

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

**Volume 1 — Chapters 1–19**



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Non-domestic Renewable Heat Incentive (RHI) Scheme**

**and**

**Department of Finance**

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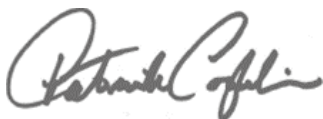
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## Introduction

I.1 On 1 July 2016 the Comptroller and Auditor General for Northern Ireland and head of the Northern Ireland Audit Office, Kieran Donnelly, published his report<sup>1</sup> dealing with the Department of Enterprise, Trade and Investment (DETI) Resource Accounts for the financial year 2015-16. That report specifically considered the development and performance of the Northern Ireland Non-Domestic Renewable Heat Incentive Scheme (the NI RHI scheme). After completing a detailed analysis Mr Donnelly concluded:

“This scheme has had serious systemic weaknesses from the start. The fact that the Department decided not to mirror the spending controls in Great Britain has led to a very serious ongoing impact on the NI budget and the lack of controls over the funding has meant that value for money has not been achieved and facilitated spending which was potentially vulnerable to abuse. I am very concerned about the operation of the scheme and it is an area which I expect to return to in the very near future.”<sup>2</sup>

Mr Donnelly’s concerns<sup>3</sup> included that the NI RHI scheme:

- was not designed to include any viable cost controls despite the clear indication in April 2011 that the scheme would not be funded without limit by Her Majesty’s Treasury (HMT);
- did not take the opportunity in 2013 to mirror the equivalent GB RHI scheme and introduce some cost control measures at that time;
- did not take account of changes to underlying costs since 2012 and therefore was over-generous in incentivising renewable heat;
- could not be changed quickly when it became apparent that demand was rising quickly;
- was not approved by the Department of Finance and Personnel (DFP) after April 2015, which resulted in irregular expenditure. If the need for this approval had been identified at the right time then it could have been the catalyst for a wider review of the scheme;
- had at least facilitated the possibility of payments that were, at best, not in line with the spirit of the scheme and, at worst, possibly obtained by fraud (though there was no *prima facie* evidence of fraud at that time);
- was not properly monitored and controlled by the Department, which solely relied on the work being done by Ofgem that administered the scheme; and
- did not identify the risks of overspending at an earlier stage, even though Annually Managed Expenditure (AME) allocations had been previously advised. This had led to an impact on the Northern Ireland block grant which was likely to be measured in hundreds of millions of pounds.

1 Dated 28 June 2016. See CAG-01351 to CAG-01368. Where footnotes in this Introduction or in the Inquiry Report give references in the format above, this refers to pages within one of the Inquiry’s evidence bundles. This page numbering system is sometimes referred to as ‘Bates’ numbering and was explained during the course of Senior Counsel to the Inquiry’s Opening: see TRA-00038 to TRA-00039. Documents referred to in this way in the Inquiry Report may be found on the Inquiry’s website (unless, exceptionally, the Chairman considers that there is good reason for restricting publication in accordance with the Inquiry’s protocols).

2 CAG-01365

3 Set out in the conclusion of his report at CAG-01365

- I.2 At that time Mr Donnelly estimated that, after taking into account the NI RHI funding HMT had confirmed it was making available through the five years' 2015 Spending Review, the NI RHI scheme would produce a deficit in the finances of the Northern Ireland devolved administration over the subsequent five years of in or around £140 million.<sup>4</sup>
- I.3 Prior to the publication of Mr Donnelly's report the Public Accounts Committee (PAC) of the Northern Ireland Assembly,<sup>5</sup> which, already aware of the emerging problem, had determined at its meeting on 22 June 2016<sup>6</sup> that it would conduct an investigation into what had gone wrong with the NI RHI scheme, using its powers to compel witnesses to attend and give evidence. A number of PAC meetings then took place during the autumn of 2016.
- I.4 Mr Donnelly's report and the consequent PAC meetings stimulated public and media interest but it was not until the broadcast of a BBC 'Spotlight' documentary on the issues on 6 December 2016<sup>7</sup> that the interest of the general public in Northern Ireland really became engaged. A short excerpt gives a flavour of the broadcast:
- “Did you hear the one about the Renewable Heat Incentive? It was a government scheme which went hugely over-budget. Supposedly a green scheme reducing our reliance on fossil fuels, but, believe it or not, as well as being economically a disaster, it actually turned out to be damaging to the environment. There was a series of extraordinary – extraordinary blunders, and now, because of those blunders, we are likely to spend the next 20 years picking up a tab of hundreds of millions of pounds. Tonight, on 'Spotlight', we hear about the missed alarm bells, and we reveal a previously unseen email from a whistle-blower which was ignored by Arlene Foster's Department.”<sup>8</sup>
- I.5 That well-explained documentary by the reporter Conor Spackman simplified and repackaged the findings of the Comptroller and Auditor General's report for easy public understanding and focused on the absence of, first, tiering of the medium biomass subsidy and, second, cost control of the NI RHI scheme. The documentary also contained a reference to a person described as a 'whistle-blower' who had contacted the DETI Minister, Ms Foster, in late 2013 and engaged with departmental officials.
- I.6 Mr Spackman's documentary was followed by a series of television interviews shortly before Christmas 2016, which focused on the regulations amending the NI RHI scheme in November 2015.<sup>9</sup> Those regulations implemented a new system of tiering in respect of the most popular biomass tariffs which would affect those applicants entering the scheme on or after 18 November 2015. For the small and medium biomass tariffs, tiering limited the payment of the pence per kilowatt hour initial higher tariff to a fixed amount of 1,314 hours per year, after which the payment was substantially reduced to a second lower tariff for any subsequent hours of heat produced. An annual cap was also imposed on the total heat output that would be eligible for payment of subsidy: 400,000kWh.<sup>10</sup> Attention was also directed to the further amendment

4 CAG-01363

5 The Public Accounts Committee (PAC) is a Standing Committee of the Northern Ireland Assembly established in accordance with section 60(3) of the Northern Ireland Act 1998 and under Assembly Standing Order 56.

6 PAC-03314 to PAC-03316

7 DOF-16579 to DOF-16598

8 BBC Spotlight, 6 December 2016, TRA-00019

9 The Renewable Heat Incentive Schemes (Amendment) Regulations (Northern Ireland) 2015 (2015 No. 371)

10 Approximately the equivalent of running a 99kW biomass boiler at its full capacity for just over 4,000 of the available 8,760 hours in a common year.



of the scheme regulations in February 2016<sup>11</sup> which provided power for the Department, by notice, to suspend the NI RHI scheme to new applicants.

- I.7 These interviews were conducted by the radio and television broadcaster Stephen Nolan, the first being with Jonathan Bell, who had been the DETI Minister from May 2015 to May 2016, and the second with Arlene Foster who had been the DETI Minister during the development and implementation of the RHI schemes from 2008 to May 2015, subsequently appointed Minister for Finance and, latterly, First Minister. Mr Nolan characterised the RHI scheme as “the biggest financial scandal ever to hit Northern Ireland politics.”<sup>12</sup> His interview with former Minister Bell<sup>13</sup> proved to be politically explosive containing, as it did, allegations by the former Minister that his desire to bring the scheme under control had been continuously thwarted by DUP Special Advisers (SpAds) and that First Minister Foster had ordered him to keep the scheme open for an additional two weeks when he wanted to close it because of overspending.
- I.8 For her part, in the course of her interview with Mr Nolan,<sup>14</sup> First Minister Foster took strong issue with Mr Bell’s allegations and, on 19 December 2016, she made a formal statement to the Assembly about the scheme and her involvement with it.<sup>15</sup> Ms Foster resolutely rejected the allegations made by Mr Bell and strongly maintained that she had never been provided with any warning during her time as DETI Minister that scheme spending was out of control or that cost controls were urgently required.
- I.9 As a consequence, 2016 came to an end amid a veritable firestorm of political and media allegations and counter-allegations. The one common feature appears to have been an agreed desire for an independent investigation, free from political influence, to establish the facts relating to the NI RHI scheme.
- I.10 On 9 January 2017 the then deputy First Minister, the late Martin McGuinness, resigned from that post, which he had held for some 10 years. The content of his letter of resignation,<sup>16</sup> which ranged over a variety of political complaints, included a reference to “the current scandal of the Renewable Heat Incentive.” The late Mr McGuinness referred to “a public mood which is rightly outraged at the squandering of public money and the allegations of misconduct and corruption” and he added that he had urged First Minister Foster to stand aside, given her involvement in the creation of the NI RHI scheme, so as to “ensure confidence in the necessary investigation and in the wider public interest.” The deputy First Minister’s resignation had the effect of removing the First Minister from office, given the joint nature of their appointments.
- I.11 On 19 January 2017 the Minister then with responsibility for the Department of Finance in Northern Ireland announced<sup>17</sup> his intention to establish a Public Inquiry into the Non-Domestic Renewable Heat Incentive Scheme. Minister Ó Muilleoir made a formal statement to the Northern Ireland Assembly on 24 January 2017<sup>18</sup> providing further details of the proposed inquiry. Following this, the “Independent Public Inquiry into the Non-Domestic Renewable Heat

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11 The Renewable Heat Incentive Schemes (Amendment) Regulations (Northern Ireland) 2016 (2016 No. 47)

12 DFE-228963

13 DFE-228963 to DFE-228988

14 DFE-424313 to DFE-424345

15 INQ-00107 to INQ-00162

16 INQ-00105 to INQ-00106

17 INQ-00177 to INQ-00188

18 INQ-00006 to INQ-00020

Incentive (RHI) Scheme” (generally referred to as ‘the RHI Inquiry’) commenced its work on 1 February 2017.

- I.12 In his impressive opening statement to the Inquiry Mr Scoffield QC, Senior Counsel to the Inquiry, asked rhetorically how such a relatively unexciting scheme to incentivise businesses to meet their heating needs from renewable sources came to be in the news at all, let alone becoming a contributing factor to the downfall of devolved government in Northern Ireland, thereby striking at the very heart of our democratic institutions. It has been the task of this Inquiry to attempt to answer the questions raised by Mr Scoffield QC, a task that has involved considering and processing some 1.2 million pages of evidence and arranging for witnesses to provide oral evidence over a period of some 114 days of Inquiry hearings, inclusive of opening and closing statements.

### The purpose of the Inquiry

- I.13 This Inquiry was established in accordance with section 1 of the Inquiries Act 2005 (the 2005 Act). The purpose and scope of the Inquiry was defined in its Terms of Reference (TOR), a full copy of which is both available on the Inquiry’s website and is included among the appendices to this Report. Paragraph 1 of the TOR defines the purpose and scope of the Inquiry as follows:

“To investigate, enquire into and report on the Non-Domestic Renewable Heat Incentive scheme (“the RHI scheme”). This includes its design, governance, implementation and operation, and efforts to control the costs of that scheme, from its conception in 2011 to the conclusion of the Inquiry.”

