



**INQUIRY INTO THE RENEWABLE HEAT INCENTIVE SCHEME**

**RHI REF: DoF Supplementary Statement 3 of 2018**

**DATE: 30 May 2018**

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**Witness Statement of: EMER MORELLI**

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I, Emer Morelli, will say as follows: -

1. The solicitor to the Renewable Heat Incentive Inquiry, under cover of correspondence dated 12 February 2018, to the Department of Finance (DoF), (formerly the Department of Finance and Personnel (DFP) and hereafter referred to as the Department), has advised that the consideration of the RHI Domestic Scheme business case in 2014 will be considered as part of the overall Inquiry into the Non-Domestic RHI Scheme given that the Domestic and Non-Domestic Schemes were operationally intertwined. It is noted that the approval and the operation of the Domestic Scheme itself is outside the terms of the Inquiry.
2. This statement will set out the Department's role in the consideration, leading to the approval, of the Domestic Scheme including what Supply Division did in terms of engaging with Departmental economists and the queries raised by those economists. The documents relating to the approval of the Domestic business case demonstrate that it gave rise to a number of misconceptions and opportunities to clarify the funding available for the Non-Domestic and Domestic Schemes within the Department. As the RHI Domestic Scheme did not at that time give rise to the problems associated with the Non-Domestic Scheme these issues did not come to the fore. The Department has given careful consideration to these matters and has implemented a number of changes to



practice and procedure as set out below.

3. The Inquiry has raised a number of specific queries regarding the role of the Department in the AME forecasting process and the guidance provided by the Department to other NI departments in respect of same. This information is currently being collated and will be provided in a further statement to the Inquiry.

### **Domestic RHI Scheme Business Case - DoF Role**

4. As previously advised to the Inquiry under cover of DoF's corporate statement, the DoF role in respect of expenditure approval is set out at A.2.3 of Managing Public Money Northern Ireland (<https://www.finance-ni.gov.uk/sites/default/files/publications/dfp/a.2.3-dfp-approval-of-expenditure.pdf>).
5. The primary guidance to the completion of expenditure appraisal, evaluation, management and approval in the Northern Ireland public sector is set out within the Northern Ireland Guide to Expenditure Appraisal and Evaluation (NIGEAE) (<https://www.finance-ni.gov.uk/articles/introduction-northern-ireland-guide-expenditure-appraisal-and-evaluation-nigeae>). It reflects much the same principles as the Treasury Green Book but is tailored to suit Northern Ireland's particular circumstances.
6. The principles of appraisal apply to all decisions and proposals involving expenditure or resources. They apply equally to policies, programmes and projects. While the terms economic appraisal and business case tend to be used interchangeably, a business case is a document containing an economic appraisal plus additional information including the proposed arrangements for financing, management, marketing, procurement, monitoring and evaluation of the relevant policy, programme or project.

7. DoF consent is required for all expenditure and resource commitments. In practice, DoF delegates to departments the authority to enter into commitments and to spend within predefined limits. Where a spending decision exceeds the departmental delegated authority it must be submitted to DoF for approval. In 2014 DETI was required to seek DFP approval for any General Capital/ Programme Delivery spend over £6million. In recommending a spending decision (which will be justified through a proportionate business case) to DoF the relevant department must confirm, on behalf of the departmental Accounting Officer, that it is content with the regularity and propriety of the spending proposal, that it represents value for money for the department and that it has been reviewed by its own departmental Economists.
8. Accounting Officers are responsible for ensuring that prior DoF approval is obtained in all cases where it is needed (A.2.3.2 Managing Public Money NI).
9. On receipt of any business case from a NI department, Supply Division's primary function is to assess, on the basis of the information provided to it, whether the subject of the business case represents value for money. Within DoF, business cases from other departments are considered by the relevant Supply team within the Public Spending Directorate usually in conjunction with economists from DoF's Strategic Policy Division. The business cases are reviewed against the requirements set out within NIGEAE to determine whether the spending decision has the potential to deliver a value for money outcome. The value for money assessment is based primarily on the balance of costs, benefits and risk. This review can often be an iterative process, with queries issuing to departments. Supply has a 15 working day target to provide a meaningful response to departments, which can involve seeking additional information, approval or refusal. Approval is granted once DoF Supply and DoF SPD are satisfied that the business case contains sufficient evidence to justify the spending decision. Each case is considered on its own merits and on a stand-alone basis.



