, so the total overpayment would be £12,688,113.00.”<sup>2513</sup>

48.56 The paper revealed that in October 2014 Ofgem had been advised by a heat pump installer that installations were being oversized with the aim of increasing Tier 1 payments on the GB RHI scheme. This was not new information for Ofgem. The paper also indicated that Ofgem was aware of the November 2014 article in the *Daily Mirror* newspaper, referred to previously

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2510 OFG-260762

2511 WIT-114700

2512 WIT-114696

2513 WIT-114700

in this Report, which said that the GB RHI scheme was facilitating the rich to enjoy free fuel and taxpayers’ millions through the use of multiple boilers. Under the heading “Conclusion” Ms Read highlighted the following:

- “There is potentially a significant amount of heat waste occurring on the RHI.
- The Regulations do not allow OFGEM to address these issues as described in the paper.
- The example provided appeared to go against the intent of Regulation 34 (p) [Regulation 33 (p) in the NI Regulations] and the overarching intent of UK energy policy to reduce carbon emissions by replacing fossil fuel use with renewable energy.
- There are risks to Ofgem and DECC as there is growing attention on the potential payment of taxpayer funds to people wasting heat and there may be the perspective that nothing is being done to address this. This also presents a risk to the achievement of carbon savings.”<sup>2514</sup>

48.57 It seems that it did not occur to anyone in Ofgem who was familiar with Ms Read’s January 2015 paper to furnish a copy of that paper to DETI. Dr Ward told the Inquiry that the paper had been shared with DECC and that he had discussed the conclusions expressed in Ms Read’s papers with Mr Wightman and Mr Hughes in a meeting in January 2015. He also said that a summary of the paper was shared with DETI by Ms Read later in 2015.<sup>2515</sup> However, it does not appear that any part of the papers themselves was made available to DETI; instead, in response to an enquiry from Mr Hughes about interpretation in respect of multiple boilers, Ms Read supplied him with an extract from the conclusions of her January paper.<sup>2516</sup>

## Impact and cost of allowing multiple boilers

48.58 Ofgem accepted in its closing written submission to the Inquiry that its interpretation of ‘heating system’ permitted gaming of the regulations, although it qualified that acceptance by stating that it had no choice but to comply with the regulations.<sup>2517</sup> This resulted in the design and operation of installations that would not have been so configured in the absence of the RHI scheme. The approach undermined both banding and tiering, with a considerable number of users under or over-sizing boilers to maximise the tariff that they could access.

48.59 Almost two-thirds of all biomass accreditations in Northern Ireland across the life of the non-domestic RHI scheme were in respect of installations that form part of multiple boiler configurations.<sup>2518</sup> Furthermore, in the financial years 2016-17 and 2017-18 almost three-quarters of all payments made in respect of biomass installations were in respect of those that form part of multiple boiler configurations.<sup>2519</sup>

48.60 Until the introduction of tiered tariffs and amended banding in November 2015, three-quarters of all boilers were also exactly 99kW in capacity. However the fundamental problem of multiple boilers was not resolved in November 2015. After the changes in November 2015, which included the introduction of tiering and extending the upper capacity of boilers eligible for the medium band to 199kW, the Inquiry found very clear evidence of how a new set of design and

2514 WIT-114707

2515 TRA-09103

2516 DFE-310157

2517 SUB-01005

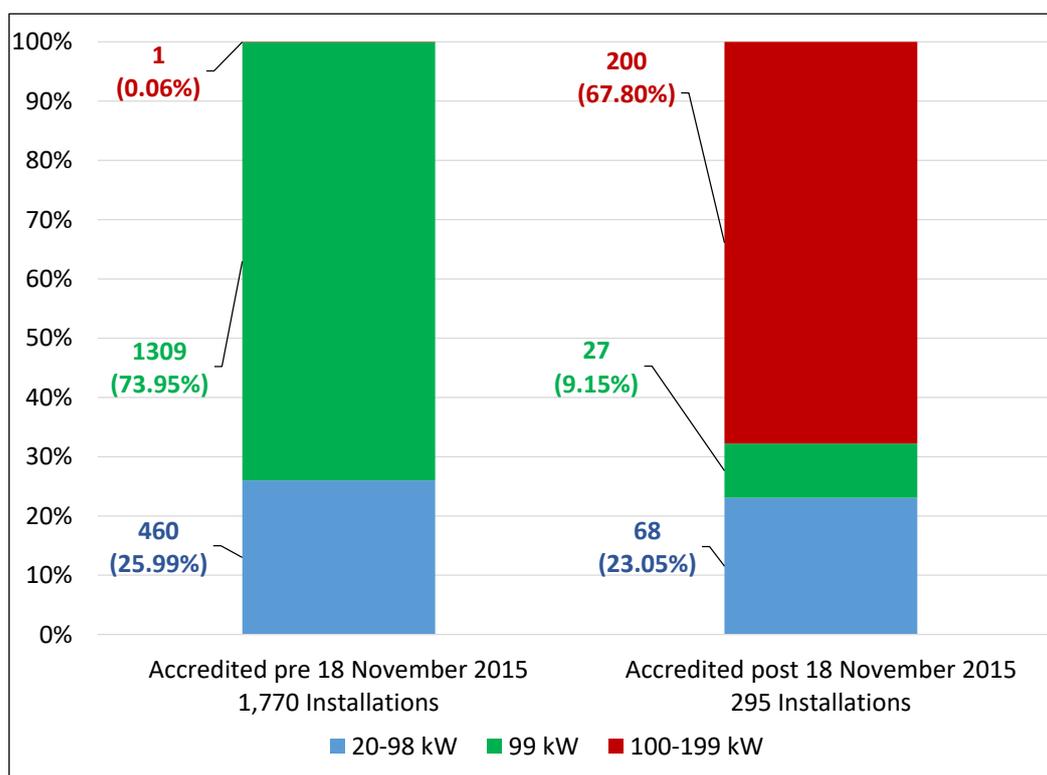
2518 OFG-137208

2519 OFG-137205; OFG-137208

operation characteristics developed by still using multiple boilers. Figure 7 below, provided to the Inquiry by DfE, shows the impact the November 2015 changes had on installation patterns and demonstrates a switch away from the previously ubiquitous 99kW boilers to much larger ones, many at or near the new medium biomass upper limit of 199kW.<sup>2520</sup>

**Figure 7 – Comparison of Installation Patterns**

**Comparison of Installation Patterns of 20-199kW Solid Biomass Boilers Accredited Pre and Post 18 November 2015**



48.61 As the above figure illustrates, post-November 2015, the share of the market for 99kW boilers fell to less than 10% within three months (it had previously been in excess of 70%).

48.62 As a consequence of the introduction of tiering in November 2015, which limited the higher Tier 1 tariffs in the small and medium biomass bands to the first 15% of renewable heat produced, the previously high average annual load factor of biomass boilers dropped from about 45% to almost exactly 15%. However, users continued to benefit from Ofgem’s approach to multiple boilers by installing multiple larger units which could produce the same amount of renewable heat at much lower load factors but continue to attract the highest tariff payments. As a result, and despite DETI’s expectations, the average tariff paid out to users after the changes only reduced by 6%.<sup>2521</sup>

48.63 In its evidence to the Inquiry CEPA estimated that avoiding the problems with multiple boilers could have saved about half of the projected lifetime cost of the scheme.<sup>2522</sup>

2520 DFE-467804

2521 DFE-467803

2522 WIT-107931

48.64 Based on the NIAO Report, produced by the Comptroller and Auditor General for Northern Ireland, on DfE’s Resource Accounts for 2018-19,<sup>2523</sup> the Inquiry notes that by 2016-17 annual RHI scheme costs were running at £42 million – equivalent to roughly £840 million over a 20-year period. About two-thirds of these payments were, and are, being made in respect of multiple boiler installations - equivalent to about £560 million over 20 years. The following table, produced by the Inquiry based on figures supplied by the NIAO, shows the potential savings that could have resulted from paying the large biomass tariff of 1.5p/kWh (if multiple boilers had been accumulated), rather than the higher medium biomass tariff of 6.0p/kWh (for each separate boiler), based on a given proportion of the multiple boilers.

**Table 5 – Potential Savings**

Proportion of multiple ‘ineligible’ boilers on lower tariff	A = Cost of lower tariff	B = Cost of higher tariff	Potential savings £560m – A – B
100%	£140m	£0m	£420m
75%	£105m	£140m	£315m
50%	£70m	£280m	£210m
25%	£35m	£420m	£105m

48.65 Therefore, prior to further corrective measures since taken by DfE to reduce costs, the impact of Ofgem’s interpretation of multiple boilers has been to increase the lifetime costs of the scheme by a sum that, subject to the caveat below, the Inquiry estimates to be measurable in the hundreds of millions of pounds.

48.66 The Inquiry heard representations which suggested that some multiple boiler users had valid reasons for their design and were not exploiting the scheme. It is important to record that the Inquiry accepts that this is likely to be the case in some instances, but, even if there was a good technical reason for some multiple rather than single installations, the Inquiry questions whether compensation of these larger users who had economies of scale and chose such a design for their own further benefit should have been paid at the highest rate out of public expenditure.

### **DETI’s understanding of the interpretation**

48.67 Ofgem claimed that the approach to multiple boilers which it had adopted was based upon DETI’s policy intent as reflected in the 2012 NI RHI regulations. DETI was not to become properly aware of Ofgem’s approach until December 2014 or January 2015 when a meeting was called between Ofgem and DETI to discuss the matter.

- 48.68 Mr Hutchinson of DETI told the Inquiry that his original belief was that if two or more boilers were used to heat the same building/space their capacities should be viewed as cumulative for the purpose of assessing the appropriate tariff.<sup>2524</sup> In his written evidence to the Inquiry he stated that he believed that he derived that understanding from discussions with Ofgem officials during consultations on the DETI/Ofgem RHI guidance documents in 2012, and he gave that advice in response to enquiries from applicants with the caveat that Ofgem was the final arbiter of accreditation.
- 48.69 Mr Hutchinson told the Inquiry in written evidence that if he, or other colleagues in Energy Division’s Renewable Heat Branch, had been informed of the relevant working definition adopted by Ofgem, DETI would have advised that it did not appear to be consistent with the policy intent of the NI RHI scheme. He said DETI would have sought an explanation from Ofgem as to how the definition had arisen, and the potential implications for the scheme, and required an assessment of the potential financial impact. If necessary, legislative amendments might have been discussed.<sup>2525</sup>
- 48.70 In his oral evidence to the Inquiry Mr Hutchinson accepted that his understanding was different from Ofgem’s approach in practice and it was possible that he had not fully understood the term “hydraulically separate”, and that in the circumstances his understanding in 2012 was wrong. He acknowledged that Ofgem had given a warning about the need to have a clear definition of ‘heating system’ in the 2011 Legal Review of the regulations.<sup>2526</sup>
- 48.71 As noted earlier in this Report, in December 2014 Mr Hughes received an enquiry from David Hamilton, a potential applicant, relating to the appropriate tariff for five hydraulically separate 99kW boilers heating a common airspace. Mr Hughes responded that it was really a matter for Ofgem which administered the scheme. However, Mr Hughes did indicate “What I can say, however, is that RHI tariff would be based on the total heat requirement in this instance 500kW...”.<sup>2527</sup>
- 48.72 Mr Hughes said that he would raise the matter with Ofgem. The issue was discussed during the course of a teleconference with Ofgem on 27 January 2015. The note of the discussion made by Mr Hughes confirmed that he was told that the working technical definition of a heating system in GB was that boilers had to be hydraulically connected to form a single system and there was no specific definition in NI.<sup>2528</sup> He was unhappy with Ofgem’s interpretation, stating that “this was never the policy intent” and he and his colleagues then attempted, unsuccessfully, to agree the necessary changes to the regulations and/or their interpretation with Ofgem.<sup>2529</sup>
- 48.73 In Ofgem’s communication setting up the conference call on 27 January 2015 it confirmed that its approach to multiple boilers risked applicants “abusing the system”.<sup>2530</sup>

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2524 WIT-09313

2525 WIT-09312 to WIT-09315

2526 TRA-04862 to TRA-04867

2527 DFE-106803 to DFE-106810

2528 DFE-385810

2529 DFE-120640

2530 OFG-31155 to OFG-31161

## Findings

261. The Inquiry concludes that DETI’s policy intent was for the RHI to provide an incentive, not to reward. This was explicit in paragraph 3.24 of the July 2011 DETI consultation document.<sup>2531</sup>
262. As part of the intention to incentivise and not reward, DETI’s policy intent for multiple installations, as reflected in paragraph 3.26 of its 2011 RHI consultation document,<sup>2532</sup> was to avoid a number of smaller installations being installed to provide heat for one heat source in order to avail of higher tariff levels. This was to be achieved by multiple installations being regarded as one heating system with the accumulated capacities of the various installations determining the payable tariff.
263. In November 2011 Ofgem had warned of the need to define properly the term ‘heating system’ in the NI RHI regulations as there was a risk, without a proper definition, that, amongst other things, some participants may install multiple smaller units in order to avail of higher tariff. Ofgem also said it was not acceptable for the term to be clarified in guidance.
264. DETI did not take Ofgem’s advice, repeating a similar course taken by DECC, and the NI RHI regulations were introduced with no definition of ‘heating system’. The regulations should not have been introduced without a proper definition of the term ‘heating system’, if this was to be the means to achieve the policy intent relating to multiple installations as set out in July 2011.
265. The policy intent expressed in the 2011 consultation document was not adequately reflected in the form in which the 2012 regulations were drafted and implemented.
266. During 2012 Ofgem adopted a working interpretation of ‘heating system’ based on the concept of ‘hydraulic separation’. The effect of that interpretation, however unintended, was to facilitate (as Ofgem said itself in the context of the 2015 teleconference) abuse of the RHI scheme. It did so without recourse to DETI; it should not have done.
267. Ofgem should have told DETI in 2012 of the interpretation Ofgem was adopting, as soon as it adopted it. Ofgem should also have told DETI of the potential consequences of the interpretation that Ofgem was adopting.
268. Ofgem should have told DETI each time Ofgem became aware of an actual instance of Ofgem’s ‘heating system’ interpretation facilitating the introduction of multiple boilers, thereby exploiting the tariffs.
269. Ofgem should have provided DETI with the findings of Ricardo/AEA as set out in its November 2013 presentation, and drawn DETI’s specific attention to the fact that, in respect of multiple installations, Ricardo/AEA had found unintended developments that represented a significant financial cost to the RHI scheme. Ofgem should also have informed DETI of Ricardo/AEA’s recommendations as to how to deal with the problem it found in respect of multiple installations.

2531 DFE-29670

2532 DFE-29670

- 270. Ofgem should have provided DETI with the feedback that Ofgem was getting about the abuse of the RHI schemes through the installation of multiple boilers. The information should have been conveyed quickly to DETI as and when it was received by Ofgem.**
- 271. As Ofgem has acknowledged in its representations to the Inquiry, its interpretation of the term ‘heating system’ was a key contributing factor to the multiple boiler problem. Ofgem’s failure to communicate with DETI about that interpretation, and how it facilitated the fruition of the risk Ofgem had identified and warned DETI about in November 2011 (together with Ofgem’s failure to consider the potential consequences of that interpretation and its failure to share scheme data that demonstrated multiple boiler installations on the NI RHI scheme), deprived DETI of an opportunity to receive additional material. Such material would have supported the need to take appropriate steps to prevent the significant waste of public money that was occurring in the NI RHI scheme each time multiple installations were accredited by Ofgem without accumulation for tariff setting purposes, as well as to address the risk of overcompensation and potential breaches of State Aid. In these circumstances, and given the loss of this opportunity to DETI, the Inquiry is unable to accept Ofgem’s claim that there was no causal link between its failings and the NI RHI scheme overspend.<sup>2533</sup>**

## Heat waste

### The policy intent

48.74 The main reservation about revenue support mechanisms for heat is that there could be an incentive to produce the heat simply for the purpose of receiving the payments and to ‘open the windows’ to get rid of the excess heat, there being no ready means of transporting it to others or any market for it. The risk of this perverse incentive could arise at any time if the payments exceed the costs of producing heat. There is an added risk with heat systems that rely on fuel, as opposed to solar power, geothermal or air and ground-sourced heat, since the price of fuel may change at any time, potentially impacting on this perverse effect, even if initial tariffs are calculated correctly. Both DECC and DETI recognised these risks from the outset.

48.75 There was a clear policy intent by DETI to reward only the production of useful and efficient heat for eligible purposes and to avoid wasting heat or producing it simply to increase payments. This was embodied, at least to some degree, in the NI RHI regulations, especially 33(o) and (p) which set out the ongoing obligations of scheme users:

“(o) they must, if requested, provide evidence that the heat for which periodic support payments are made is used for an eligible purpose;

(p) they must not generate heat for the predominant purpose of increasing their periodic support payments.”<sup>2534</sup>

### Evidence of exploitation

48.76 Many examples of installations not meeting the policy intent and/or involving exploitation were brought to Ofgem’s attention from within the GB RHI scheme.

48.77 An internal presentation to the Ofgem RHI Implementation Board on 9 July 2013 warned that Ofgem E-Serve might shortly have to approve a large heat pump on the GB RHI scheme being used to heat a recreational lake which would be “against DECC policy intent”. The presentation also recorded that Ofgem E-Serve would have to approve applications from a poultry farm arguably installing separate heating networks “in order to maximise RHI payments by exploiting the tiered tariff”.<sup>2535</sup>

48.78 In its November 2013 presentation, referred to earlier in this Report, Ofgem’s site audit sub-contractor Ricardo/AEA, provided an overview of its experience of RHI auditing of installations on the GB scheme at that point and drew attention to “Challenging Audits” including an example of an installation using multiple hydraulically separate systems heating the same space to maximise RHI benefits. Ricardo/AEA saw this as an:

“Example of a participant reading the guidance documentation and identifying loopholes...this installation is an example of a system designed to maximise RHI benefits, [it] would not have been designed this way without RHI.”<sup>2536</sup>

48.79 That presentation also gave the examples of drying biomass to be used in RHI installations and claiming RHI on the heat used for drying, noting that these were some of a number of practices that represented a significant financial cost in terms of RHI payments. The presentation was also critical of the failure of the current regulations to provide a definition of “useful heat”.

2534 LEG-00018 to LEG-00019

2535 OFG-59175 to OFG-59176

2536 OFG-87874

- 48.80 Mr John, who from January 2014 led the Ofgem teams responsible for the operational delivery of the GB and NI non-domestic RHI schemes, was unable to say whether that Ricardo/AEA presentation had been supplied either to DECC or to DETI.<sup>2537</sup> The Inquiry found no evidence that DETI was ever provided with a copy of the presentation. Despite the fact that the presentation took place at a relatively early stage in the operation of the NI RHI, it appears that such documents were not shared with DETI although Mr John could not think of any reason why that should have been the case. The Inquiry also notes that Mr John has told the Inquiry that he personally had no knowledge of ‘gaming’ issues in the GB RHI scheme until the middle of 2014,<sup>2538</sup> when he became aware there was potentially: “like a looseness in the regulations or an opportunity for applicants/participants to enjoy a reasonable return.” However, he added that he had not seen any economic or policy analysis from which he could conclude that the return was unreasonable until much later.
- 48.81 Industry feedback about the GB RHI scheme emailed to the non-domestic RHI team in Ofgem in June 2014 recorded that “This topic keeps coming up, not least at Ofgem Industry Forums, where there has been much concern over the potential gaming on technologies which have a tiered tariff.”<sup>2539</sup> The same email recorded that there did not appear to be anything stopping the installation of over-sized equipment in order to increase the allowable kWh before a reduced tier payment was invoked and referred to a potential “perverse incentive to waste heat”. The topic of gaming was included in the agenda for the Ofgem Industry Advisory Group meeting on 30 October 2014 as a discussion topic and there was discussion about oversizing boilers and wasting heat.<sup>2540</sup>
- 48.82 The November 2014 article in the *Daily Mirror*,<sup>2541</sup> referred to earlier, and referenced in Ms Read’s paper of January 2015, was followed by two similar articles in *The Guardian* in January 2015<sup>2542</sup> which covered the same subject matter. In the second *Guardian* article, the scheme was described as one that “encourages as much waste as possible” producing astonishing returns sometimes in the region of 20%, 30% and even 40%. These articles have been dealt with in further detail earlier in this Report.

### Ofgem’s approach to scheme exploitation or ‘gaming’

- 48.83 It is important to emphasise that the Inquiry takes the view that the rather neutral term ‘gaming’ should not be permitted to detract from any activity that was clearly designed to exploit and maximise the financial profit from a scheme supported by public funds and conceived as being value for money.
- 48.84 On 19 January 2012, when discussions between Ofgem and DETI were at an early stage, Mr Cook, then Managing Director of Ofgem E-Serve, was sent an internal email from his deputy, Robert Hull, relating to the costs of administering the NI RHI scheme. The final sentence said:

“On strategy, a key value add which is not really mentioned is the benefit we provide in terms of fraud, error and gaming prevention and detection. This is of far greater value than any efficiency savings of us operating the scheme.”<sup>2543</sup>

2537 TRA-08967

2538 TRA-08869

2539 OFG-260793

2540 OFG-260767

2541 MED-05966 to MED-05970

2542 MED-05947 to MED-05951; MED-05956 to MED-05960

2543 OFG-03036

- 48.85 In the course of giving oral evidence to the Inquiry, Ofgem Chief Executive Dr Nolan accepted this January 2012 email, sent at a time before the NI RHI scheme came into existence, as indicating that the plan was for Ofgem E-Serve to add value in the area of reducing scheme exploitation.<sup>2544</sup> Documents from as early as 2011 clearly showed Ofgem’s intention to deal with ‘gaming’. The Ofgem RHI Fraud Prevention Strategy from March 2011 stated at paragraph 3.2:
- “This Fraud Prevention Strategy has a wider scope than activities that fall within the strict definition of fraud. Gaming opportunities and abuse of the system by participants are also considered.”<sup>2545</sup>
- 48.86 A later version of the Fraud Prevention Strategy from December 2013, which purported to apply to both the GB and NI RHI schemes,<sup>2546</sup> at Section 3.2, provided that:
- “This Fraud Strategy has a wider scope than activities that fall within the strict definition of fraud. Gaming opportunities and abuse of the system is also considered... our power to investigate, request information and take enforcement action is limited to participants.”
- 48.87 In section 7 of the document, paragraphs under a title of “Gaming Opportunities” pointed out that:
- “Participants may generate heat for eligible purposes but which do not meet the spirit of the RHI Regulations (e.g. heating empty buildings or empty greenhouses, using inappropriately sourced fuel), or may waste heat in a compliant manner by using heat in a non-energy efficient way.”<sup>2547</sup>
- 48.88 The same document continued to lay out options for prevention at section 7.3:
- “To help combat this, the RHI Regulations stipulate what constitutes eligible heat and give Ofgem the power to ask participants for evidence to demonstrate that the heat they are claiming RHI for is being used for eligible purposes. The Regulations also clearly state that participants should not generate heat purely for the purpose of increasing RHI payments. In addition, the tiered tariff for biomass (meaning a higher tariff rate is paid for the first 15% of annual heat generation hours) reduces the incentive to purposefully generate then waste heat.”<sup>2548</sup>
- 48.89 Despite being entitled as a strategy for the GB and **NI Non-Domestic Renewable Heat Incentive Scheme** (the Inquiry’s emphasis) that policy/strategy document, which was said to have “set out the means by which Ofgem will fulfil its responsibility to manage fraud, non-compliance and abuse within the GB and NI Non-Domestic Renewable Heat Incentive Scheme”,<sup>2549</sup> was not provided to DETI.
- 48.90 However, at an earlier RHI Implementation Board in July 2013 Ofgem considered that its powers were limited in applying sanctions to anyone who was “generating heat for the predominant purpose of increasing their periodic data support payments.”<sup>2550</sup> It explained that, in most

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2544 TRA-16366 to TRA-16368

2545 OFG-134842

2546 OFG-88519

2547 OFG-88523

2548 OFG-88523

2549 OFG-88518

2550 OFG-59176

cases, participants would be using the heat and that establishing the “predominant purpose” would not be straightforward. The line taken was:

“We have alerted the Government to this issue. However, this is a Government scheme that we administer, and only ministers can make the necessary changes to prevent this happening.”<sup>2551</sup>

48.91 An ever more passive approach to exploitation then appears to emerge over time, and the version of the RHI Fraud Prevention Strategy document from January 2015 sets out at paragraph 3 the scope and limitations of the RHI Fraud Prevention Strategy and, at paragraph 3.3, it contained a reference to ‘gaming’ opportunities stating that “We are aware that, as with many schemes, the design may allow for ‘gaming’ opportunities” followed by the words:

“It is important to note that such occurrences are not fraud as they are not in breach of the Regulations, however if we become aware of gaming activity we will report it to the NDRHI Development team so they can make DECC aware of areas where a legislation amendment might be considered.”<sup>2552</sup>

48.92 The Inquiry notes that, once again, there was no suggestion of a similar report to be made to DETI, which was purportedly part of a strategy applicable to both GB and NI RHI schemes.

48.93 The Inquiry also notes the contribution of Charles Hargreaves, who by 2019 led all of Ofgem’s RHI activities, to the Ofgem ‘Lessons Learned’ workshop at Millbank on 5 January 2017. He advanced the view at paragraph 6 of his contribution with regard to language that:

“We should have controlled the use of ‘gaming’ and been firmer in saying it was not appropriate for auditors to use this language – it’s either within the regulations or not.”<sup>2553</sup>

48.94 The Inquiry found it difficult to reconcile this view with the emphasis that Mr Hull had given in his January 2012 email to the “key value” which included gaming prevention and detection as well as the detailed late 2014 and early 2015 papers from Mr Pelizzi and Ms Read. The view expressed by Mr Hargreaves would appear, if implemented, to inhibit the flow of advice/warning from one Government Department to another which, if the advice/warning is provided, could lead to a reconsideration of relevant legislation in the interest of protecting public funds.

48.95 It is also difficult to reconcile such a view with the nature and quantity of material brought to the attention of Ofgem about the extent of the problem, or with the clear wording of paragraph 3.3 of the Ofgem RHI Fraud Prevention Strategy document of January 2015 quoted above. As noted earlier in this Report, as a result of the retrospective tariff changes introduced by DfE since 2017, which removed the perverse incentive to generate waste heat above 1,314 hours of operation, heat production has declined by 44% and scheme payments have halved.<sup>2554</sup>

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2551 OFG-59176

2552 OFG-134226

2553 OFG-131065

2554 INQ-115005 to INQ-115006

## Findings

- 272.** Ofgem should, at the time of introduction, have provided DETI with a copy of the RHI Fraud Prevention Strategy it had adopted after the NI RHI scheme was added to the Strategy. It should also have provided DETI with any subsequent version of the policy, together with an explanation for any changes to the approach being adopted.
- 273.** Each time Ofgem became aware of an allegation of exploitation of the RHI schemes it ought to have informed DETI about it immediately, and, as appropriate, made recommendations about how the exploitation said to be occurring could be addressed.

## Mixed domestic and non-domestic use

- 48.96 When the non-domestic NI RHI scheme was introduced in November 2012 installations generating heat solely for the use of one domestic premises were not eligible (see regulation 15(1)).<sup>2555</sup> The Renewable Heat Premium Payment scheme (RHPP) had been introduced much earlier in May 2012 by DETI and was to remain available for domestic premises until the domestic RHI scheme was launched.
- 48.97 The support levels under the non-domestic RHI scheme were higher than under the RHPP, and even when the domestic RHI scheme was introduced the non-domestic scheme offered more attractive returns, being available for twenty years rather than just seven.
- 48.98 The availability of more attractive returns meant that there was an incentive for individuals to explore the possibility of arranging for the heating of their domestic premises to be included in the non-domestic scheme. There were certain circumstances under which this might be permissible, often referred to as mixed use scenarios.
- 48.99 In the Northern Ireland context, the rules of the NI RHI scheme concerning what constituted “domestic” and “non-domestic” premises took on particular importance given the rural nature of the economy and the fact that many potential applications were to come from applicants engaged in agricultural activities of one type or another upon farms comprising both domestic and non-domestic premises requiring heat.

## The policy intent

- 48.100 Regulation 4 of the 2012 NI RHI regulations specified that a plant met the criteria to be an eligible installation for the non-domestic RHI scheme provided that, amongst other things, regulation 15 did not apply.
- 48.101 Regulation 15 (1) of the 2012 NI RHI regulations provided that:
- “Excluded Plants
- (1) This regulation applies where the plant –
- (a) is generating heat solely for the use of one domestic premises;
- (b) is, in the department’s opinion, generating heat solely for an ineligible purpose.
- (2) For the purposes of this regulation –
- ‘domestic premises’ means single, self-contained premises used wholly or mainly as a private residential dwelling where the fabric of the building has not been significantly adapted for non-residential use.”
- 48.102 The NI RHI scheme guidance repeated that installations heating one single domestic premises were ineligible. It went on at paragraph 4.43 to state that:
- “Accordingly, where a premises consists of a main property and other buildings such as outhouses, pool-houses, lean-tos etc. which are together treated as one self-contained unit in single occupation for Domestic rates, this would be likely to be treated as a ‘single self-contained’ premises for NI RHI purposes. Where such premises are ‘used wholly or mainly as a private residential dwelling where the

fabric of the building has not been significantly adapted for non-residential use,’  
the premises will therefore be treated as ‘domestic’ for the NI RHI.”<sup>2556</sup>

## Ofgem’s interpretation and approach

- 48.103 In order to understand how Ofgem approached the question of mixed domestic and non-domestic use in practice, the Inquiry has considered the illustrative example of how Ofgem dealt with Mr Brimstone’s installation. Mr Brimstone was a DUP Special Adviser (between August 2008 and November 2016) when he applied to the non-domestic NI RHI scheme. The Inquiry was considering Mr Brimstone’s application in any event, given his position and alleged involvement in relevant decision making about the scheme. His application was one in respect of which there was considerable debate within Ofgem as to the question of mixed use, which is dealt with in the section below.
- 48.104 It is important for the Inquiry to take into account its duty to be fair to both Mr Brimstone and Ofgem. In so doing the Inquiry wishes to acknowledge that Ofgem and Mr Brimstone were dealing with poorly drafted legislation which left open the possibility of domestic premises benefitting from the more generous subsidy paid for non-domestic use by reason of a minimal use of heat for non-domestic purposes and thereby opening the way to potential gaming/exploitation. In addition, while Mr Brimstone would have been aware of the non-domestic RHI subsidy being more generous than the domestic subsidy, the Inquiry acknowledges that the outcome of the enquiries/investigations referred to in this section of the Report have not resulted in any findings adverse to Mr Brimstone.
- 48.105 Mr Brimstone installed a biomass boiler on 6 August 2015 in a stand-alone shed, accessed from the back yard of his dwelling house, to heat both the shed and his domestic home premises. He applied for accreditation under the non-domestic RHI scheme, which was granted by Ofgem in April 2016. That accreditation was backdated to the date of application in August 2015. In the application letter the space within the shed was said to be “used as an agricultural workshop/storage and shed for both machinery and at times animal pens.” The shed was said to be used as “non-domestic” and to have been exempted from rates by the Land and Property Services (LPS) on the ground that its use was agricultural.
- 48.106 On 10 May 2016 Ofgem received an anonymous allegation of fraud on the part of Mr Brimstone which alleged that the installation by Mr Brimstone of a wood pellet boiler in the shed was fraudulent in that the use of the shed was not agricultural and that the installation was being used to obtain the more lucrative non-domestic subsidy for the domestic premises than would be available under the domestic scheme. Teri Clifton, then Ofgem Head of RHI Operations, immediately forwarded the anonymous allegation to the Ofgem Counter Fraud Team.<sup>2557</sup> Internal emails show a discussion took place about whether this “borderline case” merited a site audit.
- 48.107 It is clear that Ofgem were also aware that “it could be politically sensitive given that the installation’s authorised signatory is a Special Adviser to the First Minister of Northern Ireland”.<sup>2558</sup> Ms Clifton referred to the ensuing investigation as “our special case”.<sup>2559</sup> In her

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2556 INQ-30050

2557 OFG-128251

2558 OFG-65218

2559 OFG-113892

written evidence to the Inquiry she emphasised that while the case was treated with “additional sensitivity”, and consideration of it was “escalated to a greater extent than would ordinarily be the case”, it was subject to normal processes as regards a compliance and counter fraud investigation.<sup>2560</sup>

48.108 Within Ofgem E-Serve, in addition to the RHI Operations Team, there was both an RHI Audit and Compliance Team and a separate E-Serve Counter Fraud Team. The audit team had responsibility for setting up and receiving audits as well as deciding whether any further information was required in order to determine whether an installation was compliant. The Counter Fraud Team had responsibility for all fraud prevention and detection activity across Ofgem E-Serve.

48.109 Later in May 2016 a counter fraud case relating to Mr Brimstone was opened within Ofgem, stating that:

“From our initial assessment of the available information, it appears that the party in question might have dishonestly made a false representation and through this act intends to make a gain for themselves or another.”<sup>2561</sup>

A site audit was directed.

48.110 The audit of Mr Brimstone’s installation was carried out by Ricardo/AEA, on Ofgem’s behalf, on 30 June 2016.<sup>2562</sup> At section 3.1.2.4. of the subsequent report the auditor noted the description of the building that had been provided in Mr Brimstone’s application, namely that “It is used for both machinery & at times animal pens for out-farm livestock (namely sheep) that require close monitoring & heat during lambing season. The water heating will also be used to wash the farm and farm areas.” The audit report recorded that:

“During the audit the auditor identified that the building accommodated a tractor, some shelving, temporary fencing posts and a number of tools. However there were also children’s toys being stored. There was no sign of animals having been stored there or any adaptation for that purpose.”

48.111 With regard to non-compliance the report recorded that “The auditor could find limited evidence of the building described as agricultural/storage being used for agricultural purposes. Action; Ofgem were to investigate”. The Executive Summary of the report included the observation that:

“The auditor could find no evidence of the building described as an agricultural workshop/storage being used as a workshop or for animal pens as described in the non-domestic questionnaire.”<sup>2563</sup>

48.112 The initial version of the audit report recorded the above lack of evidence of agricultural use as not amounting to non-compliance but after communication between Ofgem and Ricardo/AEA that was amended to a positive finding of non-compliance (see version 2 of the report).<sup>2564</sup>

48.113 Mr Brimstone was on holiday at the material time and the audit was attended by a relation. Mr Brimstone was notified of the outcome of the audit by letter dated 5 August 2016 signed by Shaneigh Turner, Ofgem non-domestic RHI Audit Manager. That letter drew attention to the auditor’s observation of non-compliance and sought evidence of the workshop/storage being

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2560 WIT-285207

2561 OFG-69067

2562 OFG-113661 to OFG-113684; OFG-42549 to OFG-42572

2563 OFG-42549

2564 OFG-42549 to OFG-42572

used for agricultural purposes. Mr Brimstone replied on the same day pointing out that the audit had been carried out in his absence, despite the audit company having been notified that he would be on holiday. He sought assistance in providing the information required by Ofgem.<sup>2565</sup>

48.114 On 10 August 2016 Mr Brimstone provided photographic evidence demonstrating use of the shed and confirmed that it may be used to accommodate sheep during lambing<sup>2566</sup> stating that “In the Spring this shed does be used to accommodate sheep during lambing if weather conditions demand so pens are not constructed until they are needed.”

48.115 On 19 August after a video conference involving Teri Clifton, Dr Ward, Mark George and a number of other Ofgem officials it was decided, by Mark George, after collective discussion on the evidence provided, that the shed was being heated as a workshop and farmhouse and would not be regarded as using heat solely for domestic purposes.