- I.14 The purpose of such an investigation is specified as a need to restore public confidence in the workings of Government. Particular requirements of the Inquiry’s task are then set out and they include an examination of the role of Ministers, Special Advisers, Civil Servants, and any others involved in the RHI scheme (including external consultants) and whether their actions and/or advice met appropriate professional standards, were ethical, within the law and compliant with standards in public life including, in particular, the Nolan Principles, the Ministerial Code of Conduct, the Civil Service Code of Conduct, the Code of Conduct for Special Advisers and Conditions of Employment. The Inquiry was required to examine the work on the scheme by relevant Government Departments (particularly the Department for Enterprise, Trade and Investment which, in May 2016, became the Department for the Economy (DETI/DfE), the Office for Gas and Electricity Markets (Ofgem) and others) with a view to determining what, if anything, went wrong. Under the heading “Principles” the TOR specified that: “The Inquiry will be wholly independent and not accountable to the Executive, Assembly, or any public body.”
- I.15 The Inquiry panel has been particularly concerned to preserve the independence of the Inquiry, which is supported by the impartiality provisions contained in section 9 of the 2005 Act. Independence is a key feature of any inquiry established in accordance with that legislation and, while the Inquiry was established by a Minister of the Northern Ireland Executive, as required by section 1 of the Act, the Inquiry panel has also relied upon a Ministerial Statement promising full independence made at the time of setting up the Inquiry; and the panel members are satisfied that they have been able to carry out their functions as they think fit, independently, without fear or favour and free from any external pressures of any kind whatsoever. By agreement, the TOR were made as broad as possible with an emphasis upon the keystones of openness and

transparency and in his statement to the Assembly on 24 January 2017 the then Minister of Finance, Mr Ó Muilleoir, confirmed that the Inquiry would extend beyond financial matters to questions of governance and probity on the basis that such wider issues would go some way towards rebuilding what was said to be the shattered public confidence in the institutions.

## The structure of the Inquiry

- I.16 The Inquiry panel was chaired by the Right Honourable Sir Patrick Coghlin, a retired Northern Ireland Court of Appeal Judge. He was assisted by a panel member, Dame Una O’Brien and a technical assessor, Dr Keith MacLean.
- I.17 Dame Una O’Brien enjoyed a long and distinguished career in the Home Civil Service. She was the Permanent Secretary at the Department of Health in London, a post which she held for some six years, having earlier acted as Director General of Strategy at the Department. As Permanent Secretary Dame Una was the Accounting Officer for the overall performance of the health system in England with an annual budget in excess of £115 billion. She also held executive membership of the Civil Service Board, the Department of Health Board and the NHS Management Board, as well as non-executive membership of the Government Legal Service Board. Dame Una holds Honorary Doctorates at the universities of Birmingham and Coventry and was also Chair of The Charity for Civil Servants with a benevolent fund of £36 million. She was awarded a CB in 2010 and created a Dame for public service, particularly in health, in the Birthday Honours List of 2015. She had previous experience in public inquiries, including acting as Secretary to the Kennedy Inquiry into the NHS and Children’s Heart Surgery in Bristol.
- I.18 Dr Keith MacLean served as an assessor to provide technical advice and guidance to the Inquiry. After graduating from Heriot-Watt University, Edinburgh with a first class degree in chemistry and the University Prize for Merit, Dr MacLean worked in industry for over thirty years, including ten years as Policy and Research Director for SSE. In that position he had responsibility for research and development, energy and climate change policy, public affairs and stakeholder engagement on major projects and sustainability. He has worked extensively with technology developers and regulators across Europe and has been regularly invited to give evidence to Select Committees. Dr MacLean is a member of the Institute of Directors and, as a former SSE Telecoms Managing Director, he has very considerable commercial experience, which brings an additional dimension to the Inquiry’s expertise. Following early retirement from SSE, he now acts as an independent adviser on energy to private and public bodies including both the UK and Scottish Governments. He has also served as industry Co-Chair of the Energy Research Partnership as well as Chair of the UK Energy Research Centre and UKRI’s Scientific Advisory Committee. As a board member of a number of trade associations and policy groups he has worked with government on, *inter alia*, the design and review of policy and legislation for low carbon energy support mechanisms. This has included work on issues such as banding and revision of support levels. He is an honorary fellow of Energy Policy at the University of Exeter and was awarded an OBE for services to energy in the 2017 New Year Honours List.
- I.19 The Chairman wishes to acknowledge the invaluable benefit that both he and the Inquiry generally have derived from the respective contributions of Dame Una O’Brien and Dr Keith MacLean. This report is a joint production of all three individuals assisted by the legal team.
- I.20 The Inquiry legal team consisted of David Scoffield QC, Donal Lunny BL, Joseph Aiken BL and the Inquiry Solicitor Patrick Butler. The members of the Inquiry panel are extremely grateful

for the long hours of preparation and analysis, together with the high degree of forensic ability, demonstrated on a daily basis by the legal team.

- I.21 It is also important for the panel to acknowledge the high quality of the work carried out by the legal and administrative support teams headed by the Inquiry Secretary Andrew Browne OBE and later Paula Dawson MBE. Quite simply, it would not have been possible to process, analyse and present the documentary and oral evidence, stretching over a period of some three years and more than 1.2 million pages without the high quality of work, application and intellectual ability displayed by the Inquiry support team.
- I.22 The Inquiry Counsel and Solicitor are also grateful for the invaluable support and assistance they received from the team of lawyers in the Inquiry legal support team and the Inquiry's executive and administrative staff.
- I.23 It would not be right to complete this introductory section of the Report without also expressing the gratitude of the Inquiry panel for the much appreciated support that it received from all the other providers of services to the Inquiry, including the communications, technological, administrative, joinery, catering and security staff at Parliament Buildings, both before and during the 114 days of public hearings. This was a public inquiry carried out fully in the public eye in order to restore a degree of confidence amongst the general public of Northern Ireland in the structures and arrangements by which they are governed. To that end it was the intention and hope of the Inquiry that the online streaming of its proceedings, during the taking of oral evidence, would enable each member of the viewing public to have an opportunity to see and consider for themselves the evidence of the witnesses as they gave it on a daily basis.
- I.24 The Inquiry also appreciates the quality of the media coverage which the proceedings attracted which was generally fair, non-sensational and careful, with appropriate attention to detail.
- I.25 Finally the Inquiry wishes to record its sincere thanks to all those who provided evidence for its consideration and, in particular, to those who gave oral evidence. The experience of giving oral evidence in public can be daunting at the best of times and that must be particularly so when proceedings are streamed online.

## The procedure of the Inquiry

- I.26 A public inquiry is not a court and its procedure has, certainly in recent times, been inquisitorial as opposed to adversarial. Section 2 of the 2005 Act expressly prohibits a public inquiry from ruling on or purporting to determine any person's civil or criminal liability, although an inquiry panel is not inhibited in the discharge of its functions by any likelihood of liability being inferred from facts that they determine or recommendations that they make. In adversarial systems the responsibility for collecting and presenting evidence lies generally with one of two or more parties who make allegations and counter-allegations; a judge will then decide the case on the evidence presented. Public inquiries are different. In the Bloody Sunday Inquiry Lord Saville explained the purpose of a public inquiry in the following terms:<sup>19</sup>

“An Inquiry like the present Inquiry is quite different. Here the Tribunal takes the initiative in trying to ascertain truth. Unlike an adversarial contest, it is for the Tribunal to seek all the relevant material. Its task is not to decide the matter in

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19 Opening statement of the Tribunal, 3 April 1998, found at A2.1 of Volume X to the Report of the Bloody Sunday Inquiry.

favour of one party or another. Indeed, from the point of view of the Tribunal there are no parties or sides. There will, of course, be those who have material evidence to give or who have a legitimate interest in challenging such evidence, but the Tribunal will not treat them as sides or parties in an adversarial contest, but rather as a means of seeking out the truth.”

- I.27 A public inquiry generally applies the inquisitorial approach because it considers it most likely to assist it to get to the truth of a matter of public controversy by way of its own extensive investigation and examination of all the evidence.
- I.28 Section 17 of the 2005 Act provides that “subject to any provision of this Act or of rules made in accordance with section 41, the procedure and conduct of an inquiry are to be such as the Chairman of the inquiry may direct.” Section 17 also provides that “in making any decision as to the procedure or conduct of an inquiry the Chairman must act with fairness and with regard also to the need to avoid any unnecessary cost (whether to public funds or to witnesses or others).” While rules have been made in accordance with section 41 of the Inquiries Act 2005 relating to inquiries set up by a Minister of a Westminster Department<sup>20</sup> or a Minister of a Scottish Government Department,<sup>21</sup> no such rules have been made to date in the Northern Ireland jurisdiction either by Westminster or by the Northern Ireland Assembly. Furthermore, Rules 13 to 15 of the Inquiry Rules 2006 (the 2006 Rules), which required a particular form of warning letter process, have now been the subject of adverse comment by a House of Lords Select Committee<sup>22</sup> and a report for the Treasury Select Committee<sup>23</sup> both of which recommended the need for change.
- I.29 Accordingly, it was necessary for this Inquiry to issue a number of protocols and orders dealing with the Inquiry’s procedures and the taking of evidence. The Chairman indicated that, where appropriate, when he was exercising a discretion he would take into account any relevant provisions of the 2006 Rules, although bearing in mind that they did not apply in this jurisdiction or to this Inquiry. The protocols and orders issued by the Inquiry Chairman are published on the Inquiry’s website.
- I.30 Public inquiries are not bound by the formal rules of evidence. Flexibility and fairness are the key concepts. Hearsay evidence is admissible but individuals must be given a fair opportunity to defend themselves against adverse criticism.
- I.31 The Inquiry provided ‘core participant’ status to those government Departments that it considered most involved with the NI RHI scheme, and which the Inquiry considered were most likely to face significant or explicit criticism: DETI/DfE, the Department of Finance and Personnel/ Department of Finance (DFP/DoF)<sup>24</sup> and Ofgem. This status gave the relevant Departments certain participatory rights in the inquiry process, designed to ensure fairness. They were each also legally represented.
- I.32 Further, the Chairman of the Inquiry, in the exercise of his discretion, afforded ‘enhanced participatory rights’ to 27 individuals or organisations whom the Inquiry considered could be subject to significant or explicit criticism. This status again provided the individuals

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20 The Inquiry Rules 2006 (2006 No.1838)

21 The Inquiries (Scotland) Rules 2007 (2007 No.560)

22 House of Lords Select Committee on the Inquiries Act 2005 “The Inquiries Act 2005; post-legislative scrutiny” HL Paper 143

23 For the Treasury Committee “A Review of ‘Maxwellisation’”.

24 DFP became DoF in May 2016

and organisations with certain participatory rights and, as necessary, such individuals and organisations were legally represented before the Inquiry.