10. It is not the function of Supply Division to propose a project or programme nor to determine the policy of a project or programme. DoF will liaise with the department to consider whether the proposal has the potential to be affordable within the departmental budget. It should be noted however that the affordability of a proposal will often depend on the priority attributed to it by the spending department and therefore DoF approval relates solely to the agreement to proceed with a proposal, it does not imply approval for expenditure to be incurred beyond existing agreed public expenditure controls.

11. As was in fact the case with the Domestic business case approval letter, Supply approval letters usually contain the following form of words:

*“It should be noted that this approval relates solely to agreement to proceed with the project. It does not imply approval for expenditure to be incurred beyond existing agreed public expenditure controls”.*

12. This means that budget management is the responsibility of individual departments. That is, it is for individual departments to consider whether a project is affordable within its budget allocation and, where for example contractual commitments are entered into, these can also be managed going forward. The Department (DoF) has considered the various representations made to the Inquiry to date and the position stated above remains DoF's view.

13. DETI (Accountability and Casework Branch) submitted the business case for the RHI Domestic Scheme “the Domestic business case” to Supply Division of the Department for consideration and approval on 15 August 2014 (DOF-100001). Annexed to the Domestic business case was the NI RHI Phase 2 final report prepared by Cambridge Economic Policy Associates and Ricardo-AEA (dated June 2013). DETI additionally submitted a cover note, DFP proforma and synopsis of the Casework Committee in support of the business case.

14. It is clear from the documents now available to the Department (DFE-501268 and DFE-501271) that there was some discussion within DETI as to the need



for DFP/DoF Supply approval of the Domestic business case given that it was regarded as Phase 2 of the RHI Scheme and that DFP/DoF had already approved the total budget of £25m for the Non Domestic Phase of the Renewable Heat Incentive Scheme. In addition the Domestic Scheme appears to have been subject to internal casework which DFP/DoF did not attend.

15. In the event the Domestic business case was submitted to the Department for Supply approval.
16. This business case was recorded in Supply Division on the Information Management System (IMS) and subsequently sent to Economic Appraisal Branch (EAB) within DFP/DoF's Strategic Policy Division, for assessment, on 18 August 2014. This assessment would inform Supply Division's consideration of whether approval could ultimately issue.
17. The process outlined above was in line with the established procedure in Supply Division 1 at that time. On 1 September 2014 the EAB economists raised with Supply Division a number of concerns and queries (DOF 100210/11) arising out of its consideration of the business case including the structure of the business case, the future of the Scheme after the seven year running period, impact on wider Executive priorities including fuel poverty and lack of Net Present Value calculations. EAB specifically queried the amount of funding available including apparent discrepancies in the references to the funding available in the business case and supporting documentation.

*"It is mentioned that there is funding of £25m up to 2015/16 for the scheme and then in other places as £6.35m in 2014/15 and £9.5 in 2015/16, is this £15.85 on top of the £25m (Section 3.5)? Is there any confirmation of the funding coming to Northern Ireland - has it been agreed by CED that any Barnett consequential of GB RHI will be allocated to DETI?"*