48.116 On 22 September 2016 Ofgem senior managers confirmed that they were now satisfied with Mr Brimstone’s response to the various email and letter exchanges that resulted from the audit and that there should be no restrictions of payments. The next day Mr Brimstone was sent a letter confirming that he was now compliant. It does not appear that any notification was provided to DfE. In written evidence Ms Clifton stated:

“I do not believe that the views of DfE were sought on the question of interpretation at this time. I do not consider that it would have been appropriate to seek such input given the respective responsibilities of Ofgem and DETI/DfE i.e. **it was Ofgem’s job to administer the Scheme.**”<sup>2567</sup> (the Inquiry’s emphasis).

48.117 Ms Clifton instructed the team that:

“Based on the Regulations and the evidence supplied we (those concerned in the decision of 19 August) are satisfied that the site meets the eligibility criteria and ongoing criteria. Please can you go ahead and close this off as no further action needed.”<sup>2568</sup>

48.118 The non-compliance investigation having been completed, Ofgem was in the process of closing the parallel counter fraud investigation when a further anonymous allegation came to Ofgem’s attention.

48.119 In October 2016 this further anonymous letter was passed on to Ofgem by Jim Allister QC MLA, who had also supplied a copy of the letter to the police and the NIAO.<sup>2569</sup> On 14 October an officer from the Police Service of Northern Ireland (PSNI) contacted Ofgem with regard to this second anonymous letter, which again alleged that Mr Brimstone was claiming non-domestic RHI subsidy when he should have been limited to the domestic RHI subsidy. The officer noted that the matter was under investigation by Ofgem and sought a meeting.<sup>2570</sup> On 18 October, during a telephone conversation with Ms Samantha Turnbull, from Ofgem E-Serve Counter Fraud, the officer asked for “any relevant information.”<sup>2571</sup>

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2565 OFG-41980

2566 OFG-200002

2567 WIT-285216 to WIT-285217

2568 OFG-67801

2569 OFG-200012

2570 OFG-200013

2571 OFG-68077 to OFG-68078

- 48.120 This second anonymous complaint was also brought to the attention of DfE by the NIAO. Lucy Marten from DfE emailed Dr Ward at Ofgem and asked for the findings that led to Mr Brimstone being deemed eligible.<sup>2572</sup> That was followed by a further email on 11 October 2016 from DfE’s Mr Wightman on behalf of Dr McCormick, Permanent Secretary at DfE (successor department to DETI from May 2016), who was shortly to meet the DfE Minister and was planning to provide him with a letter confirming the case was currently under investigation.
- 48.121 Mr Wightman’s communication stated that it was “very difficult to justify that there is an eligible heat use” and that it looks “very like the Category 4 installations that PwC identified. We therefore need assurances that Ofgem’s decision not to proceed with further enforcement has been based on robust evidence.”<sup>2573</sup>
- 48.122 Mr Wightman then emailed Dr Ward on 14 October seeking an explanation as to why DfE had not been informed of the previous May 2016 allegation, citing paragraph 3.2 (b) of the Arrangements.<sup>2574</sup> That paragraph in the Arrangements provided that Ofgem would: “Inform DfE of any complaint, request for a formal review...that is received by GEMA [Ofgem] in connection with the carrying out by it of the Conferred Functions or the Ancillary Activities”.
- 48.123 Dr Ward responded stating that the allegations had already been investigated, Mr Brimstone was found to be compliant and the matter did not fall into any section of the Arrangements.<sup>2575</sup> In the light of this exchange it appears to the Inquiry that it was Ofgem’s policy not to inform DETI that an allegation of fraud relating to the scheme had been received.
- 48.124 On 25 October 2016 Ofgem responded to the email from PSNI by asking PSNI for a formal application for information.<sup>2576</sup>
- 48.125 An internal email exchange over 27 and 28 October 2016 involved Ofgem officials questioning whether or not to send the 1 July 2016 audit report and the compliance team’s assessment to PSNI.<sup>2577</sup> On 27 October John Jackson, an Ofgem lawyer, emailed Ms Turnbull and Ms Clifton advising that the PSNI information request only enquired whether any application had been made by Mr Brimstone to join the scheme and:
- “Therefore, although it might not seem right to withhold the audit report and the compliance team’s assessment, if we were to furnish them [PSNI] with the audit report, in my view, to do so would go beyond the scope of the actual request”.<sup>2578</sup>
- 48.126 Ms Turnbull responded on the following day explaining that:
- “When I spoke to the police officer, she was keen to understand if we had done any investigations, in order to prevent the duplication of the work, so I think the audit report and subsequent documents will be critical to them.”
- 48.127 Further internal exchanges on 31 October in Ofgem between Ms Turnbull and Mr Jackson concluded with the latter advising that with regard to the audit: “I still feel, having regard to the

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2572 OFG-68077 to OFG-68078

2573 OFG-68077

2574 OFG-68080 to OFG-68081

2575 OFG-68075 to OFG-68077

2576 OFG-68332

2577 OFG-68328; OFG-210236

2578 OFG-68328

nature of their request for information, that we shouldn’t share it [the audit report] unless they ask for it.”<sup>2579</sup>

48.128 He went on to suggest that the PSNI should be informed that Ofgem had completed its investigation and that there wasn’t any cause for concern and that PSNI might then conclude its own investigation. In such circumstances he advised that only a copy of Mr Brimstone’s application to join the scheme should be shared.<sup>2580</sup> Mr Jackson relied upon section 29 of the Data Protection Act 1998 as limiting Ofgem to disclosure of only such information and/or its existence as was specifically requested by PSNI.

48.129 On 1 November 2016 the PSNI made a formal request for disclosure of the results/evidence of the audit for an RHI fraud investigation, in accordance with the provisions of the Data Protection Act 1998.<sup>2581</sup> In the meantime Ofgem had emailed a copy of the application to the PSNI on 31 October.<sup>2582</sup> The PSNI then accepted Ofgem’s assertion that there was no cause for concern in relation to the application and that no further action was needed on the part of the PSNI. Ofgem treated that communication as justifying not dealing further with the 1 November PSNI request.

48.130 In a written statement of evidence to the Inquiry Mr Jackson restated his belief that Ofgem was “well placed to determine whether the police had good reason to be investigating Stephen Brimstone” and “it was entirely appropriate for the Authority [Ofgem] to satisfy itself about the veracity of the police fraud investigation” before disclosing the material in question.<sup>2583</sup> He added that “Ofgem could rightly consider that the police request for information could be viewed as ‘Speculative’”.<sup>2584</sup>

48.131 The Inquiry notes that Michael Knight, a more senior Ofgem lawyer than John Jackson, who was on leave at the material time, subsequently confirmed to Mr Jackson that he “probably” would have provided the audit report to the PSNI.<sup>2585</sup>

48.132 The Inquiry notes that at this point Ofgem had:

- (i) The material that it had received from Mr Brimstone including the further information that he had supplied after he had received correspondence from Ofgem post the May 2016 audit.
- (ii) The May 2016 anonymous fraud allegation that had not been supplied to the police by Ofgem.
- (iii) The two versions of the Ricardo/AEA May 2016 audit report that had been considered by Ofgem and in respect of which the non-compliance of the shed as used for agricultural purposes had been upgraded by Ofgem from negative to positive.
- (iv) An Ofgem Counter Fraud investigation which had been open since May 2016 and had not been closed despite the compliance investigation having been completed and Mr Brimstone being reconfirmed as a member of the scheme.

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2579 OFG-210231  
2580 OFG-210231  
2581 OFG-128555  
2582 OFG-128558  
2583 WIT-286025  
2584 WIT-286026  
2585 WIT-286027

48.133 In November 2016 Ms Turnbull prepared a summary of the Brimstone investigation to be supplied to DfE.<sup>2586</sup> A second document, Ofgem Counter Fraud’s internal ‘Suspected Fraud Case Closure Report’ was also under preparation. The draft Case Closure Report had been approved by the Head of Ofgem Counter Fraud on 8 November 2016 and included the observation that:

“While the audit reported that there was no evidence of the premises being non-domestic, the participant provided further photographic evidence to support the non-domestic eligibility.”<sup>2587</sup>

48.134 The report went on to record that the site was found to meet eligibility requirements and no further action was required. The draft did not contain any reference to the PSNI/Ofgem exchanges. Ms Turnbull sent an internal email setting out a summary of the Case Closure report which included the statement that:

“The auditor could find no evidence of the building described as agricultural workshop/storage being used as a workshop or for animal pens as described in the application.”<sup>2588</sup>

48.135 Mr Knight confirmed that disclosure of the summary to DfE would be consistent with the Arrangements in place between DfE and Ofgem, adding:

“My advice is also that once the summaries are disclosed then given recent events we should anticipate that DfE will press us to take some action in terms of the scheme administration regarding these participants or explain why we are not.”<sup>2589</sup>

48.136 On 8 December 2016 Ms Turnbull emailed Ms Clifton to confirm Mr Knight’s approval to share the summary with DfE. That email contained the following passage:

“To complete the action from the previous board, I wondered if you’re happy to share the below wording on the Brimstone case...Also, please let me know what you think about removing the crossed-out line.”<sup>2590</sup>

The “crossed-out line” effectively removed the reference to the auditor being unable to find any evidence of the building being used as a workshop or for animal pens.

48.137 On 9 December in an email to Ms Clifton, Ms Turnbull expressed concern as the summary did not “give the full picture.”<sup>2591</sup> On the same day James Robinson, Ofgem E-Serve Acting Legal Director, emailed Ms Turnbull confirming that, in terms of data protection compliance and the Arrangements he was content to share the information with DfE.<sup>2592</sup> On 12 December Dr Ward supplied the amended draft to Lucy Marten at DfE.<sup>2593</sup>

48.138 In written evidence to the Inquiry Ms Turnbull stated that the reason for removal of the reference to the auditor finding no evidence of agricultural/workshop use was that:

“The inclusion of a sentence that suggested that the auditor could find no evidence could create confusion and lead to further questions. The auditor’s report had been

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2586 OFG-70511  
2587 OFG-49265  
2588 OFG-210218 to OFG-210219  
2589 OFG-210217  
2590 OFG-210217  
2591 OFG-210217  
2592 OFG-210225  
2593 OFG-70652

superseded by the further information provided by the applicant which had been considered ‘sufficient to determine compliance’.

48.139 She thought that there was a desire from her operational colleagues “not to create confusion” which could result in further questions for the RHI team to manage when (in their view) it was Ofgem’s responsibility to make compliance decisions.<sup>2594</sup> To be fair to Ms Turnbull, as noted above, she did express concern that the amended version of the Case Closure Report did not “disclose the full picture” when emailing the draft to Ms Clifton on 9 December 2016. In her own written evidence Ms Clifton expressed the view that the removal of the reference to the auditor’s finding would have been to avoid confusion. She said:

“If the DfE summary had contained a reference to an audit which stated that it had found no evidence of non-domestic status I believe that this could have resulted in confusion as to why the installation was determined to be compliant.”<sup>2595</sup>

48.140 The problem for the Inquiry is why full disclosure could not have been made in the interest of openness and transparency, with the auditor’s findings included, indicating non-compliance, as well as the Ofgem investigative response thereto.

48.141 Ofgem directed a second audit of Mr Brimstone’s installation. On 30 March 2017 this second audit of Mr Brimstone’s installation was carried out by Ricardo/AEA and the report was finalised in May.<sup>2596</sup> That report noted non-compliance issues and concluded that the site audit class was “unsatisfactory” on the basis that major eligibility issues had been identified and/or there were suspicions of abuse, misuse or fraud.<sup>2597</sup> The “workshop/livestock birthing area” appeared to be a workshop/garage and contained an old tractor reported to be a renovation project, a large log pile for use in the house, children’s toys, a workshop area/benches and some soiled wood shavings. The report also recorded that the participant stated that there was a biomass boiler installed previously which heated the house but not the workshop.<sup>2598</sup>

48.142 There were differing views amongst the Ofgem officials about the significance of this audit report and a meeting was held on 4 July 2017. Ms Clifton presented the RHI view, Karen Boyle presented the Counter Fraud view and Michael Knight presented the legal view.

48.143 Also at the meeting was Sarah Cox, who joined Ofgem in May 2016 in the newly created role of Chief Operating Officer (COO). She commissioned a report from Ofgem’s auditors, Deloitte,<sup>2599</sup> into how Ofgem had handled the Brimstone application. She received the report in May 2017 and then engaged with officials involved with the case. In her written evidence to the Inquiry she said that during the course of the internal Ofgem meeting on 4 July 2017 she had:

“Expressed concern that it might not be in the interest of protecting the public purse to allow Mr Brimstone to continue to claim under the Scheme...where the evidence pointed to minimal compliance.”<sup>2600</sup>

48.144 She discussed this with Dermot Nolan, the Ofgem Chief Executive, and repeated her public interest concern but ultimately concluded that such a consideration was not relevant for the

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2594 WIT-284726 to WIT-284727

2595 WIT-285226

2596 OFG-200388

2597 OFG-200389

2598 OFG-200389

2599 OFG-200494 to OFG-200516

2600 WIT-282319 to WIT-282320

purposes of the decision to permit Mr Brimstone to continue to claim under the scheme.<sup>2601</sup> On 24 July 2017 she emailed Gareth John, referring to her meeting with Dr Nolan and stating that:

“We [herself and Dr Nolan] talked about other issues and my nagging concern remains the fact that we should always apply the public duty/public purse argument....With the case in question (Mr Brimstone) we should still ensure that PSNI have been given all the information they should have received following their request some time ago.”<sup>2602</sup>

- 48.145 Another attendee at the 4 July meeting was Patricia Dreghorn, who joined Ofgem in September 2016 as E-Serve Chief Operating Officer (E-Serve COO) and took over from Mr Poulton as Managing Director of Ofgem E-Serve in April 2018. She stated in her written evidence to the Inquiry that she was critical of the decision-making process whereby the RHI team made the decisions without the involvement of the Counter Fraud team.<sup>2603</sup> She noted in relation to this 4 July 2017 meeting that the two teams had conflicting views with regard to the accreditation of Mr Brimstone’s installation.<sup>2604</sup>
- 48.146 On 24 July she sent an email relating to the transfer of information to the PSNI in which she stated “CF (Ofgem’s Counter Fraud team), RHI (Ofgem’s RHI team) and Legal (Ofgem Legal) should have collated all evidence and findings and issued one comprehensive pack to PSNI.”<sup>2605</sup>
- 48.147 In her evidence to the Inquiry she qualified the view expressed in the email by stating that she was not aware at the time that there were any issues relating to the provision of information to the PSNI adding that, in general terms, she would expect disclosure of information to be in accordance with Ofgem’s legal obligations.<sup>2606</sup>
- 48.148 On 24 July 2017 Ms Turnbull contacted the PSNI informing them that Ofgem’s legal team had reviewed the Brimstone case and now believed that Ofgem should have supplied further documentation (e.g. audit reports) at the time. She offered the opportunity to view the further material. However, Ms Turnbull added that Ofgem’s opinion remained unaltered in that, in Ofgem’s view, the participant was entitled to claim under the scheme.<sup>2607</sup>
- 48.149 The Ricardo/AEA audit reports of July 2016 and May 2017 were made available to the PSNI via a secure sharing network by Craig Johnstone, an Ofgem Counter Fraud manager, on 28 July 2017.<sup>2608</sup> Unfortunately the PSNI appear to have encountered some difficulty in obtaining access to the secure sharing network<sup>2609</sup> and the Inquiry cannot be sure that the PSNI received the 2016 audit report as well as the 2017 report. The PSNI response to Mr Johnstone referred to only the 2017 report<sup>2610</sup> and that was the only audit report annexed to the detailed PSNI report of 27 November 2017.<sup>2611</sup>

2601 WIT-282320 to WIT-282321

2602 OFG-200296 to OFG-200297

2603 WIT-284512

2604 WIT-284516

2605 OFG-200842

2606 WIT-284516 to WIT-284517

2607 OFG-201419

2608 OFG-200874

2609 OFG-200448 to OFG-200449

2610 OFG-200447 to OFG-200448

2611 OFG-201410

- 48.150 On 30 August 2017, after Mr Brimstone replied to various further information requests, Ofgem reaffirmed that the installation was compliant and reinstated payments.<sup>2612</sup>
- 48.151 During August through to November 2017 the PSNI continued to ask questions of Ofgem, referring back to Ofgem’s initial response in October 2016 that there was no cause for concern. However on 27 November 2017 the PSNI, having read the 2017 audit report rather than just the application form that Ofgem originally sent in 2016, raised a number of concerns, e.g. that the agricultural shed appeared to be a domestic garage and that the farming activities were only documented by a picture of five sheep in an adjacent field. The PSNI concluded by informing Ofgem that it was seeking pre-prosecutorial advice and believed that despite the Ofgem findings there might be a case of fraud by false representation.<sup>2613</sup> The PSNI then pursued external lines of enquiry as well as seeking further material from Ofgem.<sup>2614</sup> The police met with Ofgem in March 2018 and shared a detailed November 2017 report of its investigation with Ofgem at that time. The report concluded by stating that its purpose was to ascertain whether Ofgem intended to make any complaint to the PSNI.
- 48.152 On 11 May 2018, Ofgem formally replied to the PSNI and indicated that due to the potential for police action, it did not wish to take any steps as part of a review of this accreditation in case that might prejudice the PSNI actions and asked to be kept informed of matters by the PSNI.<sup>2615</sup>
- 48.153 In the same detailed letter, by way of explaining its approach to interpreting such mixed use cases, Ofgem pointed out:
- “Support is available in cases in which there are mixed uses of heat, as between one domestic premises and other premises. In such cases, there is no requirement in the 2012 regulations I mentioned above about the proportions that the two types of heat use should bear to one another. Neither are there requirements that the scheme participant should also be the user of heat that is supported under the scheme, or about the size, turnover or scale of any business making use of the heat.”<sup>2616</sup>
- 48.154 With regard to the question about the allowable proportions of domestic and non-domestic heat production the Inquiry notes the earlier evidence of Dr Ward from Ofgem to the Assembly’s Public Accounts Committee hearing into the RHI problems on 28 October 2016 where he confirmed that Ofgem would accredit under the non-domestic RHI scheme even if the domestic usage was as much as 99% of the total.<sup>2617</sup>

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2612 IND-25925

2613 OFG-201410 to OFG-201413

2614 OFG-201411

2615 OFG-201406 to OFG-201409

2616 OFG-201407

2617 PAC-05498 to PAC-05500

## Findings

- 274.** The Inquiry notes that Ofgem responded to a PSNI information request in October 2016 by withholding relevant information. Some of this was subsequently provided after a significant delay, but other relevant material, like the 2016 audit report, was not disclosed until more than a year after the audit had taken place. The Inquiry finds this approach by a Government Department towards a police service unacceptable. The Inquiry accepts the importance of ensuring receipt of a lawful request for information and of complying with the provisions of the Data Protection Act 1998 but, in the particular circumstances of the case under consideration, such requirements should not have been allowed to inhibit a Government Department from properly and fully assisting a police investigation and disclosing full information both supportive of and inconsistent with compliance with the NI RHI scheme.
- 275.** The Inquiry finds it unacceptable that a conscious decision was made by Ofgem officials in December 2016 to withhold relevant material about audit findings from DfE to avoid further questions from it.
- 276.** The regulations relating to non-domestic/domestic use appear to have allowed the higher levels of support under the non-domestic scheme as long as Ofgem was satisfied that there was any evidence of heat being used for non-domestic purposes, no matter how little, and regardless of whether it was for the benefit of the applicant or of any other third party.
- 277.** The Inquiry accepts the difficulty of interpreting the regulations on mixed domestic and non domestic use and the problem of deciding eligibility where an installation was not solely used for domestic heating. However, it was also necessary to consider the need to protect the public purse and achieve value for money. Those considerations heightened the need for Ofgem to have clearly and, if necessary, repeatedly, informed DfE of the approach that it was taking and the perverse outcome that it might produce. Had it done so, DfE would have had greater opportunity to consider whether it should have taken steps to deal with the problem.

## Carbon Trust loans

48.155 Prior to, and during, the lifetime of the RHI scheme, Invest NI created a fund to promote energy efficiency, low carbon and renewable energy technologies to businesses. These interest free loans were provided and administered by the Carbon Trust on behalf of Invest NI. These loans constituted State Aid, which created a potential conflict with the RHI scheme, itself also constituting a form of State Aid. The central problem which emerged was whether a recipient of a Carbon Trust loan could also be a recipient of subsidy payments from the NI RHI non-domestic scheme. The Inquiry gave consideration to the relevant regulations.

48.156 Regulation 23 of the 2012 NI RHI regulations originally provided that:<sup>2618</sup>

“(1) The Department must not accredit an eligible installation unless the applicant has given notice (which the Department has no reason to believe is incorrect) that, as applicable —

(a) no grant from public funds has been paid or will be paid or **other public support** [the Inquiry’s emphasis] has been provided or will be provided in respect of any of the costs of purchasing or installing the eligible installation; or

(b) such a grant or support was paid in respect of an eligible installation which was completed and first commissioned between 1st September 2010 and the date on which these Regulations come into force, and has been repaid to the person or authority who made it.

(2) In this regulation, ‘grant from public funds’ means a grant made by a public authority or by any person distributing funds on behalf of a public authority and ‘public support’ means any financial advantage provided by a public authority.”

48.157 The inclusion of the phrase “or other public support” in the regulations had been upon the advice of Ofgem. The intent had been to make ineligible for RHI any applicant who had acquired their installation with the assistance of the type of public loan of which, although not specifically referred to in the regulation, the Carbon Trust loan was a particular example.

48.158 On 10 December 2012 Wayne Cullen of BS Holdings Ltd emailed Ofgem’s ‘RHI Enquiries’ email account asking:

“If a new biomass installation capital cost is funded by means of the carbon trust interest free type loans can the RHI funding still be applied for and achieved assuming all other criteria is [sic] eligible.”<sup>2619</sup>

48.159 Despite the fact that it had advised the insertion of “other public support” into the 2012 NI RHI regulations (so as to render this type of loan incompatible with the NI RHI scheme – a provision not in the GB RHI regulations), Ofgem responded:

“The Carbon Trust interest free loan is not defined as a grant from ‘public funds’ under the RHI regulations and therefore, it is compatible with the RHI.”<sup>2620</sup>

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2618 LEG-00011

2619 OFG-14622

2620 OFG-14622

48.160 When Mr Cullen posed the same question to DETI in January 2013, DETI referred the matter to Ofgem, having said that the Carbon Trust loan was not compatible with the RHI scheme. Ofgem responded by repeating the incorrect advice that it had given to Mr Cullen, namely that the Carbon Trust loan was compatible with the RHI.<sup>2621</sup>

48.161 Six months later on 28 June 2013 Mr Hendle, an Assistant Fraud and Compliance Manager in Ofgem, identified Ofgem’s previous mistake.<sup>2622</sup> He highlighted the difference in the wording between regulation 23 in the Northern Ireland regulations and the similar regulation 23 of the GB regulations. Whilst both provisions excluded from their respective RHI schemes installations which had benefited from a grant from public funds, the Northern Ireland regulation 23 went further and also excluded installations which have benefited from “other public support”. There was then debate within Ofgem over the summer and the uncertainty continued into September.<sup>2623</sup> A decision was eventually made culminating in the following email from Dr Ward to Ms Clifton on 1 October 2013:

“This [application] was rejected on the basis of a soft loan from the Carbon Trust, which would be accepted in GB but not in NI. Applicant had spoken to our team and was under the impression it was fine to take the loan.

Part of the root cause is that the Carbon Trust appear to be giving out advice which is not consistent with the NI regs.”<sup>2624</sup>

48.162 Ofgem was now claiming that “part of the root cause” was the Carbon Trust telling people this – despite the fact that Ofgem itself had emphatically told both BS Holdings and DETI that Carbon Trust loans were compatible with the NI RHI scheme. This ‘U-turn’ by Ofgem was not greeted well by DETI officials. On 9 October 2013 Ms McCutcheon stated in an email to Ms Clifton and Dr Ward:

“This is of great concern to me and I will need to speak to Fiona Hepper as to how we move forward as I think this has serious implications for the reputation of the NI RHI and our Department. Members of the public have gone ahead in good faith on the basis of information provided directly from Ofgem and also from ourselves (on the basis of advice Ofgem gave us) and are now considered to be ineligible for the incentive.”<sup>2625</sup>

48.163 The email also pointed out to the Ofgem officials that it was in fact Ofgem who advised DETI during the drafting of the regulations to expand the wording of regulation 23 to include “other public support”.<sup>2626</sup>

48.164 At this relatively early stage in the NI RHI scheme, in October 2013, only two applicants with Carbon Trust loans had been accredited. Ms Hepper in her oral evidence told the Inquiry:

“We would’ve been quite happy with the interpretation at the very start that, ‘No, they are not compatible’ and if that had been consistently applied.”<sup>2627</sup>

She explained that changes after accrediting the first applicants would have been a problem.

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2621 DFE-86968

2622 OFG-207063

2623 OFG-23906

2624 OFG-14428

2625 OFG-126830

2626 OFG-126844

2627 TRA-05312

- 48.165 Subsequently, DETI, Ofgem and the Carbon Trust all received calls from applicants who had benefited from Carbon Trust loans and prospective applicants who were seeking to utilise Carbon Trust loans. Minister Foster was also apprised of the situation via a submission on 1 October 2013 and on 25 October 2013.<sup>2628</sup> During this period one of the applicants whose accreditation had been refused by Ofgem, because he had used a Carbon Trust loan to finance his installation, exercised his statutory right of appeal to DETI under regulation 50 of the 2012 NI RHI regulations.<sup>2629</sup>
- 48.166 DETI and Ofgem were faced with essentially two problems. The first related to the Northern Ireland regulations, namely whether interest free loans from the Carbon Trust did indeed fall within the prohibition in regulation 23. If it was considered that Carbon Trust loans did not fall within regulation 23 and, therefore, recipients of the loans were not excluded from the RHI scheme, this then raised a second question of whether the addition of the Carbon Trust loans to some RHI recipients had an impact on the State Aid clearance for either the RHI scheme as a whole or for the individual recipients who were benefiting from both RHI and Carbon Trust support.<sup>2630</sup>
- 48.167 In relation to overcoming the regulation 23 issue, DETI and Ofgem were encouraged by the fact that the Carbon Trust’s own lawyers did not consider it, the Carbon Trust, was a ‘public authority’.<sup>2631</sup> However, the Departmental Solicitors Office (DSO) was of the opinion that the relationship between Invest NI and the Carbon Trust was such that the loans would be regarded as having been “provided by a public authority” within regulation 23.<sup>2632</sup>
- 48.168 In relation to the second issue regarding the impact of a recipient getting both a Carbon Trust loan and RHI payments on the State Aid approval, Mr Moore from DETI’s State Aid unit proffered the solution whereby DETI would notionally extract the Carbon Trust/RHI cases from the RHI State Aid approval achieved using an exemption under paragraph 109 of the 2008 Community Aid Guidelines on State Aid for Environmental Protection (2008/c 82/01) and instead categorise them for example under the State Aid ‘*de minimis*’ exemption.<sup>2633</sup> The *de minimis* rule was contained in Commission Regulation (EU) No 1407/2013.<sup>2634</sup> In essence this rule provided a ceiling of EUR 200,000 in respect of the amount of aid that a single undertaking could receive over a three-year period without the need for the State having to notify the Commission for approval. At recital (3) the regulation provided that:
- “It is appropriate to maintain the ceiling of EUR 200,000 as the amount of *de minimis* aid that a single undertaking may receive per Member State over any period of three years. That ceiling remains necessary to ensure that any measure falling under this Regulation can be deemed not to have any effect on trade between Member States and not to distort or threaten to distort competition.”
- 48.169 The appeal by the applicant against the decision by Ofgem to reject his application culminated in a submission from Ms McCutcheon to DETI Deputy Secretary, Mr Thomson, on 11 December 2013. In order to assist Mr Thomson to make the decision Ms McCutcheon set out two options for him.<sup>2635</sup>

2628 DFE-242315 to DFE-242319; DFE-33697 to DFE-33701

2629 LEG-00027

2630 DFE-240482 to DFE-240483

2631 OFG-14966 to OFG-14967

2632 DSO-04764 to DSO-04765

2633 DFE-240444 to DFE-240445

2634 DFE-241313 to DFE-241320

2635 DFE-240928 to DFE-240943

48.170 The first option was to affirm Ofgem’s revised legal interpretation of regulation 23 and refuse the application to the NI RHI scheme, which would also be in accordance with DSO’s legal definition on the regulation. This, however, would have the consequential effect of depriving all businesses which had used a Carbon Trust loan to buy their boilers from availing of the RHI scheme. In addition that would mean installations in NI and GB would be treated differently.

48.171 The second option was to reject DSO’s legal advice on the interpretation of the regulation and grant the application to avail of the RHI scheme, despite having obtained a Carbon Trust loan, subject to the State Aid *de minimis* regulations, thus adopting an interpretation which was vital from a policy perspective as businesses often encountered difficulty in raising the initial capital for renewable projects from more traditional funding sources.<sup>2636</sup>

48.172 Ms McCutcheon recommended to Mr Thomson that Ofgem’s recent decision should be overturned and he agreed to the second option.<sup>2637</sup>

48.173 Ofgem subsequently drafted a ‘factsheet’ giving guidance to applicants on grants and public support and also a State Aid declaration template for *de minimis* aid for use by persons in receipt of Carbon Trust loans.<sup>2638</sup> However, it became apparent in April 2014 that Ofgem were still not accrediting Carbon Trust loan recipients on the RHI scheme despite that decision. Ofgem considered that processing applications under the State Aid *de minimis* regulation rather than the Commission notification in respect of the RHI scheme fell outside the powers conferred upon it by the Arrangements.<sup>2639</sup>

48.174 Following a meeting with Ofgem on 18 June 2014, Mr Moore emailed a DETI colleague observing:

“Ofgem meeting quite difficult. *De minimis* only a possible solution in 4 of the 8 cases. Energy Division going to have to take a least loss decision, possibly having to ask the Minister to give a Direction, on the others. The decision may also destabilise the situation in GB. Some in Ofgem looking to wriggle out of the hole, others seem intent on making the hole deeper.”<sup>2640</sup>

48.175 The culmination of all the debate and negotiation was reached on 10 July 2014 with a letter from DETI’s Mr Wightman to Ofgem’s Mr Poulton detailing DETI’s proposals on how to proceed:<sup>2641</sup>

“Category 1 covers applicants currently not in receipt of a Carbon Trust loan or any other public support. These applications are provided for under the existing regulations as approved in our original submission to the European Commission. This could include applicants who have paid off previous carbon trust loans (before the RHI regulations came into force).

Category 2 covers applicants whose relevant state aid funding (including carbon trust loans) and likely RHI income would not exceed the relevant *de minimis* amount over three rolling years. Subject to meeting other eligibility requirements, these applicants would be able to access the RHI.

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2636 DFE-240932 to DFE-240934

2637 DFE-240935; DFE-240965

2638 DFE-241137 to DFE-241141

2639 DFE-241143 to DFE-241145

2640 DFE-241232

2641 OFG-28827 to OFG-28831

Category 3 covers applicants whose relevant state aid funding (including carbon trust loans) and likely RHI income would exceed the relevant *de minimis* amount over three rolling years. These applicants are not able to access the RHI under the current regulations.”

- 48.176 Nadia Carpenter of Ofgem responded on 20 August 2014 indicating Ofgem was only prepared to make decisions in relation to Category 1 applications; for Category 2 and 3 applications the decision-making power would “transfer” to DETI. Mr Hughes and Mr Wightman agreed to this course.<sup>2642</sup>
- 48.177 This agreement was reflected in revised Arrangements between DETI and Ofgem of 13 October 2014, which amended the ‘Retained Functions’ section.<sup>2643</sup>
- 48.178 Mr Hutchinson in his oral evidence told the Inquiry that, even though the situation was not resolved before he left in May 2014, it “really took a lot of our time” and “a lot of the engagement with Ofgem was really around the Carbon Trust issues.”<sup>2644</sup> He also explained that they had had to park work on data sharing to work on the Carbon Trust loan issue.
- 48.179 Mr Hughes, who joined DETI on 30 June 2014, told the Inquiry that alongside working on the domestic RHI and Ofgem data sharing, dealing with the Carbon Trust loans was one of the three priorities set for him by Mr Wightman when he joined DETI.<sup>2645</sup> The Inquiry notes that this work was taking precedence over matters that ought to have been occupying the minds of DETI officials, such as cost controls and tariff reviews in relation to the non-domestic RHI scheme.
- 48.180 It seems that the problem was ultimately resolved by amending the 2012 NI RHI regulations to allow Carbon Trust loans to be paid back, thereby enabling Ofgem to accredit a relevant application. The change was effected through regulation 61(2) of the 2014 NI Domestic RHI regulations.

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2642 OFG-29591 to OFG-29592

2643 OFG-59975 to OFG-59976

2644 TRA-04929

2645 TRA-05810 to TRA-05811

## Findings

- 278.** Ofgem advised DETI to provide in its regulations for the exclusion of those applicants availing of “other public support.” That was intended to rule out those applicants who had availed of loans such as those provided by the Carbon Trust. Ofgem then gave the opposite advice to potential applicants (and DETI) that Carbon Trust loans were compatible with the NI RHI scheme. This led to the accreditation on the NI RHI scheme of applicants in receipt of Carbon Trust loans. Ofgem later changed its position and refused to accredit any further applicants who had received Carbon Trust loans.
- 279.** Ofgem’s initial failure to consider properly and take account of the amendment it had suggested to regulation 23 of the NI RHI regulations, and the subsequent reversal of its advice regarding Carbon Trust loans created a difficult and unnecessary situation for DETI to manage. The prolonged work necessary to deal with Ofgem over this issue, in the context of DETI’s limited resources, meant that less time was available to effectively deal with other, more fundamental, challenges of scheme management.

## Ofgem’s assertion of no causal link between its failings and what went wrong with the RHI scheme

48.181 Ofgem, in its closing written submissions to the Inquiry, stated that:<sup>2646</sup>

“Ofgem’s position that there is no causal link between its failings and what went wrong with the Scheme is not to detract from the clear failings by Ofgem. Ofgem was the expert administrator, in sole possession of important primary material relating to the Scheme. Ofgem had a special responsibility to share that information and accepts that it is a serious failing not to have done so. However, this is materially different to an acceptance that Ofgem caused the overspend of public funds. Ofgem’s position is that it did not.”

48.182 Ofgem maintained that position during the Inquiry’s representations process in respect of the Inquiry’s finding set out below. The reasons given for the position taken by Ofgem are that: Ofgem was obliged to interpret the NI RHI regulations and that, as there is only one correct lawful interpretation of legislation, Ofgem did not have discretion as to the interpretation it could adopt. Further, by reason of the above, Ofgem further contended that any analysis of the impact of the interpretation adopted by Ofgem was simply irrelevant to its work, and it ought not to be criticised for failing to carry it out. Ofgem also said that as it did not have competence to correct or amend the NI RHI regulations and had warned DETI about problems with the legislation, it (Ofgem) could not be said to have had a causative role in respect of something that was beyond its control.