- I.33 During the course of its work the Inquiry gathered evidence through the service of over 800 statutory ‘Section 21 Notices’. Of those Notices that required production of documents, individuals or organisations were required to provide material that they knew to be potentially relevant to the Inquiry’s work, as well as specific material that the Inquiry knew to exist and wished to receive. In turn, the Inquiry provided organisations and individuals with sight of relevant documents amassed during the Inquiry’s evidence gathering process where this was necessary or desirable to facilitate their giving of evidence.
- I.34 Notices also required the provision of witness statements. Invariably, Notices seeking witness statements would ask questions of witnesses, including questions about events, interactions or documents with which they were involved. Some witnesses received a number of Notices. Where necessary, individuals or organisations had legal representation to assist with the provision of a witness statement or statements in response. Relevant material from this process has been published on the Inquiry’s website and there is now a very great deal of such material available to the public through the work of the Inquiry.
- I.35 Where necessary, individuals were also given the opportunity to expand upon their statements in oral evidence. It was not necessary for all witnesses who provided written statements to give oral evidence to the Inquiry. Questioning during oral evidence sessions was conducted by Inquiry Counsel, and by the panel. Most witnesses, including core participants and those with enhanced participatory rights, were legally represented during the process and had an opportunity to contribute to suggested lines of questioning in respect of themselves or, more importantly, others. Transcripts of the oral evidence received by the Inquiry can also be found on the Inquiry’s website, along with copies of the documents considered during the relevant evidence session.
- I.36 The Inquiry also provided core participants, and those with enhanced participatory rights, with the opportunity to make closing submissions. The closing submissions received by the Inquiry are also published on the Inquiry’s website.
- I.37 In addition, in accordance with the duty to act fairly, the Inquiry also engaged in a representations process in respect of those individuals or organisations that the Inquiry considered, after its hearings, should be the subject of significant or explicit criticism in the Inquiry’s Report. Written representations received during the course of this process, although referred to at relevant points in the course of the Inquiry Report, are one of the few categories of relevant documentation received by the Inquiry which are not being published by it. This is because the representations were made in respect of draft material shared by the Inquiry as it continued to work on this Report. This Report is itself the culmination of that process.
- I.38 The Inquiry is grateful for the level of co-operation it received during its work from individuals, organisations, private businesses and government Departments. Significant volumes of relevant documentary material, often prejudicial to its author or holder, were produced to the Inquiry. In the event, the Inquiry did not encounter the need to utilise any of the civil and criminal processes open to it beyond its use of Section 21 Notices.
- I.39 The Inquiry is also grateful for the collaborative engagement it sought and received from those legal representatives engaged on behalf of those involved with the Inquiry.

- I.40 As with any public inquiry, the application of the concept of fairness will of course depend, to some extent, on the particular nature and circumstances of the controversy that the inquiry has to consider. As Sir Richard Scott observed in delivering an address to the England and Wales Chancery Bar Association in 1995 entitled “Procedures at Inquiries - The Duty to be Fair”:
- “The golden rule, in my opinion, is that there should be procedural flexibility, with procedures to achieve fairness tailored to suit the circumstances of each Inquiry.”<sup>25</sup>
- I.41 For example, in the circumstances of this Inquiry fairness required the Inquiry panel to avoid hindsight and ensure the context was properly understood when considering the actions of individuals. Those who were responsible for the implementation, administration and control of the NI RHI scheme did not have the benefit of the 1.2 million pages currently available to the panel or the current experience and knowledge as to how matters were to develop over the years. Context also required fair consideration to be given to the under-resourced and overburdened conditions of work in which officials were required to perform their duties against a background of recession and reduction in Northern Ireland Civil Service staff (not to mention the regular political crises so familiar to those with knowledge of the devolved administration in Northern Ireland).
- I.42 On the other hand, while hindsight must be avoided when considering events in the past, it is important to recognise that it may discharge a very helpful function with regard to determining what should happen in the future. There may well be some basis for the traditional Irish saying that “Hindsight is the best insight into foresight.”

## The nature and structure of this Report

- I.43 In the main body of this Report the Inquiry considers the evidence it received during its investigation, sets out the facts it established as well as its detailed findings on those facts, and then provides a summary and its recommendations for the future.
- I.44 The next 55 chapters contain a detailed narrative in respect of the Northern Ireland Non-Domestic Renewable Heat Incentive scheme (generally referred to in this Report as the ‘NI RHI scheme’). Each chapter contains findings which are associated with the relevant narrative. This is to assist the reader to understand the findings the Inquiry has made, each of which is based on the evidence provided to the Inquiry in the course of its investigation into the matters within the Inquiry’s Terms of Reference. In total there are in excess of 300 findings and, together, these represent the Inquiry panel’s conclusions in relation to those matters.
- I.45 The Inquiry panel’s intention is that anything which they consider to constitute an explicit or significant criticism of an individual or organisation will be contained in one of those findings. It is within the findings that a reader of this Report will find the Inquiry’s specific conclusions on many aspects of the detailed evidence which it heard and the panel’s commentary on how the problems with the NI RHI scheme emerged.
- I.46 While, in general terms, a finding will be supported by the narrative text in the relevant chapter, it may well also be based on text to be found elsewhere in the Report and/or in the published written and oral evidence received by the Inquiry (to which detailed reference has been made in the footnotes to the text of the Report). In the interests of brevity and readability, not all relevant evidence has been rehearsed in each instance in respect of each point addressed by a finding.

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25 Scott “Procedures at Inquiries – the duty to be fair” LQR 1995 page 616

- I.47 After the explanation of some key background topics, the chapters proceed in a broadly chronological fashion, detailing the historical background and subsequent development of the scheme from the early years of the 21st century to suspension of the scheme in 2016 and further amendment of the tariffs in 2017.
- I.48 The Report then analyses in detail a number of specific areas in which problems arose with the NI RHI scheme, including the departmental relationship with Ofgem; the failure to establish and maintain an effective system of review; and the failure to create and maintain an effective system of budget control.
- I.49 Further important themes are then addressed, which relate to issues of wider import or application but which were brought into acute focus in the context of the NI RHI scheme, namely the failure to ensure that important meetings, particularly those involving Ministers, were properly minuted and recorded; the law and practice relating to Special Advisers (SpAds); and the failure to ensure an adequate and effective system of departmental governance and control.
- I.50 After the detailed narrative and accompanying findings the Inquiry, in its concluding chapter, summarises some important themes or key points which emerged from the evidence before setting out the Recommendations that the Inquiry makes for the future. The summary in the final chapter is not intended to go, and should not be seen as going, beyond the criticisms contained in the Inquiry's detailed findings.
- I.51 There are a number of important matters that the Inquiry wishes to make clear to any reader of this Report. The first is that the Report, including the findings and the narrative on which they are based, must be read as a whole in order for the context to be properly understood and in order to ensure fairness to those individuals and organisations that the Inquiry has criticised.
- I.52 Second, it is neither necessary, nor desirable, for the Inquiry to make a finding in this Report on every issue that arose during the Inquiry's work or in respect of which it heard evidence. To do so, given that the Inquiry's investigation involved events spanning a number of years, and involved a multitude of individuals and over 1.2 million pages of relevant documentation, would in the Inquiry's view result in an already lengthy Report running to many more hundreds of pages without any worthwhile benefit.
- I.53 Third, the Inquiry considers that there were many issues of factual controversy which arose in the course of the evidence which it is extremely difficult, at this remove, to resolve with a high degree of confidence or which are unnecessary for the panel to seek to resolve in order to discharge the obligations imposed upon it by its Terms of Reference, notwithstanding the interest which a number of those issues may have generated in the media or public eye.
- I.54 Rather, the Inquiry in this Report has addressed the issues that it considered needed to be addressed, criticised those individuals or organisations that it considered warranted criticism, and in the form that the Inquiry considered appropriate, and has made those findings and recommendations that were necessary in the circumstances. On a range of other issues, the Inquiry considers that the evidence it has received and put into the public domain should be permitted to speak for itself or should be left to others to judge. The transparency generated by the gathering and publication of evidence on a broad range of matters relevant to the body politic in Northern Ireland, in particular through the 114 days of oral hearings which were streamed online, has, the Inquiry hopes, already served a vital public interest.



- I.55 Fourth, it should be emphasised again that it was not part of the Inquiry's Terms of Reference to investigate or comment upon those individual members of the NI RHI scheme (those with accredited installations) affected by the 2016-17 amendments to the non-domestic NI RHI scheme and who entered the scheme in good faith relying upon Government promises or guarantees. Their position is the subject of ongoing judicial review litigation; and energy expert Mr Andrew Buglass has also been appointed by DfE to examine the issue of hardship suffered by participants in the scheme.
- I.56 Ultimately, the Inquiry's hope is that if its recommendations are followed, both in letter and spirit, it will be much more difficult for the types of general problems discovered in respect of the NI RHI scheme to re-occur. Hopefully that will, in turn, lead to a better functioning Northern Ireland Civil Service, and provide for a much healthier devolved administration in Northern Ireland. The Inquiry is aware that work has already progressed within the Northern Ireland Civil Service with regard to a number of matters which are covered by the Inquiry's Recommendations. That said, the Inquiry would counsel against any tendency to conclude that some of the necessary changes have already been fully achieved. The Recommendations set out in the concluding chapter of this Report require sustained, system-wide change and will take time to implement effectively.
- I.57 Further, the Inquiry recognises that often, once a public inquiry has completed its work, recommendations that it made may not be given effect by those whose responsibility it is to do so. There can be a wide variety of reasons for this; some better than others. In the interests of ensuring, so far as possible, that this does not occur in respect of this Inquiry's Recommendations, the Inquiry has asked the Comptroller and Auditor General for Northern Ireland to monitor and, as necessary, pursue the effective implementation of this Inquiry's Recommendations. The Inquiry is very grateful that the NIAO has agreed to undertake this task.



## Chapter 1 – The origins of the RHI in GB and Northern Ireland

### Renewable energy developments

- 1.1 During the late 20th century and the early years of the 21st century widespread concerns about climate change and global warming resulted in greatly increased efforts, both political and technological, to identify and implement a meaningful mitigation strategy. The Kyoto Protocol, an international treaty, had committed signatories to reduce greenhouse gas emissions, such as carbon dioxide, resulting from burning fossil fuels.<sup>26</sup> An important element of that strategy has been the search for appropriate schemes to support and, if necessary, incentivise the transition from traditional fossil fuels to renewable and low carbon alternatives.
- 1.2 The United Kingdom has been among the front runners in the search for alternatives for use in the power, heat and transport sectors. By implementing the Renewables Obligation 2002<sup>27</sup> it was one of the first nations to adopt a policy for stimulating the use of renewables, including biomass, for the production of electricity. Renewable energy schemes were also perceived as beneficial for the security of fuel supply by utilising indigenous energy sources and reducing reliance on imports, as well as increasing the potential to boost the local economy and employment levels.
- 1.3 After the initial focus on the stimulation of renewable energy sources for the production of electricity, interest also began to turn to renewable energy sources for heat. In the UK, sources of fuel for the production of renewable heat and supply chains were relatively under-developed and some of the technologies new or unfamiliar. Following an Energy White Paper published in 2003 by a combination of the Department of Transport and the Department of Environment, Food and Rural Affairs (DEFRA) a Biomass Task Force was appointed to assist the Government and the industry to optimise the contribution of biomass energy to renewable energy targets.<sup>28</sup> The 2004 Royal Commission on Environmental Pollution suggested the introduction of a renewable heat obligation, a quota mechanism similar to that relating to electricity, although the Task Force recommended the introduction of a capital grant scheme when it reported in October 2005.<sup>29</sup>
- 1.4 It was appreciated by policy makers that there was a significant difference between providing a scheme for electricity generation targeted at the owners of a limited number of power stations and one that would have to persuade many hundreds of thousands of individual commercial operators, large and small, as well as millions of homeowners to change their heating systems. However, using the Renewables Obligation as an example, the Renewable Energy Association and other similar organisations began to agitate for some form of financial support for a heat equivalent.
- 1.5 An initial proposal for such a quota-style instrument took the form of a Renewable Heat Bill in January 2005, the progress of which was brought to an end by the 2005 general election.<sup>30</sup> Debate continued after the election, including a suggestion that a tariff support system might be

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26 INQ-101316 to INQ-101336

27 LEG-31501 to LEG-31518

28 INQ-101337 to INQ-101478

29 INQ-101541 to INQ-101636

30 INQ-101479 to INQ-101483

more economically attractive than one based on quotas. On 23 May 2007 the UK Department of Trade and Industry (DTI) published a White Paper entitled ‘Meeting the Energy Challenge’, which set out a short summary of the position across the European Union (EU) and noted that in March 2007 the European Council had agreed to set a target for 20% of the EU’s energy to be from renewables by 2020.<sup>31</sup>