18. EAB also queried whether Northern Ireland was committed to/or obligated to invest in the Domestic Scheme or whether the funding could be used for another purpose e.g. gas (DOF-100210/11).
19. As a consequence of the EAB queries, the Supply team proactively engaged with DETI on the business case. Supply did not raise any other issues with DETI over and above those raised by EAB. The Department accepts that the Domestic business case was not regarded as contentious or novel by DFP/DoF and was prioritised accordingly within the Supply team. The Department accepts that the Supply team relied on assurances that Supply approval was also in place for the Non-Domestic business case. DoF accepts that in not checking or challenging these assurances an opportunity to seek an update on progress in respect of earlier DFP/DoF approval requirements was missed. DoF also accepts that its own scrutiny of the case failed to identify inconsistencies in the information provided.
20. As a result of that engagement, in addition to the papers submitted to the Department on 15 August 2014, (DOF-100001-100209), a number of supporting documents were subsequently submitted to the Department on 5 September 2014, (DOF-100214-100230). It is apparent that this additional documentation was provided to Supply Division following a conversation between an official in Accountability and Casework Division of DETI and an official in the Department's Supply Division. These documents were:-
- An email from Stuart Wightman to Rachel Linton dated 4 September 2014;
  - Letter from Gregory Barker MP to Arlene Foster MLA dated 29 November 2013;
  - Letter from Arlene Foster MLA to Gregory Barker MP dated 16 December 2013;
  - Letter from Gregory Barker MP to Arlene Foster MLA dated 7 January 2014;





- An email exchange between Jon Parker and Alison Clydesdale dated April 2011; and
- AME Allocation Revised Profile.

21. The supporting documentation referenced above was provided by DETI to inform the Supply Division in its consideration of the Domestic business case and to address the queries raised by DFP/DoF. These documents were viewed solely in the context of the Domestic business case provided. Had their significance to the wider funding of the RHI been appreciated, these documents may have been shared with the Central Expenditure Division (CED) of the Department and that may have prompted CED to query the earlier Spending Review settlement letter which had been formally communicated to the NI Executive by the Chief Secretary to the Treasury on 8 July 2013, which stated:-

*“The NI Executive Annually Managed Expenditure (AME) Budget for 2015/16 remains in line with the latest Office for Budget Responsibility forecast provided by you for Budget 2013”.*

22. DoF accepts that had it recognised that there was an opportunity to clarify the funding arrangements for the RHI Scheme going forward in September 2014 with HM Treasury (HMT), this may have removed some of the funding ambiguity that was present in summer 2015 when the position remained as set out in the settlement letter referenced above. That is there was no upper limit placed on the AME profile by HMT thereby meaning that the scenarios set out in the Jon Parker email and DECC/Foster correspondence did not apply in Northern Ireland in 2015-16.

23. The Department has no evidence that the above correspondence was sent to the Finance Minister, at least not through Finance officials. Had DETI alerted DFP, contemporaneously, to the contents of the 29 November 2013 letter from DECC (DOF-100218), as it advised it would, then clarification could have been



sought at that stage and in a timely manner. In its response to DECC on 16 December 2013 (DOF-100217) DETI advised;-

*"You may be aware that the previous budget for Northern Ireland of £25m between 2011-15 came as a pro-rata share of the GB budget; I therefore assume that similar arrangements have been considered for 2015/16. I will, of course, pursue this with my colleague, the Minister for Finance and Personnel, however if you are able to provide clarity that would be most helpful."*

This was a clear opportunity for DETI to formally advise DFP/DoF of the funding issue at that time.

23. Based on evidence provided by witnesses to the Inquiry, the Department is also aware that there was further correspondence between DECC and DETI on the Renewable Heat Incentive Scheme including the introduction of cost controls including digression for the Domestic Scheme (DFE 54094). The department has carried out a due diligence check of its records to ascertain whether this correspondence was shared with DFP/DoF by DETI. The Department can find no evidence that the letters were shared with DFP/DoF.
  
24. On 8 September 2014, the Department issued a response to DETI advising that a number of issues still required clarification as set out below (DOF-100231):
  - the availability of NPV calculations. The approval of the business case was conditional on DETI providing the NPV calculations. These were provided and agreed with EAB economists;
  - Benefits realisation plan – This again was an omission from the original business case;
  - Objectives of the Scheme to show targets for the end of the project as well as interim targets for 2015; and
  - the completion of the Risks and Non - Monetary Sections of the business case for the comparison of options.