48.183 The Inquiry has carefully considered all that Ofgem has said in evidence, by way of submissions and during the representations process in relation to this, including that its submission as to lack of causal effect was not made to detract from the clear failings of Ofgem in respect of the NI RHI scheme, which have been outlined in the previous two chapters of this Report in particular (and many of which Ofgem accepted during the Inquiry’s hearings). However, the Inquiry considers that the position that Ofgem has taken on the causation issue is too simplistic. Whilst there is only one correct legal interpretation of legislation, what that correct interpretation is, at least in the United Kingdom, can only be conclusively established by a Court of competent jurisdiction. If a public body adopts an interpretation of legislation which it considers to be the correct interpretation, but which it knows, or becomes aware, raises issues of potential exploitation and value for money, then it cannot be correct to say that the public body is entitled to ignore those issues, to fail to analyse their impact, or fail to communicate about that impact with the person (in this case DETI) with the power to take remedial action. As previously indicated in this Report, the Inquiry considers Ofgem should have properly explained to DETI the approach it was taking to matters of interpretation (examples of which have been considered in this chapter), and should have informed DETI of each of the relevant instances of exploitation of which Ofgem became aware. The repeated failure to do so (whatever previous warnings had been given) deprived the scheme owner, in this case DETI, of being confronted with and/or reminded of the need to take action to deal with issues. Therefore, in that sense, Ofgem’s failings may well have contributed to what went wrong with the NI RHI scheme since, in the absence of those failings, corrective steps may have been taken by DETI at an earlier point. At the very least, the Inquiry does not consider that it can be positively asserted that Ofgem’s failings had no causative effect on, or link to, what went wrong with the scheme.

2646 SUB-01005 to SUB-01006

## **Finding**

**280. The Inquiry disagrees with Ofgem that there was no causal link between its failings and what went wrong with the scheme. It was Ofgem’s interpretation and application of the regulations to the accreditation process which it administered that contributed to considerably more public money being spent on incentives than was the original and clear policy intent. Having previously warned that this might occur, it is not only a failing that this was not communicated to DETI when it did happen, but also that Ofgem had not analysed the financial consequences of its interpretation of the regulations and how they were being implemented.**

## Chapter 49 – Tiering

- 49.1 In this chapter, and chapters 50 to 55 which follow it, the Report addresses a number of specific topics which, although considered in earlier chapters as part of a broader subject or issue, also merits consideration on its own as a discrete theme. In the circumstances, there will in this chapter, and those which follow, be some necessary repetition of material which has appeared in earlier chapters.
- 49.2 This chapter addresses one of the major issues which captured the attention of both the PAC and the public in late 2016 and early 2017 (and which has been considered in some depth by the Inquiry), namely the concept of ‘tiering’ of tariffs and its absence from the NI RHI scheme when it was launched in November 2012.
- 49.3 Prior to the controversy surrounding the NI RHI scheme, the concept of tiering in this context is unlikely to have been generally known or understood. As indicated above, throughout the course of this Report up to this point the Inquiry has addressed tiering in its discussion of the development, introduction and operation of the NI RHI scheme. In this chapter the Inquiry specifically examines tiering itself.

### What is tiering?

- 49.4 DECC published an RHI Impact Assessment (IA) in March 2011,<sup>2647</sup> alongside its Renewable Heat Incentive policy document. That IA set out a number of key economic, technical and behavioural assumptions underpinning the proposed GB RHI scheme, including a ‘hurdle rate’ or rate of return on investment of 12%, and specifically cautioned that “Uptake of renewable technologies is highly dependent on the relative costs of heat generation from a renewable source compared to fossil fuel heating.”<sup>2648</sup>
- 49.5 The IA also referred to a potential “perverse incentive” to over generate heat which could arise if installations were offered an opportunity to receive a tariff payment per kWh that exceeded their marginal costs of generating that unit of heat.<sup>2649</sup> DECC recognised that this perverse incentive may well arise in some of the proposed biomass boiler tariffs, particularly for those boilers beneath 1MW in size. In order to address the risk of creating such a perverse incentive to overgenerate heat, the IA explained that the final GB RHI proposals “include a 2 part biomass tariff (or tiered tariff).”<sup>2650</sup>
- 49.6 The higher, or Tier 1, tariff was available for a portion of the potential maximum annual heat output of a biomass boiler. This limited portion was to be the equivalent of 1,314 hours multiplied by the installed capacity of the boiler.<sup>2651</sup> This was based on the assumption that average users would utilise their biomass boiler for 15% of the available hours in the year (15% of the available 8,760 hours in a year being 1,314). The percentage of use in a year was referred to as ‘the load factor’.

2647 INQ-20879 to INQ-20916

2648 INQ-20888 to INQ-20889

2649 INQ-20891

2650 INQ-20893

2651 The IA, at paragraph 26 (see INQ-20893), in an obvious error refers to “the first 1300kWh of heat.” The Inquiry considers that this error would likely have been obvious to any reader of the IA, given the fact that at Table 1 (see INQ-20886) the “tier break” of “installed capacity (kWth) x 15% peak load hours (i.e. 1,314)” is clearly set out.

- 49.7 The aim of the higher/Tier 1 tariff was to cover, over the lifetime of the incentive scheme, the capital costs associated with the change to renewable heat, such as the additional cost of acquiring the biomass boiler, as well as the additional cost of running such a boiler. Accordingly, an RHI claimant with a medium biomass boiler with a load factor of approximately 15% should receive, over the life of the scheme, compensation amounting to the additional costs incurred by them in acquiring and running the biomass boiler (as opposed to a ‘counterfactual’, fossil fuel boiler) plus an appropriate rate of return (approximately 12%, as mentioned above).
- 49.8 If an RHI claimant ran their biomass boiler at full capacity for more than 1,314 hours in a year, then all subsequent hours of use would receive the lower, or Tier 2, tariff.
- 49.9 The lower/Tier 2 tariff was set at a level designed to cover only the additional running costs, and not the additional acquisition costs, of a biomass boiler and was set at a level which removed any incentive to overgenerate heat.<sup>2652</sup> Paragraph 26 of the IA document stated:
- “The Tier 2 tariff (at 1.9p/kWh) has been set in a way that removes the perverse incentive to over generate and vent heat for that segment while based on our evidence on gas and biomass prices also provides generators with sufficient support to cover the net cost of the renewable fuel (in line with the principle of the RHI).”<sup>2653</sup>
- 49.10 In due course, regulation 36 of the GB RHI regulations dealt with payment of the periodic support payments to scheme participants, and provided that such payments must accrue from the tariff start date (the date of accreditation of an installation) and be payable for 20 years (the so-called “grandfathering” principle). The tariffs were set out in a schedule to the regulations and were subject to adjustment each year in accordance with the retail prices index.<sup>2654</sup> A user of a biomass boiler accredited to the GB RHI scheme would therefore expect to receive the Tier 1 tariff, and then the Tier 2 tariff, depending on the number of hours for which the boiler was used, each year for 20 years from the date of accreditation.
- 49.11 It is important also to record the express recognition at paragraph 28 of the IA that tiering of tariffs was necessary not only to guard against the perverse incentive to overgenerate heat but also to prevent excessive compensation in respect of installations that had genuine heat requirements greater than that assumed for the relevant reference installation:<sup>2655</sup>
- “In addition to the elimination of the perverse incentive the two tiered tariff also provides the additional advantage of eliminating rents for installations that have higher heat requirements than the reference installation and face lower costs (this is achieved as the installations receive a lower ongoing fuel costs tariff (tier 2) to cover their higher operational time instead of the previously proposed high single tariff which aimed to also cover capital costs).”<sup>2656</sup>
- 49.12 It can therefore be seen that, from a very early stage, DECC recognised the utility and importance of including tiering in the GB RHI scheme as a means of moderating both the income and return available to scheme participants in order to deliver on the scheme’s policy objectives and safeguard public funds.

2652 INQ-20893

2653 INQ-20893

2654 INQ-20956

2655 INQ-20893

2656 INQ-20893

## Tiering in the CEPA reports

49.13 The potential for overcompensation to occur without tiering was clearly explained by CEPA in the following passage in a document sent to the Northern Ireland Assembly's PAC on 2 December 2016, after its appearance before the Committee on 23 November:

“Second, over the twenty year life of the scheme, in many cases because of the high load factors, the level of subsidy is not only paying for the conversion to the renewable technology, it is also effectively providing an additional revenue line (and/or subsidising the underlying economic activity, such as poultry farming). The intent was only ever to subsidize the shift to the renewable technology so there is no justification for providing a subsidy that goes beyond this.”<sup>2657</sup>

49.14 As discussed previously, DETI retained CEPA to advise it about, amongst other things, potential options for the delivery of a Northern Ireland Renewable Heat Incentive, including an assessment of appropriate tariff levels.<sup>2658</sup> In the CEPA draft final report of 31 May 2011 it considered subsidy levels for the NI RHI scheme.<sup>2659</sup> The Inquiry bears in mind that when designing a scheme to encourage people to switch their heating source from fossil fuels to renewables, a central question is always: how much subsidy will be enough to incentivise a switch, without overcompensating? The authors of the CEPA report looked at a number of approaches to setting the subsidy levels for a Northern Ireland scheme using DECC methodology for commercial and industrial heat users but based upon Northern Ireland specific input assumptions.<sup>2660</sup>

49.15 Both the Draft Final Report of 31 May 2011, and the Final Report of 28 June 2011 considered ‘Tiering’, providing a short description of the tiering approach being considered for GB but, crucially for the Northern Ireland scheme, failing to recommend that tiering be adopted. CEPA's analysis of the issue, set out at page 65, paragraph 6.7.1 of its Final Report, was as follows:

“The rates shown include two “tiers” for some technologies. This is an approach taken by the GB RHI where technologies receive one rate (the “tier 1” rate) for output up to a certain annual limit (15%) and then a second, lower, rate (the “tier 2” rate) for any additional output. Tiered incentive rates for investors with high load factors were calculated to limit subsidy to any incremental fuel expense should they breach the DECC tiering threshold of 15% load factor. We considered tiering for the NI RHI rates, using the DECC approach. However, when setting the NI recommended levels for this report, the incremental fuel cost was higher than the subsidy rates in all cases. Therefore no tiering is provided in the rates in this report.”<sup>2661</sup>

49.16 That analysis appears not to have taken account of the fluctuating costs of fuel. So while the statement could have been accurate at the time it was made, it may not have remained accurate in circumstances where the fuel cost dropped to below the applicable subsidy rate. In fairness to CEPA, it did give a number of warnings in the Final Report regarding, amongst other things, the inherent uncertainty in the figures relied upon by it when setting NI RHI tariff rates (including, in particular, the relative prices of biomass and fossil fuels and the relative

2657 DFE-182643

2658 WIT-105246

2659 DFE-187754 to DFE-187887

2660 DFE-187958

2661 DFE-188184

technology costs)<sup>2662</sup> and the importance of monitoring the scheme<sup>2663</sup> and reviewing it after 2-3 years.<sup>2664</sup>

- 49.17 Mr Cockburn, a director of CEPA, confirmed in his oral evidence to the Inquiry that the reference to tiering in the 2011 reports was in the context of guarding against the perverse incentive and did not deal with the risk of overcompensation as a result of high levels of usage or high load factors.<sup>2665</sup> This was in spite of what had been said about tiering in the March 2011 DECC documents referred to above. In this regard, Mr Cockburn maintained during his oral evidence that, in his opinion, the primary purpose of tiering was to guard against the perverse incentive, rather than to guard against the risk of overcompensation involving those with high load factors.<sup>2666</sup>
- 49.18 By February 2012 when the Addendum was produced by CEPA, it was clearly alive to the potential for tiering and Mr Cockburn accepted, in his evidence to the Inquiry, that CEPA even suggested tiering of the Ground Source Heat Pump (GSHP) subsidy in discussion prior to issuing the report.<sup>2667</sup> Crucially, Tables A25 and A27, which were only a page apart in the Addendum, recorded the price of wood pellets for small commercial biomass boilers as 4.39p/kWh and also a higher tariff of 5.9p/kWh. No regard appears to have been had to the contents of paragraph 6.7.1 of the earlier reports, and the issue they raised, and no reference was made to the need for tiering.
- 49.19 As outlined in chapter 5 of this Report examining the work of CEPA, its own 2012 model had actually flagged up the fact that the tariff level was now higher than the cost of heat production; but this too was not noticed and acted upon.<sup>2668</sup> In the course of giving evidence to the Inquiry Mr Cockburn conceded that “It shouldn’t have been [missed].”<sup>2669</sup> Mr Cockburn’s CEPA colleague, Iain Morrow, in his written evidence to the Inquiry, acknowledged that the 2012 model used by CEPA to determine the RHI tariffs may well have flagged up the necessity for tiering.<sup>2670</sup> However, this would not have helped DETI officials since neither the full 2012 model, nor the relevant part of it, was shared with them.
- 49.20 Nevertheless, CEPA has made the point to the Inquiry that this disparity between the level of subsidy and the price of biomass was sufficiently obvious to have been picked up by Mr Hutchinson and other DETI officials and committees who were involved. While it is a fact that the problem could have been spotted by others, this does not change the fact that CEPA were the expert consultants whose responsibility it was to design the tariffs properly.

## The DETI officials

- 49.21 The question of who should have been alert to this issue was also the subject of evidence to the Inquiry from Ms Hepper. At paragraph 188 of her written statement of 10 November 2017, Ms Hepper accepted that she had not noticed the difference between fuel price and tariff, stating:

2662 WIT-00657

2663 WIT-00606; WIT-00691

2664 WIT-00606 to WIT-00607; WIT-00678 to WIT-00679; WIT-00691

2665 TRA-01368 to TRA-01369

2666 TRA-01366

2667 TRA-01330

2668 TRA-01348 to TRA-01350

2669 TRA-01349

2670 WIT-108229

“I did not notice these, nor did any other part of the scrutiny chain at this time. I noted the increase in the tariff and accepted the explanation that this was driven by the change in banding and the reference installation, the addition into the tariff of additional barrier costs, inflation and changes to some technology costs.”<sup>2671</sup>

49.22 At paragraph 189 of the same statement Ms Hepper said:

“I noted that CEPA-AEA had recommended tiering for a specific tariff and I did ask the team if it was required for any others and the answer was that the model had been re-run by CEPA-AEA and no other tariff required tiering.”<sup>2672</sup>

49.23 In her oral evidence to the Inquiry Ms Hepper said: “We would have seen what the cost of fuel was and we would have seen the tariff.”<sup>2673</sup> She explained that she had raised the question, “The tariffs have gone up. One of them is now tiered. Should any of the rest of them be tiered?” with the DETI team.<sup>2674</sup> In this regard, she further said that Mr Hutchinson had raised the question with Mr Morrow of CEPA who had confirmed that no other tariff required to be tiered.

49.24 The Inquiry notes that, when it was drawn to its attention, no-one at CEPA had any recollection of such an enquiry after 16 February 2012, nor is there any written or electronic record of such an exchange. Ms Hepper was asked why, as a matter of common sense as opposed to expertise, three clearly incorrect references to the cost of heat production being higher than the tariff had been missed within DETI. Ms Hepper accepted that, with hindsight, the significance of that distinction should have been picked up but said that, at the time, the team “had a logic as to how you got from the price of fuel and the other elements that had to be worked through to give you the tariff and to cover the elements of it.”<sup>2675</sup>

49.25 She explained further:

“... what we did was we said the price of the fuel is x. You take the efficiency of the boiler into account because you pay out on heat combustion. That takes you up to 5.2 pence and then you’ve to add in the other elements of the tariff, and that was our logic and our thinking at the time.”<sup>2676</sup>

49.26 Based on this evidence from Ms Hepper, DETI officials ‘logic’ appears to the Inquiry to have been that the starting point for the tariff was the cost of renewable fuel and that all the other elements to be covered by the tariff were added on top. It follows from this that their expectation (wrongly) would be for the tariff to be higher than the fuel cost.

49.27 The Inquiry considers that such ‘logic’ represents a fundamental misunderstanding of the basis for tariff calculations and is flawed because the tariff was never designed to pay for scheme members’ fuel, only for the cost difference between the counterfactual fossil fuel (oil in Northern Ireland) and the renewable fuel, which in most cases in Northern Ireland was biomass. In any event, in Northern Ireland biomass was generally cheaper than oil; no tariff payment was actually needed to cover this element so the starting point should have been zero (assuming that they would not impose a negative tariff), not the price of biomass.

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2671 WIT-16676

2672 WIT-16676 to WIT-16677

2673 TRA-01926

2674 TRA-01924

2675 TRA-01926

2676 TRA-01925

- 49.28 Whatever the logic or rationale, it should still have been clear that, for the small and medium biomass tariffs, the phrase used by DETI officials in their own documents, based on CEPA's statement that "the incremental fuel cost was higher than the subsidy rates in all cases" and the conclusion that "therefore, no tiering is provided in the rates" was simply wrong.
- 49.29 Mr Connolly, the DETI economist assisting with the development of RHI policy, was asked about the clear difference between the proposed subsidy level and the biomass fuel price in the CEPA Addendum. He said he was aware of the perverse incentive risk but he did not pick up the difference at the time.<sup>2677</sup>

## The DETI Minister and her SpAd

- 49.30 The submission to the Minister on 8 June 2011,<sup>2678</sup> dealt with in detail in chapter 6 of this Report and based on the CEPA draft final report of 31 May 2011, made no specific reference to tiering, and the preliminary proposed tariffs for the NI RHI scheme were shown to be considerably lower than for the GB RHI scheme. The submission did not draw to the Minister's attention the passage about tiering in the CEPA draft final report, and a copy of the report was not provided to the Minister along with the submission.
- 49.31 The later submission to the Minister of 5 July 2011,<sup>2679</sup> which was accompanied by a copy of the CEPA final report of 28 June 2011, also made no mention of tiering, and consequently no mention of why it was not included for the proposed tariffs for the NI RHI scheme, which were set out in the submission<sup>2680</sup> and the attached July 2011 NI RHI consultation document.<sup>2681</sup> The final CEPA report<sup>2682</sup> did contain the reference to tiering referred to above, at page 65, paragraph 6.7.1, which explained why it was not required for the NI RHI scheme.
- 49.32 When the Minister was asked to approve the introduction of the NI RHI scheme through the submission of 16 March 2012<sup>2683</sup> the revised proposed tariffs, based upon the CEPA Addendum of February 2012, were set out. The tariff table provided what was said to be the equivalent GB tariffs, and the table showed that each GB biomass tariff was tiered. A footnote<sup>2684</sup> then explained that "Tiering is used to ensure the technology is not 'over-used' just to receive an incentive", before going on to say "Tiering is not included in the NI scheme because in each instance the subsidy rate is lower than the incremental fuel cost."
- 49.33 As previously discussed in this Report, the Minister confirmed to the Inquiry that she would not have read economic appraisals like the CEPA reports; she relied on the advice from officials. She also relied on her SpAd to read the technical contents of reports/submissions, brief her generally and draw to her attention anything of significance with the potential to affect her decision-making.<sup>2685</sup> Her SpAd did not refer her to the absence of tiering of subsidies in the NI RHI scheme and conceded in evidence that, despite the Minister's apparent reliance on him, he had not read any of the CEPA reports.<sup>2686</sup> That said, had the Minister's SpAd read the

2677 TRA-03560

2678 DFE 29542 to 29552

2679 DFE-29905 to DFE-30167; DFE-30246 to DFE-30247

2680 DFE-30162 to DFE-30163

2681 DFE-29928 to DFE-29929

2682 DFE-30015 to DFE-30159

2683 DFE-31746 to DFE-31772

2684 DFE-31750

2685 WIT-20570

2686 TRA-07556 to TRA-07557

CEPA final report of 28 June 2011 he would have seen in paragraph 6.7.1 that the experts had considered tiering for the NI RHI scheme and, because the incremental fuel cost was (erroneously) thought to be higher than the subsidy rates in all cases, tiering was not included in the NI RHI scheme.

## Ofgem and tiering

49.34 The absence of tiering was not recorded as a risk in the risk register appended to the Ofgem Feasibility Study of November 2011. However, consideration by Ofgem in July 2012 of the differences between the draft NI RHI regulations and those in force in GB included an internal email from Oliver More, copied to Marcus Porter of Ofgem’s legal department, which contained the observation that:

“The tiered tariff has proved a good way of reducing the incentive to waste heat in the scheme (i.e. once they have generated beyond the tier threshold, their fuel costs will often be higher than the RHI payments so boilers are only run if heat has a real value). So taking it out **increases the likelihood of abuse and heat wastage.**”<sup>2687</sup> (the Inquiry’s emphasis).

49.35 When questioned by the Inquiry as to why such a view had not been communicated to DETI, Mr Porter stated that his “assumption” had been that it was “something that DETI had thought about.”<sup>2688</sup> The Inquiry has already examined the circumstances surrounding the failure to pass on Mr More’s warning in this regard and, despite the entirely correct observation from Mr More, how Ofgem’s RHI Fraud Prevention Strategy positively asserted the presence of tiering on the schemes the strategy was covering. This was an erroneous assertion of considerable importance, because while the GB RHI scheme had the protection of tiering, the NI RHI did not.

## Effect of the absence of tiering

49.36 As discussed more generally in this Report, the absence of tiering in the NI RHI scheme (for the reasons summarised in this chapter) left the scheme vulnerable to the very issues a tiered tariff was designed to avoid, namely the creation of a perverse incentive to generate heat unnecessarily in order to attract subsidy income and the overcompensation of scheme participants as compared with the original policy intent.

2687 OFG-205614

2688 TRA-06319

## Findings

- 281.** With regard to the perverse incentive, the original tariff structure proposed in the June 2011 final CEPA report indicated that there was no need for tiering because in all cases the tariff was set below the cost of heat production. However, in the course of his oral evidence, Mr Cockburn of CEPA recognised that, in addition to the perverse incentive, tiering also provided potential protection against overcompensation, although he did not consider it to be “the core issue” or the primary purpose of tiering.<sup>2689</sup> The Inquiry finds that CEPA ought to have indicated to DETI that tiering of tariffs might be worth considering as a means of attempting to reduce the risk of overcompensating those with legitimately high load factors.
- 282.** Following CEPA’s Addendum of February 2012, tiering was still not introduced despite the proposed medium biomass tariff exceeding the cost of heat production. As an organisation competitively selected for its professional experience and expertise, CEPA ought to have picked this up and appropriately advised DETI.
- 283.** The Inquiry finds that the need for tiering of subsidy for medium biomass boilers was not spotted by any DETI officials or others involved in developing the scheme or reviewing and approving it, despite the clear excess of tariff over the cost of heat production being recorded in the CEPA Addendum of 2012 and subsequently reproduced in documents that the officials had drafted, such as the synopsis for the Casework Committee<sup>2690</sup> and the 2012 RHI business case.<sup>2691</sup>
- 284.** The Inquiry considers that Ms Hepper, Mr Hutchinson and Ms McCutcheon, perhaps understandably, did not fully understand the CEPA approach to modelling or the uncertainty in the assumptions upon which the tariff calculations were based.
- 285.** One of the assumptions, for example the average load factor (hours of heat production per annum) made for the reference case by CEPA of 17%, would prove to have little relevance in practice for usage by the large agricultural sector in Northern Ireland, including the poultry sector which was expanding in response to Moy Park’s growth strategy from 2010 onwards.<sup>2692</sup>
- 286.** It did not require any special expertise on the part of Energy Division officials to see that the cost of fuel was less than the subsidy and to question this as it came to be included in documents for which they were responsible and on which scheme decisions were based.

2689 TRA-01366

2690 DFE-398068 to DFE-398070

2691 DFE-00162 to DFE-00163

2692 TRA-06013 to TRA-06019

**287. The Inquiry notes that even though tiering was introduced for new applications in November 2015, the fact that the tariff for all other earlier accredited medium biomass installations still continued to be above the cost of heat production was said to have not been properly appreciated by DETI officials until the publication of the NI Audit Office Report in 2016. The Inquiry found extensive evidence, detailed earlier in this Report, that, in contrast, market participants required less than a few weeks to uncover this unintentional and damaging flaw, namely the failure to apply tiering to the small and medium biomass tariffs, resulting in the risk of overcompensation and/or exploitation.**



## Chapter 50 – Review

- 50.1 Another significant issue that was considered during the Inquiry's work was the failure of DETI to conduct any meaningful review of the NI RHI scheme, in spite of the warnings that had been received regarding the need to do so and the various undertakings given by DETI to do so.

### The nature of the NI RHI scheme

- 50.2 As mentioned earlier in this Report, the NI RHI scheme was an innovative, volatile, demand-led scheme, differing from the equivalent scheme in GB in a number of significant respects. For example, it lacked tiering of certain biomass tariffs, despite the relevant subsidy being higher than the cost of biomass fuel, and it also lacked any overall mechanism of budgetary control. It was also being introduced into a new market and had, in the circumstances, been designed on the basis of a number of untested assumptions about how that market would perform.
- 50.3 The risks associated with a scheme that has been designed based upon assumptions about a new or immature market, and the consequent need to monitor the operation of such a scheme and remain alert to the possibility that it may require review at an early stage, are perhaps evidenced by developments in the GB RHI scheme during 2013. On 31 May 2013 then DECC Minister Barker wrote<sup>2693</sup> to the then DETI Minister explaining that DECC had conducted a review of the tariffs on the GB RHI and was launching a consultation on the outcome of that work, and was also making the first degression announcement which would see its medium biomass tariff reduced. The letter detailed the rationale behind the review of tariffs. DETI Private Office referred the letter to Ms Hepper, who in turn asked Ms McCutcheon to consider it.<sup>2694</sup> Ms McCutcheon informed Private Office that the DECC letter provided an update and a reply was not required.<sup>2695</sup> However, the DECC ministerial letter had clearly underlined the significance of drawing on market intelligence, stakeholder views and expert opinion when reviewing tariffs, rather than relying primarily on assumptions and modelled outputs (which had been the approach when the tariffs were originally being devised).
- 50.4 Important assumptions, relied upon when designing and establishing tariff levels within the NI RHI scheme, included those in respect of fuel costs, capital costs, access to finance, consumer confidence, market capability, technology efficiency, technology use, load factors and the required return on investment. In such a context, in view of the risks involved and the number of variables, it is clear that regular review of the NI RHI scheme as it progressed, in order to test the validity of the assumptions upon which its design had been based, was a fundamental requirement. This is because changes were bound to occur in relation to a number of these assumptions as the market matured and the number of installations increased. Such a requirement could have been included in an appropriate project management programme, record or log in order to ensure continuity, uniformity of approach and supervisory control. However, as discussed earlier in this Report, no such programme was instituted.

### References to the need for review of the NI RHI

- 50.5 The absence of formal project management structures and processes in relation to the NI RHI has already been addressed earlier in this Report. This meant that the general requirement

2693 DFE-53262 to DFE-53264

2694 WIT-02450

2695 WIT-02449

to keep the NI RHI scheme under review, and any more particular requirement to carry out a review of the scheme at a defined point in time, was not captured in a project log, a dynamic risk register or similar such project management document. Had it been, the Inquiry considers it more likely that the planned review of the scheme would have been progressed; or that, at least, any decision to defer or cancel the planned review would have been given more detailed consideration.

50.6 Nonetheless, the requirement to keep the NI RHI scheme under review, and the more specific intention to carry out such a review (initially scheduled to commence in early 2014), was referred to in a number of significant documents, including the following:

- (i) DECC's GB RHI Impact Assessment (IA) of March 2011 pointed out that a number of economic, technical, and behavioural assumptions underpinned its modelling projections and emphasised the need to bear in mind that all modelling based upon assumptions is, at best, illustrative and had to be treated with the appropriate degree of caution, pointing out that:

"In reality the uptake under the RHI will be demand-led and will be driven by uncontrollable factors, and therefore even short-term projections of costs are subject to a wide range of uncertainty."<sup>2696</sup>

In such circumstances the IA emphasised the importance of regular, scheduled and, if necessary, early reviews.<sup>2697</sup> At Annex 1 the IA referred to powers that the DECC Secretary of State might adopt to introduce an early review noting that the criteria for the exercise of such a power were still to be resolved and that they would be subject to consultation.<sup>2698</sup>

- (ii) In Northern Ireland, CEPA also stressed at various points throughout its reports that regular review of the NI RHI was essential due to the high degree of uncertainty in the underlying assumptions, as well as to the likely changes in market conditions with time. Paragraph 8.2.1 of the final report of 28 June 2011<sup>2699</sup> referred to the need for regular, planned reviews of subsidy levels; at paragraphs 11.4 and 11.5 there was a recommendation that a full review should take place after two or three years, together with ongoing periodic monitoring.<sup>2700</sup>

- (iii) The NI RHI consultation document published by DETI in July 2011 stated that:

"The NI RHI will be monitored and evaluated and reviewed to ensure that the objectives are being met and that any barrier or problems are identified and addressed ... the first review will be initiated in January 2014 and involve stakeholder consultation, analysis and development of proposed changes, if required. It would be anticipated that the out-workings of the review would be in place by 1 April 2015."<sup>2701</sup>

- (iv) Paragraph 29 of the synopsis of the case for an RHI scheme submitted to the DETI Casework Committee on 9 March 2012 stated:

2696 INQ-20901

2697 INQ-20879 to INQ-20916

2698 INQ-20910

2699 DFE-398339 to DFE-398340

2700 DFE-398352 to DFE-398354

2701 DFE-61712

**“The NI RHI will have scheduled reviews built-in to the scheme to allow DETI to ensure that the scheme remains fit for purpose and value for money for the duration.** [Bold emphasis in the original] The scope of these reviews will include analysis of tariffs (either to be reduced or increased), the appropriateness of technologies (remove existing technologies or add new innovative ones) and the assessment of effectiveness and success.”<sup>2702</sup>

- (v) The Risk Register for the NI RHI of 1 March 2012 identified as risk ‘A’ that of “Incorrect tariff levels set (either too high or too low)”. It said the risk of it occurring was medium, but that the impact if it occurred was high. The register identified “planned reviews of the scheme so tariffs could be revised depending on market conditions” as an additional action “to fully manage the risk”.<sup>2703</sup> In the section documenting the criticality of review as high, the target date for review was specified as 2014. The document named Mr Hutchinson and Ms McCutcheon as the ‘risk owners.’ Planned reviews, with a target date of 2014, were also recorded as a measure to manage other identified risks such as low uptake, harm to other sectors, the risk of insufficient budget being secured for the RHI payments or for administration of the scheme and the failure to meet EU and Executive targets.<sup>2704</sup>
- (vi) During the Casework Committee meeting on 9 March 2012 Ms Hepper explained that the NI RHI scheme would have scheduled reviews “built-in” to allow DETI to ensure the scheme remained fit for purpose and value for money.<sup>2705</sup> The Committee was told that the RHI scheme would be reviewed in 2014 and at regular intervals thereafter and that tariff levels might be adjusted for new installations if appropriate.<sup>2706</sup> In his evidence to the Public Accounts Committee (PAC) on 28 September 2016, Dr McCormick described the Casework Committee as having been told there was a “commitment to review.”<sup>2707</sup>
- (vii) On 16 March 2012 Ms Hepper sent a submission to the Minister and her SpAd again confirming that the NI RHI scheme would have scheduled reviews “built-in” to allow DETI to ensure that the scheme remained fit for purpose and value for money.<sup>2708</sup> The Regulatory Impact Assessment document<sup>2709</sup> enclosed with that submission, ultimately signed off by the Minister on 13 April 2012,<sup>2710</sup> confirmed that it was DETI’s intention to have regular, planned reviews of subsidy levels after a number of years of experience with the subsidy and that it was currently proposed that the first review would begin in January 2014, with any required changes to be implemented by 1 April 2015.<sup>2711</sup>
- (viii) The RHI Business Case produced by DETI and sent to DFP on 22 March 2012<sup>2712</sup> for the purpose of obtaining DFP approval for the proposed Northern Ireland non-domestic RHI also contained a number of references to reviews of the scheme including at paragraphs

2702 DFE-398071

2703 WIT-07064

2704 WIT-07065 to WIT-07069

2705 DFE-382570 to DFE-382582 at DFE-382576

2706 DFE-382576

2707 DFE-00058

2708 DFE-31747 to DFE-31755

2709 DFE-31788 to DFE-31799; DFE-70749 to DFE-70760

2710 DFE-70760

2711 DFE-31790

2712 DFE-82632

7.53, 7.54 and 10.4, which, like the Regulatory Impact Assessment, recorded that the first review was to begin in January 2014 with any changes implemented by 1 April 2015.<sup>2713</sup>

- (ix) The DFP approval of the NI RHI scheme dated 27 April 2012 included two specific conditions, the first of which was that reapproval by DFP was to be sought if the scheme was to proceed beyond March 2015 and the second of which was that:

“As outlined in section 7.53 of the Business Case, arrangements are put in place for scheduled reviews to allow the progress of the scheme to be monitored, assessed and, if necessary, changes implemented. It is noted that the first review is scheduled to start in 2014 and that the reviews will be carried out by DETI.”<sup>2714</sup>

- (x) On 17 October 2012 the submission to Minister Foster with draft speaking notes for the Assembly motion debate seeking approval of the draft NI RHI regulations included the statement:

“However, to ensure the scheme is cost effective the tariffs will be reviewed over time and new tariffs will be applied to anyone joining the scheme...a review of the RHI will take place in 2014/2015.”<sup>2715</sup>

- (xi) Mr Hutchinson’s handover document referred to one of the “immediate actions (by end August 2014)” as being review of the current non-domestic scheme in terms of biomass tariffs under 100kW and consideration of tiered tariffs to prevent excessive payments.<sup>2716</sup>
- (xii) In the Energy Division paper for the heads of branch meeting on 15 May 2014, shortly before he left the Department, Mr Hutchinson included an entry noting the potential need for review of tariffs (particularly for biomass less than 99kW) given advice from Ofgem regarding the use of these systems and suggesting that tiering might be appropriate.<sup>2717</sup>
- (xiii) In all drafts of the ‘Composite Divisional Plan, Energy Division, 2014-2015’ (mentioned in chapter 18 of this Report) from around 13 May 2014 onwards, a “key action” of “monitor[ing] the uptake of the non-domestic RHI and carry[ing] out policy reviews as required” appeared along with a risk that “tariffs under the scheme are overly generous and lead to higher than expected uptake and excessive payments, impacting on budgets.”<sup>2718</sup>
- (xiv) One of the last documents prepared by Mr Hutchinson before he left DETI was a six-monthly update document for the ETI Committee which was sent to Minister Foster for her approval on 15 May 2014.<sup>2719</sup> At paragraph 14 of the update it was stated, in respect of the non-domestic RHI scheme, that “it may be appropriate to review the existing tariffs based on the experience of the first 18 months of the scheme.”<sup>2720</sup>

50.7 In spite of the importance of the need for review, and the references to review in the various documents referred to above, the power to review was not placed on a statutory footing as it had been for Northern Ireland’s renewable electricity incentive scheme, the ‘NIRO’. Article 31

2713 DFE-82703; DFE-82712

2714 DFE-171219 to DFE-171220

2715 DFE-33145 to DFE-33158 at DFE-33155

2716 DFE-383318

2717 DFE-410161

2718 DFE-377626

2719 DFE-230084 to DFE-230090

2720 DFE-230090

of the Renewables Obligation Order (Northern Ireland) 2009 had conferred upon DETI a specific statutory power to hold regular and discretionary reviews of banding provisions relating to the amount of electricity to qualify for payment.<sup>2721</sup> A similar power to review the banding of heat output for installations, and the associated tariffs, was noticeably absent from the NI RHI regulations, just as it was also absent from the GB RHI regulations. Although it was not necessary for there to be a statutory power to facilitate DETI conducting a review of the NI RHI scheme, the presence of such a power in a scheme has a number of potential advantages, including predictability for the market and a reduction in the likelihood of the responsible Department overlooking the need to perform either a scheduled or an emergency review.<sup>2722</sup>