## Developing the UK’s renewable heat policy

- 1.6 The Department of Business Enterprise and Regulatory Reform (BERR), which had inherited many of the functions of the disbanded DTI, commissioned from NERA Economic Consulting a report entitled ‘Quantitative Evaluation of Financial Instruments for Renewable Heat’, which was published on 23 June 2008.<sup>32</sup> The report looked at a range of policy options that could be used to provide financial support for renewable heat technologies and concluded, at section 12, that the two most realistic were either a Renewable Heat Obligation (RHO) or a Renewable Heat Incentive (RHI).<sup>33</sup> The central policy challenge underlying most of the early research was striking the right balance between, on the one hand, compensating applicants for the capital costs and any additional fuel expense incurred by those entering the scheme and, on the other, the risk of exposing public funds to exploitation as a consequence of ‘overcompensation’ and/or ‘gaming’ of the system.
- 1.7 On 26 June 2008 BERR published a consultation document entitled ‘UK Renewable Energy Strategy’, chapter 4 of which dealt with heat and included a section describing the key characteristics of a renewable heat incentive scheme. Responses were sought by 26 September.<sup>34</sup> The strategy document was accompanied by a series of impact assessments, one of which dealt specifically with renewable heat.<sup>35</sup>
- 1.8 On 1 September 2008 NERA provided BERR with a second report examining in some detail the two preferred options identified in the earlier report.<sup>36</sup> NERA stated that the resource cost of renewable heat was highly dependent upon input assumptions, including fuel price assumptions, and advised of the importance of sensitivity analysis in the context of such uncertainty.<sup>37</sup> This report also dealt with banding of tariffs in terms of producing an appropriate return at different scales. It was emphasised that the future of biomass prices was “very uncertain” and that the prices used in the modelling were “broadly based on a combination of assumptions.”<sup>38</sup> These early notes of caution can be seen to be both particularly prescient and important in light of some of the difficulties which later arose with the Northern Ireland Non-domestic RHI scheme.
- 1.9 NERA summarised its findings by warning that an RHI offered much less certainty about meeting a target level of output than an RHO with a strict quantity target.<sup>39</sup> BERR commissioned research from a number of independent bodies on the design of measures best suited to encourage the adoption of renewable heat systems. Information and reports were shared with DETI. These exchanges were formally concluded by the passage of section 100 of the Energy

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31 INQ-21610 to INQ-21953 at INQ 21632

32 WIT-175107 to WIT-175218

33 WIT-175213

34 INQ-21157 to INQ-21445

35 INQ-20001 to INQ-20112

36 WIT-175025 to WIT-175106

37 WIT-175080

38 WIT-175048

39 WIT-175092

Act 2008, by which time the Department of Energy and Climate Change (DECC) had been created (DECC took over some of the functions of BERR relating to energy). Section 100 empowered the Secretary of State for Energy and Climate Change to make regulations for the purpose of establishing an incentive scheme to facilitate and encourage renewable generation of heat.<sup>40</sup>

- 1.10 The passage of the 2008 Act was almost certainly influenced by the debates that were taking place in the EU that led to the adoption of the 2009 Renewable Heat Directive 2009/28/EC in April 2009.<sup>41</sup> Article 1 of the 2009 Directive explained that the Directive established a common framework for the promotion of energy from renewable sources and set mandatory national targets for the overall share of energy from renewable sources.<sup>42</sup> Article 3.1 provided that:

“Each Member State shall ensure that the share of energy from renewable sources, calculated in accordance with Articles 5 to 11, in gross final consumption of energy in 2020 is at least its national overall target for the share of energy from renewable sources in that year, as set out in the third column of the table in Part A of Annex 1.”<sup>43</sup>

- 1.11 The sub-target for the UK was 15% of total energy demand from renewable sources by 2020 and in July 2009 the UK published its Renewable Energy Strategy,<sup>44</sup> with a foreword by the then Secretary of State for Energy and Climate Change, setting out in its Executive Summary the indicative sector contributions: more than 30% of electricity from renewables, 10% of transport energy from renewables and 12% from heat. The heat target was to be met from a range of sources including biomass, biogas, solar and heat pumps.<sup>45</sup>

## The development and introduction of the GB RHI

- 1.12 An RHI consultation document was published by DECC in February 2010 and, reflecting stakeholder feedback, Government policy focused upon a phased introduction.<sup>46</sup> The consultation document explained that Northern Ireland (also referred to as NI) would not be included in the proposed RHI as it was “not covered by the legislation in the Energy Act 2008.”<sup>47</sup>
- 1.13 The GB Renewable Heat Incentive Regulations 2011, which applied in Great Britain (“the GB RHI regulations”), were prepared by DECC and laid before Parliament by its Secretary of State in exercise of the powers contained in section 100 of the Energy Act 2008. The GB RHI regulations came into force on 28 November 2011 with the overarching objective of facilitating the heat sector’s contribution to the Government’s legally binding target of supplying 15% of total energy consumption from renewable sources by 2020.<sup>48</sup>
- 1.14 The explanatory memorandum accompanying the GB RHI regulations recorded that, as the first incentive of its kind worldwide, it generated considerable interest from the public, manufacturers

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40 LEG-00596 to LEG-00598

41 LEG-01706 to LEG-01752

42 LEG-01717

43 LEG-01718

44 INQ-23307 to INQ-23542

45 INQ-23317

46 WIT-177123 to WIT-177209

47 WIT-177199

48 LEG-00947 to LEG-00986

and installers as well as the international community.<sup>49</sup> The stated aim was to encourage the uptake of renewable heat technologies and stimulate the market to meet the objective of increasing renewable heat from 1.5% to 12%. It was recognised that, in order to achieve that end, it would be necessary to subsidise to some extent the movement from fossil fuels to renewable sources.<sup>50</sup> The GB RHI regulations specified the criteria for eligible plant and the eligible purposes necessary to attract subsidy and provided for the scheme to be introduced in two phases – the non-domestic sector followed by the domestic sector, both of which were to be the target of long-term tariff support.<sup>51</sup>

## Protections for the GB RHI

- 1.15 It has been necessary for this Inquiry’s work to highlight relevant steps taken in respect of the GB RHI scheme, which may stand in contrast to what occurred in respect of the NI RHI scheme. It has also been essential for the Inquiry to look at important information and learning that was available from the GB RHI scheme in the context of decisions taken in respect of the NI RHI scheme.
- 1.16 However, it is important that the Inquiry points out that it has not examined the efficacy of the GB RHI scheme, and the Inquiry should not be seen as endorsing (or indeed criticising) any aspect of the GB RHI scheme which may, or may not, have the same, or different, problems to the NI RHI scheme.

## The perverse incentive and its mitigation

- 1.17 The main reservation about revenue support mechanisms for heat is that there could be an incentive to produce heat simply for the purpose of receiving payments and to ‘open the windows’ to get rid of the excess heat, there being no widespread means of transporting it to others or any market for it.
- 1.18 The risk of a ‘perverse incentive’ could arise at any time if payments exceed the costs of producing the heat. There is an added risk with those heat systems that rely on fuel, since the price of fuel can change at any time, potentially impacting on this perverse effect, even if initial tariffs are calculated correctly. However, it is possible to mitigate the perverse incentive, either by ‘deeming’ the amount of heat produced or through ‘tiering’ the tariffs when output is metered.
- 1.19 Deeming, where a fixed rate of payment is set based on an assumed level of production of heat, actually decreases the risk of wasted heat since it is in the operator’s interests to keep usage and costs down, knowing that the income will remain constant regardless. Deeming was not used in the GB or NI non-domestic RHI schemes but has been used for the domestic RHI schemes in GB and NI.
- 1.20 Where there are difficulties in setting a deemed level of heat use, e.g. for the more diverse applications in the non-domestic sector, tiering of tariffs can be used. This allows support to be differentiated to cover separately the additional up front investment costs and any additional ongoing running costs, i.e. when compared to the fossil fuel alternative. This is shown in Figure 1 prepared by the Inquiry below:

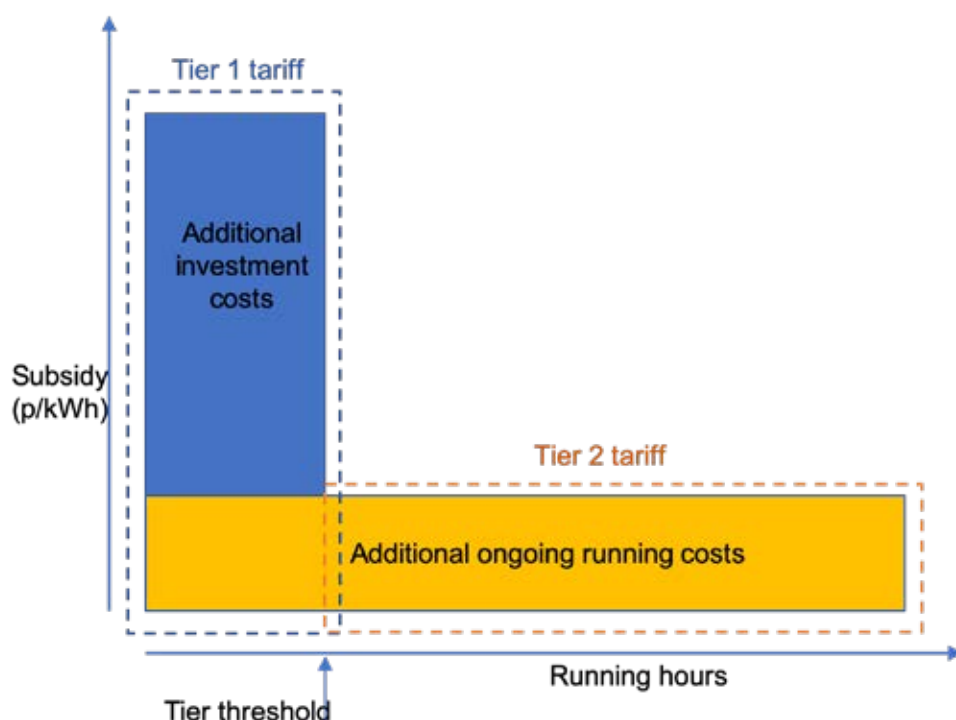
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49 LEG-00987 to LEG-00991

50 LEG-00988

51 LEG-00947 to LEG-00986; LEG-00762

Figure 1 – Subsidies and Tiering Tariffs



- 1.21 In the GB scheme, a combined ‘Tier 1’ tariff was set that covered the combination of the additional capital and running costs for all heat produced up to the tier threshold, which was set at 1,314 hours, equivalent to 15% of the maximum possible production in each year. This ensured that the capital costs would be repaid, even for users with relatively low heat usage and that for heat produced above the threshold, only the additional running costs would be covered.
- 1.22 Above the tier threshold the perverse incentive is reduced or eliminated if the Tier 2 tariff is set at a level below the cost of heat production. However, the combined Tier 1 tariff is more likely to be greater than the cost of heat production, so there is often still the potential for a perverse incentive to maximise production up to this threshold.
- 1.23 Where a scheme is designed with a low tier threshold (e.g. in the GB RHI this was 15% of potential production capacity) the level of the Tier 1 payment has to be relatively high to ensure capital pay-back. This increases the risk of incentivising exploitation, and creates the potential for inappropriate design and operation of installations to maximise production at the higher Tier 1 tariff. One example of this would be to install multiple over-sized boilers, all to be run at or below the tier threshold.