25. DETI responded to these DFP queries on the same date with the information provided passed from Supply to EAB (DOF-100233). EAB provided further comments (on 9 September 2014) and again sought clarification on the NPV calculation (DOF-100235).
26. The business case was formally approved by Supply on 15 September 2014 (DOF-100249).
27. In its covering letter (DOF-100003) DETI refers to the Domestic Scheme as being Phase 2 of the RHI Scheme. The covering letter advises that Phase 1 of the RHI Scheme was *“limited to the non-domestic sector”*. The covering letter also advised that *“Funding of 25M is available to 2015/16 for this scheme”*. DOF accepts that it did not recognise, from this message that Phase 1 and 2 were to be funded from the same initial pot of money allocated to NI Executive by the Chief Secretary to the Treasury in the Spending Review period 2011 to 2015. It is accepted that page 5 of the business case (DOF-100023) states:-
- “The proposals outlined within this business case are within the original funding envelope of Phase 1 of the scheme.”*
28. The proforma attached to the business case, completed by DETI, is found at DOF 100005/7. Against the question, “Costs Outlined in Business Case”, there is stated, *“Capital Cost 103M (HM Treasury money – AME budget) Resource Cost £1.4m (includes £800k existing staffing costs)”*. In giving its approval for the Domestic RHI Scheme the Department approved the amount of £103 million as requested by DETI (DOF-100249). The Department now accepts that this £103 million is misleading and is predicated on both the Domestic and Non-Domestic funding profiles. The Department has seen through its monitoring of the Inquiry process that the figure of £103 million appears to emanate from an email dated 10 January 2014 from Jeff Partridge (at that time DETI Finance) to Trevor Cooper (also at that time DETI Finance) about AME Forecasts, (DFE-268206).



*“Trevor,*

*In relation to AME RHI Budgets, I actually checked this out with DFP last month (short memory lapse on my part!), and it was confirmed that the AME forecasting exercises are used to formulate the Northern Ireland AME budgets...”*

29. This email advises that the Department has confirmed AME forecasting exercises are used to formulate the NI AME budgets. This was a reference to the normal AME process. There is no reference to the atypical nature of RHI AME funding that it was subject to a cap. The Department, having carried out a due diligence search of TRIM Containers and spoken to relevant members of staff, has no record of the particular question posed by Mr Partridge which elicited this advice nor is the Department aware as to which official(s) in the Department provided this advice. Having considered the email from Mr Partridge to Mr Cooper, it seems clear that this information was in turn contained in the cover letter from Iain McFarlane (DOF-100004), at paragraph 7, and also in the Synopsis of Casework Committee (DOF-100016).
30. Supply did not challenge the “£103m” reference and how it related to other information in the business case and the Foster/Barker correspondence which stated that there is £25m up to 2014-15, (in some places 2015-16 is inaccurately used) and the Barnett consequential of £430 million for 2015-16 or earlier advice as contained in the Jon Parker email. As stated above DoF recognises and accepts that this was an opportunity to clarify the funding arrangements for the RHI Scheme going forward. It should be noted, however, that at that time the RHI Scheme AME profiles indicated that the Scheme was underperforming against profiled spend and there were no alarm bells raised by DETI nor was there any indication to the Department that DETI regarded the Scheme as unaffordable going forward. In addition, the profile for 2014-15 was within the cap set out in the SR2010 settlement letter, the 2015-16 profile was reflective of a population share of £430 million and with no spending review in place for future years these profiles could only be viewed as forecasts. DoF accepts with the benefit of hindsight that the status of the documentation provided by DETI and the assurances contained therein should have been



tested further with CED and HMT.

31. In addition to the above, the Department accepts that it did not recognise that the DECC/Foster correspondence advised as to additional steps being taken in England to manage the funding of the Non-Domestic RHI Scheme. While the Northern Ireland Domestic Scheme did not mirror the English scheme in so far as the Northern Ireland Scheme was a combination of Renewable Heat Premium Payment (RHPP) grant level support (Capital AME) and ongoing payments for seven years (Resource AME) DoF did not identify the need to query the need for cost controls with DETI in September 2014,

32. As stated, DoF accepts with the benefit of hindsight that the amount requested by DETI, some £103 million, in respect of the Domestic Scheme did in fact include both Phase 1 and Phase 2 of the RHI Scheme, that is Domestic and Non-Domestic Schemes. At the end of 2015-16, when greater clarity as to the spend on the Domestic and Non-Domestic Scheme emerged, it became apparent to DFP/DoF that there had been a breach in one of the standard conditions of approval in respect of a 10% differential on cost for the Domestic Scheme namely the Scheme was significantly below the 10% approval level. The relevant condition set out at DoF-100249 is:-

*“that resource or capital costs or assumptions vary by no more than 10% from the value stated”;*

33. A breach of any conditions of approval requires revised DoF approval which takes account of the following factors:

- Where Supply is approached on the earliest indication that compliance with one or more of the above conditions is under question.
- Adherence to correct appraisal procedure.