### DETI officials' awareness of the need for review

- 50.8 Ms McCutcheon told the PwC interviewers that DETI had appreciated the need for a review, given the huge range of assumptions that required to be monitored. In her interview she said that there was to be a review of the scheme in 2014 and that development of the scheme was “an evolving process”. As the GB RHI scheme was roughly a year to eighteen months ahead of the NI RHI scheme, DETI officials were watching what DECC was doing and learning from DECC. She also said that she and her colleagues did not think that the scheme was “written in stone” but, rather, “knew that this scheme was built on a huge range of assumptions and had to be very, very carefully monitored”. Since there was a finite budget, there was to be a formal review in 2014 but, meanwhile, they were “obviously...to keep a very careful watch on it...”.<sup>2723</sup>
- 50.9 Ms McCutcheon also said to PwC that a review may not have taken place in January 2014 because of the six-month delay in the scheme’s original starting date (i.e. the January 2014 review date was predicated on a scheme start date before summer 2012, rather than the actual start date of November 2012), but she was unable to recall any conscious decision to delay the promised review, and when she left in April 2014 she expected a review to take place that year.<sup>2724</sup>
- 50.10 Mr Hutchinson acknowledged in his evidence to the Inquiry that the start of the scheme had been delayed but he accepted that a review would have had to be completed and any changes decided upon by 31 March 2015, the date by which DFP reapproval was to be sought.<sup>2725</sup>
- 50.11 Mr Thomson told the Inquiry that he was aware of the need for a review of the non-domestic RHI scheme (and also of the need for reapproval of the scheme by DFP). When he met with Ms Hepper towards the end of 2013, he said that she had talked of the need for a review and that such a review was a central requirement.<sup>2726</sup> Mr Thomson was unable to think of any reason why Ms Hepper would not have shared the same views when she met Mr Mills.<sup>2727</sup> He was of the view that the handover passed from Ms Hepper to Mr Mills should have included the need for a review (and also the need for reapproval by DFP in March 2015).<sup>2728</sup> Mr Mills, in the course of his PwC interview in October 2016, said he was not aware of the need to start

2721 LEG-03300

2722 See, for instance, the discussion of this issue in Mr Hutchinson’s oral evidence to the Inquiry at TRA-01521 to TRA-01522

2723 PWC-04551

2724 PWC-04551

2725 TRA-05139 to TRA-05141

2726 TRA-05737 to TRA-05738; TRA-05985

2727 TRA-05989

2728 TRA-05994 to TRA-05995

a review in January 2014<sup>2729</sup> and did not recall any discussion with Mr Thomson in which the need for a review was passed on.<sup>2730</sup>

- 50.12 In his evidence to the Inquiry Mr Mills also disputed whether any such condition had been highlighted to him during the course of his verbal handover discussion with Ms Hepper.<sup>2731</sup> It is the case that the documentary handover material provided to Mr Mills<sup>2732</sup> did contain a lengthy Strategic Energy Framework 2010 implementation plan updated as of September 2013, which did refer, in one entry, to an RHI Review “by end March 2015”.<sup>2733</sup> However this needs to be contrasted with the fact that the specific RHI summary provided with the first day briefing material did not mention the need for review or the need to seek further DFP approval, nor did it draw attention to any potential problems with the scheme.<sup>2734</sup>
- 50.13 Mr Mills, who took over from Ms Hepper as head of Energy Division in January 2014, told the Inquiry that his first substantial briefing from the officials in Renewable Heat Branch in March 2014, with Ms McCutcheon and Mr Hutchinson, focused upon discussing the business case for the introduction of the domestic RHI scheme and he was unable to recall any discussion of the need to review the non-domestic RHI scheme.<sup>2735</sup> With the benefit of hindsight, he felt that there had not been a sufficient uptake of the scheme for a useful tariff review to take place and he added that he simply did not have adequate resources to commission a full review of the scheme.<sup>2736</sup>
- 50.14 The Inquiry notes that, as discussed earlier in this Report, the business case for the domestic RHI scheme was prepared by Mr Hutchinson, revised by Mr Wightman and approved by Mr Mills in 2014. In many iterations of the document, paragraph 10.10 stated that:
- “The first formal review of the commercial RHI will begin in early 2015 with necessary changes implemented in 2016. The primary focus of this review will be the level of tariffs and the appropriate banding.”<sup>2737</sup>
- 50.15 Although the date had slipped by a year, the reference to review was still part of the document that Mr Mills approved. Mr Mills also said that he did not remember reading the earlier 2012 business case for the non-domestic RHI scheme or the subsequent April 2012 DFP approval and, in any event, he “did not have time to go through historical material.”<sup>2738</sup> He said that he was unsure what the review referred to; that is to say whether it referred to a review restricted to tariffs or a fundamental root and branch review and, as mentioned previously, in respect of the latter he emphasised that he simply did not have the resources.<sup>2739</sup>
- 50.16 There are a number of documents potentially showing that Mr Mills was aware of the need for review, or an intention to carry one out. Reference has already been made above to the Strategic Energy Framework 2010 Implementation Plan recording progress to 30 September 2013.<sup>2740</sup>

2729 PWC-04568

2730 TRA-07100 to TRA-07101

2731 TRA-07084 to TRA-07085; TRA-07089; WIT-14519

2732 WIT-14519; WIT-14700 to WIT-14748; DFE-399077 to DFE-399085

2733 DFE-399083

2734 WIT-14700 to WIT-14748

2735 TRA-07104 to TRA-07105

2736 TRA-07134 to TRA-07140

2737 DFE-269932

2738 TRA-07130 to TRA-07131

2739 TRA-07139 to TRA-07140

2740 DFE-399077

- In addition to recording the requirement to introduce Phase 2 of the NI RHI by the end of 2013 and to have Phase 2 fully operational by the end of September 2014, the document recorded a further requirement, by the end of March 2015, to carry out a review of the RHI scheme.<sup>2741</sup>
- 50.17 In addition, a DETI ministerial answer to an Assembly question raised by Daithí McKay MLA in March 2014 (in relation to renewable energy and performance against the 4% interim target by 2015) indicated that: "...to verify progress, DETI will carry out analysis as part of a future review of the Renewable Heat Incentive."<sup>2742</sup> The answer purported to have been prepared by Mr Mills<sup>2743</sup> and Mr Thomson believed it to have come from, and been signed off by, Mr Mills,<sup>2744</sup> which Mr Mills accepted it would have been. In his oral evidence, Mr Mills also said that he could not gainsay that that was a reference to a review.<sup>2745</sup>
- 50.18 Furthermore, a submission from Mr Mills to Minister Foster of 15 May 2014<sup>2746</sup> contained a draft update on the RHI scheme to the ETI Committee. In the course of that update, the Committee was told that, "In addition, it may be appropriate to review existing tariffs based on the experience of the first 18 months of the scheme." By that time, of course, the scheme had been running for just under 18 months. Mr Mills said in evidence that he considered this to refer to a more focused tariff review, rather than a full review of the scheme; but also that it was not considered an imperative at that point. He accepted, however, that there should have been consideration given at that point about how the review would be resourced and taken forward.<sup>2747</sup> In his written evidence Mr Mills also referred to this submission from May 2014 (as well as the heads of branch meetings discussed below) as a document on the basis of which he should have known about the justification for carrying out a tariff review in May 2014.<sup>2748</sup>
- 50.19 Mr Wightman, who joined DETI on 30 June 2014 as the new head of Energy Division's Energy Efficiency Branch (which included responsibility for RHI amongst other matters, and replaced the narrower focused Renewable Heat Branch), did retain the first three pages of Mr Hutchinson's handover document and, consequently, he should at least have been aware of the fourth bullet point under the heading "immediate actions (by end of August 2014)".<sup>2749</sup> That bullet point referred to a specific review of the current non-domestic scheme with particular regard to review of biomass tariffs under 100kW and consideration of tiered tariffs to prevent excessive payments.<sup>2750</sup> The Energy Division heads of branch update for the meeting scheduled for 15 May 2014 also recorded the:

"Potential need for review of tariffs (particularly for biomass less than 100kW) given advice from Ofgem regarding the use of the systems. A system of tiered tariffs might be appropriate."<sup>2751</sup>

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2741 DFE-399083

2742 DFE-417745

2743 DFE-417746

2744 TRA-05993

2745 TRA-07158 to TRA-07159

2746 DFE-234637 to DFE-234642

2747 TRA-07161 to TRA-07163

2748 WIT-26007

2749 WIT-17709

2750 DFE-383318

2751 DFE-410161

- 50.20 The bullet point was retained in the contribution for the Energy Division heads of branch meeting scheduled for 3 July 2014.<sup>2752</sup> The bullet point was however removed from Energy Efficiency Branch’s update for the Energy Division heads of branch meeting scheduled for 25 July 2014.<sup>2753</sup> Though removed from that update, the bullet point was transferred into the Energy Efficiency Branch plan of 28 July 2014 discussed further below. Mr Wightman accepted in the course of his oral evidence that he would have been the person most likely to have removed the bullet point about the need to review the non-domestic tariffs, but he was unable to say why he would have decided to do so.<sup>2754</sup> He explained to the Inquiry that it may have been because the heads of branch notes were “quite immediate”, intended to relate to just the coming weeks.<sup>2755</sup>
- 50.21 As mentioned above, Mr Hutchinson’s bullet point about the tariff review was transferred to the Energy Efficiency Branch plan. The first draft of the Energy Efficiency Branch, Branch Plan 2014-15, of 16 July 2014, as far as it related to the non-domestic RHI scheme, gave, as an objective for Mr Wightman, the introduction of Phase 2 of the non-domestic RHI scheme by 31 March 2015,<sup>2756</sup> with the relevant detailed activities, including finalising policies, securing approvals and the amendment of the existing regulations, being assigned to Mr Hughes who had taken over Mr Hutchinson’s role on 30 June 2014.
- 50.22 The seventh draft or revision of the branch plan, of 28 July 2014, again had the same responsibilities for Mr Wightman and Mr Hughes,<sup>2757</sup> but the detailed activities now included a review of biomass tariffs under 100kW and consideration of tiered tariffs to prevent excessive payments (which was the content that had been in the heads of branch update of 3 July 2014). The understanding of the question of tiered tariffs to prevent excessive payments was recorded as having to be checked with Mr Hutchinson.<sup>2758</sup> It appears that the plan was a “living document” which was subject to amendment during the relevant year.<sup>2759</sup> A similar entry was contained in the tenth draft or revision, dated 5 August 2014.<sup>2760</sup> The draft or revision of 29 September 2014 prepared by Mr Wightman recorded that a meeting had taken place with Mr Hutchinson on 12 August; but in the course of giving evidence to the Inquiry Mr Hutchinson said that only the domestic scheme regulations were discussed,<sup>2761</sup> and, although the reference continued to appear in the above form in Energy Efficiency Branch plans until February 2015, the matter was never subsequently raised with Mr Hutchinson, nor taken forward by Energy Efficiency Branch by the time the scheme was recognised to be in major difficulty in May and June 2015.

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2752 DFE-410186

2753 TRA-06914

2754 TRA-06914

2755 TRA-06929

2756 DFE-419606 to DFE-419612

2757 DFE-419557 to DFE-419565

2758 DFE-419562

2759 TRA-06920

2760 DFE-419533

2761 WIT-06112; WIT-09333

## Loss of need to review

- 50.23 The DETI Operating Plan for 2013-14, dated June 2013, did not contain any reference to the need to review the non-domestic RHI scheme.<sup>2762</sup> There also appears to have been no reference to the review in the Energy Division composite plan for 2013-14.<sup>2763</sup>
- 50.24 The DETI Operating Plan for 2014-15, dated April 2014, also did not contain any reference to the need to review the non-domestic RHI scheme or to consider cost controls.<sup>2764</sup> The composite divisional plan for Energy Division, dated May 2014, also did not refer to the need for review.<sup>2765</sup>
- 50.25 In her personal performance review before leaving DETI in November 2013 Ms Hepper included at target number (6):
- “Ensure all policy, legislative and operational work is complete in relation to Phase 2 of the Renewable Heat Incentive including incentivising the domestic market.”
- 50.26 She did not include any documentary reference to the need to start or to commence arrangements for a review of the non-domestic RHI scheme in January 2014 or any later date.<sup>2766</sup>
- 50.27 As a consequence, despite the knowledge of officials and the existence of relevant documents which referred to the need for and intention to review, no preparations or practical arrangements were made to commence a review of the non-domestic RHI scheme, including the tariff structure, in January 2014 or thereafter.
- 50.28 Mr Sterling was unable to account for the fact that, whilst the need for a review in January 2014 was clearly recognised and documented (at least to some extent) prior to Christmas 2013, this appears to have been replaced, in May 2014, by a proposed review in early 2015; and then the intention to review disappeared thereafter.<sup>2767</sup> He thought that the requirement for a review should have featured in both the Divisional and Operating Plans. He told the PAC in November 2016 that he regarded the absence of a major review as being “critical” and “a major contributory factor” to the RHI problems.<sup>2768</sup> He was asked why he had not taken steps to initiate a review in January 2014, consistent with the business case requirement, and he replied that he had not been conscious at the time of the need to do a review. He accepted that that was not a particularly good excuse.<sup>2769</sup>

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2762 DFE-386454 to DFE-386514

2763 DFE-377431 to DFE-377470 at DFE-377451

2764 DFE-386515 to DFE-386562

2765 DFE-377471 to DFE-377512 see DFE-377503 to DFE-377504

2766 DFE-430338 to DFE-430339

2767 TRA-06991

2768 DFE-02166; DFE-02171

2769 DFE-02164 to DFE-02165

## Findings

- 288.** While not preventing the carrying out of a review, the failure to incorporate a specific power to review the NI RHI scheme in the NI RHI regulations, even if this was absent from the original GB RHI regulations, was an unfortunate omission on the part of DETI considering that it had knowingly introduced NI-specific tariffs, had received multiple warnings about the uncertainty of assumptions and modelling, and had knowledge of the market volatility of fuel prices.
- 289.** Even without such a statutory provision, there was knowledge amongst officials of the need for a review. Reference to it existed in a number of Energy Division Renewable Heat Branch (later, Energy Efficiency Branch) documents, yet no preparations or practical arrangements were made to commence a review of the scheme, including of the tariff structure, in January 2014 or thereafter.
- 290.** This failure by DETI to carry out any review of what was a novel and volatile scheme represented one of the major failings that allowed expenditure to race out of control. In spite of the issue having been raised orally and/or in writing with many witnesses, the Inquiry has never been provided with any adequate explanation as to why there was a failure to carry out a review.
- 291.** This failing once again demonstrates the dangers of inadequate project management, the lack of recognised processes to manage staff turnover and the handover of important information to assure business continuity and maintain institutional memory.

## Chapter 51 – Budget control – scheme suspension and degression

51.1 The Inquiry considers it to be important to differentiate between the concepts of cost control and budget control – it is possible to manage individual costs (e.g. through tiering of tariffs), but still lose control of the scheme budget because overall spend for an incentive scheme is dependent on both individual costs and the volume of uptake. In this chapter the Inquiry will focus on the issue of budget control, although it notes that in much of the evidence received by it the term “cost control” was used to refer to what are, in fact, budget controls (e.g. in the context of the Phase 2 public consultation). Indeed, upon occasions the terms were used interchangeably.

### Background

51.2 Ms Hepper, Mr Hutchinson and Ms McCutcheon all indicated in their interviews with the PwC investigation team that they had recognised the need for budget controls from the inception of the NI RHI scheme. As appears elsewhere in this Report, each of them was aware of the warnings from HMT and DETI Finance contained in the 2011 Parker and Clydesdale email exchanges relating to the need for controls to prevent overspend impacting on the DEL budget. However, each referred to the financial modelling undertaken by CEPA in designing the tariffs as a key cost control.

51.3 Ms Hepper told PwC that the first budget control they put in place in discussions with the consultants was to say: “your model has to be within the framework and ring-fenced to £25 million.”<sup>2770</sup> Mr Hutchinson agreed, referring to the CEPA model as the “first cost control”, and Ms McCutcheon confirmed that “Whenever I arrived the whole work that CEPA had been given to do was to live within that budget and to maximise the output of renewable heat living within that budget.”<sup>2771</sup>

51.4 This misplaced reliance upon the CEPA modelling needs to be contrasted with the following facts, of which all three DETI officials were aware:

- (i) CEPA’s own clear and repeated warnings as to the uncertainties behind the modelled outcomes and the resultant need to monitor the variables and assumptions upon which the models had been constructed and the tariffs computed in order to see if the scheme performed in line with the assumptions.<sup>2772</sup>
- (ii) The clear advice about the significant challenge represented by the capped budget contained in the emails from Alison Clydesdale and Bernie Brankin.<sup>2773</sup>
- (iii) DETI’s own RHI risk register produced by the same Energy Division officials in 2012 which included the risk of “Insufficient budget secured for the RHI payments or for the administration of the scheme.” The impact of the risk was assessed as “high” with a “medium” likelihood of the risk materialising. One potential cause was identified as tariffs being set at too high or generous a level leading to a higher than expected uptake.<sup>2774</sup>

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2770 PWC-04531

2771 PWC-04597; PWC-04550

2772 WIT-00678 to WIT-00679

2773 DFE-62072 to DFE-62076

2774 WIT-07068

## Warnings about the need for budget control

- 51.5 The Department received a number of further warnings about the risks of the non-domestic NI RHI scheme and the need for controls.
- 51.6 For instance, in its October 2011 response to the 2011 DETI public consultation on the NI RHI, Biomass Energy Northern Ireland (BENI) informed DETI of the risk that the then envisaged banding between the small and medium biomass tariffs risked the installation of multiple systems just to “harvest” the higher RHI payment. BENI repeated this point in its October 2013 response to the public consultation on the domestic RHI scheme, and pointed out that the risk of exploitation it had warned about was now materialising in practice.<sup>2775</sup>
- 51.7 On 16 December 2011 Ofgem informed DETI at paragraph 6.9 of its Feasibility Study for Ofgem’s administration of the NI RHI:
- “At present there are no mechanisms in place to control costs of the scheme in the event that uptake is considerably higher than anticipated.”<sup>2776</sup>
- 51.8 In her oral evidence to the Inquiry Catherine McArthur, who carried out the work on the December 2011 Feasibility Study in Ofgem, said that she recalled cost control had been discussed with DETI, although she could not recall the detail. In retrospect, she explained that the main discussion was about the need for regular review and general monitoring of costs with emphasis upon the proposed joint DETI/Ofgem Administration Board as a good way for DETI to remain close to the operation of the scheme and to be able to get regular updates on application volumes and what that would mean for costs.<sup>2777</sup>
- 51.9 However, while cost control mechanisms could be built in to the NI RHI scheme itself, she said that the officials in DETI were very conscious, both in terms of operational and overall costs, to keep costs to a minimum and that to build in cost control to the scheme might reduce the incentive to invest. Ms McArthur said that her impression had been that cost controls were discussed as something that would be sensible.<sup>2778</sup>
- 51.10 As discussed in detail elsewhere in this Report, on 26 June 2012 during a teleconference with Ofgem, Ms McCutcheon and Mr Hutchinson were warned in clear terms that in GB it had been considered necessary to amend the GB RHI regulations and Ofgem could see logistical and presentational issues with the NI RHI scheme initially being without these “improvement updates” otherwise DETI would be replicating the issues that it had proven necessary to address in GB. One of the measures being introduced through the GB RHI amendment regulations, in July 2012, was the Stand-by Mechanism (SBM) as a form of interim budget control (involving the automatic temporary suspension of the scheme to new entrants if there was a threat to the budget). Ofgem’s advice was that DETI should wait until the GB amendments were introduced, as replicating those amendments in the NI RHI regulations would negate any risk that the draft NI RHI regulations currently posed.<sup>2779</sup>
- 51.11 The context of the Ofgem warning was apparent to Mr Hutchinson, who told the Inquiry that he was familiar with the March 2012 consultation document published on the DECC website setting

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2775 DFE-98994 to DFE-98999

2776 DFE-79801

2777 TRA-03721

2778 TRA-03722 to TRA-03723

2779 OFG-03517 to OFG-03519; WIT-09052 to 09060; TRA-02200 to TRA-02207

- out the need for its SBM, which it had referred to as an “interim cost control” when it published its consultation document. He had also received the warning of a need to guard against the “large financial risk” contained in the email from Mr Patel of DECC on 8 June 2011.<sup>2780</sup>
- 51.12 Nonetheless, Ofgem officials were informed that DETI would not wait for the DECC GB RHI changes because they had a commitment to their Minister to bring the NI RHI regulations into force by the end of September 2012 and there was a risk of putting funding in jeopardy. Ofgem officials were also told that DETI intended to have a Phase 2 update in the summer of 2013 when, rather than adopt interim cost controls, they would reproduce the full degression mechanism about which DECC was to consult in the summer of 2012.<sup>2781</sup> Ms Hepper was informed of the Ofgem warning and gave evidence that she considered that it was important enough to refer to Mr Thomson with a view to referring it to Minister Foster.<sup>2782</sup>
- 51.13 In April 2013 degression, the reduction in tariffs triggered by certain volumes of uptake and/or budget spend being reached, was introduced in GB by further amendment to the GB RHI regulations. On 31 May 2013 DECC Minister Barker wrote to Minister Foster informing her that the deployment of small and medium sized biomass installations had been so successful that a 5% degression of the relevant tariff would occur.<sup>2783</sup> As discussed previously in this Report, that letter was referred to Ms McCutcheon but, unfortunately, she did not consider that a response was required and it was not referred to Minister Foster.<sup>2784</sup>
- 51.14 The first automatic tariff reduction took place in July 2013 because of the popularity of the small/medium biomass installations. The more sophisticated degression mechanism had replaced the SBM, the interim system of budget control, involving the automatic temporary suspension of the scheme to new entrants if there was a threat to the budget. As discussed previously in this Report, this interim solution had been consulted upon just four months after the GB RHI scheme launch. This was despite low uptake levels but due to DECC’s concerns about the potential risk of runaway demand and uptake levels.
- 51.15 Mr Hutchinson of DETI clearly felt that the need for budget control was sufficiently important to persuade him to draft the trigger system applicable to both non-domestic and domestic RHI schemes, and which was then set out in the July 2013 Phase 2 RHI public consultation.
- 51.16 In the course of her oral evidence to the Inquiry Minister Foster agreed that she had read the 2013 RHI public consultation documents and understood that the ‘cost control’ described was necessary “So that we didn’t exceed our budget”. She also agreed with the statement in the cost control section of the consultation document that “DETI must retain the right to suspend the scheme if budget limits could be breached.”<sup>2785</sup>
- 51.17 On 10 December 2013 Ms McCutcheon forwarded a submission<sup>2786</sup> to Minister Foster drawing to her attention a letter from Minister Barker dated 29 November<sup>2787</sup> which provided an overview of the GB RHI schemes as they stood then. That overview included details of the degression mechanism applicable to both GB non-domestic and domestic RHI schemes, details of which

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2780 TRA-02202; DFE-05426 to DFE-05429

2781 OFG-03517

2782 TRA-02687 to TRA-02692

2783 DFE-53262 to DFE-53264

2784 WIT-02449 to WIT-02454

2785 TRA-08321 to TRA-08324

2786 DFE-33748 to DFE-33750

2787 WIT-18705 to WIT-18712

were annexed to the letter. The letter explained that degression had been implemented by regulations in April 2013 and was:

“...designed to ensure that the RHI remains financially sustainable and provides value for money to the taxpayer. Under this mechanism we reduce the tariffs paid to new RHI recipients if uptake of the scheme is higher than the trigger levels set out in advance in legislation, based on forecast deployment for each technology. This is designed to protect the budget and ensure value for money for the taxpayer.”<sup>2788</sup>

51.18 However, the submission provided to the Minister did not engage with the issues of budget management set out in the letter from the DECC Minister, did not explain what DETI intended to do (if anything) in respect of degression, and did not contrast the DECC approach with the budget control on which DETI had just finished consulting. Minister Foster was asked to, and did, sign a letter in reply to Minister Barker in which she confirmed that:

“My Department has recently consulted on similar proposals to expand the Northern Ireland non-domestic RHI scheme and to introduce new tariffs for more innovative technologies. In addition, consideration has been given to issues such as enhanced preliminary accreditation, biomass sustainability and **cost control**.”<sup>2789</sup>  
(the Inquiry’s emphasis)

## Proposed budget controls for the NI RHI

51.19 As discussed previously in this Report, on 26 June 2013 Ms Hepper sent a submission to the Minister and her SpAd providing details of the proposed consultation document in relation to Phase 2 of the NI RHI scheme.<sup>2790</sup> The submission itself did not highlight the budget control issue, but one of the proposals at paragraphs 4.13 to 4.17 of the consultation document provided details of budget control measures that would be applicable to both non-domestic and domestic RHI schemes with the objective to:

- maintain confidence and consistency in the NI RHI scheme;
- ensure that budgetary levels would not be breached; and
- remove the need for emergency reviews or reductions in tariffs at short notice.

51.20 Although it was noted in the DETI consultation document that DECC was in the process of introducing degression in GB, such a system was in fact already in force, and had been since April 2013. It was stated that DETI expected to introduce similar degression measures in the future but, in the interim, it was proposed that a simpler system was to be put into place.<sup>2791</sup> This was contrary to the reasoning provided by the DETI officials to Ofgem in June 2012 for not introducing DECC’s interim measures from the outset of the NI scheme.<sup>2792</sup>

51.21 The proposed budget control system was to be applied to both the NI domestic and non-domestic RHI schemes based upon the percentage of the annual budget that was committed in any one year and the activation of a series of triggers. For example:

- 50% of the annual budget being committed would trigger a public notification.

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2788 DFE-152866 to DFE-152873

2789 WIT-18703

2790 DFE-97307 to DFE-97359

2791 DFE-97352

2792 OFG-03517

- 60% would trigger a public notification and warning that the domestic RHI scheme might need to close.
- Where 70% of the annual budget was committed, trigger three would require a further public notification and the commencement of procedures to close the domestic RHI for the financial year.
- Trigger four was reached at 80% budget committal at which point DETI was required to make a public notification and warn that the non-domestic RHI would have to close.
- 90% commitment of the annual budget would then trigger closure.<sup>2793</sup>

51.22 The submission of 26 June 2013 also attached a draft letter for the Minister to send to the Chair of the ETI Committee, Mr McGlone.<sup>2794</sup> In that letter, which was sent on 2 July, Minister Foster confirmed that, *inter alia*, the consultation would gather views on introducing the proposed cost (budget) control system.<sup>2795</sup>

51.23 The Inquiry notes that there were no serious objections to the system of interim budget controls raised in consultation responses.

### Loss of budget controls

51.24 Mr Mills told the Inquiry that he assumed that officials had, prior to his taking up post, acquired “some authority” to proceed with prioritisation of the domestic NI RHI scheme without the trigger mechanism for budget controls. He said that there had been a discussion with Mr Hutchinson and Ms McCutcheon in March 2014 when he was told that cost controls were “part of the technical stuff and could be done later”.<sup>2796</sup>

51.25 When asked who he thought was responsible for the fact that the budget control proposal in the 2013 public consultation document did not make its way into implementation in 2014 through the domestic RHI regulations Mr Mills replied “I think responsibility is shared, and I, for myself – I didn’t know enough to have questioned the course of action that was already set.”<sup>2797</sup> He didn’t realise that not including the cost control proposal in the domestic proposals involved not including a cost control that had been proposed, not only for the non-domestic but also for the domestic scheme.<sup>2798</sup>

51.26 On 15 May 2014 Mr Mills advanced a submission to Minister Foster containing a six-monthly update on the RHI schemes for the ETI Committee.<sup>2799</sup> The update from Mr Mills did not specifically refer to the removal of budget controls in the context of the impending launch of the domestic RHI although it did note that the non-domestic scheme could experience a higher volume of applications than GB but for smaller installations.<sup>2800</sup>

51.27 Thus, budget controls, which the 2013 RHI consultation document had indicated to the public were to be applicable to both schemes, were now detached from the domestic RHI scheme and effectively delayed along with the other matters from the 2013 consultation. Mr Mills told

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2793 DFE-97352 to DFE-97353

2794 DFE-97315 to DFE-97318

2795 DFE-97363 to DFE-97365

2796 TRA-07184

2797 TRA-07194

2798 TRA-07195

2799 DFE-230075 to DFE-230080

2800 DFE-230077

the Inquiry that he had not been made aware of the warning from Ofgem in the 26 June 2012 teleconference with regard to the introduction by DECC of interim cost controls or of any subsequent discussion that had taken place between Ms Hepper and Minister Foster. Mr Mills told the Inquiry in oral evidence that, on reflection, when drafting this submission of 15 May, he should have “stood back and given the Minister options.”<sup>2801</sup>

51.28 In a further submission to Minister Foster on 17 June 2014 Mr Mills sought approval of a draft Government response to the domestic scheme element of the 2013 RHI consultation and a draft SL1 to be tabled at the ETI Committee meeting on 3 July for the purpose of seeking subordinate legislation to launch the domestic RHI scheme.<sup>2802</sup> The submission informed the Minister that DECC had launched its domestic scheme and then contained the following statement: “We have decoupled the domestic RHI from other Phase 2 changes in an attempt to speed up its implementation.”<sup>2803</sup>

51.29 The ‘trigger’ scheme of cost control, upon which the public had been consulted, appears to have been designed by Mr Hutchinson, in agreement with Ms McCutcheon, after discussions about budget unpredictability.<sup>2804</sup> The Inquiry was not informed why the GB RHI interim cost control (or SBM), or the subsequent degression provisions were not adopted or even considered. Mr Hutchinson could not recall a conscious decision to decouple the cost controls or being involved in such a decision.<sup>2805</sup> In a written statement to the Inquiry he provided the following explanation:

“Personally speaking, as someone involved in drafting the Synopsis Paper and Domestic Business Case, I may have felt that the cost control elements (and other administrative/technical issues) fell outside the scope of the papers relating to the Domestic Scheme. Those papers were designed to secure the approval of the Domestic Scheme rather than any other administrative issues. I possibly had considered that the cost control elements (and other technical issues) would not be subject to Casework Committee or Business Case approval – rather it would be for Senior Management to agree the final proposals and oversee the necessary legislative amendments.”<sup>2806</sup>

51.30 Mr Hutchinson having left in May 2014, and after Ms McCay had looked after RHI for 6 weeks (including taking the domestic scheme through the casework process on 9 June 2014 along with Mr Mills), Mr Wightman and Mr Hughes arrived at the end of June 2014 and took forward the introduction of the domestic RHI scheme.

51.31 On 16 September 2014 Mr Wightman sent Minister Foster and her SpAd a submission seeking approval of the business case and implementing the domestic NI RHI scheme.<sup>2807</sup> The submission did not draw attention to the absence of the budget control mechanism that had been the subject of public consultation. Neither the Minister, who had read the NI RHI consultation document in July 2013, more than a year earlier, and been a party to the November/December 2013 exchange with Minister Barker, nor her SpAd, appear to have

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2801 TRA-07201 to TRA-07205

2802 DFE-144514 to DFE-144567

2803 DFE-144532

2804 WIT-09308

2805 WIT-09327

2806 WIT-09328

2807 DFE-184099; DFE-193697; DFE-192902 to DFE-192904

questioned its absence. Dr Crawford said in written evidence that he assumed that the controls “would be taken forward” and that “There was no advice from officials regarding this issue, and I had no reason to question their approach.”<sup>2808</sup> Minister Foster told Inquiry Counsel in her oral evidence that “it wasn’t a live issue in my head at that particular time”. She said that she had not received, but that she should have received, the public responses relating to the proposal to introduce the mechanism for budget control, adding “All I can say to you; at that time, the issue of cost control was not at the forefront of officials’ minds, and, because of everything else that was going on in the Department, it wasn’t at the forefront of my mind either.”<sup>2809</sup> When asked about the absence of any reference to cost control in the submission of 16 September 2014 Minister Foster said “It wasn’t brought to me, so I didn’t consider it. Could I have actively considered it myself if I had thought it was an issue? Yes, I could have.”<sup>2810</sup> On 29 September 2014 Minister Foster annotated the 16 September submission adding “get this launched ASAP.”<sup>2811</sup>

## Officials’ knowledge of the loss of budget controls

51.32 The Inquiry heard evidence relating to the ‘decoupling’ process and the ultimate loss of any budget controls.

- (i) The submission from Ms Hepper of 26 November 2013 to Minister Foster providing an update on the NI RHI for the ETI Committee simply pointed out that “Given that the domestic RHI does not require State Aid approval, it is likely that it can be launched earlier than the non-domestic aspects of phase 2 - probably Spring 2014” without any reference to or suggestion that such an early launch might result in the proposed system of budget control being detached from both schemes.<sup>2812</sup> In the course of giving oral evidence to the Inquiry Ms Hepper said that when she left the original team dealing with RHI in November 2013, she did not think that anyone could have doubted that the cost control mechanism would be implemented. She said:

“...regardless of what time frame and in what order the domestic or non-domestic scheme was going to be worked through in 2014, the cost control – the interim measure – would’ve been needed for both of those schemes, because, when you look at the mechanism, one of the first actions that’s taken is to close one of the schemes ahead of the other, so it was going to have to be brought in regardless of how you phased the bringing in of either the domestic or the other non-domestic technologies. So, I don’t think, from that point of view there could’ve been anything else in anybody’s mind other than, ‘This has to be done’.”<sup>2813</sup>

She agreed that, even if the domestic RHI scheme was introduced first, the cost control should have been introduced with the domestic scheme. She was unable to suggest any explanation as to why that fundamental point had been missed by Mr Hutchinson and Ms McCutcheon, who were still in post, and Mr Mills who replaced Ms Hepper in early 2014. She maintained that the cost control mechanism would have to be “nested” into

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2808 WIT-21603

2809 TRA-08382 to TRA-08384

2810 TRA-08330

2811 DFE-184099

2812 DFE-33720 to DFE-33724

2813 TRA-05376 to TRA-05377

a set of regulations and that it was a fairly “simple translation from that into ‘If you’re doing your domestic scheme first’ – and that hadn’t necessarily been decided as I left – that would be the first set of regulations and you would put this clause into that set of regulations.”<sup>2814</sup>

- (ii) Mr Hutchinson was unable to recollect any discussions over the issue beyond that which was quoted above.<sup>2815</sup> The Inquiry found it difficult to comprehend how the necessity for controls applicable to the single budget for both schemes could be reduced to ‘administrative’ or ‘technical’ matters in the context of the specific warnings from DETI Finance Branch in 2011 and Ofgem in 2012, as well as of the mechanisms devised and already adopted in GB and proposed in paragraphs 4.13 – 4.17 of the 2013 NI RHI consultation document.
- (iii) In an interview with PwC, Mr Mills explained that cost control:  
“Wasn’t consciously done away with, it was consciously deferred...It was consciously deferred, that is, or rather all the other elements of phase 2, as it was called, were consciously deferred to get the Domestic Scheme in.”<sup>2816</sup>
- (iv) He said that priority of the domestic RHI scheme had been agreed in and around November 2013, before his arrival in DETI in January 2014, and that, in order for that to be achieved, all the departmental RHI resources had to be devoted to that end.<sup>2817</sup> Mr Mills told the Inquiry he assumed that the Minister had set that priority after discussion but conceded that he did not have any evidence to support that assumption.<sup>2818</sup> As discussed earlier in this report, Mr Mills’ assumption was wrong.
- (v) Mr Thomson, who was the predecessor of Mr Stewart and who was in DETI up to June 2014, said that he had no recollection of a conscious decision to drop cost control, which he would have expected to be the subject of objective recording and communicated both to himself and to the Minister. He believed that the controls should have been brought in and could provide no good reasons as to why that had not been done.<sup>2819</sup>
- (vi) Mr Wightman told PwC that the launch of the domestic scheme had been his objective from day one. The domestic business case was just going through the internal DETI casework process when he arrived and the priority was to get the necessary approvals and get the domestic scheme launched.<sup>2820</sup> In answer to a question as to who would have made the decision to defer cost controls, he said: “I would have thought it would have been John [Mills] as director...in consultation with Chris [Stewart].”<sup>2821</sup> Again, this assumption was wrong; Mr Stewart had not arrived in DETI until August 2014, and the ‘decoupling’ had already occurred before Mr Mills arrived in January 2014.
- (vii) When this was raised with Mr Stewart by PwC, he was able to recall a number of conversations with Mr Mills in which Mr Mills emphasised that introducing the domestic

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2814 TRA-05378

2815 WIT-09328 to WIT-09329

2816 PWC-04427

2817 PWC-04570

2818 TRA-07202 to TRA-07203

2819 TRA-05746 to TRA-05747

2820 PWC-04660

2821 PWC-04664

RHI scheme was a top priority but that he did not remember being a party to any decision to defer cost controls. When asked by PwC at what level such a decision should have been taken, based on his experience, he confirmed that it should have been the subject of senior advice from officials, which was then referred to the Minister.<sup>2822</sup> As discussed earlier in this Report, that did not happen.