### Tiering in the GB RHI

- 1.24 When the GB RHI scheme commenced in November 2011 it did have tiering in some of its biomass tariffs.<sup>52</sup> In its March 2011 Renewable Heat Incentive consultation document,<sup>53</sup> DECC set out that the RHI tariff structure could provide a “perverse incentive” to generate (useless) heat in order to maximise returns. It recognised that the perverse incentive would

52 LEG-00981 to LEG-00982

53 WIT-177210 to WIT-177310

arise in those cases where the tariffs payable under the scheme were higher than the cost of the required fuel.<sup>54</sup> It considered that the potential for a perverse incentive did exist in respect of some of its biomass tariffs and determined that the risk would be dealt with through tiering the relevant tariffs.<sup>55</sup>

1.25 In Annex II of the consultation on the “Details of Tariffs”, DECC explained:<sup>56</sup>

“Under the tiered structure, a higher initial tier allows installations to receive most of the support needed, upon generating a minimum level of heat generation that any reasonable installation can be expected to require. Upon reaching a prescribed level of heat generation, the tariff drops to a lower tier 2 tariff, which ensures that participants still receive sufficient support to help with fuel costs of further heating requirements, but do not actually make a profit by generating heat purely for the purpose of gaining more support.”

The subject of tiering is highly significant in respect of the NI RHI scheme and will be returned to throughout the Inquiry’s Report.

## The concept of degression

1.26 Degression mechanisms are commonly used around the world on feed-in tariff schemes for renewable electricity. These automatically ratchet down the tariff levels in a predictable manner as pre-set deployment and cost triggers are reached.

1.27 Although not part of the GB RHI scheme when it commenced, DECC was also considering degression as a different form of long-term protection to avoid over subsidising.

1.28 In NERA’s February 2010 report for DECC on ‘The Design of the Renewable Heat Incentive’,<sup>57</sup> at paragraph 4.3.4<sup>58</sup> the authors discussed the concept of degression. They described it as the process by which subsidies might be reduced in a step-wise fashion over time depending upon the developing circumstances of the scheme. The same report emphasised the importance of sensitivity analysis, cautioning that many inputs to a scheme would be highly uncertain and citing, in particular, variation in fossil and renewable heat source prices over time.

## The 2012 GB RHI interim cost control

1.29 While DECC was working on the development of its long-term degression mechanism, and despite it having only launched the GB RHI scheme just four months earlier, in November 2011, it began a consultation in March 2012 on an interim cost control for the GB RHI scheme,<sup>59</sup> which would see the GB RHI scheme suspended if a certain percentage of the available budget was known to have been committed through accreditations on to the scheme.

1.30 In the Ministerial Foreword to the consultation document,<sup>60</sup> the DECC Minister explained that:

“...the RHI is funded from Government spending and we have to ensure that

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54 WIT-177272

55 WIT-177273

56 WIT-177291

57 WIT-175219 to WIT-175302

58 WIT-175267

59 INQ 22081 to 22086

60 DFE-53098



we maintain value for money for the taxpayer and do not spend more than the annual budgets allocated to fund it. We have to learn lessons from the Feed-in Tariffs and ensure that we maintain budgetary control whilst providing appropriate certainty to stakeholders about how we will do this. The RHI must be a long-term, sustainable policy in order to be effective. For this reason, we plan to introduce a comprehensive cost control mechanism which ensures the long-term future of the RHI whilst also providing the transparency and certainty that the market needs to drive investment. We will be consulting on a degression-based mechanism in the summer which would automatically reduce tariffs should spending against the overall budget or deployment of certain technologies exceed forecasts.

Until we are able to introduce the longer-term solution, we need assurance that the scheme will not exceed its budget for the next financial year. Therefore, we are consulting on a short-term measure to give us the confidence that spending will not exceed our budget. The measure proposed is that we suspend the scheme until the next financial year if our evidence shows that the budget could be breached.”

- 1.31 DECC acknowledged that the then current uptake levels on the GB RHI scheme were very low relative to the available budget but cautioned that RHI was a new policy in an immature market, which meant that there was a high degree of uncertainty about deployment in the short-term. Uptake of renewable heat could fluctuate based on volatile variables and, given the infancy of the renewable heat market in the UK, it was necessary to assume a significant level of uncertainty and potential for variance from modelling projections.<sup>61</sup>
- 1.32 The experience of feed-in tariffs and solar PV (usefully summarised in the Court of Appeal decision of *Secretary of State for Energy v Friends of the Earth* [2012] EWCA Civ 28)<sup>62</sup> had taught the Government that it needed to be prepared for rapid, unexpected changes in uptake and to be able to respond quickly. The Minister noted that if the Department had no way of controlling short-term spending, the long-term future of the RHI might be jeopardised. Therefore, it was being proposed that, initially, there should be a power to suspend the scheme until the next financial year if there was evidence that the budget could be breached.<sup>63</sup> A further consultation would be held with regard to the adoption of a degression-based mechanism which would automatically reduce tariffs should spending against the overall budget or deployment of certain technologies exceed forecasts.<sup>64</sup>
- 1.33 In June 2012 the Government published the response to the consultation<sup>65</sup> confirming its intention to introduce, as a temporary measure, the suspension mechanism enabling the GB RHI scheme to be closed to new accreditations for the remainder of the financial year if the forecast indicated that the budget could be breached.<sup>66</sup>
- 1.34 The March 2012 consultation document, and the June 2012 response, are two short documents. The narrative in each spanned less than 10 pages. They clearly articulated a significant potential financial risk to the GB RHI scheme, its budget and the need to have budgetary protections in place to deal with it.

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61 DFE-53098; DFE-53103

62 INQ-05001 to INQ-05016

63 DFE-53103 to DFE-53104

64 DFE-53106

65 INQ-22038 to INQ-22053

66 DFE-53139

- 1.35 The interim cost control was introduced to the GB RHI scheme in July 2012, some 4 months before the introduction of the NI RHI scheme, through the Renewable Heat Incentive Scheme (Amendment) Regulations 2012.<sup>67</sup>

### The 2013 GB RHI degression mechanism

- 1.36 In the same month, July 2012, DECC published a further consultation which dealt with, amongst other things, the long-term degression mechanism.<sup>68</sup> DECC published its response in February 2013<sup>69</sup> and replaced its interim cost control with degression through the Renewable Heat Incentive Scheme (Amendment) Regulations 2013, which came into force on 30 April 2013.<sup>70</sup>
- 1.37 The consultation document explained that degression affords a means of graduated tariff reduction to take account of anticipated breaches of forecast expenditure thresholds or “triggers.” Once an installation is accredited, participants are entitled to payment of subsidy. In effect, degression means that as the scheme becomes increasingly popular and demand rises placing the budget under pressure, the size of the tariff payments for new entrants can be reduced, thereby helping to reduce the risk to the budget from overspend. Since the mechanism only impacted on the tariff and did not control the volume of applicants, there was still a residual risk of overspend.
- 1.38 Tests were to take place quarterly to see if degression was needed, providing one month’s notice of any degression. Triggers were set for each tariff and, if a trigger were hit, a 5% to 10% reduction of that tariff would take place. If take-up of any technology were significantly higher, a “super trigger” 20% reduction might be triggered. This was not expected to occur apart from in exceptional circumstances, but it served to guard against sudden and unexpected popular deployment of any technology. Tariffs reduced as a consequence of degression only applied to new applicants. In practice the time lag of one month’s notice is mitigated by the limited number of suppliers of equipment, the requirement that equipment must be fully operational before approval, and lead times from installation to approval.
- 1.39 In the GB scheme, degression successfully avoided any significant budget over-spend, although it did lead to volatile stop-start deployment rates, which caused severe spikes in demand as degression triggers were approached, followed by periods of very low deployment thereafter. The deployment patterns can be seen in Figure 2 below. The Inquiry has produced this based on statistics from BEIS and Ofgem for monthly applications and applicable tariffs.<sup>71</sup>

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67 INQ-22062 to INQ- 22066

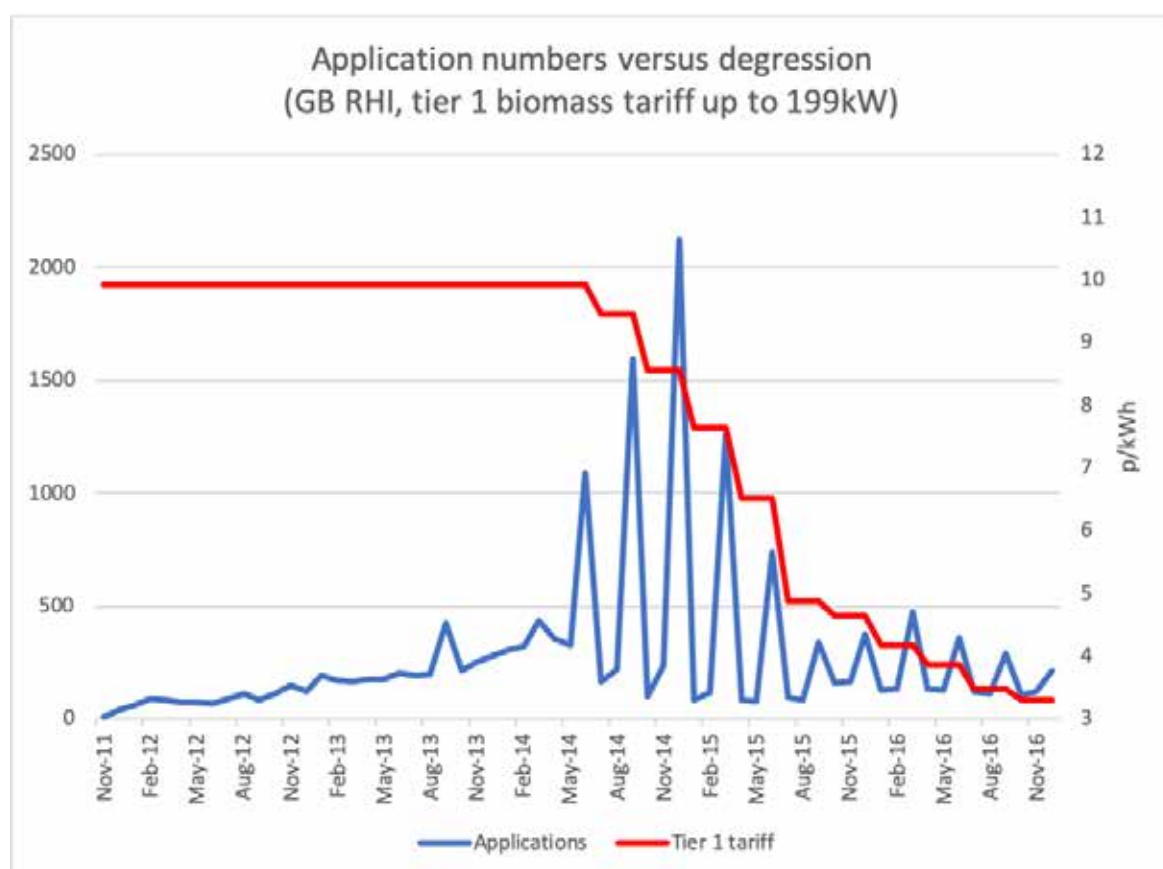
68 INQ-23042 to INQ-23112

69 INQ-23192 to INQ-23273

70 LEG-01054 to LEG-01068

71 INQ-17566; INQ-17567

Figure 2 – Application Numbers versus Degression



Ultimately, the application of degression severely inhibited deployment. The GB scheme is now only expected to deliver about a third of the renewable heat originally projected.<sup>72</sup>