34. It is the spending department's responsibility to ensure compliance with these conditions and DoF has no role in monitoring this compliance. Responsibility for



departmental expenditure rests with the departmental Accounting Officer, regardless of the any approval given previously by DFP/DoF.

35. As the initial assessment of the Domestic business case from a value for money perspective remained unchanged it was concluded by Supply that DETI should seek re-approval for the correct amount in line with the established protocol.
36. The Inquiry has queried whether there was any difference in approach between the Supply team that considered the original Non-Domestic business case and the team that considered the Domestic case. While there was no change to the procedures followed by Supply in respect of the two cases, the Supply teams considering the cases had different personnel.
37. The Supply team (Deputy Principal, Sylvia Sands and Principal Stuart Stevenson) that considered the original Non-Domestic business case did not consider the Domestic business case. This was as a consequence of the transfer of the DETI Supply function to a new Principal Supply officer in April 2014 (Michelle Scott). In addition, the Supply DP who considered the original Non-Domestic Case, Sylvia Sands retired in the summer 2014. An organisation chart showing the staff who considered the Domestic business case, including details of transfers within the team, are attached to this statement at Annex 1. In line with the protocols within Supply at that time the consideration of the case was led by the Deputy Principal, Angela Millar with administrative support from the Staff Officer, Sarah Benton.
38. The Department understands that the RHI Scheme was not included in the verbal handover between Supply teams as it was not a live business case at that time and therefore not in any forward workplan. The Department has already confirmed to the Inquiry that there was no written handover between the 2011 Supply team and the subsequent 2014 Supply team in relation to RHI or otherwise. Supply is reviewing its internal processes, including the use of the Information Management System (IMS) within Supply, to identify whether additional functionality is required to allow more information to be stored on the

existing database. These adjustments will still however rely on departments providing sufficient and accurate information when they submit business cases to Supply to allow cross-linkages etc to be made.

39. These staff changes meant that the team considering the Domestic business case did not have any previous knowledge of the approval for the Non-Domestic Scheme. While it was in line with normal Supply practice at that time to consider each business case on its own merits, the Department accepts that, with hindsight, this particular business case was unusual in that it was funded from one limited pot of money that had already had a significant call on its finances. In essence the Domestic business case should have been considered as an extension of the Non-Domestic business case. The Proforma as completed by DETI and submitted with the business case identified that this was not a resubmission (DOF-100005). This unusual situation was not however identified by Supply Division in 2014. This is despite the message at page 5 of the business case (DOF-100023) which stated:-

*“The proposals outlined within this business case are within the original funding envelope of Phase 1 of the scheme.”*

40. The Supply proforma which accompanies the submission of business cases will now be amended to require additional details including whether the case is linked to similar cases or earlier approvals. It is still however incumbent on each department to complete this correctly with all relevant accurate information.
41. Supply Division did not identify, in 2014, the fact that the funding for the Domestic Scheme was intertwined with the funding for the Non-Domestic Scheme. It is unfortunate that the officials who considered the Domestic business case were not prompted to consider the Non-Domestic business case or the terms and conditions of the extant Non-Domestic approval. Officials did not foresee that the approval of the Non-Domestic approval scheme may be relevant to the approval of the Domestic business case. Had Supply identified the link in August/September 2014, it may have provided an opportunity to seek



an update on progress in respect of the Non-Domestic Scheme including the need for a review to be completed by early 2015.