- (viii) Mr Sterling told the Inquiry that he was unable to explain why the review of the non-domestic RHI scheme and cost control were deprioritised and maintained that the decision had not been discussed with him.<sup>2823</sup>
- (ix) Dr Crawford, who was Minister Foster’s SpAd and who had the responsibility of protecting the Minister,<sup>2824</sup> was quite unable to say why the Minister was not effectively warned and advised about the disappearance of the cost control mechanism. He told the Inquiry that he was aware that this should have been a decision for the Minister based on a properly constructed submission. He appreciated that the Phase 2 consultation had discussed a single system of cost controls for both schemes and that ‘decoupling’ would leave both without any controls but stated that, at the time, they were marketing and promoting the schemes since uptake levels were low.<sup>2825</sup> Dr Crawford referred to the “volume of paperwork” and the number of projects with which the Department was concerned. He emphasised that RHI was a new area in which he had no expertise and that it was not part of his role to “check officials’ homework”.<sup>2826</sup> He did not expect to be making sure that officials put up in documents to the Minister a true reflection of what had gone before in a consultation document; he was there to give political advice and to advise the Minister on her wide range of portfolios.<sup>2827</sup>
- (x) Ms Hepper told the Inquiry that Dr Crawford read the 2013 CEPA economic analysis for Phase 2 of the RHI scheme.<sup>2828</sup> She also stated that he read the associated consultation document containing details of the proposed cost controls, that he had a meeting with the team about the consultation on 17 July 2013 and that “he could link it back to the issue in June 2012.”<sup>2829</sup> Dr Crawford was adamant that he had never been aware of the June 2012 Ofgem warning.<sup>2830</sup> There is no doubt that he read the consultation document, given he had a discussion with officials about an unrelated issue contained in it in July 2013, but, having done so, he does not appear to have expressed any curiosity in June 2014 as to what ultimately became of the proposed cost controls, nor does he seem to have drawn their disappearance to the attention of Minister Foster.
- (xi) Minister Foster told the Inquiry she had not been given an opportunity to consider in detail the decision to ‘decouple’ cost control. She said that was a matter that should have come to her in a submission for her to decide.<sup>2831</sup> She was aware that DECC had a system of cost control in place, but she had no reason to think that cost control was a

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2822 PWC-04481 to PWC-04484

2823 TRA-06814 to TRA-06815

2824 TRA-09905 to TRA-09911; TRA-07933 to TRA-07934; TRA-07615; TRA-07513 to TRA-07514

2825 TRA-09821 to TRA-09833

2826 TRA-09908 to TRA-09911

2827 TRA-09909

2828 TRA-05370

2829 TRA-05384

2830 TRA-08042 to TRA-08045

2831 TRA-08370 to TRA-08371

significant issue. She told the Inquiry that she had read the 2013 consultation document and understood that the proposal to introduce cost controls was to prevent the budget being exceeded.<sup>2832</sup> Minister Foster said that the submission of 17 June 2014 seemed to her to emphasise that it was a matter of priority to launch the domestic scheme, which had been the subject of consultation some time ago, and that cost control was “downplayed”. She said that there was no indication of overspend at that stage and that she had been on a trade mission to the United States at the time of that submission.<sup>2833</sup>

51.33 As discussed earlier in this Report, when the October 2015 Casework Committee met to consider the proposals to introduce tiering and the annual cap in the context of the emergency over RHI, Michelle Scott, the DFP DETI Supply Officer, enquired why the trigger points mechanism referred to in the 2013 public consultation had not been implemented. The minutes record that Mr Mills said that it was a:

“Ministerial decision to look at the domestic scheme rather than pushing through the trigger points on non-domestic which would have significantly delayed the implementation of the domestic scheme.”<sup>2834</sup>

51.34 In his oral evidence to the Inquiry Mr Mills said that this statement of fact had been completely incorrect, and he simply held a belief that the matter had been authorised by a ministerial decision at that time. He accepted that had been an assumption upon his part and that, having considered the relevant documentation, he was now of the view that the assumption was incorrect and that the decision to move ahead with the domestic scheme was more about practicality than the importance of the decision, given the time likely to be required.<sup>2835</sup>

51.35 At this same October 2015 meeting, the minutes record that Mr Wightman confirmed to the Casework Committee that there had been insufficient resources to introduce both the domestic scheme and cost controls and, when asked by Ms Scott what had triggered the cost control measures in GB in 2012, he was unable to answer, leading to an action point being recorded in the minutes: “Energy to identify the trigger of cost controls in England in 2012”.<sup>2836</sup> The Inquiry is compelled to conclude that the DETI representatives at this meeting in October 2015 were unaware of all the detailed information published on the DECC website and set out in Minister Barker’s correspondence with Minister Foster with regard to the need for and the implementation of cost controls.<sup>2837</sup>

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2832 TRA-08321

2833 TRA-08372 to TRA-08374

2834 DOF-04502

2835 TRA-07202 to TRA-07204

2836 DOF-04502

2837 DFE-293680 to DFE-293684

## Findings

292. It is difficult to understand how the DETI officials working with CEPA in 2011 and 2012 were able to reconcile their belief that the consultants' model offered a form of budget control with the clear warnings given to them by the same consultants as to the need to monitor the variables and assumptions upon which the models had been constructed. The Inquiry notes that the RHI risk register certainly incorporated the risk of breaching the budget despite the consultants' modelling.
293. Despite the warning from Ofgem in June 2012, none of the successive budget control amendments to the GB RHI regulations were adopted in Northern Ireland, so the NI RHI scheme operated without the type of protective mechanisms GB had put in place to keep control of its budget.<sup>2838</sup>
294. A grant-based scheme would have included an inherent and immediate mechanism to suspend spending, namely the power to stop making grants. No such equivalent mechanism to suspend payments to individuals was part of the incentive-based NI RHI scheme. Thus the need to have budget control mechanisms designed and implemented at the scheme level was all the more pressing.
295. The proposal, contained in the July 2013 RHI Phase 2 consultation, to introduce a budget control system that would apply to both schemes, and thus protect the total NI RHI budget, was not implemented through the regulations introducing the domestic NI RHI scheme in late 2014, or the amending regulations relating to the non-domestic NI RHI scheme in late 2015. Given the available and detailed information from DECC, from 2012 and early 2013, as to why it had introduced budget control mechanisms to the GB RHI scheme in spite of the fact spending on its scheme was nowhere near its annual limits, any decision or course of action by officials in DETI, which had the effect of not proceeding with the introduction of a budget control for the NI RHI scheme, should have been escalated to DETI senior management for decision with specific reasons given for, and adequate consideration of any risks arising from, the course being proposed. Escalation did not occur in this case, either in late 2013, at the time when the decoupling of the domestic scheme (from the rest of the proposed Phase 2 changes) commenced, or later, when the domestic scheme was introduced. The budget control was instead 'lost' through inadvertence. This was a serious omission, given that it left the NI RHI scheme without any form of budget protection.
296. In particular, when the approach of decoupling the introduction of the domestic RHI scheme (from the rest of the Phase 2 proposals) commenced in late 2013, no consideration, or no adequate consideration, appears to have been given to the effect of not treating the introduction of the 'trigger' mechanism of budget control, applying (as it would) to both schemes, as something to be introduced through the first set of regulations to be brought forward (those relating to the domestic scheme).

**297. The Minister was not given any, or any adequate, information about the decoupling decision, insofar as it treated the introduction of the budget control mechanism as part of the Phase 2 amendments to the non-domestic scheme, which were to be progressed after the introduction of the domestic scheme. Further, the Minister was not given any, or any adequate, information about the effect that the decoupling decision would have on the issue of budget control, leaving (as it did) both schemes without any form of budget protection. Having consulted on a budget control mechanism in 2013, and in light of the earlier steps taken by DECC on the subject of budget control in 2012 and 2013, DETI officials should have briefed the Minister in detail about what had occurred in GB in respect of RHI budget control, and why it had occurred (particularly as to the protections being introduced when there was no risk to the GB RHI budget, for the reasons that were given), and it should have been for the Minister to determine whether the NI RHI schemes were to proceed without any budget protection in those circumstances. The continued absence of any form of budget control should have been the subject of a fully informed, properly reasoned and clearly minuted decision at ministerial level.**

## Chapter 52 – Minuting of meetings with the Minister: DETI’s policy and the practice

52.1 A significant issue that hampered the work of the Inquiry to some degree was the absence of minutes or records of meetings at which important decisions relating to the NI RHI scheme were taken, or said to have been taken. In this chapter the Inquiry looks at the applicable guidance in this regard and what actually happened in practice.

### Ministerial Code

52.2 The Northern Ireland (St Andrews Agreement) Act 2006 required the preparation of a Ministerial Code for Ministers of the Northern Ireland Executive. Section 28A of the Northern Ireland Act 1998, inserted by the 2006 Act, provided that a Minister or junior Minister of the Northern Ireland Executive shall act in accordance with the Ministerial Code.

52.3 The Inquiry notes that the Ministerial Code contains a Ministerial Code of Conduct. That Code of Conduct incorporates, and requires compliance with, “the seven principles of public life”.

52.4 The seven principles of public life had been restated by the Committee on Standards in Public Life in its first report published in May 1995. They are often also referred to as the “Nolan Principles”, so named after the chair of that committee, Lord Nolan.<sup>2839</sup> The seven principles are: selflessness, integrity, objectivity, accountability, openness, honesty and leadership.

52.5 As noted above, two of those principles are “accountability” and “openness”. In respect of “accountability”, holders of office are accountable for their decisions and actions to the public and must submit themselves to whatever scrutiny is appropriate to their office. In respect of “openness”, holders of public office should be as open as possible about all the decisions and actions they take. They should give reasons for their decisions and restrict information only when the wider public interest clearly demands.

52.6 Further, paragraph 1.5(ii) of the Ministerial Code of Conduct for Ministers of the Northern Ireland Executive requires Ministers “to be accountable to users of services, including the community and, through the Assembly, for the activities within their responsibilities, their stewardship of public funds and the extent to which key performance targets and objectives have been met.”

52.7 Paragraph 1.5(iii) of the same document requires Ministers “to ensure that all reasonable requests for information from the Assembly, users of services and individual citizens are complied with; and that Departments and their staff conduct their dealings with the public in an open and responsible way.”<sup>2840</sup>

### DETI Private Office Guidance

52.8 DETI also had applicable ‘Private Office Guidance’, which appears to have been produced in 2008,<sup>2841</sup> covering matters such as the handling of ministerial correspondence, ministerial submissions, meetings, visits and engagements, and other similar matters.

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2839 DOF-00006 to DOF-00007 and Nolan Committee, Standards in Public Life, Cm 2850-1, May 1995

2840 DOF-00006

2841 TRA-07799

52.9 The Private Office Guidance for DETI provided, in paragraph 15, that the Permanent Secretary must be consulted on policy proposals which had major resource implications,<sup>2842</sup> and the Guidance contained the following provisions with regard to notes of ministerial meetings:

**“Notes of Ministerial Meetings**

37. Meeting notes are intended to record accurately any decisions taken or undertakings made by the Minister. They may also, if necessary summarise the main facts and arguments used during the meeting. They will not however record, blow by blow, each turn of a discussion.

**38. The Permanent Secretary has directed that for all internal and external meetings involving officials it will be the responsibility of the agency, branch, division etc to record a relevant note of the discussion, decisions taken and action agreed. The author should ensure that he/she has issued the minutes to any relevant official – including PS/Minister** [emphasis from original document]. This will allow the Private Secretary to concentrate on following up on the Minister’s action points. At the same time the minutes will properly record the discussions on complex issues as officials will have the advantage of a closer knowledge of topics. Please provide details of note taker in briefing, as requested.

39. Officials are normally responsible for any follow-up action detailed in the meeting notes.”<sup>2843</sup>

## What happened in practice?

52.10 Dr Crawford told the Inquiry in his oral evidence that he believed that there was always a record of meetings with a Minister and that he was unaware that there was non-compliance with the Private Office Guidance. He said that he was aware of the existence of the Private Office Guidance document, but he had never had to refer to it.<sup>2844</sup> Ms Foster said that she was not aware of the Guidance at the time and had no recollection of reading it,<sup>2845</sup> but she also told the Inquiry that she expected notes to be made of significant meetings.<sup>2846</sup> Neither the Minister nor Dr Crawford could remember being furnished with a minute or record of a meeting with the Minister in accordance with the requirements of the Private Office Guidance.<sup>2847</sup>

52.11 The Inquiry notes that the Private Office Guidance stated that notes of meetings with the Minister, as taken by officials, should be copied to the Minister’s Private Secretary. The Inquiry received evidence from those who served in Minister Foster’s Private Office such as Glynis Aiken (who served as the DETI Minister’s Private Secretary from June 2008 to May 2015)<sup>2848</sup> that they never queried the absence of notes of ministerial meetings, nor did they chase notes that did not materialise.<sup>2849</sup>

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2842 DFE-416559 to DFE-416571 at DFE-416562

2843 DFE-416559 to DFE-416571

2844 TRA-07507 to TRA-07520

2845 TRA-07799 to TRA-07802

2846 TRA-07794 to TRA-07795

2847 TRA-07798; TRA-07511 to TRA-07512

2848 WIT-13437

2849 In respect of Ms Aiken’s evidence to this effect, see WIT-13481

- 52.12 The Inquiry’s concerns about the apparent divergence between what was intended to be departmental practice and what actually happened in reality were such that they were raised by the Inquiry during the oral evidence of Mr Sterling, the Permanent Secretary of DETI between 2009 and June 2014. Mr Sterling accepted that the meeting of Ms Hepper with the Minister of 14 June 2011, referred to in detail elsewhere in this Report, should have been minuted;<sup>2850</sup> and that the conversation or telephone call said by Ms Hepper to have taken place regarding Ofgem’s warnings about the GB proposal for interim cost control in June 2012 should have been both the subject of a formal submission and minuted.<sup>2851</sup>
- 52.13 Ms Hepper told the Inquiry that the practice of officials minuting meetings had fallen into disuse, but a minute or record should have been taken.<sup>2852</sup>
- 52.14 With regard to the general practice in operation at the material time, Mr Sterling explained to the Inquiry that there was a general understanding that anybody who had reached the Senior Civil Service (grade 5 and above) would know that Ministers needed to get advice that was comprehensive, thorough and complete.<sup>2853</sup> He went on to say:
- “Now, on occasions, there would be discussions between Minister and officials that may not be minuted, but I think my view would always be that the ultimate decision needs to be reflected in a submission so there’s a clear record of what considerations the Minister took and what the final decision was and why it was taken.”<sup>2854</sup>
- 52.15 Mr Sterling said that what he had described to the Inquiry would be the sort of thing that he would expect any Senior Civil Servant to know.<sup>2855</sup> However, he also explained that an unwritten custom and practice had developed over recent years.<sup>2856</sup> He explained that the minuting of meetings with Ministers was no different in Northern Ireland than anywhere else but went on to point out:
- “... but Ministers like to have space, safe space, where they can consider difficult things, think the unthinkable and not necessarily have it all recorded. A feature of the devolved Administration here has been that the two main parties have been sensitive to criticism, and I think that it’s in that context that, as a Senior Civil Service, we got into the habit of not recording all meetings on the basis that it is safer sometimes not to have a record that, for example, might be released under freedom of information which shows that things that might have been considered unpopular were being considered.”<sup>2857</sup>
- 52.16 When Inquiry Senior Counsel referred Mr Sterling to the relevant provisions of the DETI Private Office Guidance, he explained that, during the long period of direct rule in Northern Ireland, there would have been pretty firm adherence to the Guidance. In those days (i.e. during the time of direct rule) the number of meetings that a civil servant would have had with a Minister would have been relatively small and Private Secretaries would have taken notes. If

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2850 TRA-06115 to TRA-06118

2851 TRA-06111 to TRA-06112

2852 TRA-05200 to TRA-05204

2853 TRA-06112

2854 TRA-06112

2855 TRA-06113

2856 TRA-06121 to TRA-06122

2857 TRA-06114

the meeting had involved somebody from outside, custom and practice would have been that it would have been a member of staff in the relevant branch who would have taken the note.

- 52.17 Mr Sterling said that the pace of day-to-day life had increased exponentially since 2008 and that meetings with devolved Ministers would have taken place quite often when the civil servant might have been called up at short notice for a “quick word” or the civil servant might have asked the Private Secretary for a “quick word” with the Minister. However, he fully accepted that a key decision on policy should always have been reflected in a submission at some stage, sufficient to provide a clear record of why the decision was taken.<sup>2858</sup> When questioned further about his reference to the Freedom of Information Act, and asked whether there was a conscious decision to reduce minuting and “dumb down” the routine practice, Mr Sterling said:

“The absence of routine minuting of all meetings with Minister, that wasn’t a conscious dumbing-down at all. I think it’s largely a reflection of just the changed circumstances in which we were working. So, for example, again I drew a distinction with, or the contrast with, working in direct rule, where you wouldn’t have seen your Minister very often. Now, you were in much more regular daily contact with Minister and adviser, and I would’ve encouraged openness between Minister, adviser and officials....My view was that you get more efficient policy development if policy teams are talking to the special adviser and, indeed, the Minister, at a very early stage in the policy development process. You know, there’s no greater waste of time than a policy team going away, dreaming up some great policy idea, sending in a 20-page submission, and the Minister says, “This is nonsense. I can’t run with this.” So, we did have a much more fluid involvement and engagement between Minister and adviser, and I think that’s a good thing. But I think one of the consequences of that is it becomes more difficult to apply the rigid disciplines of minuting every meeting.”<sup>2859</sup>

- 52.18 The Inquiry pointed out that with an unwritten custom and practice it might become very difficult for an individual to decide where the boundary might lie as to when a minute should be recorded and when not. Mr Sterling was careful to point out that in respect of other major decisions taken during his period in the Department there would have been a clear audit trail setting out the relevant considerations, the factors at issue, the ministerial decision and the reasons for it.<sup>2860</sup>

- 52.19 Mr Sterling emphasised that it was important not to draw conclusions as to the general practice from this particular scheme.<sup>2861</sup> He informed the Inquiry that fresh guidance had been produced which would be implemented when the Northern Ireland Executive returned.<sup>2862</sup> The Inquiry welcomes the information that fresh guidance has been prepared and is ready to be implemented. However, with regard to Mr Sterling’s assurance that such practices did not extend outside the RHI scheme, the Inquiry bears in mind his paper of November 2012 for the Senior Management Team with regard to the PAC Report on the flawed Bioscience and Technology Institute project (considered further in chapter 55). Mr Sterling specifically recorded what was said to be a ‘culture’ existing some ten to twelve years prior to 2012, which

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2858 TRA-06121 to TRA-06122

2859 TRA-06123 to TRA-06124

2860 TRA-06125

2861 TRA-06124 to TRA-06125

2862 TRA-06113

enabled procedures to be circumvented, including not recording important decisions and failure to adequately monitor the project, which led to substantial loss to the public purse. He went on to say that, speaking in November 2012, he was content that: “the culture within DETI is totally different to that which appears to have operated ten to twelve years ago.”<sup>2863</sup>

## Findings

- 298.** The Inquiry would not wish to diminish the importance of establishing and maintaining positive personal relationships within the Northern Ireland Civil Service and, particularly, between civil servants and Ministers. The ability to seek informal guidance at relatively short notice from a Minister and/or senior officials is an important feature of how a Department works. There can be little doubt but that such approaches became more frequent after devolution, when visiting GB Ministers were replaced by more accessible Northern Ireland counterparts. However, such activity has the potential to become over-familiar. For example, the meeting of 14 June 2011, as well as the conversation relating to the Ofgem warning with regard to cost controls in June 2012, undoubtedly required to be the subject of formal procedure and minuting, since they were the basis of important ministerial decisions.
- 299.** Applicable departmental Private Office Guidance about the minuting of meetings was not followed. In the absence of having been withdrawn or amended, it should have been followed.

## Chapter 53 – The handling of important RHI related ministerial correspondence

53.1 During 2013 a series of letters passed between the Rt Hon Gregory Barker MP, then Minister of State at DECC, and Minister Foster. How that correspondence was handled was important in relation to the development of the NI RHI, particularly in the context (discussed previously in this Report) where the resources available to DETI in terms of staff and expertise which could be deployed in relation to the development of the NI RHI were very considerably less than those available to its sister Department in Westminster.

### The DETI process for handling correspondence

53.2 DETI's Private Office Guidance,<sup>2864</sup> discussed in the previous chapter, provided at paragraph 1 that: "Private Office will decide whether a letter addressed to the Minister should receive a Ministerial reply, and if so which division should prepare the advice, or whether it can be answered by the Minister's Private Secretary, or an official."<sup>2865</sup>

53.3 There was also a process in place in DETI Private Office for handling and tracking ministerial correspondence.<sup>2866</sup> Where correspondence required an action, it was logged on the 'Knowledge Network' (a digital information management system used in ministerial private offices) on receipt in Private Office. Where correspondence was clearly for information only it was not registered on the Knowledge Network system. Each piece of correspondence was different and needed to be considered on its own merits but there were essentially three courses of action which Private Office could take:

- If the nature of the correspondence indicated that an action was required, for example a response from the Minister, it was issued to the relevant divisional officials for advice, decision and draft reply.
- If the correspondence was considered to be for information only, it was passed to the Minister for information as part of an information folder.
- If the correspondence was of relevance to a particular business area, it was copied to the relevant business area for information. In such cases the Minister subsequently advised Private Office officials as to whether the correspondence had been noted or whether it should be subject to any further action.<sup>2867</sup>

53.4 The outcome of this process ought to have been that the Minister at some point had an opportunity to see the correspondence which had been addressed to her.

53.5 It seems that a practice developed in accordance with which correspondence, deemed as not requiring a response, was printed by Private Office and put in a folder along with any other correspondence and provided to the Minister for information only. This folder was passed to the Minister for information, usually on a weekly basis. Once returned, Private Office staff checked the folder to see if the Minister had made any comments or had requested further briefing.<sup>2868</sup>

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2864 DFE-416559 to DFE-416571

2865 DFE-416560

2866 DFE-423437

2867 DFE-423437

2868 DFE-423437

- 53.6 Ms Aiken, who as previously noted was Minister Foster’s Private Secretary during her service as DETI Minister, added in a written statement to the Inquiry, that in her time, correspondence for ‘information only’ should have been set up on the Knowledge Network as ‘general mail’.<sup>2869</sup> In her experience the Minister would only have made notes on the correspondence on very rare occasions.<sup>2870</sup> She explained that when Minister Foster took office in DETI she asked to see a hard copy of all correspondence received in Private Office.<sup>2871</sup> That would then be saved onto the Knowledge Network system and placed in a folder to be passed to the Minister once or twice a week.<sup>2872</sup>
- 53.7 Ms Aiken explained that Whitehall Ministers would frequently write to Ministers in the devolved administrations updating them with regard to relevant policy areas.<sup>2873</sup> It was generally accepted that such correspondence did not require a response and it was not the practice in DETI to routinely acknowledge receipt of that type of correspondence.<sup>2874</sup>

### The March 2013 Barker letter

- 53.8 On 26 March 2013, by which time DECC already had its interim budget control or stand-by mechanism in place on the GB RHI scheme and was about to replace it with its degression mechanism, DECC Minister Barker wrote to Minister Foster indicating that it was DECC’s intention to extend the current Renewable Heat Premium Payment (RHPP) scheme (the forerunner of the domestic RHI) for a further financial year while the Government continued to make progress towards finalising all details of the domestic RHI scheme.<sup>2875</sup>
- 53.9 That letter was the subject of a submission to the Minister and her SpAd by Ms McCutcheon, recommending a draft reply confirming that DETI was carrying out analysis work with a view to designing a domestic RHI scheme specific to Northern Ireland and expanding the non-domestic RHI scheme to include more innovative technologies.<sup>2876</sup> The final paragraph of the draft DETI acknowledgement letter read as follows:

“Whilst the Northern Ireland and Great Britain RHI Schemes are separate, I think it would be of great benefit if our respective Officials kept in close contact over the next few months as our respective development work continues.”<sup>2877</sup>

### The May 2013 Barker letter

- 53.10 As mentioned in earlier chapters of this Report, on 31 May 2013 Minister Barker wrote<sup>2878</sup> to Minister Foster again, informing her of “significant developments” on the non-domestic GB RHI scheme. The letter was three pages in length. It related to a review of tariffs on the GB RHI scheme, a consultation on the new tariffs following the review, and information on the first degression announcement (the degression mechanism having replaced the interim cost control or stand-by mechanism on the GB RHI scheme in April 2013). The letter appears to

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2869 WIT-13476  
2870 WIT-13478  
2871 WIT-13480  
2872 WIT-13480  
2873 WIT-13480  
2874 WIT-13480  
2875 DFE-33445  
2876 DFE-33446 to DFE-33450  
2877 DFE-33448  
2878 DFE-53262 to DFE-53264

have been accompanied by a DECC RHI press announcement and a longer briefing document for information.

- 53.11 The letter was sent by DETI Private Office to Ms Hepper to consider and advise if a response was required.<sup>2879</sup> Ms Hepper sent it on to Ms McCutcheon to deal with. Ms McCutcheon then provided advice to the Minister on 3 June 2013.
- 53.12 The contents of this letter from Minister Barker would not necessarily have been news to Ms McCutcheon. On 21 May 2013 Mr Hutchinson, who worked to Ms McCutcheon in Renewable Heat Branch, had received an email from an official in DECC informing him of the forthcoming announcements of the DECC consultation following the tariff review, and of the triggering of a degression of the GB RHI medium biomass tariff. The DECC official provided the tariff review consultation document in draft form.<sup>2880</sup> It covered subjects such as exploitation of banding, overcompensation and cost control,<sup>2881</sup> with detailed annexes on the tariff model.
- 53.13 On 24 May 2013 Mr Hutchinson replied<sup>2882</sup> to the DECC official, copying in Ms McCutcheon. Amongst other things, he explained the ongoing work on the NI RHI scheme. Cost control did not feature among the long list of matters mentioned.
- 53.14 The DECC official responded twice on 29 May 2013<sup>2883</sup> to Ms McCutcheon and Mr Hutchinson and, in the second email, included DECC's weekly RHI update, which also had references to the tariff review and the degression of the medium biomass tariff.
- 53.15 Returning to the 31 May 2013 letter from Minister Barker, it now formally confirmed for DETI that DECC had conducted a tariff review as part of DECC's RHI budget management policy. The letter explained that the review had indicated that there was a case for updating tariff input assumptions and that a short consultation was to be launched. The Minister explained that:
- “In reviewing these tariffs we have taken a different approach than that taken to date in setting non-domestic tariffs: ***rather than relying primarily on modelled outputs to identify the required tariffs we have also drawn on market intelligence, stakeholder views and expert opinion to make judgements about the level of tariff to propose.***”<sup>2884</sup> (the Inquiry's emphasis)
- 53.16 The letter went on to confirm the publication of the first degression announcement as part of the GB RHI scheme's budget management mechanism. Minister Barker stated in the letter that DECC had published figures showing that deployment of small and medium sized biomass installations in the course of the non-domestic RHI scheme had proved a real success, beyond DECC's initial expectations. The forecast expenditure on the medium tariff band was such that a 5% degression of that tariff was now going to occur.<sup>2885</sup>
- 53.17 Having been asked to consider the appropriate response, on 3 June 2013 Ms McCutcheon informed DETI Private Office that she did not think that a response to the DECC Minister was required.<sup>2886</sup> Her email contained the following:

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2879 WIT-02450 to WIT-02451

2880 DFE-53210 to DFE-53252

2881 DFE-53230 to DFE-53231

2882 DFE-53253

2883 DFE-53256; DFE-53259 to DFE-53261

2884 DFE-53263

2885 WIT-02446 to WIT-02448

2886 WIT-02449 to WIT-02450

“The Minister previously received similar correspondence from Mr Barker and responded on the 16th of April 2013 thanking him and indicating that she looked forward to hearing more of the GB proposals. The current letter provides an update and the only response to this letter would be to thank him again. We continue to liaise with DECC at official level and there will most likely be further updates from them in the months to come.”

- 53.18 The Inquiry is satisfied that this was neither an accurate nor a sufficiently comprehensive description of the letter of 31 May in the circumstances. Degression had been introduced in GB by amending regulations implemented in April 2013, less than eighteen months after the passage of the 2011 GB RHI regulations bringing into force the GB non-domestic RHI, and now, less than two months later, the first degression reduction was to take place as part of the scheme’s budget management. It was important that the DETI Minister should have been made aware of this development given DETI’s decision in June 2012 not to copy DECC’s interim budget controls from the outset of the NI RHI scheme. In her oral evidence the Minister confirmed that she did not remember seeing the Barker letter of 31 May 2013.<sup>2887</sup> Private Office staff have confirmed that there is no record of comments or requests being raised by the Minister in relation to this specific piece of correspondence.<sup>2888</sup>
- 53.19 When, on 26 June 2013, Ms Hepper advanced a submission to Minister Foster with regard to the intended consultation on the proposal to introduce the domestic RHI and expand the non-domestic scheme as part of Phase 2, no mention was made of the issues raised by the Barker letter of 31 May 2013 or the other material discussed above.<sup>2889</sup> That submission did not specifically refer to the cost control mechanism proposed to apply to both the domestic and non-domestic NI RHI schemes as described in the consultation paper, and did not provide any detail as to why DETI was going to introduce its proposed form of cost control in contrast to what DECC had done.<sup>2890</sup> The draft letter to the Chair of the ETI Committee which was annexed to the 26 June submission for signature by Minister Foster, did refer to “minor administrative amendments” to the non-domestic NI RHI scheme which included “introducing a cost control mechanism.” No further information was provided.<sup>2891</sup>

## The October and November 2013 Barker letters

- 53.20 On 23 October 2013 Minister Barker wrote again to Minister Foster informing her that DECC was laying regulations to rectify two errors that had been identified within the GB non-domestic RHI regulations and to introduce an additional clause to protect applicants to the scheme from potential tariff degression due to an error.<sup>2892</sup> The Minister told the Inquiry that she “did not read that letter in detail” before passing it to officials.<sup>2893</sup>
- 53.21 More significantly, Minister Barker wrote yet again on 29 November 2013, setting out the details of three consultations directed towards extending and improving the GB non-domestic RHI scheme and ensuring that the scheme offered value for money to the taxpayer. This was

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2887 TRA-07899

2888 DFE-423437

2889 DFE-97366 to DFE-97371

2890 DFE-382732 to DFE-382743

2891 DFE-382743

2892 DFE-54350

2893 TRA-08487

a detailed five-page letter, with two annexes. It summarised the outcome of the tariff review consultation he had written about in May, and the further development and refinement of the budget management policy in relation to the non-domestic scheme to ensure that the scheme remained financially sustainable. It also confirmed that the domestic RHI budget would also be managed by degression.<sup>2894</sup>

- 53.22 On 4 December DECC Minister Barker published a detailed statement<sup>2895</sup> announcing the changes to be made as a result of considering a large number of policy questions on the GB RHI. The accompanying 94-page policy document ‘Improving Support, Increasing Uptake’<sup>2896</sup> included a chapter on budget management and the re-calibration of its degression mechanism. A document dealing with the proposed GB domestic scheme was also published, the major portion of which was concerned with budget management.<sup>2897</sup>
- 53.23 On 10 December 2013 Ms McCutcheon lodged a submission with the Minister with a proposed draft response to the letter of 29 November for the consideration of Minister Foster.<sup>2898</sup> That submission made no mention of budget management or cost control although the draft letter in reply to Minister Barker did refer to cost control in its heading, but no further detail on that subject was included.
- 53.24 The Inquiry does not consider that the submission of 10 December 2013 was adequate given the potential significance of the information provided by DECC, nor was it a response that would have helped to focus the Minister’s attention on the development and significance of a cost control mechanism.
- 53.25 Following this submission from Ms McCutcheon, Minister Foster replied to the 29 November Barker letter on 16 December 2013<sup>2899</sup> using the suggested draft and expressing her appreciation of the shared information. Minister Foster indicated in her letter that there had been an encouraging level of uptake with a number of applications for the non-domestic NI RHI scheme being around 7% of the GB applications during the first year of operation. She confirmed that DETI had recently consulted on a similar proposal to expand the NI non-domestic RHI scheme and to introduce new tariffs for more innovative technologies. She continued:
- “In addition, consideration has been given to issues such as enhanced preliminary accreditation, biomass sustainability and cost control.”<sup>2900</sup>
- 53.26 The letter also sought clarity on the RHI funding arrangement, given that Minister Barker’s letter of 29 November had referred to the DECC RHI budget for 2015-16. That request would elicit a subsequent reply from Minister Barker on 7 January 2014.

### The use made of such correspondence from DECC

- 53.27 The enquiry made in Minister Foster’s letter of 16 December 2013 about the DECC RHI budget for 2015-16, referred to immediately above, is one of the very limited instances of DETI picking up on information which had been provided to it in a letter from the DECC Minister and making

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2894 WIT-18705 to WIT-18709

2895 INQ-40893 to INQ-40895

2896 INQ-24901 to INQ-24997

2897 INQ-24886 to INQ-24900

2898 DFE-33748 to DFE-33750

2899 WIT-02469 to WIT-02470

2900 WIT-02469

further enquiries of DECC in order to assist it (DETI) in the exercise of its own functions in relation to RHI.

- 53.28 Quite apart from the DETI Private Office process for handling correspondence and the information and correspondence files, Minister Foster assured the Inquiry that it was always her habit to respond to a letter from a fellow Minister in Westminster by way of a courtesy acknowledgement, even if no detailed response was required. That does not appear to have occurred in respect of all of the Barker correspondence and it may be that some of the letters did not even reach the Minister. Minister Foster accepted that some of the letters sent to her by Minister Barker were quite significant and, whilst advice that she received from officials was that there was no need to respond, she considered that a formal reply should have been sent even just to acknowledge the fact that the information had been sent to her.<sup>2901</sup>
- 53.29 Whilst the Inquiry certainly appreciates the propriety of responding to such letters as a matter of courtesy, the Inquiry considers that it is more important to have a proper system in place to ensure that important information contained within letters from other Departments (such as those from DECC which may have assisted DETI in the exercise of its functions, or caused it to make some further enquiries) is both appreciated and acted upon appropriately.
- 53.30 Whilst acknowledging the evidence received by the Inquiry about the processes in place for dealing with correspondence to a Minister, (as mentioned earlier in this chapter) the totality of the evidence considered by the Inquiry was not such as to permit the Inquiry to gain a clear picture of precisely how such ministerial correspondence was dealt with generally or in every particular case relating to the RHI scheme. Indeed, it appears that there may not have been an entirely consistent approach to classification and management of such correspondence. This might well have been because of the judgment required in each case – which might not have been straightforward, depending on the subject matter – as to whether the correspondence was ‘for information only’ or not; and, even if it was for information only and did not require a letter in response, whether the information provided was of such significance that it required some further action to be taken within DETI.