- 1.40 The GB RHI scheme has continued to be subject to change, including in respect of the form of protections on the scheme. The GB RHI scheme itself has also been the subject of an investigation by the National Audit Office<sup>73</sup> and an inquiry by the Westminster Parliament’s Public Accounts Committee.<sup>74</sup>

72 INQ-26011

73 INQ-26001 to INQ-26069

74 INQ-91001 to INQ-91129

## Findings

- 1. There were strong environmental policy pressures to move towards low-carbon and renewable energy sources.**
- 2. In 2009 the UK adopted legally binding EU targets for the deployment of renewable energy as part of the wider European Directive.**
- 3. The UK indicative target of 15% renewable energy included an aspiration of 12% for the heat sector. This was very challenging due to the low starting point.**
- 4. As appears later in this Report, the original 2011 GB RHI regulations formed the basis of the Northern Ireland RHI scheme. For the purposes of this Inquiry certain provisions contained in the GB RHI regulations, and how they were subsequently amended, are of particular significance and are revisited later in relevant sections of this Report.**

## **Chapter 2 – Developments in Northern Ireland (2008 to early 2011): the development of Northern Ireland’s renewable heat policy**

- 2.1 Energy (apart from nuclear energy) had been devolved to Northern Ireland in accordance with the provisions of the Northern Ireland Act 1998<sup>75</sup> and the branch of the Government in NI with responsibility for the development of energy policy was, at that time, the Department for Enterprise, Trade and Investment (DETI), later to become the Department for the Economy (DfE).<sup>76</sup>
- 2.2 DETI was divided into the Policy Group and the Management Services Group, each of which was headed by a deputy secretary who was responsible for a number of divisions. One of the divisions within Policy Group was Energy Division. As Director of the Energy Policy Division at DETI, Ms Jenny Pyper had responsibility from August 2004 to May 2010 for the promotion of the strategic development of the energy industry in Northern Ireland in collaboration with the regulator, the Northern Ireland Authority for Utility Regulation (NIAUR). Her role included management and overall strategic responsibility for a number of branches including the renewables team in Sustainable Energy Branch, which was established in July 2009 to develop departmental policy in relation to the use of renewable energy. In that role she developed energy policy options, provided strategic advice for the DETI Minister and oversaw the development and implementation of The Renewables Obligation Order (Northern Ireland) 2005, including subsequent amendments thereto, which obligated suppliers to source a specified proportion of electricity from renewable energy resources.<sup>77</sup>
- 2.3 New schemes pursuant to the devolution of energy matters, like the NIRO, required primary legislation to be passed by the Northern Ireland Assembly, or by the UK Parliament in conjunction with a Legislative Consent Motion (LCM). Existing powers already facilitated grant support schemes and had been used for the implementation of ‘Reconnect’, a programme to encourage renewable energy (mainly heat) in domestic premises which ran between 2006 and 2008.
- 2.4 DETI was still linked into developments in GB and had the potential to keep abreast of all relevant activities through its permanent seat on the Renewables Advisory Board (RAB). Although NI attendances at meetings of RAB appear to have been limited to four out of 15 between 2006 and 2010, DETI was supplied with copies of papers produced at the meetings. The likelihood of an EU Directive on renewable energy had been appreciated in Northern Ireland during 2007 and 2008 and Ms Pyper’s role as Director of Energy Division included the development of Northern Ireland’s Strategic Energy Framework (SEF) and consideration of emerging renewables initiatives driven by EU Directives. RAB had also specifically considered DECC proposals for renewable heat and so DETI was kept aware of all relevant developments.
- 2.5 The Inquiry notes that while Olivia Martin (responsible for the relevant part of Sustainable Energy Branch within Energy Division, and reporting to Jenny Pyper) was leading the renewable heat development work in DETI she was the Department’s representative on RAB and attended at least one meeting in person. She and her successor, Alison Clydesdale, would have received

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75 LEG-03581 to LEG-03684

76 DETI was renamed DfE in May 2016

77 LEG-03277 to LEG-03326; LEG-03327 to LEG-03477; WIT-09916 to WIT-09918

all relevant documentation. Ms Martin was identified by BERR as the NI contact in the 26 June 2008 BERR ‘UK Renewable Energy Strategy’ consultation document<sup>78</sup> and she had been the recipient of the 50-page BERR draft policy document<sup>79</sup> setting out the reasons why the Government preferred an RHI to an RHO for GB.<sup>80</sup>

- 2.6 BERR officials approached DETI about participating in a joint seminar in September 2008 with a view to NI being included in the proposed 2008 Energy Bill amendment, which would have extended to NI the power to make its own regulations relating to renewable energy or, if it chose to do so, the opportunity of being included in the GB scheme. Scotland and Wales were included and benefitted from the expertise and resources available to what, in October 2008, became DECC. Wales had no relevant devolved powers for energy and automatically became part of all GB/UK schemes, while Scotland became part of the GB RHI scheme after negotiating an understanding with Westminster that the Scottish Ministers would have to agree or be consulted upon all scheme policy and development matters necessary for any scheme.
- 2.7 However, despite the potential benefits of following the other devolved administrations, in Northern Ireland it was considered that renewable heat policy did not have either an adequate evidential or statutory basis, and so Energy Division advised<sup>81</sup> that time and consultation would be needed to understand the specific implications for Northern Ireland in order to develop a policy rationale and strategy tailored to the jurisdiction while, at the same time, maintaining close links with thinking in GB and the Republic of Ireland.
- 2.8 The tension between these two potential approaches was reflected by the observations of the officials who were directly involved during development of the scheme. In oral evidence, Fiona Hepper, who was later to become head of Energy Division in DETI, described Ms Pyper as emphasising how keen the NI Assembly was, at the time, on making its own legislation, stating that she read that as meaning that proceeding by LCM to become subject to the GB Energy Act in 2008 would have seemed like re-devolving powers back to Westminster.<sup>82</sup>
- 2.9 Catherine McArthur, a policy development manager at Ofgem who was responsible for Ofgem’s Feasibility Study in respect of the NI RHI in December 2011, explained to her colleagues in an internal briefing note that DETI officials regarded it as “imperative to differentiate the NI scheme from Great Britain’s.”<sup>83</sup>
- 2.10 Ms Hepper referred in her written evidence to the fact that DETI did “benefit from following in their [DECC’s] slip stream” but also told the Inquiry in oral evidence that the feeling was that “we need to plough our own furrow and we need to see what is appropriate for the Northern Ireland-specific conditions.”<sup>84</sup>
- 2.11 It is important to remember that this was taking place in the context of restoration of a devolved administration in NI in May 2007 after a period of three years of Direct Rule from Westminster. Chris Stewart, who later became deputy secretary in DETI from 2014 to 2016, succeeding David Thomson, referred the Inquiry to the:

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78 INQ-21157 to INQ-21445 at INQ-21184

79 DFE-25101 to DFE-25158

80 DFE-25146 to DFE-25147

81 DFE-25263 to DFE-25268; DFE-25605 to DFE-25608; DFE-25683 to DFE-25685; DFE-26736 to DFE-26742

82 TRA-01775 to TRA-01776

83 OFG-17384

84 WIT-15028 to WIT-15029; TRA-01777 to TRA-01778

“...very strong desire on the part of Ministers to make the most of devolution and to show that the value of devolution is that it’s locally elected, locally accountable policy – eh, [sic] politicians, who are making the policy decisions that shape society and shape Northern Ireland.”<sup>85</sup>

- 2.12 However when DETI later sought legal advice, with regard to drafting the RHI regulations from both the Departmental Solicitor’s Office (DSO) and the Belfast office of the independent firm of solicitors, Arthur Cox, in contrast with the views of Mr Stewart, Nicola Wheeler of DSO explained that the working practice was not to “...deviate from what GB’s doing unless there’s a very good reason to do so.” and Alan Bissett of Arthur Cox, the externally consulted firm of solicitors, also agreed that consistency with GB was “an overarching principle.”<sup>86</sup>
- 2.13 There was also concern as to the practicality of obtaining an LCM from the Assembly in the relatively short time available. In the autumn of 2008 the LCM, which at that time required 25 stages, was not a well-developed nor understood procedure and was felt to be only appropriate for uncontroversial matters with no cross-cutting implications. Understanding was improved by a subsequent Assembly inquiry and report by the Committee on Procedures in September 2009<sup>87</sup> which sought to bring about greater clarity and codification.<sup>88</sup> Nevertheless the Inquiry notes that an LCM had already been passed relating to the Renewables Obligation earlier in 2008 during the passage of the same Energy Bill which passed into legislation in November 2008.
- 2.14 This issue was brought to Minister Foster’s attention in the form of a submission from Ms Pyper on 22 September 2008.<sup>89</sup> There was clearly time pressure on Northern Ireland to decide quickly whether or not to be included in the UK-wide RHI enabling powers being added to the Energy Bill, by then at its later stages in parliament. The balance of the advice was clear and Minister Foster agreed with the recommendation that Northern Ireland “should not seek to be included in these potential amendments to the Energy Bill” and “should not be covered by a UK heat strategy” at least for that round of legislation. Ms Pyper referenced not only the problems with seeking an LCM in such a short time frame but also a range of other cross-cutting policy implications. She wrote:

“I cannot see how we could develop a credible position in the timeframe so instead I propose that we give BERR a positive form of words for a short section on Northern Ireland which would allow us to be included in general terms but spell out areas of policy difference which will require a tailored NI plan.”<sup>90</sup>

## Developing a renewable heat strategy and support mechanism for Northern Ireland

- 2.15 In order to progress the RHI’s further development Ms Pyper’s team held a series of focus groups in February and March 2009.<sup>91</sup> In April, she and her team reviewed the DECC Heat and Energy Savings Strategy that had been published in February of the same year and which

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85 TRA-11536

86 TRA-02845; TRA-02902

87 INQ-101484 to INQ-101540 (Committee on Procedures Inquiry into Legislative Consent Motions, 34/08/09R, 15 September 2009)

88 INQ-101484 to INQ-101540

89 DFE-25263

90 DFE-25267

91 WIT-09925

included a renewable heat incentive proposal as a response to the 2009 Directive.<sup>92</sup> On 30 April she forwarded a submission to Minister Foster seeking agreement for a work programme leading to the development of a renewable heat strategy and support mechanism for Northern Ireland.<sup>93</sup> The submission received ministerial approval in May.<sup>94</sup> In June Minister Foster approved a business case to engage consultants to assist Ms Pyper’s team and it was noted that an economic appraisal would be needed in due course.<sup>95</sup> In September Minister Foster was briefed on proposals to form a DETI-led project steering group (later renamed the ‘Oversight Group’) to guide and manage the work of the consultants.<sup>96</sup> It was suggested that the group include representatives from other NI Departments, academia and key stakeholders including Action Renewables, the Carbon Trust and the Ulster Farmers’ Union (UFU). This group was chaired by Ms Pyper from January to May 2010.<sup>97</sup>

2.16 The Energy Division did already have some relevant experience having previously run ‘Reconnect’, its own renewable energy incentive scheme. Early in 2009 it received a report by KPMG that reviewed the outcome of that grant programme, which had run from 2006 to 2008.<sup>98</sup> The scheme had been very successful in stimulating installation of renewable energy in homes – mainly renewable heat in the form of biomass with some solar applications.