42. The Department entirely accepts that the correspondence between the DETI Minister and DECC Minister between 29 November 2013 and 7 January 2014 was received by the Department earlier than previously advised in the Department's opening statement to the Inquiry. In its opening submission, the Department advised that DoF did not have sight of the correspondence until June 2015. The Department wishes to correct that statement, which is inaccurate, and to formally record that the correspondence was in fact received in Supply Division in September 2014, see paragraph 20 above
43. As stated at the outset of this statement a further statement will be submitted to the Inquiry addressing AME funding.

Statement of Truth

I believe that the facts stated in this 17 page witness statement to be true.

Signed: Ernest Morelli

Dated: 30 May 2018



APPENDIX 1

**SUPPLY STAFFING OVERVIEW**

**Staffing – DETI Supply Team**

In August 2014 the DETI Supply team comprised Michelle Scott, Angela Millar and Sarah Benton. The Grade 5 with responsibility for this Supply team from May 2014 was Joanne McBurney.

Ms McBurney joined Supply at Grade 5 level in May 2014. Pending a restructuring of Supply, Ms McBurney initially replaced Jack Layberry as the Head of Supply 1 (which at that time covered DETI, DARD, DCAL and OFMDFM). It was also the intention that Ms McBurney would replace John McKibbin, who headed Supply 2 (which at the time covered DRD, DoE, DHSSPS, DE, DEL, DFP and DoJ) on his retirement. During this transition/handover period Ms Burney worked alongside Mr McKibbin on a number of Supply 2 issues and was also responsible for oversight of the Supply input to Public Expenditure exercises e.g. Budget and In-Year monitoring exercises.

Ms Scott replaced Stuart Stevenson in April 2014, when he transferred to Accountability and Financial Management Division (AFMD). As part of the restructuring of Supply Mr Stevenson's post was suppressed and his DETI Supply duties were assigned to Ms Scott, in addition to her existing role in respect of DARD and OFMDFM. Supply responsibilities in respect of DCAL were carried out by Maryann Smith.

Sylvia Sands was the DP reporting to Mr Stevenson in April 2014 until her retirement in August 2014. Ms Millar took over Ms Sands duties in respect of DETI in August 2014, in addition to her existing role in respect of DARD and OFMDFM.





Sarah Benton was the Staff Officer in the DETI Supply team (dates). Ms Benton, who worked part time, was also the Staff Officer in the DCAL Supply Team.

The Staff Officer on the DARD and OFMDFM Supply team was Una Tallon.

### **Workload**

Between 1 August 2014 and 30 September 2014, the DETI, DARD and OFMDFM Supply team reviewed 11 business cases, as outlined below:

#### **DARD (Ms Scott, Ms Millar and Ms Tallon)**

- Fishing ports, landing sites and shelters measure of the European Fisheries Fund
- Reform Area Based Scheme Delivery Sub-Programme
- Homeowner Flood Protection Grant Scheme

#### **DETI (Ms Scott, Ms Millar and Ms Benton)**

- Forthriver
- Co-Investment Fund Uplift
- Domestic RHI
- Intertradelreland lease of premises

#### **OFMDFM (Ms Scott, Ms Millar and Ms Tallon)**

- Household Energy and Thermal Efficiency
- Social Investment Fund – Invest in Play
- Mazelongkesh (MLK) Development Company Pay Remit
- ILEX Senior Staff Pay Remit

Ms Benton also had responsibilities in respect of DCAL casework revived during this period.



In addition to the management of the above listed casework, in this two month period the DETI, DARD & OFMDFM Supply team also managed ongoing work issued as outlined below:

1. 2015-16 Budget Exercise – Supply teams were responsible for assessing departmental budget requirements and formulating recommendations for allocations.
2. 2014-15 In-year Monitoring Exercise – the Executive agreed as part of the June monitoring exercise in 2014 that departments (excluding those protected) deliver savings in the 2014-15 year on non-ring fenced resource of 2.1%. The June and October in-year monitoring exercises were therefore more resource intensive than usual.
3. Other routine business – including the review of a number of Management Statement and Financial Memorandum (MSFM) and Business Plans. Ms Millar as also assisting with the training of a new Supply DP during this period.