## Findings

- 300.** The Inquiry notes that in some instances the Minister was provided with summaries of correspondence relevant to the NI RHI scheme that were neither accurate nor sufficiently comprehensive descriptions of the content of that correspondence.
- 301.** The Inquiry finds that officials did not always provide the Minister with good quality advice to form the basis of an adequate draft response to correspondence which the Minister signed. In particular, there was a failure to provide either an adequate summary or an appropriate draft response to the Minister Barker letter of 31 May 2013 and, to a somewhat lesser extent, his letter of 29 November 2013.
- 302.** Despite the Minister's evidence that it was always her intent to respond to a letter from a fellow Minister in Westminster by way of a courtesy acknowledgement even if no detailed response was required, this does not appear to have occurred in respect of all correspondence from Minister Barker.
- 303.** There can be little doubt that the repeated references to degression in the correspondence from DECC should have alerted the Minister and her SpAd, and more particularly the relevant officials, to the need for careful consideration of cost controls in Northern Ireland, bearing in mind the similarities of the GB and NI RHI schemes. The Inquiry considers that the collective failure to identify the significance of this issue was unacceptable in the circumstances.
- 304.** The departmental procedures that were in place for dealing with correspondence in relation to the RHI scheme do not appear to have been adequate and DETI do not appear to have adhered consistently to those which were in place. This was particularly unfortunate given the additional resource and expertise which was available to DECC, as compared with DETI, and the DETI Minister's laudable avowed intent that the Departments should work closely together.



## Chapter 54 – The role of the Special Adviser

54.1 Special Advisers ('SpAds') and the role played by them at significant points in the life of the NI RHI scheme have already featured in several parts of this Report. In this chapter the Inquiry examines the structures governing both the role of the SpAd, and their relationship with an appointing Minister, and then looks at some specific examples of SpAds' activity which came to the attention of the Inquiry in the course of its work.

### The legal and employment framework

54.2 It appears that there are generally three types of SpAd: expert, political and both (expert and political) combined. In the Northern Ireland devolved administration, it seems that the most common type of SpAd appointment has been a political one, although such SpAds can of course, over time, develop some expertise in the work of the Department to which they have been appointed.

54.3 All three types of SpAd are paid from public funds and have the employment status of temporary civil servants. In spite of the fact they are paid from public funds, they are permissibly distinct from mainstream civil servants by the way they are appointed and by their exemption from, for example, the normal duty of civil servants to give impartial advice.

54.4 The convention in Northern Ireland's devolved administration has been for there to be one Special Adviser per Minister, except for the Office of First and deputy First Minister (now known as The Executive Office) where the First Minister and deputy First Minister each had four SpAds.

54.5 The legal and employment framework governing the role of SpAds in Northern Ireland is grounded in a number of different sources. As with all civil servants, SpAds are subject to the provisions of legislation such as the Official Secrets Act 1989, the Civil Service Commissioners (Northern Ireland) Order 1999 and the Civil Service (Northern Ireland) Order 1999. They are also bound by their contract of employment. Their contract of employment incorporates various codes, such as the NICS HR Policy, which itself contains the NICS Standards of Conduct and the NICS Code of Ethics.

54.6 For instance, and as mentioned earlier in this Report, where a conflict of interest arises, SpAds, as with other civil servants, must declare an interest to their Establishment/Personnel Division in accordance with the terms of paragraph 2.1g of the Standards of Conduct section of the NICS HR Policy. This declaration is required "so that a decision can be made as to the best way to proceed". The extent to which this requirement was observed in relation to matters relevant to the RHI scheme is addressed later in the chapter.

### The 2013 Act

54.7 In addition, there is also specific legislation relating to Special Advisers in Northern Ireland, namely the Civil Service (Special Advisers) Act (Northern Ireland) 2013 ('the 2013 Act').<sup>2902</sup> The 2013 Act specifically addressed, amongst other things, the code of conduct for Special Advisers, albeit there was such a code in existence before the coming into force of the Act. A code of conduct for Special Advisers had been issued by DFP (now DoF), the Department

which has responsibility for the civil service, and it broadly reflected the procedures followed in Westminster.

- 54.8 However, the passage of the 2013 Act, a specific piece of legislation relating to SpAds, is significant. The 2013 Act was passed by the Assembly, the body described in Strand One of the Belfast Agreement of 1998 as “the prime source of authority in respect of all devolved responsibilities operating where appropriate on a cross-community basis.”
- 54.9 The 2013 Act began life as a private member’s bill, initiated by Jim Allister QC MLA. It reflected growing concerns at the time about the number of SpAds, their pay, the way they were appointed and the backgrounds of some appointees. The 2013 Act set out new provisions as to how SpAds were to be appointed. Section 7, as discussed further below, required DFP to issue a code of conduct for Special Advisers. The 2013 Act also provided for greater transparency in relation to SpAd numbers and their pay.
- 54.10 Section 1 of the 2013 Act defined a Special Adviser as a person who was appointed to a position in the Northern Ireland Civil Service by a Minister and who was appointed only in order to advise the Minister.<sup>2903</sup> Section 1(4) provided that “The terms and conditions of the appointment provide that [the person] will cease to hold that position on or before the date the Minister ceases to hold office.”<sup>2904</sup> Accordingly, a Special Adviser’s holding of office is linked to that of the relevant Minister.
- 54.11 Section 2 of the 2013 Act provided that a person was not eligible for appointment as a Special Adviser if that person had a serious criminal conviction, as defined by the Act.<sup>2905</sup>

### The codes required by the 2013 Act

- 54.12 Section 7, as mentioned previously, and section 8 required DFP to issue codes for, respectively, the conduct and the appointment of Special Advisers within two months of the sections coming into operation.<sup>2906</sup>
- 54.13 Section 7 required that the code of conduct for Special Advisers had to provide that SpAds could not authorise the expenditure of public funds, exercise any power in relation to the management of any part of the NICS (save over another Special Adviser) or otherwise exercise any power conferred by or under any statutory provision, or any power under the prerogative. Section 7 also required the DFP Minister to lay the code before the Assembly and it would thereafter form part of the terms and conditions of appointment of Special Advisers.
- 54.14 With regard to appointments, section 8(2) specifically provided that “Where a Minister proposes to appoint a Special Adviser, such an appointment **shall be subject to the terms of the code**”, (the Inquiry’s emphasis)<sup>2907</sup> that is the code governing the appointment of Special Advisers.

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2903 LEG-03694

2904 LEG-03694

2905 LEG-03694

2906 LEG-03697

2907 LEG-03697

## The code governing appointment, the model contract and the code of conduct

- 54.15 Codes governing conduct and appointment were duly issued and laid before the Northern Ireland Assembly in accordance with sections 7(4) and 8(4) of the 2013 Act by DFP on 20 August 2013.<sup>2908</sup>
- 54.16 The ‘Code Governing the Appointment of Special Advisers’, which set out the appointment process for Ministers to follow, had an Appendix which contained a model contract for Special Advisers. The model contract itself, which was in the form of a letter of appointment, had three schedules: the first schedule set out the main terms and conditions for Special Advisers; the second schedule set out the code of conduct for Special Advisers; and the third schedule set out the system of remuneration.
- 54.17 The main terms and conditions for Special Advisers had a section on conduct at paragraphs 24 to 30.<sup>2909</sup> This was in addition to the code of conduct for Special Advisers itself. The conduct provisions in the main terms and conditions corresponded almost exactly with paragraphs 14.1-14.7 of a previous version issued by DFP in March 2007,<sup>2910</sup> although that earlier code was not issued under statute.

## The appointment process

- 54.18 Section 8 of the 2013 Act provided that the appointment of SpAds by Ministers shall be subject to the terms of the code governing the appointment of Special Advisers, which was therefore, and is, a mandatory code as far as an appointing Minister is concerned.<sup>2911</sup> That code is designed to ensure that good practice is followed in the appointment process and that individual Ministers, as the “appointing authority”, provide equality of opportunity and avoid unlawful discrimination.<sup>2912</sup> SpAds are public appointees with the status of temporary civil servants and are remunerated from public funds.<sup>2913</sup> Their remuneration is set within two different pay bands, with the relevant Permanent Secretary, Head of the Civil Service and the Minister jointly determining which grade (and the starting salary within the grade) should apply in accordance with the system for remuneration set out in schedule 3 to the model contract.
- 54.19 Ministers having a key role in the appointment and oversight of SpAds is only to be expected, since a SpAd works directly to a Minister and the role is to provide advice of a political nature that is beyond the permissible remit of the permanent civil service. In this regard the Inquiry notes that paragraph 2.13 of the 2000 Northern Ireland Ministerial Code (which was 76 pages long)<sup>2914</sup> made direct reference to SpAd appointments and provided that:

“Ministers are expected to observe the Code of Practice on the Appointment of Special Advisers. While Special Advisers are temporary civil servants they have a very different role from that of other civil servants and need to have a particularly close working relationship with their Ministers. The appointments of Special

2908 DOF-00592 to DOF-00631

2909 DOF-00612 to DOF-00613

2910 WIT-21862 to WIT-21863

2911 LEG-03697

2912 DOF-00593

2913 DOF-00593

2914 INQ-15805 to INQ-15880

Advisers are made personally by Ministers, and are not subject to the requirements of the normal civil service recruitment process. Consideration of the suitability of appointment of any individual special adviser is entirely the responsibility of the appointing Ministers. ***Each Minister should therefore be personally satisfied that any proposed appointee is in all respects suitable for appointment and has the ability, aptitudes and character needed for the duties of the post.*** (the Inquiry's emphasis)

- 54.20 The Ministerial Code of 2000 was, it appears, superseded by the shorter (14 page long) statutory Ministerial Code for the Northern Ireland Executive published in 2006 and approved by the Transitional Assembly on 20 March 2007.<sup>2915</sup> At its meeting on 10 May 2007 the NI Executive noted that the statutory Code had taken effect from 8 May 2007. This occurred after the Northern Ireland Act 1998 was amended in 2006 by the Northern Ireland (St Andrews Agreement) Act 2006. The latter Act amended the former by inserting a new section 28A into the Northern Ireland Act 1998. The new section 28A provided for a statutory ministerial code. The new, shorter, statutory ministerial code set out the rules and procedures to be followed by Ministers and junior Ministers of the Northern Assembly as specified in the Belfast Agreement, the Northern Ireland Act 1998, the St Andrews Agreement and the Northern Ireland (St Andrews Agreement) Act 2006 – particularly with regard to the obligation to refer to the Executive for discussion and agreement of certain matters which were significant or controversial, or which cut across the responsibilities of two or more Ministers.
- 54.21 The 2007 version of the Ministerial Code did not repeat the paragraph set out above relating to Special Advisers, which had been in the 2000 version. The Inquiry considers the 2000 Code to have been a much more detailed and comprehensive document than the Code of 2007. Schedule 1 to the 2006 Act paragraph 4(5) provided that in the event that a draft Ministerial Code had not been approved by the Transitional Assembly by 24 March 2007 the obligation would pass to the Secretary of State to prepare an appropriate draft. Paragraph 4(6) provided that such a draft was to include any parts which had been approved by the Transitional Assembly and, otherwise, be in the form of the former Ministerial Code. In the event, it seems that the residual elements of the 2000 Ministerial Code were intended to be reproduced in non-statutory guidance but, for various reasons, that does not seem to have occurred.
- 54.22 Returning to the 2013 Act, the code governing the appointment of Special Advisers issued under it emphasised, in paragraph 3, the personal nature of such appointments requiring “a high degree of rapport and trust between the parties involved to make them a success.”<sup>2916</sup>
- 54.23 Paragraph 4, of the same appointment code says that:
- “Getting the balance right between the undoubted personal nature of the relationship with a Special Adviser and the concept of fairness required by the law should not be seen as an onerous task, but as one designed to provide the Minister with a candidate field which will ensure the selection of a candidate who fully meets the Minister's needs in terms of competence and attributes.”<sup>2917</sup>
- 54.24 Paragraphs 5 to 13 of the appointment code established a framework for selection and appointment of Special Advisers providing that while, ultimately, it is for Ministers to decide

2915 DOF-00001 to DOF-00018

2916 DOF-00593

2917 DOF-00594

how they select their Special Advisers, there are a number of basic procedures which must be followed, including the provision of a job description and personal specification that is to be used by the Minister in deciding how wide the trawl of candidates should be, the key being that the pool of candidates *must* (the Inquiry’s emphasis) be broadly based.<sup>2918</sup>

## The purpose of, and requirements on, the Special Adviser

54.25 Schedule 2 to the model contract for Special Advisers contained the ‘Code of Conduct for Special Advisers’. The code of conduct defined the function of Special Advisers in the following terms:

“Special Advisers are employed to help Ministers on matters where the work of the Northern Ireland Administration and Minister’s party responsibilities overlap and it would be inappropriate for permanent civil servants to become involved. They are an additional resource for the Minister, providing advice from a standpoint that is more politically committed and more politically aware than would be available to a Minister from the Civil Service.”<sup>2919</sup>

54.26 Paragraph 5 of the same Code of Conduct for Special Advisers provides that:

“Special Advisers should conduct themselves with integrity and honesty. They should not deceive or knowingly mislead the Assembly or the public. They should not misuse their official position or information acquired in the course of their official duties to further their private interests or the private interests of others. They should not receive benefits of any kind which others might reasonably see as compromising their personal judgement or integrity. They should not without authority disclose official information which has been communicated in confidence in the Administration or received in confidence from others.”<sup>2920</sup>

54.27 Paragraph 6 of the Code of Conduct for Special Advisers provides:

“Special Advisers should not use official resources for party political activity. They are employed to serve the objectives of the Administration and the Department in which they work. It is this which justifies their being paid from public funds and being able to use public resources, and explains why their participation in party politics is carefully limited. They should act in a way which upholds the political impartiality of civil servants. ***They should avoid anything which might reasonably lead to the criticism that people paid from public funds are being used for party political purposes.***”<sup>2921</sup> (the Inquiry’s emphasis)

54.28 Not only is it important to record that the appointment code and the code of conduct are statutory codes approved by the Assembly but it also needs to be emphasised that an important public interest is involved in that, according to the mandatory codes, while they have a very different role to ordinary civil servants, SpAds are public appointees, paid from public funds and not party employees.<sup>2922</sup> When dealing with relations with the appointing Minister’s party, paragraph 10 of the Code of Conduct provides:

2918 DOF-00594 to DOF-00597

2919 DOF-00616

2920 DOF-00618

2921 DOF-00618

2922 DOF-00593

“In providing a channel of communication in these areas of overlap, Special Advisers paid from public funds have a legitimate role in support of the Administration’s interest, which they can discharge with a degree of party political commitment and association which would not be permissible for a permanent civil servant. In all contacts with their party, Special Advisers must observe normal Civil Service rules on confidentiality unless specifically authorised, in a particular instance, by their Appointing Authority.”<sup>2923</sup>

- 54.29 Three particular areas of such legitimate activity are identified in paragraphs 8 and 9, namely:
- obtaining a full and accurate understanding of the Party’s policy analysis and advice;
  - ensuring that Party publicity is factually accurate and consistent with Administration policy; and
  - ensuring that Assembly Members and officials of the Minister’s Party are briefed on issues of the Administration policy.<sup>2924</sup>

### The appointment practice as found by the Inquiry

54.30 Despite the guidance concerning the appointment of SpAds, repeated in successive codes on Special Advisers, and made mandatory following the 2013 Act, what happened in practice appears, at least in some cases during the period subject to the Inquiry’s investigation, to have been radically different. The Inquiry identified divergences concerning how appointments were made, the functions of SpAds and their relationship with Ministers.

54.31 Ms Foster told the Inquiry in oral evidence that, in her experience, the then First Minister and the DUP Party Officers had selected Dr Crawford to act as her SpAd when she became DETI Minister, although she had no complaints about that selection.<sup>2925</sup>

54.32 According to Mr Ó Muilleoir the 2013 Act, in prohibiting the appointment of Special Advisers with serious criminal convictions, was seen by Sinn Féin as:

“...an attack on the peace process, as undermining the inclusion which is the foundation of the peace process, and it was not our intention to discriminate against former political prisoners who had helped build the peace.”<sup>2926</sup>

54.33 As a result, Sinn Féin set up a centralised system under which Aidan McAteer, who did have a proscribed conviction and who was now to be neither appointed nor paid as a civil servant, was engaged to “manage and co-ordinate” on a day-to-day basis the work of all Sinn Féin Special Advisers.<sup>2927</sup>

54.34 It seems that all of the Sinn Féin SpAds were aware that Aidan McAteer was acting as the senior Sinn Féin adviser with the direct authority of the deputy First Minister, the late Martin McGuinness. In his evidence to the Inquiry Sir Malcom McKibbin accepted that when he was first introduced to Aidan McAteer, he was told by the then deputy First Minister that he would be working underneath his (Mr McGuinness’s) direction and authority.<sup>2928</sup> As such, according to Mr Ó Muilleoir, he was seen as occupying an elevated position with more authority than any

2923 DOF-00620

2924 DOF-00619

2925 TRA-13604

2926 TRA-16250

2927 WIT-161024

2928 TRA-16724

of the other SpAds.<sup>2929</sup> In effect, an individual who could not legally have been appointed as a SpAd and who was not subject to the mandatory code, or other relevant codes, managed and co-ordinated those who were employed and paid from public funds as temporary civil servants and who were subject to the relevant legal structure and codes.

- 54.35 Such a practice may not, in itself, involve any breach of the 2013 Act but it did have the potential to inhibit or undermine the personal relationship between the relevant Minister and his or her SpAd which was intended to be established by the 2013 Act and associated codes, which had been democratically approved by the Assembly.
- 54.36 Timothy Cairns, who worked as a SpAd for Minister Bell, told the Inquiry that he did not believe anyone would be appointed as a Special Adviser within the DUP without the assent of Timothy Johnston, who was one of the First Minister’s SpAds.<sup>2930</sup> He said that he received a telephone call from Mr Johnston in October 2015, during a period when Mr Cairns had taken up alternative employment as a consequence of the policy of ‘in/out’ Ministers adopted by the DUP after speculation that the murder of Kevin McGuigan had been the work of members of the IRA.<sup>2931</sup> By way of protest the DUP adopted a policy of resigning from government and then returning to office before the expiry of seven days after which their ministerial portfolios would have been reassigned. Mr Cairns was told that if he returned to be a SpAd for Minister Bell he would be retained in the “core DUP SpAd team.”<sup>2932</sup>
- 54.37 Mr Cairns also told the Inquiry that, at the time of his appointment as a SpAd, he had been aware of the appointment code and the official procedure contained therein; but he indicated that the DUP exercised an “unofficial procedure” which took precedence.<sup>2933</sup> His evidence to the Inquiry was that “whilst there is an official procedure, the Democratic Unionist Party exercise an unofficial procedure.”<sup>2934</sup> He accepted that the “unofficial procedure” conflicted with the mandatory appointment code in many respects.<sup>2935</sup> According to Mr Cairns, the decision as to the appointment of a SpAd was taken by a combination of then First Minister Robinson and two of his SpAds, Mr Johnston and Mr Bullick, constituting:
- “The triumvirate that would be making those decisions and those calls.”<sup>2936</sup>
- 54.38 The term ‘*realpolitik*’ was used by a number of the witnesses and appears to have referred to what took place in reality as opposed to what was required by the relevant public and transparent codes and statute.
- 54.39 For his part, Mr Johnston did not disagree with this evidence, conceding that the process had “evolved” since 2007 when his appointing Minister, the late Dr Paisley, had been very much involved in it.<sup>2937</sup> He told the Inquiry that he had never seen one of the letters of confirmation of a SpAd’s appointment sent by the appointing Minister to the relevant Department Permanent Secretary and suspected that “they were a tick-box exercise by the system.”<sup>2938</sup>

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2929 TRA-16248

2930 TRA-12576

2931 TRA-12577, <https://www.belfasttelegraph.co.uk/news/northern-ireland/widow-of-murdered-kevin-mcguigan-100-believes-shooting-was-sanctioned-by-leadership-of-the-ira-36039720.html>

2932 TRA-12577

2933 TRA-12592 to TRA-12593

2934 TRA-12593

2935 TRA-12593

2936 TRA-12602

2937 TRA-14115

2938 TRA-14118 to TRA-14120

- 54.40 When trying to account for the degree of “evolution” or “drift” away from the stipulations of the appointment code, Mr Johnston accepted that there was “an element of centralisation” and a “sense of trying to mirror what was a very centralised operation for a number of the parties.”<sup>2939</sup> He accepted that this was not satisfactory from the point of view of transparency and democracy but said that “as time went on things became very comfortable in the sense of how our party and other parties appointed these positions.”<sup>2940</sup>
- 54.41 Evidence of this drift or evolution can perhaps be seen in the immediate aftermath of the confrontations between Minister Bell and Mr Cairns in London in June 2015 (mentioned earlier in this Report), when Mr Johnston telephoned Minister Bell to tell him that he had no power to dismiss Mr Cairns and then later played the major role in mediating the attempt to restore their relationship.<sup>2941</sup>
- 54.42 In relation to his role in the original appointment of Mr Cairns as SpAd to Minister Bell when he was a Junior Minister in OFMDFM, Minister Bell signed a letter, dated 6 June 2012, to the then Head of the Northern Ireland Civil Service confirming the initial appointment of Mr Cairns as his SpAd and containing the following passage:
- “Having considered a number of potential candidates I have concluded that on the basis of Tim’s considerable experience, qualifications and knowledge of the political environment in which I work that he is the most suited candidate to fulfil the post.”<sup>2942</sup>
- 54.43 When Mr Cairns was again appointed as Minister Bell’s SpAd in late November/early December 2014, Minister Bell signed a similar letter to the relevant Permanent Secretary repeating, in the third paragraph, that he had: “assessed a range of potential candidates as well as considering both the job description and person specification” and concluding that, at the end of the process, Mr Cairns was “by far the most qualified candidate available.”<sup>2943</sup> In fact, it does not appear that any other candidates were considered or that a formal selection process took place.<sup>2944</sup>
- 54.44 When questioned about the content of the two letters of appointment Mr Bell accepted that they were not accurate but described them as simply “standard form.”<sup>2945</sup> He said that he was given a pre-written letter that he neither wrote nor authorised, but he did agree to sign it and accept the appointment of Mr Cairns as “my party had instructed me to do so.”<sup>2946</sup>
- 54.45 As already noted above, in the course of his oral evidence to the Inquiry Mr Johnston, who was seen by a number of witnesses as being at the head of the SpAd ‘hierarchy’ within the DUP described these letters as “tick-box” exercises.<sup>2947</sup> He confirmed that his view was that the Senior Civil Service were aware of the reality as to how SpAds were appointed. Mr Johnston also said that the Senior Civil Service simply wanted to get the appointment process over and

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2939 TRA-14123

2940 TRA-14124

2941 TRA-14121; TRA-14158 to TRA-14159; TRA-12686

2942 DOF-82182 to DOF-82183

2943 DOF-82057

2944 TRA-12600 to TRA-12601

2945 TRA-12280

2946 TRA-12279 to TRA-12280

2947 TRA-14118 to TRA-14119

done with quickly for the functioning of each Department.<sup>2948</sup> Sean Kerr, Minister Bell's Private Secretary in DETI confirmed in written evidence relating to this topic that he had been supplied with a skeleton draft letter by DETI HR to which he had added some biographical information that he obtained from Mr Cairns.<sup>2949</sup>

- 54.46 Minister Bell also told the Inquiry that the DUP Party Officers appointed SpAds for DUP Ministers.<sup>2950</sup> He said that when he was contacted in 2015 by First Minister Robinson over the weekend to discuss his appointment as DETI Minister, he was told that Mr Cairns would be his SpAd because "all the other SpAds had been taken."<sup>2951</sup> When asked if he were happy with Mr Cairns as his SpAd Mr Bell said that he was "content".<sup>2952</sup> Mr Bell confirmed to the Inquiry that, at the material time, he was not aware of the existence of the mandatory code relating to the appointment of SpAds nor was he given any relevant guidance either by the DUP or the Department.<sup>2953</sup>
- 54.47 In a written statement of evidence former DUP First Minister Mr Robinson said: "Frankly, our abiding priority was to work the new, historic, yet difficult arrangements of forming and operating an Executive with age-old adversaries" and that 'delivery' was of critical importance.<sup>2954</sup> He doubted whether any of the three Executive parties "spent any time reflecting on protocols when making SpAd appointments" but denied that there had been any malign motive in circumventing the 'protocols' such as the appointment code for Special Advisers.<sup>2955</sup>
- 54.48 Mr Robinson's attitude is probably succinctly captured in his observation that "We plied our trade on the front-line of Northern Ireland politics; we functioned in a rough and inauspicious climate and we did not live our lives consulting a rule book at every moment."<sup>2956</sup> The "rule book" would appear to have included the provisions of the 2013 Act, the mandatory appointment code issued under the provisions of the 2013 Act, the Northern Ireland Ministerial Code and other relevant codes and practices.
- 54.49 In written representations made to the Inquiry, Mr Robinson again emphasised the difficulties in which politicians in Northern Ireland operated under the arrangements for the devolved administration that required mandatory coalition government. He noted that:
- "The nature of the devolved government in Northern Ireland led to the provisions of the code of conduct for Special Advisers being stretched to, and beyond, their limits to make the system of government work in the peculiar structures that prevailed at the time."
- 54.50 Mr Robinson accepted that "certain SpAd appointments did not follow the provisions of the Code, and that on occasions the actions of certain Special Advisers fell outside the code"; but made the entirely fair point that this was not the case in all instances or for every Special Adviser.

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2948 TRA-14126

2949 WIT-25845

2950 WIT-22513

2951 TRA-12276

2952 TRA-12278

2953 TRA-12281 to TRA-12282

2954 WIT-156020

2955 WIT-156021

2956 WIT-156022

54.51 The divergence from the appointment code, and appointment being the responsibility of the Minister, may in turn have caused, or certainly had the potential to cause, misunderstandings about where authority rested, an issue which has been touched upon earlier in this Report on a number of occasions as regards the relationship between Minister Bell and Mr Cairns, including as it related to the RHI scheme. For instance, Mr Stewart was asked in his oral evidence to the Inquiry about the relationship between Mr Cairns and Mr Bell and where authority rested. Mr Stewart said:

“Jonathan took the very clear view that authority rested in him and in him alone. Timothy took rather more of a *realpolitik* view that the Minister may, in law, be the head of the Department and the person who controls and directs the Department – that’s absolutely correct – but the Minister owes his or her position to the nominating officer, usually the party leader, and the *realpolitik* consequences of that are that there is a degree of central control from Minister to party leader. Sorry, the other way round: party leader to Minister.”

54.52 In a written statement of evidence, Mr Stewart referred to the relationship between Mr Cairns and Minister Bell as “tense” and went on to say:

“The tension in the relationship did not appear to stem from any fundamental difference on policy, nor to any lack of personal chemistry. The root cause appeared to be resentment on the part of Minister Bell to Mr Cairns’ *party liaison*’ role and how it was exercised.”<sup>2957</sup>

## The role exercised by SpAds in practice

54.53 The evidence presented to the Inquiry contained a number of examples of the power and control exercised by SpAds. On occasion, such exercises of power may have been legitimate, where the SpAd was acting with the knowledge and authority of their Minister in relation to a matter where the Minister could appropriately exercise direction and control. In other instances, questions have been raised as to whether SpAds were acting without the knowledge of their Minister, on their own authority or outside of their legitimate functions. One consequence of this Inquiry may well be, and ought in the Inquiry’s view to be, much more transparency as to how Special Advisers work and a greater delineation between their functions and obligations as temporary civil servants and any additional responsibilities they exercise on behalf of their political party.

54.54 Mr Stewart told the Inquiry that; “Policy work, I think works best when there’s trust and confidence between Ministers, officials and spads. I have to say, in the summer of 2015, at times, it felt more as if we were being treated as the opposition.” When asked by whom officials were being so treated he replied “Ministers and spads.”<sup>2958</sup>

54.55 Minister Bell considered, with some justification, that his confrontation with Mr Cairns (discussed in detail earlier in this Report) constituted a challenge to his authority. However, he was told by Mr Johnston that he could not sack Mr Cairns, and both Mr Cairns and Dr Crawford considered they had authority to remove material from important documents without reference to their respective Ministers (described in more detail in chapters 39 and 40 of this Report).

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2957 WIT-27526

2958 TRA-11641

- 54.56 Mr Johnston appears to have had more influence in the appointment of Mr Cairns than Minister Bell and it was he, not Minister Bell, who directed Mr Cairns to liaise with Dr Crawford in relation to energy matters. In his email to Minister Bell’s Private Secretary of 4 February 2016, with regard to the submission on closing the NI RHI scheme, Mr Cairns wrote: “Have the Minister read it, I have cleared it and he should and then I await the voice on high to tell me when it can be issued.”<sup>2959</sup> Mr Cairns clarified during his oral evidence that he believed the “voice on high” was a reference by him to Mr Johnston.<sup>2960</sup>
- 54.57 A further example of the power and control exercised by some SpAds was the agreement by Mr Sterling with regard to Dr Crawford’s removal of the reference to Moy Park from the January 2016 submission (considered earlier in the Report) in the interests of finalising a decision stating “...frankly, I didn’t think it was worth having a major set-to with Dr Crawford about it.”<sup>2961</sup>
- 54.58 Sir Malcolm McKibbin, former Head of the NICS (but in post at the time when several of the SpAd appointments the Inquiry has considered took place), told the Inquiry that he had been unaware of the practice adopted by the DUP with regard to the appointment of SpAds and that he was both surprised and disappointed by the evidence that emerged in the course of the Inquiry with regard to the letters that he had received as Head of the NICS relating to the appointment of OFMDFM SpAds. He had regarded such letters as “written assurance that the relevant procedures had been followed.” He accepted that what now appears to have been the “camouflaging function” of those documents was “unsatisfactory”.<sup>2962</sup>
- 54.59 Sir Malcolm was also asked about the system established by Sinn Féin in accordance with which an individual who could not be appointed as a SpAd because of a relevant conviction exercised weekly management and co-ordination of the Sinn Féin SpAds under the direct authority of the deputy First Minister. Sir Malcolm described Mr McAteer as being quite similar to Mr Johnston as both were “fixers” and they worked together very well whenever there was a high profile issue.<sup>2963</sup> In the interests of fairness, the Inquiry records that Timothy Johnston informed Sir Malcolm that Mr McAteer was regarded as a constructive pragmatist who helped to resolve issues.
- 54.60 Sir Malcolm observed in oral evidence that even before he became Head of the Civil Service, both the First Minister and deputy First Minister held passes for two or three additional ‘unofficial’ advisers to gain access to Stormont Castle. He said that he had been told of the existence of that arrangement between his predecessor and the First Minister and deputy First Minister and that it ‘mirrored’ the situation in 10 Downing Street. Sir Malcolm used a word employed by other witnesses, including Mr Johnston, describing the situation as one of *realpolitik*.<sup>2964</sup>
- 54.61 As mentioned previously, the type of work which might be undertaken by the Special Adviser is defined in paragraph 3 of their Code of Conduct and includes reviewing papers going to the Minister and “devilling” for the Minister, as well as checking facts and research findings from a party-political viewpoint.<sup>2965</sup> However the evidence established that, in the case of Minister

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2959 DFE-293218

2960 TRA-12950

2961 TRA-16538

2962 TRA-16710 to TRA-16718

2963 TRA-16725 to TRA-16726

2964 TRA-16723 to TRA-16733

2965 DOF-00616

Foster and her SpAd, Dr Crawford, there was a complete misunderstanding as to his duties with regard to reading technical reports. In a written statement of evidence Minister Foster said:

“My usual practice was that my Special Adviser would read the detail of technical reports before they were provided to me and and draw particularly significant parts to my specific attention. He also would have advised me generally on the content...”.<sup>2966</sup>

54.62 In fact, according to the evidence, he did not read such documents and told the Inquiry that he did not believe that he was expected to do so.<sup>2967</sup> Nonetheless, Minister Foster believed that he did and she could not recall having read any technical reports relating to energy herself. It seems that there was no clear agreement as to Dr Crawford’s ‘devilling’ duties with regard to such reports. As discussed previously in this Report, in the context of the initial non-introduction of tiering to the NI RHI scheme, the Inquiry found that the level of communication between Minister Foster and her SpAd was apparently so weak that he did not tell her he had not read the reports and she continued in her unspoken reliance on him, not asking him whether he had, even though it was her clear expectation that this was part of his job. The Inquiry considers this gap in their working relationship to have been a significant and obvious failure. There is no indication that the manner of appointment of Dr Crawford gave rise, or contributed, to this misunderstanding; but it is an important example of why a high level of communication and rapport between the Minister and his or her SpAd was essential.

## Conflicts of interest

54.63 As mentioned earlier in the Report, the Northern Ireland Civil Service HR Policy, in the chapter on Standards of Conduct at paragraph 2.1.g,<sup>2968</sup> which was referenced in the SpAd’s model contract, requires conflicts of interest to be declared to the individual’s Establishment/Personnel Division. Neither Dr Crawford nor Mr Brimstone, a SpAd in the First Minister’s office in late 2015 and early 2016 when the NI RHI was being discussed, made such a declaration of interest in circumstances that required them to do so.

54.64 As is also discussed elsewhere in the Report, Dr Crawford had a brother and two cousins who received RHI payments for their installations accredited on to the NI RHI scheme. One cousin was a poultry farmer who was considering installing biomass boilers and Dr Crawford sent him a confidential draft of the 2013 NI RHI consultation document three weeks before it was released to the public. Dr Crawford’s disclosure took place without the knowledge of Minister Foster. Dr Crawford accepted in oral evidence that he had been wrong to do this.<sup>2969</sup> That disclosure would have been potentially contrary to paragraph 2.1.2 of the Northern Ireland Civil Service Code of Ethics<sup>2970</sup> (the NICS Code of Ethics is Annex 1 to the Standards of Conduct chapter of the NICS HR Policy).

54.65 Paragraph 2.1.2 of the NICS Code of Ethics provides at (a) that as a civil servant “You must not misuse your official position, for example by using information acquired in the course of your official duties to further your private interests or those of others” and at (b) prohibits disclosure of official information without authority.