2.17 According to written evidence from DfE, despite high levels of uptake it actually underspent its budget for grants, administration and marketing (which appears to contradict the KPMG finding that the administration and marketing budgets had been overspent).<sup>99</sup> The scheme also successfully stimulated the supply chain with the number of installers increasing from 38 to 673.<sup>100</sup> In that context the Inquiry has taken into account the criticism of Neil Elliott of Future Renewables who told the Inquiry in oral evidence that a number of “pop-up installers” had installed bad technology, taken the grant and then removed the installation if it did not work.<sup>101</sup> In addition, Bernie Brankin, in DETI Finance, would later (in May 2011) remind DETI Energy Division, in the context of her warning relating to RHI funding, that the Reconnect grant scheme, had been “fraught with control problems.”<sup>102</sup> However, as would be seen later, relative value for money in Reconnect was considerably better than would be achieved by the RHI scheme – the total capacity supported under the RHI scheme would have cost about £40 million at Reconnect rates, equivalent to about 1p/kWh.

## The 2010 AECOM/Pöyry report

2.18 In November 2009, following a tendering process, the consultancy firm AECOM Ltd was awarded a contract to provide an assessment of the potential development of renewable heat in Northern Ireland. The terms of reference prepared by Peter Hutchinson, who joined DETI Energy Division as a deputy principal in 2009, for Ms Pyper, then head of Energy Division, included requirements to:

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92 INQ-24742 to INQ-24884

93 DFE-26722 to DFE-26735

94 DFE-26736 to DFE-26742

95 DFE-26798 to DFE-26810

96 DFE-26848 to DFE-26852

97 WIT-09925 to WIT-09926

98 DFE-39373 to DFE-39498

99 WIT-24136 to WIT-24137; DFE-39484

100 DFE-39454 to DFE-39455

101 TRA-04627 to TRA-04628

102 WIT-00840 to WIT-00841



- (a) undertake an independent assessment to identify and quantify the current scale, future sustainable growth and optimum size and scale of the renewable heat sector in Northern Ireland;
  - (b) make recommendations as to the options for encouraging the deployment of renewable heat technologies in Northern Ireland; and
  - (c) make recommendations for an evidence-based renewable heat target and consider how this target might impact upon existing energy markets in Northern Ireland.<sup>103</sup>
- 2.19 AECOM worked with the energy economists Pöry Energy Consulting. As previously mentioned, the work was overseen by an Oversight Group which was chaired by Ms Pyper and comprised representatives from Government Departments and agencies including the then Department of Agriculture and Rural Development (DARD), and Invest NI, as well as Action Renewables, academics with relevant expertise and other interested parties such as the UFU.
- 2.20 As her last involvement in the development of policy, Ms Pyper briefed Minister Foster on the interim report findings in April 2010.<sup>104</sup>
- 2.21 The final report, the production of which was overseen by Ms Clydesdale, was provided in July and concluded that the level of renewable heat in Northern Ireland was currently very low at 1.7% of overall demand, a large proportion of which was installed under the Reconnect programme and mostly met by biomass, with a small amount from heat pumps and solar thermal systems.<sup>105</sup>
- 2.22 The authors concluded that a 10% renewable heat market share was achievable in Northern Ireland but would require significant Government intervention, and that a long-term strategy for renewable and low carbon heat should be developed including options for incentivisation.<sup>106</sup> The report identified two main alternative means of providing financial support, namely capital grants and renewable heat incentives, and, in relation to the latter, it referred to the scheme being pioneered in GB.<sup>107</sup>
- 2.23 AECOM expressed the view that the GB scheme appeared to be inefficient for Northern Ireland by over-incentivising some technologies and not encouraging the most cost effective options. The advice was that Northern Ireland should develop a specific incentive scheme and also put in place interim measures to help meet the 10% target while the details of an NI-specific scheme were being further assessed.<sup>108</sup>
- 2.24 AECOM predicted that capital grants would have a very limited impact if the main cost of heat was ongoing maintenance and fuel and not the initial capital expenditure, in which case grants would have been better.<sup>109</sup> They also noted that grants offer an ability to differentiate and target support, helping to avoid overcompensation as well as to avoid overspend.<sup>110</sup>
- 2.25 AECOM also warned that the costs for an RHI scheme could be up to four times higher than for the most cost-effective approach because it was designed to provide a similar rate of

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103 DFE-26804 to DFE-26810

104 DFE-380299 to DFE-380308; DFE-43009 to DFE-43173

105 WIT-00368 to WIT-00541

106 WIT-00376

107 WIT-00462

108 WIT-00508

109 WIT-00507

110 WIT-00462 to WIT-00463

return to all technologies, no matter how expensive or efficient.<sup>111</sup> They pointed out that some applications, including non-domestic solid biomass from 45kW upwards, already appeared to be cost-competitive and may not require any tariff support.<sup>112</sup> AECOM advised that more work was required, including assessment of what should be incentivised, analysis of options for each sector, assessment of finance and consultation with stakeholders.<sup>113</sup>

2.26 With regard to the introduction of incentive schemes the advice was:

“While it is not possible to state the time for the above actions to take place, it is anticipated that this will require at least 1-2 years to complete, suggesting an incentive could possibly be introduced during 2012, which will also allow DETI to benefit from the outcomes of the DECC RHI experience.”<sup>114</sup>

During the Department’s consideration of the AECOM report, in June 2010 Ms Hepper replaced Ms Pyper as DETI’s Director of Energy Division after being asked to take up the position by the then Permanent Secretary of DETI, David Sterling. Ms Hepper was a grade 5 civil servant in DETI who had been director of the Strategic Planning Directorate, which covered a wide range of policy and operational issues. In her new role she assumed responsibility for all aspects of energy policy, including the development of renewable heat. She had held an economic portfolio but had no experience in the field of energy, nor was any such policy experience specifically required or sought by those making the appointment to the post. Ms Hepper was known to Ms Pyper and two half-day meetings took place between them before Ms Pyper departed during which Ms Pyper took her through the main issues with which she had been dealing.<sup>115</sup> Ms Hepper said that she received a portfolio of papers from the Division but there was no formal handover or brief from Ms Pyper.<sup>116</sup> There does not appear to have been any requirement or expectation of a formal handover at the time.

2.27 Ms Hepper was aware of the AECOM/Pöyry Consultancy work, the report based upon which had been submitted to DETI and adopted by the steering committee when she arrived. Ms Hepper told the Inquiry that her role had been to make sure the report was absolutely finalised and the Minister briefed.<sup>117</sup> It seems likely that it would have been discussed in the context of Ms Pyper’s submission to Minister Foster in April 2010<sup>118</sup> and it was the subject of Ms Hepper’s ministerial submission in August 2010, discussed below.

## The 9 August 2010 ministerial submission

2.28 On 9 August 2010 Ms Hepper briefed Minister Foster and her Special Adviser (SpAd), Dr Crawford, with a submission on the findings of the AECOM/Pöyry study and advised her as to the need for statutory powers and liaison with DECC on the overall funding position.<sup>119</sup> A copy of the Executive Summary of the AECOM/Pöyry report was supplied. Ms Hepper noted that funding was yet to be agreed by Her Majesty’s Treasury (HMT) and that any arrangements

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111 WIT-00467 to WIT-00468

112 WIT-00463 to WIT-00464

113 WIT-00509 to WIT-00510

114 WIT-00510

115 TRA-01767

116 TRA-01767 to TRA-01769

117 TRA-01770

118 DFE-36797 to DFE-36505

119 DFE 27683 to DFE-27698

would have to be agreed by the Department of Finance and Personnel (DFP).<sup>120</sup> She pointed out that there had been increased interest in renewable energy from a number of NI sources including MLAs, industry representatives and RHI lobbyists.<sup>121</sup> In the course of her submission Ms Hepper stated that the AECOM/ Pöyry study had reached a number of conclusions including the following:

“Northern Ireland needs to develop a specific RHI scheme and further economic work is required to assess the actual incentivisation levels required. The GB Renewable Heat Incentive scheme appears to be inefficient for Northern Ireland, by over-incentivising some technologies and not encouraging the most cost-effective options.”<sup>122</sup>

Consequently, there was a need to engage a consultancy body to undertake an economic appraisal of a Northern Ireland RHI scheme. Included with the submission Ms Hepper provided Minister Foster with two draft letters: the first was a draft letter to Rt Hon Chris Huhne MP, then Secretary of State at DECC, seeking further information as to funding; the second was a draft letter to the ETI Committee Chair, Alban Maginness MLA.<sup>123</sup> The submission also looked ahead to a potential NI scheme, noting the developments in GB, and advised that there could be clear economies of scale to be gained by “piggybacking” on Ofgem’s experience and software design developed for its administration of the GB RHI scheme.<sup>124</sup>

- 2.29 In a related submission on the same date advising Minister Foster on a response to correspondence from Mark Durkan MP MLA, which sought an update in respect of the renewable heat study, Ms Hepper told the Minister that all details relating to the design and implementation of an RHI for Northern Ireland would have to be subject to public consultation but that it could be expected that many elements of an NI scheme, barring tariff levels, would be similar to the GB scheme.<sup>125</sup>

## The September 2010 press release

- 2.30 The Minister subsequently approved the appointment of external consultants, notified the Chairman of the ETI Committee, Mr Alban Maginness, of progress to date<sup>126</sup> and issued a press release referring to the GB RHI scheme on 20 September 2010 stating that:

“The Department of Enterprise, Trade and Investment study examined the need for a similar scheme and has concluded that a RHI which takes into consideration the specific Northern Ireland heat market should be developed provided that it is economically viable.”<sup>127</sup>

- 2.31 In September 2010 DETI also published a Strategic Energy Framework for Northern Ireland with a foreword by Minister Foster.<sup>128</sup> The Strategy had been in development for some time and was one of the key pieces of work transferred by Ms Pyper to Ms Hepper. It included

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120 DFE-27683 to DFE-27684

121 DFE-27689

122 DFE-27685

123 DFE-27692 to DFE-27695

124 DFE-27687

125 DFE-27536 to DFE-27544; DFE-27538

126 DFE-28808 to DFE-28819

127 DFE-29641 to DFE-29642

128 DFE-15192 to DFE-15237

an endorsement of the target of a 10% contribution from renewable heat by 2020 and the Department undertook to consider how best to encourage new entrants into the renewable heat market. DETI also agreed to publish a Renewable Heat Route Map by March 2011.<sup>129</sup>

- 2.32 The target of 10% of heat from renewable sources was adopted in the NI Executive’s 2011-15 Programme for Government.<sup>130</sup> Minister Foster wrote to the Secretary of State at DECC on 16 September 2010 confirming that the lack of time and local evidence had prevented Northern Ireland from being included in the GB RHI scheme.<sup>131</sup> She recorded the completion of the AECOM/Pöyry study and asked to be kept up to date with regard to funding and further developments of the GB scheme.