2966 WIT-20569 to WIT-20570

2967 TRA-07547 to TRA-07552

2968 DOF-00026

2969 TRA-08172 to TRA-08182

2970 DOF-00050

- 54.66 Dr Crawford told the Inquiry that when RHI “became a live issue in DFP” in 2015 he wanted to put on record that he had family members involved in the NI RHI scheme. He said that he did so in a verbal conversation with Mr Sterling, Mr Brennan and, possibly, the relevant DFP Minister, about budgetary issues to do with the RHI scheme at Clare House in October/November 2015. Dr Crawford said that he had a “vague recollection” that Mr Sterling told him that it was not necessary to put the information in writing.<sup>2971</sup>
- 54.67 Mr Sterling maintained, in both written and oral evidence to the Inquiry, that he was unable to recall any such conversation.<sup>2972</sup> In oral evidence Mr Sterling said that he would have recalled such a conversation had it occurred. Mr Sterling accepted that, at the time, there was no distinct formal system for recording SpAds’ conflicts of interest but such a system had been under consideration during the Assembly talks process in 2017.<sup>2973</sup>
- 54.68 Mr Brimstone became a beneficiary of the non-domestic RHI subsidy, by applying to the scheme in respect of his agriculturally rated shed and utilising the heat for his domestic premises. The Inquiry has dealt earlier in this Report with how the poorly drafted 2012 NI RHI regulations led to an interpretation that facilitated such mixed use arrangements on the NI RHI scheme. Mr Brimstone had become committed to installing a biomass boiler in June 2015 and the installation and subsequent application to the RHI scheme took place later that year. However, Mr Brimstone did not formally declare that interest when Mr Cairns sent him a copy of the 8 July 2015 submission for Minister Bell either on receipt of the document or when replying to Mr Cairns (albeit his reply was to the effect that it was hard to argue with the submission). He also did not formally declare his interest when the NI RHI scheme became an issue involving OFMDFM in early 2016. Mr Brimstone said that he had verbally notified Minister Foster of his interest in the scheme in January 2016, although she had no specific recollection of being so informed.<sup>2974</sup>
- 54.69 Nevertheless, despite the potential conflict of interest, Mr Brimstone remained present during the meeting between the Head of the NICS and the First Minister and deputy First Minister on 9 February 2016, where the NI RHI scheme was one of the issues being discussed.<sup>2975</sup> He accepted in oral evidence to the Inquiry that he should have made an appropriate declaration and withdrawn from any interchanges on the scheme.<sup>2976</sup>

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2971 TRA-13219 to TRA-13221

2972 WIT-05187; TRA-16503

2973 TRA-16504 to TRA-16506

2974 TRA-13728 to TRA-13729

2975 TEO-00191

2976 TRA-14010 to TRA-14036

## Findings

305. It is clear from the evidence received by the Inquiry that both of the two main parties in the Executive, the DUP and Sinn Féin, breached the spirit and/or provisions of the 2013 Act passed by the Assembly and the mandatory codes issued by DFP in accordance with sections 7 and 8 of that Act in one way or another.
306. At the time of Mr Cairns' appointment as SpAd to Minister Bell in DETI in 2015, some two years after the passage of the 2013 Act and the mandatory appointment code, the procedure was not, as required by the appointment code, by way of a competitive selection from a candidate pool set up after a trawl by Minister Bell, but was instead conducted by the DUP through its then leader, and the then First Minister, Mr Robinson.
307. Minister Bell accepted that the practice adopted in signing the letter of appointment effectively "camouflaged" the complete failure to comply with the appointment code. Those letters were apparently drafted by civil servants who may have been aware of the lack of conformity between the provisions of the appointment code and what happened in practice. The Inquiry has no difficulty in sympathising with civil service officials, given the onerous workload and the lack of resources they faced. Moreover, in the unique political context of devolution in Northern Ireland, they were trying to deliver in the highly charged atmosphere of an enforced coalition between two major parties with radically conflicting political ideologies.
308. A key purpose of the mandatory codes made under the 2013 Act (the code of appointment for Special Advisers and the code of conduct for Special Advisers), was to ensure that a high degree of rapport and trust existed between the people involved in order to make the personal nature of the appointment of a SpAd by the relevant Minister and the subsequent personal relationship a success. The Inquiry finds that the practices adopted by the DUP and Sinn Féin in centralising the appointment, control, and management of SpAds effectively frustrated that purpose of the democratically enacted legislation. As a consequence, some SpAds wielded very significant power and were encouraged to see themselves as more directly responsible to the central authority or OFMDFM and their political parties, than to their individual Ministers.
309. Several indications of the outworking of this approach have arisen in the course of the evidence provided to the Inquiry. Most of these are dealt with in detail elsewhere in this Report, in discussion of the appropriate evidence. Some notable examples have been referred to above.
310. Neither Dr Crawford nor Mr Brimstone formally recorded potential conflicts of interest in 2015 and 2016 when they ought to have done so and, notwithstanding such conflicts, both appear to have taken part in meetings relating to the NI RHI scheme which they should not, in fact, have attended. While declarations of conflicts of interest were required, in accordance with the Standards of Conduct contained within the NICS HR Policy referred to above, the Inquiry finds that there should have been a system in existence for the periodic registration of interests and potential conflicts, in

writing, which was clearly communicated to all relevant officials and which served as an objective and transparent record. Even without such a system, officials, including SpAds, with a potential conflict of interest should not have taken part in meetings where an actual conflict might arise.

311. Sir Malcolm McKibbin confirmed to the Inquiry that he regarded a Minister's letter confirming appointment of his or her SpAd to constitute a written assurance that there had been compliance with the code and the Inquiry heard no evidence to indicate that other Permanent Secretaries held a different view. The *realpolitik* observed by some Ministers in these circumstances appears to have produced a number of advisers with wide powers and influence who were appointed and operated in practice outside the code of conduct for Special Advisers.
312. Nevertheless, it is important to bear in mind that SpAds were civil servants, albeit of a special type, and, as such, there is a public interest in ensuring that the appointment process was operated, and was seen to operate, in accordance with the relevant codes. Section 6 of the 2013 Act provides that DFP must issue a report about Special Advisers employed at any time during the previous financial year, which must then be laid before the Assembly. The Inquiry notes that such reports simply provided the mandatory information required by section 6, namely details of numbers and earnings.



## Chapter 55 – DETI systems of governance and control

### The issue of governance within DETI

- 55.1 One of the many issues which the Inquiry has had to investigate is why risks relating to the NI RHI scheme materialised, but yet were not sufficiently appreciated by officials or picked up sooner by DETI's systems of governance.
- 55.2 Officials working on the NI RHI scheme within DETI had identified some potential risks relating to the scheme from the outset. They were recorded on an initial scheme risk register. Several risks were also the subject of warnings to DETI from bodies like CEPA and Ofgem during the creation of the scheme, whilst the same or other risks became apparent to commercial entities in the renewable energy sector shortly after the scheme launched, some of which were drawn to DETI's attention.
- 55.3 Governance systems were the Department's safety net, there to ensure that commitments were met and to draw attention to any mounting problems, such as those of the NI RHI, before they went out of control. Shortcomings in the design and implementation of the NI RHI scheme, and the impact of the lack of project management, could and should have become visible to senior management through such systems; but this did not begin to become reasonably apparent until the middle of 2015 and not in a sufficiently structured form until the DETI Internal Audit report of May 2016.<sup>2977</sup>
- 55.4 Alongside arrangements for the management of civil servants (using mechanisms such as annual appraisals, objective setting and regular personal performance reviews), DETI's governance systems were intended to give assurance to the Permanent Secretary and senior management that the Department's activities were being well managed. Responsibility for making sure that these governance systems were in place and working satisfactorily rested ultimately with the Permanent Secretary.
- 55.5 Mr Sterling, in his written evidence to the Inquiry, explained that section 3 of 'Managing Public Money Northern Ireland' required him, as Accounting Officer, to ensure that the organisation operated effectively and to a high standard of probity, meaning specifically that he had to ensure his Department:
- had a governance structure which transmits, delegates, implements and enforces decisions;
  - had trustworthy internal controls to safeguard, channel and record resources as intended;
  - operated with propriety and regularity in all its transactions; and
  - used its resources efficiently, economically and effectively, avoiding waste and extravagance.<sup>2978</sup>

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2977 DFE-223638 to DFE-223682

2978 WIT-04049

## Previous similar issues – the BTI and Bytel cases

- 55.6 Governance within DETI was a topic of some considerable interest and activity during the years 2009-2016. Changes and intended improvements were introduced within the Department to the systems of risk management and governance reporting and, for a time, Internal Audit focused on improvements in project management. At the same time, as discussed in chapter 4 of this Report, there was external pressure, generated in particular by two reports produced by the Northern Ireland Audit Office (NIAO) which involved DETI: ‘The Bioscience and Technology Institute Report’, dated November 2011<sup>2979</sup> and ‘The Bytel Report’, dated March 2015.<sup>2980</sup> These reports were highly critical of aspects of DETI’s governance and approach to project management. While both reports referred to events pre-2010, they nevertheless resulted in discussions at DETI’s Audit Committee and hearings at the Public Accounts Committee in the Assembly, at least some of which occurred during the lifetime of the NI RHI scheme, albeit prior to DETI’s full awareness of its problems.
- 55.7 In respect of the Bioscience and Technology Institute (BTI), the NIAO report was published on 29 November 2011, at a time when the NI RHI scheme was being created. Amongst other things, it recorded that project monitoring and control was weak<sup>2981</sup> and its recommendations included the need for active monitoring of projects.<sup>2982</sup>
- 55.8 The Bytel project, being one which aimed to provide high-speed broadband connectivity linking Belfast, Craigavon, Armagh, Dundalk and Dublin,<sup>2983</sup> gave rise to a co-ordinated examination between the NIAO and the Office of the Irish Comptroller and Auditor General which was published in a report on 3 March 2015. This was at a time at which significant problems with the non-domestic RHI scheme were first beginning to be appreciated within DETI.<sup>2984</sup> That report highlighted DETI’s failure to deal effectively with information from a ‘whistle-blower’; a failure to keep proper notes and records; and a failure to employ relevant project management.<sup>2985</sup> A PAC hearing on 18 March 2015, attended by Dr McCormick and Mr Sterling, considered the NIAO’s report on Bytel and committee members were particularly critical of DETI.<sup>2986</sup>
- 55.9 Subsequently, on 1 July 2015, the PAC issued its report in respect of Bytel,<sup>2987</sup> the executive summary of which stated that warning signs were “effectively ignored” by the Department which “behaved as if nothing was wrong” and left “the impression that DETI hoped that silence and inaction would make these issues disappear.”<sup>2988</sup> The report also recorded that:
- “The Committee is very concerned that poor project management and disregard for value for money appear to have been endemic within the Department at that time.”<sup>2989</sup>

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2979 INQ-05023 to INQ-05113

2980 INQ-90001 to INQ-90107

2981 INQ-05035

2982 INQ-05038

2983 INQ-90010

2984 INQ-90066 to INQ-90107

2985 INQ-90098 to INQ-90099

2986 INQ-90139 to INQ-90180

2987 INQ-90108 to INQ-90226

2988 INQ-90113

2989 INQ-90113

- 55.10 The fact that DETI had “provided unsubstantiated assurances over many years” was noted, and the report emphasised that “Important as systems and processes are, it is vital that these work in practice.”<sup>2990</sup>
- 55.11 These factors formed part of the context to the evidence this Inquiry heard on the question of governance. The Inquiry was particularly concerned to probe whether there were systemic problems with governance within DETI which contributed to, or failed adequately to identify or mitigate, the difficulties with the RHI scheme that are addressed in detail elsewhere within this Report.

### Five particular aspects of the DETI governance system

- 55.12 The Inquiry focused on five particular aspects of DETI’s governance systems: the forward looking Operating Plan (sometimes referred to as the business plan) and the linked divisional and branch plans; assurance statements; risk management; Internal Audit (particularly important, as its role was to ensure that DETI’s governance was in order); and the arrangements for ensuring quality of advice to the Minister. Each is discussed below.

#### DETI’s operating, divisional and branch plans and the planning process

- 55.13 DETI’s Operating Plan was derived from its longer-term Corporate Plan, which in turn was informed by the relevant Programme for Government of the Northern Ireland Executive. The DETI Operating Plan was produced annually and gave rise to further specific plans for each of DETI’s divisions – the ‘divisional plans’. Mr Sterling told the Inquiry that the Operating Plan included the 13 commitments which fell to DETI from the 2011-15 Programme for Government, three of which were shared with other Departments. The Operating Plan also set out the objectives for each business area of the Department.<sup>2991</sup>
- 55.14 As Mr Thomson stated, “the DETI operating plan would have been a combination of ‘top down’ objectives – key priorities of the Executive and minister and ‘bottom up’ – key objectives being identified by Heads of Divisions.”<sup>2992</sup> He explained that DETI’s Operating Plan “was the key driver of performance”; that “Heads of Division were required to formally report progress against each of the targets contained in the DETI Operating Plan on a quarterly basis”; and that, in terms of his own managerial practice, “I met with my respective heads of division at the reporting stage to review quarterly performance.”<sup>2993</sup>
- 55.15 References to RHI in the DETI Operating Plan, it turns out, were few in number and at a very general level. For example, in the 2011-12 Operating Plan there were 97 specific targets, with one relating to RHI that read: “By 31 March 2012, have in place all necessary arrangements to facilitate the operation of a Renewable Heat Incentive in Northern Ireland.”<sup>2994</sup> The 2012-13 Operating Plan again contained just one reference to RHI: “By 31 March 2013, have progressed all necessary arrangements for introduction of Phase II of the Renewable Heat Incentive in Northern Ireland.”<sup>2995</sup> In both years, the RHI-related target was one of more than twenty set for the Energy Division as a whole.

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2990 INQ-90113 to INQ-90114

2991 TRA-06064

2992 WIT-13518

2993 WIT-13516 to WIT-13518

2994 DFE-386409

2995 DFE-386439

- 55.16 Some further detail about RHI was set out in the divisional plans relating to Energy Division. These divisional plans contained specific tasks which were assigned to the relevant branches within Energy Division, and the officials responsible for their respective completion. An example considered by the Inquiry was such a plan for 2011-12 (as at September 2011), where the Energy Division Renewable Heat Branch was listed, on one page, as having six tasks related to the NI RHI scheme including developing, clearing and consulting on the policy.<sup>2996</sup>
- 55.17 The following year, the format of the Energy Division’s divisional plan was changed to include a column on ‘Risks’, so that any issues which jeopardised the achievement of ‘key actions’ and ‘performance targets’ could be recorded. In that year, 2012-13, the Renewable Heat Branch (as at June 2012), was listed as having three ‘key actions’ related to RHI on one page of the plan: “Launch of Phase 1 of Renewable Heat Incentive”; “Development (with Ofgem) of systems to manage the administration of the RHI”; and “Development of RHI Phase 2 Policy”.<sup>2997</sup> Against these actions, in the risks column, and as explained by Mr Thomson, two risks were referenced as follows: “State Aid approval required” and “Secondary legislation required.”<sup>2998</sup>
- 55.18 In the 2013-14 plan for the division (as at September 2013),<sup>2999</sup> the RHI actions focused on the setting up of RHI Phase 2<sup>3000</sup> with only limited mention of Phase 1 in the context of administration. Monitoring the NI RHI scheme was not recorded.
- 55.19 In his written evidence to the Inquiry Mr Thomson explained that:
- “At departmental level therefore, the implementation and operation of the RHI, having been launched, was considered best handled at divisional level – it wasn’t either a Programme for Government or Operating plan objective.”<sup>3001</sup>
- 55.20 The Inquiry notes that plans at both the corporate and divisional level for 2013-14<sup>3002</sup> and 2014-15<sup>3003</sup> lacked a reference to the scheduled first review of the NI RHI scheme that was to take place in 2014. Mr Sterling accepted that the need for a review would have been more likely to have been recognised and acted upon:
- “If it was in the operating plan for 14/15 or, indeed, to have been flagged up earlier in the previous year, 13/14. And even if those charged with doing the review had concluded for whatever reason that they weren’t going to do it to the same timescale, the fact of it being included in our operating plan would’ve meant there would’ve been a challenge to why it wasn’t happening in line with the expected timescale.”<sup>3004</sup>
- 55.21 There was a third level of plan, at branch level, but branch plans were not in universal use. When he joined as the head of the Energy Efficiency Branch in the summer of 2014, Mr Wightman created and started using a plan specifically for his branch (the Energy Efficiency Branch plan, referred to earlier in this Report). He did not believe there had been such a plan at branch level since 2009. Mr Wightman explained to the Inquiry that branch-level plans were

2996 DFE-363984 to DFE-364017 at DFE-363993

2997 DFE-367854 to DFE-367893 at DFE-367870

2998 WIT-13516 to WIT-13517; DFE-367870

2999 DFE-374215 to DFE-374254

3000 DFE-374234 to DFE-374235

3001 WIT-13516 to WIT-13517

3002 DFE-386482 to DFE-386483; DFE-374234 to DFE-374235

3003 DFE-386537; DFE-377503 to DFE-377504

3004 TRA-06825

not a necessity, with branch teams often relying on the divisional level process. He, however, had been used to a branch level plan in his previous roles: “I found it good practice; I’ve always had branch plans.”<sup>3005</sup>

55.22 The Inquiry considered iterations of this Energy Efficiency Branch plan for 2014-15 and 2015-16, which were more detailed documents. In the early versions of the plan in the summer of 2014, Mr Wightman included actions brought across from the handover note left by Mr Hutchinson. As set out in Chapter 50, there was a reference to a possible “review of the biomass tariffs of under 100kW” and “consideration of tiered tariffs to prevent excessive payments”.<sup>3006</sup> In the event, no such actions took place in the summer or autumn of 2014. There was also an action for the team to speak to Mr Hutchinson, by now having left DETI and in his new role, to check their understanding about what was meant by the need to “consider tiered tariffs.”<sup>3007</sup> As noted earlier, while a meeting with Mr Hutchinson did happen, it focused on the domestic scheme; this particular action on tiered tariffs remained unaddressed until the middle of 2015.

55.23 In summary, the planned review of the NI RHI scheme was not included on the Department’s Operating Plan or the relevant divisional plan; and whilst a more limited review was included on the relevant branch plan, it was not translated into action within an appropriate timescale.

#### Assurance statements on the system of internal control

55.24 Assurance statements, completed on a six-monthly basis, were another component of DETI’s department-wide governance system. Mr Thomson referred to this process as “a very important aspect of the governance arrangements.”<sup>3008</sup> He explained that the Permanent Secretary commissioned these statements from branches across the Department and, once completed (and after they had moved up through the divisions and been reviewed and signed off by the Deputy Secretary, who also provided his own accompanying statement), they were returned to the Permanent Secretary as well as being sent to Finance Division and to DETI’s Audit Committee.<sup>3009</sup>

55.25 The process involved completion of a template and a signature to affirm that “appropriate internal controls were in place and risks identified” across ten management procedures, including business planning, business cases, monitoring of expenditure and third-party organisations. The purpose was to seek confirmation twice a year that the required governance arrangements were in place and being used. There was also a section inviting comment on ‘other issues.’<sup>3010</sup>

55.26 The front cover of each assurance statement described the purpose of the system. For example, in the autumn of 2012, the front cover of an assurance statement signed by Mr Thomson stated:

“The system of internal control is based on an ongoing process designed to identify and prioritise the risks to the achievement of my Group’s policies, aims and objectives, to evaluate the likelihood of those risks being realised and the

3005 TRA-06921

3006 DFE-419562

3007 DFE-419562

3008 WIT-13519

3009 WIT-13519 to WIT-13520

3010 WIT-13519 to WIT-13520

impact should they be realised, and to manage them efficiently, effectively and economically.”<sup>3011</sup>

55.27 However, in his oral evidence to the Inquiry Mr Thomson further said of the assurance statements that:

“It became a very laborious system. I still think it was very good to ask heads of divisions to personally sign a statement to say that these things were all being done but...it has become too cumbersome and there is so much documentation that you don’t get the critical things out. But certainly some of the key things in the RHI were not flagged – being flagged to me.”<sup>3012</sup>

55.28 Yet the assurance statement system was not simply a matter of completing the template every six months because, as Mr Thomson also explained in his first witness statement to the Inquiry, the process involved conversations between senior managers:

“I discussed the individual statements with the respective divisional heads to receive assurance that internal controls were in place, that everything was operating as expected and to identify any particular issues of concern. On the basis of these discussions I made my own statement to the Permanent Secretary to confirm the efficacy of the systems of internal control in my areas of responsibility and, where appropriate, draw the attention of the Permanent Secretary to any significant internal control issues.”<sup>3013</sup>

55.29 The assurance statements and the discussions that surrounded their completion could have been a mechanism to identify, for example, that DFP’s approval of the RHI scheme was time-limited in the section of the statement (section 2.2) that invited an affirmation that all expenditure had DFP approval.<sup>3014</sup> It could also have been a mechanism to cause questions to be asked about the adequacy of the sponsorship arrangements of Ofgem as operated by the Renewable Heat Branch in the section (section 7.4) requiring assurance on the adequacy of monitoring systems over external delivery organisations that distributed money on behalf of the Department.<sup>3015</sup>

55.30 In May 2014, Mr Thomson signed off an assurance statement giving the Renewable Heat Branch a clean bill of health for the six month period up to the end of March 2014.<sup>3016</sup> However, the assurance document that had been provided to him did not contain any reference to CEPA’s warning in 2013 that Northern Ireland was unlikely to meet its target of 10% of heat from renewable sources by 2020, any reference to the need for a review of the non-domestic RHI scheme, any reference to the introduction of cost controls having been decoupled from development of the domestic scheme, nor any reference to the risks of significant staff turnover having occurred or about to happen at that time. It seems that none of these matters had been raised by Renewable Heat Branch or Energy Division in their contribution to the document; nor had they come to Mr Thomson’s attention through any other route, be it his own questioning or what was volunteered in management conversations.

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3011 DFE-265835 to DFE-265837

3012 TRA-05781

3013 WIT-13520

3014 DFE-265844

3015 DFE-265860

3016 DFE-179862 to DFE-179865

- 55.31 The assurance statement for the six months up to the end of September 2014, when invited to affirm that all DFP approvals for expenditure were in place, recorded ‘yes’ and the accompanying ‘comments’ box stated, “Approvals already in place for RHI Phase 1.” No reference was made to the fact that the non-domestic RHI approval had less than six months left to run.<sup>3017</sup>
- 55.32 The assurance statement process could also have been a route for officials to flag up particular problems, for example in section 12.6, which provided an opportunity to raise any significant control or other matters not covered elsewhere in the six-monthly return,<sup>3018</sup> although, as discussed elsewhere in this Report, it did cause some consternation when used in this way by Mr Mills over attempts to clarify RHI funding in 2015.
- 55.33 Mr Sterling told the Inquiry that the Operating Plan, the six-monthly assurance statements and his regular dialogue with both grade 3s and with his grade 5 Heads of Division was the way he kept abreast of what was going on in the Department.<sup>3019</sup> He also told the Inquiry, however, that he endeavoured to give the message that teams should not wait for this six-monthly process to raise a problem:<sup>3020</sup>
- “I would have wanted to have a culture in place where people felt free to flag up concerns quickly so that they could be addressed before they become [sic] a bigger problem than they need to be.”<sup>3021</sup>
- 55.34 Mr Sterling accepted in his evidence to the Inquiry that there were issues that he now recognised ought to have been escalated through this system of assurance statements, but which were not. He could not satisfactorily explain why that was, other than to say it was as much about culture as about process.<sup>3022</sup>
- 55.35 The Inquiry has considered, by way of further example, the assurance statement for the six month period ended 31 March 2015, which was signed by Mr Stewart on 29 May 2015 in response to a request from the Permanent Secretary, Dr McCormick, who emphasised that completion of the statement required due diligence. This particular statement is interesting for two reasons:
- Firstly, because of the clear and positive assurances it offered about the way things were being run within the Policy Group, including Energy Division, up to that point in 2015; and
  - Secondly, because in his cover note to this statement, Mr Stewart repeated in fairly stark terms the point raised by Mr Mills in his contribution to Mr Stewart, about the need for clarity around the RHI budget for 2015-16.
- 55.36 The positive assurances from Mr Stewart on behalf of the whole Policy Group included the answer ‘yes’ to the statement that:
- “Programmes and projects are managed in accordance with good practice including, where appropriate, Gateway Reviews, Prince 2 Methodology and guidance that issues from Central Procurement Directorate.”<sup>3023</sup>

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3017 DFE-388307  
3018 DFE-388321  
3019 TRA-06065  
3020 TRA-06149  
3021 TRA-06150  
3022 TRA-06150  
3023 DFE-277250

- 55.37 ‘Yes’ was also the assurance given to the statement that “Divisions, Branches and Units within the Group have obtained necessary DFP approvals for expenditure (where appropriate).”<sup>3024</sup> A further ‘yes’ was recorded against “Divisions, Units and Branches within the group that distribute money via External Delivery Organisations (EDOs) / Third Party Organisations (TPOs) have adequate monitoring systems in place.”<sup>3025</sup>
- 55.38 There was no reference to the lack of project management in respect of the RHI scheme and no reference to the fact that the DFP approval for expenditure on the non-domestic RHI scheme had lapsed on 31 March 2015 and not been renewed (although this had not at that time been realised by those in Energy Division). In addition, an assurance was given that implied confidence in the adequacy of the monitoring of Ofgem. The assurance statement also asserted that authority, responsibility and accountability within the Group were clearly defined and that staff were made fully aware of their job responsibilities.<sup>3026</sup>
- 55.39 Yet under a heading ‘Significant Internal Control Problems’, Mr Stewart in his cover note to the assurance statement wrote:
- “Despite repeated requests for information from Finance Division (and DFP) the Division has yet to receive any clarity around the maximum available RHI budget going forward. ...Without this clarification both schemes may need to be closed to prevent overspends.”<sup>3027</sup>
- 55.40 By contrast, in the aggregated governance statement for the Department as a whole for the year to 31 March 2015, signed by the Permanent Secretary on 24 June 2015, the non-domestic RHI scheme was described under a heading “other governance issues” as “a UK-wide scheme” and, rather than any suggestion of closure, the report stated simply that “The Department is currently working to address governance and financial requirement issues arising with the scheme.”<sup>3028</sup>
- 55.41 As previously acknowledged by the Inquiry, at this point it appears that this carefully guarded reference in the annual governance statement, to be included in DETI’s Annual Report, was motivated by a concern amongst relevant officials that a clearer statement of the problem could create an unwanted spike in applications. In his written statement of evidence Mr Cooper explained that the paragraph had been developed by himself, Mr Rooney and other departmental colleagues, including Dr McCormick, with a key factor being the tension between the details that could be provided and the potential for the market to react in such a manner, with an unwarranted spike in applications, as to aggravate the problem.<sup>3029</sup> The Inquiry has already discussed elsewhere in the Report how, in reality, extensive information had already been, or was to be, passed on to market participants by more junior Energy Division officials.
- 55.42 In any event, by 24 June 2015 it was known by senior management that approval for the scheme had lapsed and that the intended review had not taken place.<sup>3030</sup> In his oral evidence to the Inquiry, Dr McCormick accepted that he did not test sufficiently whether the system of assurance statements (and the operation of Internal Audit, considered later in this chapter)

3024 DFE-277245

3025 DFE-277253

3026 DFE-277251

3027 DFE-277239

3028 DFE-394651 to DFE-394660 at DFE-394660

3029 WIT-19060 to WIT-19061; DFE-146867 to DFE-146870

3030 DFE-279565 to DFE-279570

which on their face were good processes, were actually working, but rather “assumed a bit much” that these were indeed robust processes on the basis of his expectation that lessons had been learned from previous difficulties.<sup>3031</sup> He later observed, principally in relation to the system of risk management, but also more generally – and correctly in the Inquiry’s view – that it is “not enough to have a system; you have to continually apply it. It’s the continuous present application of stress-testing” which is required.<sup>3032</sup>

### Risk management

- 55.43 In terms of risk management within DETI, risks could be raised by officials with senior managers either when reporting on progress against targets contained in the Operating Plan or when completing six-monthly assurance statements, or both. Indeed, Mr Thomson explained that the six-monthly assurance statements were an important source document for keeping the departmental risk register up to date.<sup>3033</sup>
- 55.44 In addition, there was an exercise within the Department, initially on a quarterly basis but becoming half-yearly in 2011, to gather ‘key divisional risks’ and to update risk registers held at both divisional and at departmental (corporate) level. Mr Thomson explained that “those [risks] which were considered as having a high or medium impact or a high likelihood of occurrence were reported to the Departmental Board.”<sup>3034</sup>
- 55.45 Risk registers existed within DETI at a number of levels in the organisation: there was a single corporate risk register (which would have been the one used at the Departmental Board), divisional risk registers and branch risk registers. Also, there were risk registers for individual projects and, as noted elsewhere in this Report, an initial risk register for the RHI scheme was created in 2012 but never updated and the risks it articulated were never translated into any of the mainstream risk registers in the Department. In his evidence, Dr McCormick described “having a risk register that is kept alive and is observed and checked” as one of the “obvious things” that should have been in place.<sup>3035</sup>
- 55.46 As to why the risks of the RHI scheme were not flagged during his time at DETI, Mr Sterling said:
- “... I can’t explain satisfactorily why the risks that were inherent in this project weren’t managed and monitored more frequently and, indeed, escalated to the divisional risk register and, in due course, to the corporate risk register.”<sup>3036</sup>
- 55.47 The Energy Division risk register of autumn 2013, for example, could have been a place to identify some of the key risks of the scheme. However, the nearest reference in it to the risk of something going wrong in respect of RHI was “Failure to develop a coherent heat policy for NI.”<sup>3037</sup> Mr Sterling accepted that there should have been more specific recording of RHI risks on the Energy Division risk register: “Given the novelty of the scheme and the fact that it was an incentive based scheme, there should have been a risk on the divisional risk register...”.<sup>3038</sup> He also accepted that the process did not work on this occasion and that it

3031 TRA-12046 to TRA-12050; TRA-12057

3032 TRA-12058 to TRA-12059

3033 WIT-13520

3034 WIT-13519

3035 TRA-12058

3036 TRA-06146

3037 DFE-399110

3038 TRA-06805

did not do what was intended, although his view was that this was less to do with the design of the risk system and tended more towards those whose responsibility it was to identify and escalate the risk.<sup>3039</sup>

- 55.48 Referring to the escalation of risks within the Department, Mr Sterling told the Inquiry that “no particular risks were flagged to me in regard to the RHI during the period from when it was set up until I left in 2014.”<sup>3040</sup> He said that risk was taken seriously in the Department during his time as Permanent Secretary.<sup>3041</sup> Referring to minutes of Departmental Board meetings between 2012 and 2014 he told the Inquiry that, at “pretty much every meeting there was a discussion about risk and ... new corporate risks were brought forward. As we saw the risks being managed, they then were relegated down to departmental risks again.”<sup>3042</sup>
- 55.49 As it happens, Ms Hepper attended the Departmental Board on 25 April 2012. This was part of a routine arrangement whereby heads of division were invited on occasions to the Board. Mr Sterling told the Inquiry he thought that such attendances by heads of division were “a good control...a good opportunity for the board to challenge heads of division over the extent to which they were managing risk and their assessment of risk in their particular area.”<sup>3043</sup>
- 55.50 Ms Hepper presented a paper to the Board with an overview of Energy Division risks rated as either high impact/high likelihood or medium impact/high likelihood at quarter end 31 March 2012.<sup>3044</sup> The RHI scheme was referenced briefly in her paper in the context of a concern about possible future failure to meet the target of 10% renewable heat by 2020. The paper stated: “high take up of the Renewable Heat Incentive will be needed to help attain the target – and at this early stage this is an unknown.”<sup>3045</sup> Of course, at that time, the RHI scheme was still in development and had not been launched. The practice of inviting divisional heads to attend the departmental board in order to explore and discuss divisional risks seems a laudable one. That said, it was not intended to be, nor could it have been, a replacement for the other risk reporting mechanisms discussed above.
- 55.51 By way of an example, any one of these reporting mechanisms – the Operating Plan, the six-monthly assurance statement process or the divisional and corporate risk register system – could have been a channel in 2013 to flag up CEPA’s assessment at that time that the Department was unlikely to meet the 2011-15 Programme for Government target of 10% renewable heat by 2020. Mr Sterling told the Inquiry that he could not recall being specifically alerted to the CEPA assessment. The Programme for Government progress reports submitted by DETI in late 2013 and early 2014 also did not reflect the concerns raised by CEPA, notwithstanding the fact (which the Inquiry notes) that meeting the 10% target had been at the core of the original justification for the NI RHI scheme.<sup>3046</sup>
- 55.52 Mr Sterling was asked in oral evidence whether, in so far as things did go wrong with the RHI scheme in its early stages, it was because the Department’s systems and procedures were deficient or because the systems were good systems but were not used or applied properly, or

3039 TRA-06146

3040 TRA-06107 to TRA-06108

3041 TRA-06145

3042 TRA-06145

3043 TRA-06146

3044 DFE-181165 to DFE-181168

3045 DFE-181166

3046 TRA-06103 to TRA-06104; DFE-417681; DFE-417690 to DFE-417691

whether it was a mix of both. Mr Sterling replied, “I think my analysis would be it was probably a mix of both.”<sup>3047</sup>

55.53 Mr Stewart was also asked about a range of issues with the RHI scheme that did not come to his attention through these systems. He said:

“...I think all of the permanent secretaries and all of the deputy secretaries who have given evidence to you have stressed that our role is of [sic] designers and overseers of systems rather than day-to-day managers. The corollary of that is, where the system isn’t good enough, then that’s a responsibility that I have to accept. Yes, I might’ve have been alerted to look at that [referring to data sharing issues and the absence of a joint DETI/OFGEM project board] by people escalating unresolved issues to me, and, if that didn’t happen, then, yes, that’s a mistake, and it’s something that should’ve happened. Equally, I have to accept, and the Audit Office has made this criticism, that I could’ve been proactive and could’ve been more curious and could’ve looked systematically across policy group to see whether we had the correct systems in place and were correctly being operated [sic] and I didn’t do so.”<sup>3048</sup>

## Internal Audit

### Internal Audit and the RHI 2011-14

55.54 As mentioned above, systems of internal control in Northern Ireland’s Government are intended to pick up problems early and to assure senior managers and the Permanent Secretary that activity is being managed in the Department according to the agreed rules and practices. Yet such systems can themselves contain weaknesses, either by design or in the way they are used. A Department’s Internal Audit function exists primarily to help overcome these weaknesses.

55.55 DETI had a small Internal Audit team that ranged across the Department undertaking work against an audit strategy and an annual plan, both agreed with the Permanent Secretary and with DETI’s Audit Committee. The first detailed Internal Audit report into the non-domestic NI RHI scheme was completed in May 2016.<sup>3049</sup> This was almost five years after Ms Hepper first informed Internal Audit in August 2011 about the NI RHI scheme as part of a wider discussion on the work of Energy Division’s teams.<sup>3050</sup> The Inquiry sought to understand why this important part of DETI’s governance system did not focus on RHI sooner, particularly given the novel nature of the scheme.

55.56 Michael Woods, head of Internal Audit in DETI from August 2014 (DFE from May 2016), gave the Inquiry his definition of Internal Audit, quoting directly from ‘Public Sector Internal Audit Standards’, a publication issued by a number of public sector audit standard-setters in the UK (including DoF in Northern Ireland) in collaboration with the Chartered Institute of Internal Auditors:

“Internal auditing is an independent, objective assurance and consulting activity designed to add value and improve an organisation’s operations. It helps an organisation accomplish its objectives by bringing a systematic, disciplined

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3047 TRA-06105

3048 TRA-11565

3049 DFE-138104 to DFE-138148

3050 WIT-19438 to WIT-19439

approach to evaluate and improve the effectiveness of risk management, control and governance processes.”<sup>3051</sup>

- 55.57 He explained that, in practice, there were two approaches used by Internal Audit: a ‘systems audit review’ to look at the controls and operational environment in any given area to see that they are effective; and an ‘investigation’, which would start with an allegation or proposition where the aim would be to see if it is true or not.<sup>3052</sup> Ms Dolan, Mr Woods’ predecessor, who served as head of DETI Internal Audit between June 2010 and August 2014, also referred to the provision of ‘advice and guidance’ and to the ability of Internal Audit to undertake consultancy services at the request of management.<sup>3053</sup>
- 55.58 As well as delivering reports on specific issues or on business areas of the Department, the further significance of Internal Audit’s work within DETI lay in its responsibility to provide an ‘opinion’ at the end of the financial reporting year on the effectiveness and overall adequacy of the systems of governance, risk management and control. Ms Dolan explained that this ‘opinion’ was independent and objective: “...in support of the accounting officer’s ability to sign off the annual statement on internal control or, it subsequently became, the governance statement.”<sup>3054</sup> These statements appeared in the published annual accounts of DETI and thus formed part of the Department’s overall accountability to the Northern Ireland Assembly and to the public.
- 55.59 Both Mr Woods and Ms Dolan emphasised three core features of the status of their role within the Department: their independence; the fact that they reported to and worked closely with the Permanent Secretary and an independent chair of the Department’s Audit Committee (‘DAC’); and their ease of access to the Accounting Officer, i.e. the Permanent Secretary, to discuss the Internal Audit plan and raise any issues. Neither witness encountered any difficulties with the status of Internal Audit during their time in post.<sup>3055</sup>
- 55.60 Mr Thomson, referring in a statement to his time as head of Policy Group in DETI up to the summer of 2014, told the Inquiry:
- “Each year, Internal Audit would spend some time reviewing governance arrangements throughout the department, ensuring proper systems were in place to facilitate reporting and the provision of assurances. I do not recall any significant concerns arising from these which would have called into question the reporting and assurance processes.”<sup>3056</sup>
- 55.61 Ms Dolan explained that towards the start of her tenure she considered DETI to be “risk mature”,<sup>3057</sup> meaning that she understood risk management to be embedded throughout the Department. This assessment was made in 2011 when Ms Dolan was developing the Audit Strategy for DETI for 2011-12 to 2014-15 and is set out on page 4 of the DETI Audit Strategy,<sup>3058</sup> which was presented to the Departmental Audit Committee in October 2011.

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3051 WIT-23123 to WIT-23162

3052 TRA-15981 to TRA-15982

3053 TRA-08697

3054 TRA-08697

3055 TRA-16028; TRA-15986 to TRA-15988; WIT-19416 to WIT-19417; WIT-19420

3056 WIT-13520

3057 TRA-08711 to TRA-08712

3058 DFE-260838

55.62 In written representations to the Inquiry, Ms Dolan emphasised that the Government Internal Audit Standards applicable at the time required the Audit Strategy to take into account the risk maturity of the organisation. The Strategy was based on management’s assessment of risk. In practice, this meant that Ms Dolan relied on each business area accurately completing risk registers and escalating risk; and where that was not done she expected management to convey risks to her and the Internal Audit team outside the formal risk management and assurance reporting processes.<sup>3059</sup> The Audit Strategy was also approved by the Permanent Secretary as Accounting Officer and endorsed by the Audit Committee.

55.63 On being questioned as to how Internal Audit could know about a set of risks if, for example, a project risk register had not been updated after its initial creation (as was effectively the case for RHI), Ms Dolan told the Inquiry:

“In terms of knowing that there was a risk in a particular project that hadn’t made its way onto the risk register, we would only know that when we would go in and do an audit of that business area and, potentially, we would identify that risk.”<sup>3060</sup>

55.64 In practice, although there were several occasions up to the summer of 2014 when the Internal Audit team and process touched on the RHI scheme, the first reference to the RHI scheme in an annual statement was in DETI’s resource accounts for 2014-15, published on 3 July 2015,<sup>3061</sup> by which time the governance statement included a reference to the fact that the Department was “currently working to address governance and financial requirement issues arising with the scheme” (a reference considered earlier in this chapter, and earlier in this Report).<sup>3062</sup>

55.65 No systems audit of Renewable Heat Branch business and no divisional review of the energy policy area took place during Ms Dolan’s tenure as head of Internal Audit.

55.66 The likelihood of a systems audit happening was reduced by the method used at the time to select audit topics. Ms Dolan told the Inquiry that, with the agreement of the Permanent Secretary and the Chair of the Departmental Audit Committee, Internal Audit prioritised ‘thematic reviews’ to test the degree to which project management and risk management were being applied across the Department. This focus was influenced by a desire on the part of both Ms Dolan and the Permanent Secretary to improve the way projects and risks were managed in the Department:

“I think the previous plans in the Department would’ve been very much branch-by-branch reviews, where I adopted a more thematic approach. So, I tried to do more horizontal reviews to give the accounting officer an assurance over a particular risk across the organisation rather than doing a number of individual branch, deep-dive reviews. So, that was different.”<sup>3063</sup>

55.67 Thematic reviews of project management were conducted for three successive years, and in the third such review, 2013-14, even though the RHI scheme was included in the field work in January/February 2014, no problems were picked up. Ms Dolan in her oral evidence agreed that, although a focus of this work was on payments, the absence of formal project management structures for the NI RHI scheme should have been picked up by this review and

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3059 TRA-08718

3060 TRA-08717

3061 DFE-04640 to DFE-04745

3062 DFE-04691

3063 TRA-08719

the reason this did not happen was most likely because the auditor at the time took the view “that Ofgem were responsible for monitoring and the programme management arrangements weren’t considered any further”; in effect, that Ofgem were managing the project and had it covered. No professional scepticism was applied to pursue the issue any further.<sup>3064</sup>

- 55.68 As mentioned earlier, when meeting Ms Dolan in August 2011 about Energy Division branches in general, Ms Hepper had mentioned the nascent RHI scheme. A follow-up meeting took place shortly afterwards between an Internal Audit team member and Mr Hutchinson, and a similar meeting subsequently took place between an Internal Audit team member and both Ms McCutcheon and Mr Hutchinson where a number of topics were discussed, including the administrative agreement and operating and development costs for Ofgem.<sup>3065</sup>
- 55.69 In November/December 2012, Renewable Heat Branch officials were back in touch with Internal Audit to seek advice and guidance on the issue of audit access to Ofgem’s delivery of the scheme. Ms Dolan told the Inquiry that their “starting point was full audit access should be built into the agreement” but “it soon became apparent, I think, that full audit access was not an option and that, therefore, a workaround was required.”<sup>3066</sup> She explained that if DETI’s own Internal Audit could not provide assurance then Ofgem’s Internal Audit would have to do so, but DETI should be able to feed into the scope of Ofgem’s audit reviews and see the outcomes of those reviews and take any follow-up action necessary.<sup>3067</sup>
- 55.70 Although she commented on the draft of the Arrangements between DETI and Ofgem as far as it related to audit, Ms Dolan told the Inquiry that she never saw the final version that contained some textual amendments put forward by Ofgem to the original DETI draft dealing with the audit activity undertaken by Deloitte/AEA for Ofgem, including the removal of the word “consult” with DETI and substitution of the word “communicate”.<sup>3068</sup> More significantly, she also said that she was not aware that DETI was never subsequently asked by Ofgem to contribute to the terms of reference of any audit review of Ofgem’s administration of RHI, nor was it shown the outcomes of any such reviews, let alone the reports. Asked if this left a gap in the audit coverage of Ofgem Ms Dolan said: “Yes. It left a gap in the monitoring arrangements by the business area in the Department.”<sup>3069</sup>
- 55.71 In the DETI Audit Strategy agreed by the Permanent Secretary and the Departmental Audit Committee, Ms Dolan had highlighted a number of risk factors that would be considered in audit planning for the period 2011-14. One of those was the use of external delivery organisations (known as ‘EDOs’) to deliver part of DETI’s business.<sup>3070</sup> The strategy stated:

“The use of EDOs poses a risk to the Department that funds may not be used for the purposes intended and therefore it is fundamental that adequate oversight arrangements are in place including the monitoring of governance and accountability of EDOs. As a result, Internal Audit coverage of sponsor control arrangements and governance and controls reviews of EDOs are built into the DETI (and other) strategies annually.”<sup>3071</sup>

3064 TRA-08776; TRA-08779; TRA-08782

3065 WIT-19438 to WIT-19440

3066 TRA-08747

3067 TRA-08749

3068 TRA-08752 to TRA-08753

3069 TRA-08756

3070 DFE-260833 to DFE-260884

3071 DFE-260845

- 55.72 Ms Dolan explained that, in using an EDO, a Department “relinquishes part of the control that it has around funds” and the reasons such inspections of EDOs had been introduced went back to issues raised by the NIAO in 2003.<sup>3072</sup> An EDO inspection had two parts: first, there would be an audit of the EDO itself and the arrangements between DETI and the EDO; and, second, audit of the oversight arrangements within DETI, referred to as the ‘sponsor control arrangements’.<sup>3073</sup>
- 55.73 Ofgem was initially classified as an EDO. Accordingly, its administration of the RHI scheme and the sponsor arrangements within Renewable Heat Branch were candidates for an audit in the 2013-14 audit plan, but the Inquiry heard that no such audit took place during the life of the scheme. Ms Dolan explained that, initially, the audit was deferred to 2014-15 for several reasons, including that the scheme had only recently commenced and, mindful that audit work on EDOs was to be sub-contracted, given that only one EDO (Ofgem) had been put forward, there was a case for deferral on the grounds there would be more work to tender in the following year.<sup>3074</sup>
- 55.74 Ms Dolan also told the Inquiry that she thought at the time that the audit approach might not be suitable for Ofgem as a non-ministerial Government Department and that she was aware of discussions about using a different audit approach in circumstances where public sector bodies took on delivery of DETI’s policies. In this alternative approach the Accounting Officer of that delivery body would be asked to sign an assurance about governance arrangements, although this was not something that was introduced while she was in post.<sup>3075</sup>
- 55.75 The Inquiry notes that there clearly was a plan of sorts by DETI to introduce this type of arrangement with Ofgem, as such an intent was noted in section 8 of the Energy Division’s ‘Checklist for 6 monthly assurance statement on internal control’ dated September 2014 and April 2015.<sup>3076</sup> Both documents stated “Annual assurance statement to be provided by Ofgem for administration of the non-domestic RHI scheme.” However, the Inquiry saw no evidence that this was followed through during the life of the scheme.
- 55.76 In her statement to the Inquiry Ms Dolan explained that in March 2014 she wrote to the Permanent Secretary requesting a meeting about the audit plan for 2014-15 and that in the email, amongst other things, she proposed cancelling the EDO review “as we have been advised by management that DETI currently has no EDOs”. On 28 May 2014, the audit plan for 2014-15 was agreed by the Departmental Audit Committee and the EDO review was cancelled.<sup>3077</sup> The minutes do not record any detail of discussion of the audit plan.<sup>3078</sup>
- 55.77 Ms Dolan could not explain to the Inquiry how the ‘carry forward’ of the review of Ofgem was lost. She told the Inquiry it was management’s responsibility to identify EDOs and she thought that the audit would have taken place in 2014-15 if Ofgem had still been considered an EDO, “but as to why Ofgem’s not identified as an EDO, I can’t answer that question.”<sup>3079</sup> The Inquiry considers this was a lost opportunity to audit Ofgem’s role administering the RHI scheme and to review the Renewable Heat Branch’s sponsorship of Ofgem.

3072 TRA-08798 to TRA-08799

3073 TRA-08799

3074 TRA-08801 to TRA-08802

3075 TRA-08801 to TRA-08804

3076 DFE-388318; DFE-388384

3077 WIT-19445

3078 DFE-394024 to DFE-394026

3079 TRA-08806 to TRA-08810

## Internal Audit and the RHI 2014-16

- 55.78 As noted above, Michael Woods succeeded Ms Dolan as DETI's Head of Internal Audit in the summer of 2014. During his oral evidence he told the Inquiry that in respect of the RHI scheme at that point "there was no information in terms of the audit strategy, nor the audit plan, nor in the departmental risk register."<sup>3080</sup> Unaware of the RHI at the start, but taking a look across the Department as a whole, he undertook an audit needs assessment to identify key risks. This exercise was needed anyway as the audit strategy had run its three-year course and a plan was required for 2015-16.<sup>3081</sup>
- 55.79 Mr Woods used, but did not rely on, the risk assessments that had worked their way into the corporate risk register. However, he also told the Inquiry that it can be problematic for an Internal Audit strategy to place too much reliance on risk registers that are drawn up by management.<sup>3082</sup> He therefore sought to triangulate information from the risk registers with other information from DETI Finance and from discussions with officials.<sup>3083</sup>
- 55.80 By early January 2015 Mr Woods had concluded that the RHI scheme should be subject to an audit for three reasons: it relied on an external delivery organisation; the projected size of the budget in 2015-16; and the fact that the scheme had been in place since 2012 and had yet to be subject to a systems audit.<sup>3084</sup> But he also said to the Inquiry: "I was told nothing about any problems with the scheme."<sup>3085</sup> The audit plan, including the proposal for an audit of the non-domestic RHI scheme to commence in early 2016, was approved by Dr McCormick, the Permanent Secretary, on 21 April 2015 and by the Departmental Audit Committee at its meeting on 1 June 2015, a meeting attended by Dr McCormick, Mr Cooper and Mr Rooney.<sup>3086</sup>
- 55.81 The Inquiry asked Mr Woods whether he thought the audit of the RHI should have been done earlier. Mr Woods agreed it should have been brought forward to the summer of 2015 and that information available to others in the Department at that time, had it been conveyed to him, would have caused him to ask searching questions.<sup>3087</sup> He said that, "If the response to those questions had've been say, less than perfect, I probably would've had sufficient concern to bring the audit forward."<sup>3088</sup>
- 55.82 In his oral evidence referring to the system of Internal Audit, Dr McCormick indicated that the Head of Internal Audit's direct access to him was another means of assurance to him as Permanent Secretary and Accounting Officer. However, in the case of the non-domestic RHI scheme, he said that this "didn't help because there was no transmission of a concern or risk to him [Mr Woods], so, therefore, it wasn't picked up."<sup>3089</sup> He went on to say that, in this regard, "Something wasn't getting through..." and that "there's a lot more that could have been done."<sup>3090</sup>

3080 TRA-15995

3081 TRA-15996

3082 TRA-15990 to TRA-15991

3083 TRA-15991 to TRA-15992

3084 TRA-16002 to TRA-16004

3085 TRA-16004

3086 DFE-390825 to DFE-390839; TRA-16010; DFE-279551 to DFE-279564

3087 TRA-16023 to TRA-16024; TRA-16035; TRA-16043

3088 TRA-16035

3089 TRA-12050

3090 TRA-12050

55.83 Mr Cooper stated in written evidence to the Inquiry that, in a senior management meeting on 29 May 2015, he had identified control issues with the scheme during an exchange of views with Mr Mills.<sup>3091</sup> Mr Woods had not been present at that meeting. As mentioned earlier, Mr Woods, Mr Cooper, Dr McCormick and Mr Rooney were, however, amongst those who attended a meeting of the Departmental Audit Committee on 1 June 2015. The minutes of that meeting do not record Mr Cooper (or anyone else) raising any issue as to control with regard to the RHI scheme.<sup>3092</sup> The only reference to RHI in the minutes referred to approvals for 2015-16 commitments and budget pressures due to high levels of forecast demand.<sup>3093</sup> Mr Woods told the Inquiry he could not recall anyone saying anything about control issues:

“...if somebody had said, ‘This is a result of lack of controls’, that’d have been totally different. I would’ve gone, ‘Well, hold on a second. There’s no point getting more budget if we don’t fix the hole in the roof’. That wasn’t what I understood and it wasn’t what I was told.”<sup>3094</sup>

He told the Inquiry that he probably would have insisted on bringing the audit forwards had he been told that the scheme lacked controls.<sup>3095</sup>

55.84 Nor does it appear that Mr Woods was informed that, on 3 June, Mr Cooper had told the Chair of the DAC, David Beck, and another independent member, Claire Hughes, about the absence of a tiered tariff as compared with the GB RHI scheme, that the scheme was over its AME budget, with potential for a 5% penalty, and his belief that demand was being driven by the poultry sector.<sup>3096</sup>

55.85 As discussed previously in this Report, on 17 June 2015, in a further RHI meeting involving senior officials, Mr Cooper mentioned overcompensation and possible breach of State Aid as issues with the RHI scheme. Mr Cooper did not convey these concerns to Mr Woods, who would not have been present at the meeting.<sup>3097</sup> According to Mr Cooper’s written evidence, he and Shane Murphy considered that the best approach could be to do a quick review of the whole scheme, including a detailed review of the tariffs payable under each technology. This idea was put forward at the meeting on 17 June 2015 by Mr Murphy, but was discounted. Mr Cooper’s view was that this was on the basis that the Permanent Secretary wanted amendments made as quickly as possible and that any changes beyond the introduction of tiering would take a long time to do.<sup>3098</sup> This suggestion for a quick review also does not appear to have been conveyed to Mr Woods nor, according to the minutes of the DAC, was it raised at its meeting of 24 June.<sup>3099</sup>

55.86 As alluded to in the previous paragraph, the DAC met for a second time in the same month on 24 June 2015 (their earlier meeting having been on 1 June). The minutes of the meeting of 24 June show that Mr Cooper was recorded as saying that financial and governance issues had emerged with the RHI scheme and that DETI was currently engaging with DFP on reapproval

3091 WIT-19055 to WIT-19056

3092 DFE-395329 to DFE-395342

3093 DFE-395336

3094 TRA-16027

3095 TRA-16028 to TRA-16034

3096 WIT-18553 to WIT-18554

3097 TRA-16024 to TRA-16038

3098 WIT-18544

3099 DFE-394720 to DFE-394725

and the budget for 2015-16.<sup>3100</sup> At the end of September, when the DAC met again, Mr Cooper updated the meeting, recording that the issue with RHI was a budget and an approval one.<sup>3101</sup> Mr Woods was present at all of these DAC meetings but, as the minutes suggest, his recollection is that none of the wider concerns that Mr Cooper has told the Inquiry he was expressing elsewhere were mentioned. Mr Cooper accepted that if Mr Woods was saying that was what occurred, and those matters were not mentioned, it was difficult for him (Mr Cooper) to contradict him.<sup>3102</sup> Mr Woods told the Inquiry that he believed such concerns should have been raised.<sup>3103</sup> When he was asked why this did not happen, Mr Woods said:

“The only thing I can think about is that people were so fixated on a solution that any information contrary...to that solution was ignored...So, the conception was it’s a budgetary problem, we’ll solve a budgetary problem. I think if we’d stepped outside the problem and said ‘Exactly why is this happening?’, then perhaps we would’ve understood it better and then, therefore, the solution could’ve been better.”<sup>3104</sup>

55.87 In one of his written statements of evidence to the Inquiry Mr Cooper stated that, following the unprecedented spike in applications to the non-domestic RHI scheme in October 2015, “the potential for abuse of the scheme came into focus.”<sup>3105</sup> He said that in mid-November he discussed the spike with Mr Woods and asked Mr Wightman to clarify the position.<sup>3106</sup> On 18 November Mr Cooper forwarded to Mr Woods an email that he had received from Mr Wightman on the previous day. That email, under the heading “Future Changes”, contained the following:

“It is worth highlighting that Michael’s team are to audit the Non Domestic RHI Scheme in the New Year which provides an opportunity to review Ofgem’s current system of checks.

We also hope to legislate to introduce an annual cap on maximum heat for existing installations although this will be very contentious and will require public consultation. This will help minimise the risk of boilers being run just to generate RHI income.”<sup>3107</sup>

55.88 At the DAC meeting on 2 December 2015 it was agreed, arising from the views expressed by Mr Woods, that although the audit of the domestic RHI had commenced, it would be halted and the audit of the non-domestic RHI would commence urgently in light of the issues that had arisen.<sup>3108</sup>

55.89 When asked whether a systems audit of the RHI could have been done much earlier, for example at the start of the scheme or even before it went live, Mr Woods agreed it was possible and was something that should have been done with the RHI scheme and had been done with some other projects or schemes. He gave the example of Internal Audit’s work on testing the adequacy of design of the ‘Gas to the West’ project, work that had included: advising for about

3100 DFE-394723

3101 DFE-394846 to DFE-394856 at DFE-394848

3102 TRA-15962

3103 TRA-16041 to TRA-16043

3104 TRA-16048

3105 WIT-18547

3106 WIT-18547

3107 WIT-18830 to WIT-18831

3108 DFE-289104 to DFE-289114

a year and a half; reviewing the letter of offer; testing the robustness of the business case; and how it was proposed to control the scheme.<sup>3109</sup>

- 55.90 In the event, the first full engagement of Internal Audit with the non-domestic RHI scheme took place in early 2016 and the audit report was completed and submitted to management in DETI on 19 May 2016.<sup>3110</sup> The report concluded that “the system of risk management, control and governance established by management over the ... Scheme is unacceptable.”<sup>3111</sup> Mr Woods described it to the Inquiry as the worst opinion he had ever had to give in over 500 systems audits.<sup>3112</sup>

### Janette O’Hagan emails and Internal Audit

- 55.91 Janette O’Hagan’s interactions with DETI have been dealt with in detail in chapter 23 of this Report, but her interventions also have some significance in the context of the role of Internal Audit, in particular a possible role for it in investigating issues such as those raised by Ms O’Hagan.
- 55.92 In relation to the email communication from Ms O’Hagan that arrived in DETI in October 2013, Ms Dolan told the Inquiry that Internal Audit and senior managers should have been made aware:

“I think some of the concerns were around misuse of the scheme and the scheme not necessarily being used for the purposes intended. And to me that’s indication that there’s an irregularity, and the DETI guidance at the time, the fraud response plan, and also the internal audit charter would’ve highlighted that any suspicions of irregularity should be reported immediately to the head of internal audit.”<sup>3113</sup>

She also considered that, whether or not officials believed the allegations, they should still have forwarded them on.<sup>3114</sup>

- 55.93 Mr Woods told the Inquiry that he first became aware of Ms O’Hagan’s emails in September 2016. He was particularly critical of the fact that these emails were not drawn to his attention during the work on the Internal Audit review in early 2016. But he also believed they should have been shown to him in 2015 when he was working on the audit plan and at the very least, given DETI’s anti-fraud policy, Internal Audit should have been consulted when the emails were received.<sup>3115</sup>

### Quality of policy advice to Ministers

- 55.94 As appears throughout this Report, the Inquiry has examined in depth the quality of advice provided to Ministers in DETI that formed the basis on which Minister Foster and subsequently Minister Bell took decisions in relation to the NI RHI scheme. The Inquiry has also examined advice used in support of other decision-making processes, such as that presented to the DETI Casework Committees and in the business cases presented to DFP for approval. In the course of that examination, shortcomings, omissions and errors in the advice have been identified and are set out in detail in previous chapters of this Report. A number are noted below:

3109 TRA-16015; see also TRA-16009 to TRA-16010

3110 WIT-23200 to WIT-23244

3111 WIT-23215

3112 TRA-16069 to TRA-16071

3113 TRA-08813

3114 TRA-08816

3115 TRA-16082 to TRA-16083; TRA-16022

- The submission to Minister Foster of 8 June 2011<sup>3116</sup> contained a potentially misleading statement regarding the NI RHI option, namely, that it offered “... the highest potential renewable heat output at the best value.”<sup>3117</sup>
- In turn, the potentially misleading assertion, first contained in the 8 June 2011 submission, that “the NI RHI produced the most heat at the best value” was repeated on a number of occasions, without the qualification that this was restricted to a comparison with the GB RHI scheme. Examples include regulatory impact assessments and SL1 letters, both of which invited a ministerial signature.
- The submission to Minister Foster of 5 July 2011 failed to highlight the very significant changes that had been made in the CEPA final report of June 2011 since the earlier draft of that report of 31 May 2011, upon which the submission of 8 June had been based.
- The submission to Minister Foster of March 2012 contained the erroneous statement that tiering of the tariff was not included in the NI RHI scheme because in each instance the subsidy rate was lower than the incremental fuel cost.
- The submission to Minister Foster of March 2012 also omitted to inform the Minister that the lifetime subsidy costs of the scheme had risen from £334 million to £445 million between CEPA’s final report of June 2011 and its Addendum of February 2012.
- Incomplete and/or inaccurate information was provided to the Casework Committee in March 2012 on the full lifetime costs of the different schemes. The evidence base for comparing the administration costs of a Challenge Fund and the NI RHI scheme was not well founded.
- A variety of ministerial submissions, although perhaps most notably the submission to Minister Bell of 8 July 2015, failed to make clear the unusual nature of the funding for the NI RHI scheme and the potential DEL consequences of overspend.
- The submission to Minister Bell of 8 July 2015 also inaccurately proposed tiering as the chief mitigation to contain the overall NI RHI budget.
- In the same 8 July 2015 submission, the earlier Phase 2 proposals and 2013 consultation were represented as constituting compliance with the 2012 DFP condition for review of the non-domestic RHI scheme. This was incorrect and misleading.
- The October 2015 Business Case Addendum contained numerous errors and omissions. In particular, there was an inadequate evidence base for the claim that the scheme represented “continuous and continuing value for money.”

55.95 Mr Sterling explained that one of his three roles as Permanent Secretary was to be the principal adviser to the departmental Minister but explained that this responsibility was discharged through a system of management within the Department:

“Although I am the Minister’s principal advisor with ultimate responsibility for all advice provided by the Department, I discharge that responsibility by ensuring that processes and internal controls are in place for officials to provide advice on my behalf. On any given issue I will seek to ensure that it is clear to the Minister that there is lead official [sic] who will be responsible for providing advice on the

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3116 WIT-00739 to WIT-00749

3117 WIT-00744

relevant issue. The lead official will normally be the head of the relevant division and almost always a member of the Senior Civil Service (SCS) ie an assistant secretary or above. The lead official will normally be supported by an appropriate team including specialist advice if this is considered necessary. It is then the role of the lead official to take responsibility for the advice provided to the Minister. This does not diminish my ultimate personal responsibility...”.<sup>3118</sup>

55.96 Dr McCormick also accepted that it was his responsibility as Permanent Secretary to ensure that the advice which went to the Minister was fair, accurate and comprehensive, although it is not and never has been a Permanent Secretary’s role to deal with the detailed technical aspects.<sup>3119</sup>

55.97 Mr Sterling, when asked about the ‘processes and internal controls’ on which he relied to ensure objective and reliable advice was given to the Minister, explained “it would largely be about people” and about the “element of supervision” provided by the official at grade 5 level “so what goes to the Minister is fit for purpose.”<sup>3120</sup> He made the general point:

“I would generally have had confidence in the teams working across the Department that they would have produced quality advice or, if there was an issue of particular concern, they would’ve known to come to me. And that was borne out of the fact that, as I say, we worked pretty closely together, we had a Minister that we knew, Minister and adviser that we knew very well. These things didn’t need, sort of, a great deal of formality to them.”<sup>3121</sup>

55.98 He described the team responsible for the NI RHI as:

“...a group of people who were competent in many ways but not specialist in their areas – well, that would be characteristic of many teams that we have, not just in what was then DETI and now DFE but across the Northern Ireland Civil Service.”<sup>3122</sup>

55.99 The team though, he acknowledged, was under pressure, had resource issues and did not have sufficient capacity or competence on the technical aspects of the scheme; that was why on several occasions they had obtained his and the Minister’s approval to use consultants (respectively AECOM/Pöyry and CEPA). Looking back, Mr Sterling observed that while the team at the time felt they were managing the consultants well, the experience of the NI RHI scheme had led him to reflect that “there is probably a case for having had that additional expertise to allow the team to properly manage the consultants.”<sup>3123</sup>

55.100 Mr Sterling cited two further processes on which he relied: the establishment in 2010 of the Analytical Support Unit, which has been referred to previously in this Report. The ASU comprised economists and statisticians, as a source of ‘specialist advice’ for those preparing submissions; and ‘an element of feedback’ from the Minister.<sup>3124</sup> He told the Inquiry “I took comfort from the fact that a departmental economist had looked at the scheme with a view to

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3118 WIT-04018 to WIT-04019

3119 TRA-12021 to TRA-12022

3120 TRA-06077 to TRA-06078

3121 TRA-06141

3122 TRA-06083

3123 TRA-06105

3124 TRA-06078

determining whether it was going to provide value for money.”<sup>3125</sup> He had noted the evidence given to the Inquiry by the economist Mr Connolly however, and said he would still like to understand why Mr Connolly had not felt able at the time to raise his concerns.<sup>3126</sup>

55.101 On the question of feedback from Minister Foster on submissions from Energy Division, Mr Sterling said “I think the view I would have got from the Minister and Special Adviser is: the advice we get is thorough, comprehensive, perhaps too long,” and although there would have been requests from time to time to make submissions a little shorter, Mr Sterling did not consider this to have been a major issue.<sup>3127</sup> He added:

“But I would just say, generally, the quality of submissions coming from energy division would have been regarded as probably the best in the Department.”<sup>3128</sup>

55.102 Mr Sterling considered that the broad system that applied in DETI would have been no different from that of all the Departments where he had previously worked and he believed the approach to providing advice to Ministers “is pretty consistent” across all Departments.<sup>3129</sup> When asked for his overall view of that system he said it was “generally sound”.<sup>3130</sup> In further representations to the Inquiry however, Mr Sterling made clear that he considered that there were shortcomings in some of the advice received by the Minister about RHI and accepted that the system failed to operate in order to prevent such shortcomings. He emphasised that, while believing the control system was generally sound, the application of the control system for ensuring that the Minister received good advice about RHI was deficient.

55.103 One aspect of the system of provision of advice to the Minister which the Inquiry noted was that ministerial submissions were routinely copied to a wide range of officials, often including the Permanent Secretary. It was not anticipated that the Permanent Secretary would read all of the submissions crossing his desk, and certainly not in any detail, other than those formally requiring the Permanent Secretary’s sign-off;<sup>3131</sup> and Mr Sterling firmly disavowed any suggestion that the authors of such submissions would have taken any reassurance from the fact that he had been copied into a submission. He said that:

“...nobody who was regularly submitting submissions to the Minister could have reasonably concluded that I was going to check their homework; that was not the purpose of me being copied in.”<sup>3132</sup>

55.104 There was a provision within the Private Office Guidance in force within DETI which suggested that some submissions did require to be ‘pre-cleared’ with the Permanent Secretary, in terms to the effect that:

“The Permanent Secretary must have been consulted on policy proposals which have major resource implications, raise Accounting Officer issues, or have Machinery of Government implications before a submission is sent to the Minister.”

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3125 TRA-06105

3126 TRA-06105 to TRA-06106

3127 TRA-06078 to TRA-06079

3128 TRA-06079

3129 TRA-06080

3130 TRA-06080

3131 TRA-06131 to TRA-06132; TRA-06135

3132 TRA-06135

55.105 Mr Sterling’s evidence was that there was no formal guidance given to civil servants as to when these thresholds would be met. Rather, the process was more informal: he would have been aware of sensitive issues through ongoing communication; and more junior civil servants within the Department “would just have known what were the issues where it would be sensible to take my mind.”<sup>3133</sup> Mr Sterling’s “general point” in this regard was that he:

“Would generally have had confidence in the teams working across the Departments that they would have produced quality advice or, if there was an issue of particular concern, they would’ve known to come to me.”<sup>3134</sup>

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3133 TRA-06140 to TRA-06141

3134 TRA-06141

## Findings

313. DETI's internal governance systems failed over four years as a conduit to deliver important information to senior management about the flaws and mounting risks of the NI RHI scheme. The systems were not fit for purpose where RHI was concerned. Responsibility for this must rest with DETI/DfE's successive Permanent Secretaries/Accounting Officers: Mr Sterling and Dr McCormick.
314. When, in the summer of 2015, mounting concerns about the scheme's finances were expressed in stark terms by Mr Mills and Mr Stewart using the assurance statement system, the governance statement signed by the Permanent Secretary and given to the Departmental Audit Committee was comparatively muted. The Inquiry recognises the concern about stimulating a spike but that should not have inhibited officials from ensuring that full and accurate facts were internally communicated, particularly to the DAC and the Head of Internal Audit.
315. To the extent that the failure of DETI's internal governance systems in respect of the non-domestic RHI scheme was caused or contributed to by reluctance on the part of officials to report potential problems to line managers, in particular where those officials were attempting to address the problems in question, the Inquiry finds that such reluctance reinforces the importance of the application of relevant principles of project and programme management to such schemes. The Inquiry finds that the proper application of such principles would have decreased the likelihood of potential problems going unreported through the formal governance and assurance systems.
316. It was unfortunate that the management information available to Ms Dolan, Head of Internal Audit, and her team, when preparing the DETI Audit Strategy, led to the assessment that DETI was a "risk mature" organisation. It meant in practice that between 2010 and 2014 the Internal Audit Service applied too little independent judgment and was overly reliant on information from individual branches and divisions in deciding what to include in its audits. Opportunities to scrutinise the RHI scheme as part of a project management audit and as part of an audit of external delivery organisations did not materialise, but the responsibility for decisions about the Audit Plan that led to these shortcomings must be shared with the Permanent Secretary.
317. The initial good intentions of the internal auditor, Ms Dolan, that 'full audit access' for DETI should be built into the Arrangements with Ofgem did not materialise and the agreement offered a lesser form of words. Unfortunately, Ms Dolan did not see the final wording of the Arrangements which were agreed between Ofgem and the relevant business area within DETI. In the event, DETI did not even gain access to any of the audit reports delivered by Ofgem's own auditors, nor was DETI consulted on the audit terms of reference. The implications of the Arrangements might have come to light had DETI's Internal Audit reviewed Renewable Heat Branch's use of Ofgem and Ofgem's management of the scheme. The deferral in 2013-14 and then the cancellation in 2014-15 of this audit was a significant missed opportunity to

highlight problems with implementation. The limited audit access to Ofgem provided for in the Arrangements was a further reason to seek to ensure an External Delivery Organisation audit of the arrangements with Ofgem. Responsibility for this missed opportunity must again be shared with the Permanent Secretary.

318. When in January 2015 the need became clear for the RHI scheme to be the subject of an internal audit, it took 12 months for the audit to commence. The audit of the non-domestic RHI scheme was scheduled for early 2016 and this plan was signed off by the Permanent Secretary in April 2015 and by the DAC in early June 2015. Once problems with the scheme's funding and approval came to light from early June 2015 however, it would have been open to the Permanent Secretary, or to the Senior Finance Director (Mr Rooney), or to the Director of Finance (Mr Cooper), and/or Mr Stewart at any point to have asked for the audit to be brought forward and, given what they each knew, this is what should have happened. The Inquiry cannot know what difference this would have made for certain, but given what was eventually revealed in the Internal Audit report of May 2016 it is at least possible that an earlier report might have led to better decision making in the autumn of 2015 or the beginning of 2016.
319. Whilst Mr Sterling told the Inquiry that the system for ensuring a good quality of advice to Ministers was generally sound, the Inquiry agrees with him that this was not the case as far as the RHI scheme was concerned. Indeed, the evidence suggests that further investigation could usefully be undertaken as to the reliability of this system in other areas. In relation to RHI, a range of factors discussed throughout this Report – including (although not limited to) lack of technical expertise, imprecise drafting, pressure of time and resources, and failure effectively to retain or pass on corporate knowledge – resulted in numerous mistakes and omissions being made in policy advice provided by officials. These were of significant importance and, having been made in ministerial submissions, were often repeated in later submissions or other documents used to transmit or explain decisions, thus compounding the errors. The Inquiry also finds that when, in 2015, problems with the scheme became apparent, the quality of advice to the then Minister was sub-optimal and aspects of it were unclear and inaccurate. In light of these matters, the Inquiry concludes that the system for ensuring the quality of such advice, such as it was in DETI/DfE, was not adequate.