## The 2010 Spending Review – HMT funding for RHI

- 2.33 In October 2010 the Chancellor of the Exchequer’s statement in the Spending Review provided £860 million of funding for the GB RHI scheme over the spending review period 2011-15.<sup>132</sup> In his 2010 Spending Review Settlement letter to the Northern Ireland Executive, the Chief Secretary to the Treasury informed the office of the First Minister and deputy First Minister (OFMDFM) that if the Northern Ireland Executive:

“...choose to introduce an NI Renewable Heat Incentive Scheme then AME funding of £2/4/7/12 million will be available over the SR period based on a population based share of the GB scheme, NIE officials should inform my officials of their intentions to feed into AME forecasts.”<sup>133</sup>

- 2.34 During the autumn of 2010 significant progress took place in the development of the NI RHI scheme. On 29 October Alison Clydesdale emailed Sam Connolly, a deputy principal economist at DETI within the Analytical Services Unit (ASU), who had been involved in the development of RHI policy and had been providing economic advice to Energy Division for some time, and Carmel McConville (DETI Strategic Planning & Economics Branch) noting that “...we agreed that since the funding was only being made available for an RHI that this essentially meant that our options could not proceed – so we have limited the EA to only looking at the RHI option.”<sup>134</sup> It seems clear that, at that time, Ms Clydesdale believed that the HMT funding was “ring fenced” to deliver an RHI scheme rather than a grant support system or other options.<sup>135</sup>
- 2.35 On 1 November Ms Hepper sent a submission to Minister Foster and Dr Crawford, notifying them that HMT had advised that £2/£4/£7/£12 million (i.e. a total of £25 million) of Annually Managed Expenditure (AME) funding would be available for an RHI scheme and advising that DETI would need to take enabling powers.<sup>136</sup> At paragraph 5 of that submission Ms Hepper confirmed that an economic appraisal would be commissioned shortly and should be complete by the end of February 2011. Her submission continued: “As funding has been offered, the economic appraisal can now focus on determining tariff levels, assessing eligibility requirements and developing a cost-effective RHI for Northern Ireland.”<sup>137</sup>

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129 DFE-15212

130 DFE-262049 to DFE-262112

131 DFE-28629 to DFE-28630

132 INQ-51210 to INQ-51315

133 DFE-28820 to DFE-28829

134 DFE-186559

135 DFE-186561

136 DFE-195293 to DFE-195300

137 DFE-195295

- 2.36 On the same date, Minister Foster notified OFMDFM that the offer of funding should be accepted.<sup>138</sup> She explained that Northern Ireland had not been included in the GB RHI scheme because of the different nature of the heat market, namely the dependence on oil, the need to protect the developing gas market, the different energy costs, higher levels of fuel poverty and the rural nature of the NI jurisdiction. These were all factors which made it more appropriate for a separate assessment focussing on the local situation.

### The 30 December 2010 ministerial submission to appoint CEPA

- 2.37 Ms Hepper advanced a further submission to the Permanent Secretary, Minister Foster and Dr Crawford on 30 December 2010 seeking approval of a business case formally to appoint Cambridge Economic Policy Associates (CEPA) as external consultants.<sup>139</sup> Both the submission and the supporting documentation emphasised the urgency of the matter. The submission was timed “Desk Immediate”, adding that DFP approval upon completion of the appraisal was required “...to ensure spend in 2011/12 is achievable.”<sup>140</sup> Paragraph 14 of the submission again emphasised that it was essential for the project to go ahead as soon as possible and paragraph 7.3 of the business case stated that: “Further to this, HMT has allocated £2M of funding for a Northern Ireland RHI in 2011/2012, to ensure this money is utilised this economic appraisal must proceed with further delay [sic].”<sup>141</sup> The business case document also asserted that there was “no possibility in deferring this assignment” and “delaying this project would also lead to this money being unspent.”<sup>142</sup>
- 2.38 While the Terms of Reference for the consultants specified an open requirement to make recommendations (based on the evidence gathered and the economic analysis carried out) on the most cost-effective structure of a Northern Ireland RHI scheme, to increase the level of renewable heat to 10%, the Inquiry noted that the business case to DFP to engage a consultant defined an RHI scheme in much more restrictive terms in a footnote on page 1:
- “An RHI is an incentive scheme that will reward those who install eligible renewable heat technology with a set tariff to be paid over a number of years, the level of tariff and length of payment is determined by the size and type of technology involved. The tariffs are set in order to cover the capital, operating and other non-financial costs of installing such technologies.”<sup>143</sup>
- 2.39 However, Mr Cockburn of CEPA confirmed in oral evidence to the Inquiry that CEPA had considered a full range of options.<sup>144</sup> The CEPA reports are considered in detail in chapter 5 of this Report.
- 2.40 It was also realised that for an NI RHI scheme to proceed, a legal basis was required. Section 100 of the 2008 Energy Act had conferred upon the DECC Secretary of State in GB the power to make regulations to establish a Renewable Heat Incentive scheme in GB but, as explained earlier, the legislation did not include an enabling power for a scheme in Northern Ireland.<sup>145</sup>

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138 DFE-62001 to DFE-62005

139 DFE-58027 to DFE-58063

140 DFE-58028

141 DFE-58032; DFE-58042

142 DFE-58036

143 DFE-58051 to DFE-58063; DFE-58034

144 TRA-01237 to TRA-01238

145 LEG-00316 to LEG-00318

- 2.41 By early 2011 however, with the AECOM report in hand, an announcement on the direction of travel from the Minister and a clear offer of funding from HMT, DETI was in a position to seize the opportunity of further energy legislation going through the UK Parliament.

### Obtaining enabling powers for an NI RHI

- 2.42 In February 2011 the NI Executive agreed with the proposal that NI should be included in the 2011 Energy Bill, then being processed through Parliament, with a view to being granted enabling powers to implement regulations analogous to those which had been used to establish the GB scheme. The relevant Legislative Consent Motion (LCM) was passed by the Assembly on 14 March 2011.<sup>146</sup>

- 2.43 In her letter of 24 March 2011 to DECC Secretary of State Huhne, Minister Foster said:

“I want to stress that an amendment that would extend the same powers held in section 100 of the 2008 Energy Act to Northern Ireland is vital to allowing my department to introduce a specific RHI for Northern Ireland, using separate secondary regulations, in time to utilise HMT funding and support the achievement of both DETI and UK-wide targets.”<sup>147</sup>

The Minister included with her letter a copy of instructions to Parliamentary Counsel in order to assist with the drafting of the proposed amendment.<sup>148</sup> Paragraph 2.9 of those instructions recorded the policy objective as being the implementation in NI of a “scheme that is similar to the scheme in GB” tailored to suit the NI energy market and, at paragraph 3.7, the instructions advised that the “broad scope and purpose” of the RHI scheme in NI was intended to be the same as that proposed for GB save for one point relating to the definition of biofuels.<sup>149</sup>

- 2.44 In due course, section 113 of the Energy Act 2011 conferred power on DETI to make regulations establishing a scheme to facilitate and encourage renewable generation of heat in NI and provide for the administration and financing of such a scheme.<sup>150</sup>

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146 DFE-60157 to DFE-60161

147 DFE-29305 to DFE-29311

148 DFE-29307 to DFE-29311

149 DFE-29308; DFE-29310

150 LEG-00876 to LEG-00878

## Findings

5. DETI was made aware of relevant policy developments in renewable energy including renewable heat. It received regular updates from DTI/BERR/DECC and had access to the knowledge base, resources and documentation of the Renewables Advisory Board.
6. DETI had previous experience of running a grant support scheme for renewable energy, Reconnect, and therefore DETI was not starting completely from scratch.
7. In 2008 the amendment to the Westminster Energy Bill was only proposing the grant of enabling powers. The powers were to facilitate the potential introduction of a GB RHI scheme or, potentially a UK-wide RHI in which NI could have participated. The Inquiry has no reason to believe that it would have been impossible to agree wording which allowed NI to be included in the enabling powers but still to opt out and pursue its own approach, if desired. The Inquiry notes that Scotland had already adopted such a pragmatic approach.
8. The Inquiry also notes that the NI Assembly had already passed an LCM relating to renewable electricity earlier in the passage of the same Energy Bill and that the Assembly was ultimately capable in 2011 of passing the LCM for the grant of powers for the NI RHI in eight weeks.
9. However, the Inquiry is aware of the fact that, at this time, the devolved administration had recently been returned to NI after a period of 4.5 years of direct rule from Westminster (from October 2002 to May 2007) and a number of witnesses recalled the desire to make the most of devolution and demonstrate that policy decisions were being made by local politicians. The Inquiry notes the often-conflicting evidence submitted regarding subsequent policy development in general, with regard to whether to copy and/or be part of GB initiatives or to adopt an NI specific approach. This reveals a tension between the two approaches in which it would have been very difficult for officials to decide which of two differing directions to follow.
10. Ms Pyper appreciated that there was no adequate statutory or evidential basis for renewable heat policy in NI where heating was powered principally by oil rather than gas. She understood that a renewable heat policy could have implications for four or more Departments and, therefore, could be potentially cross-cutting, in which case an LCM would have been viewed as inappropriate at the time.<sup>151</sup> She did warn of the need for resources in relation to this policy area.<sup>152</sup> In due course the AECOM/Pöyry report confirmed that the GB scheme appeared to be inefficient for NI, as it had the potential to over-incentivise some technologies and not encourage the most effective options and advised that a scheme specific to NI was required.<sup>153</sup> In all the circumstances, taking into account the contemporary political climate, on balance, the Inquiry does not criticise Ms Pyper for her decision not to seek RHI enabling powers through inclusion in the 2008 UK Energy Act.

151 WIT-09924

152 WIT-09926

153 WIT-00508





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## Chapter 3 – Funding and the RHI scheme

- 3.1 During the course of the Inquiry’s investigation it became apparent that there were issues surrounding the nature of the funding made available for the NI RHI scheme, how it was understood by various officials, whether the greater risk it carried had been properly communicated to those who should have been made aware of it, and whether the greater risk had been adequately catered for in the design of the NI RHI scheme.
- 3.2 The Inquiry received a considerable volume of detailed and often technical evidence about these matters. Government funding is often complex and technical. What follows in this chapter is an examination of some of the key issues surrounding matters of funding as far as it related to the NI RHI scheme and findings the Inquiry needs to make in relation thereto.

### AME and DEL

- 3.3 Public expenditure provided by HMT and approved by Parliament is generally classified as either Annually Managed Expenditure (AME) or Departmental Expenditure Limit (DEL). The former is for expenditure that is demand-led and/or volatile and, therefore, difficult to predict or control by a UK Department or a devolved administration.<sup>154</sup>
- 3.4 The October 2010 HMT Statement of Funding Policy (SFP) for the devolved administrations described the concepts of DEL and AME in the following way:<sup>155</sup>

“1. Departmental Expenditure Limits (DELs) set firm, multi-year spending limits. Expenditure in DEL is split between those items within the assigned budget and those within the non-assigned budget. Spending within DEL is generally undifferentiated, as the devolved administrations will have full discretion over their spending priorities; these are ‘assigned budget’ items. Changes in provision for these items are determined through the Barnett Formula (see Chapter 4). If spending in DEL, however, is exceptionally ring-fenced and specific to that spending priority, these are known as ‘non-assigned budget’ spending items; and

2. Annually Managed Expenditure (AME) covers items whose provision is reviewed and set for the coming year annually (at spring Budget) and certain self-financed expenditure. AME expenditure cannot be recycled from one AME programme to another or recycled to increase the DEL. Within AME, expenditure is classified between ‘Main Departmental programmes in Annually Managed Expenditure’ and ‘other AME’ spending. Main Departmental programme spending covers policy-specific, ring-fenced items where provision is included within the Vote from the United Kingdom Parliament. The AME element of the budget is reviewed twice-annually, and forecasts are made for a number of years ahead. Thus the AME element of the budget can move up or down and, hence, the total budget itself may move up or down in line with AME. ‘Other AME’ spending includes locally financed expenditure, including expenditure financed by the Scottish Variable Rate of Income Tax; these are not ring-fenced and may be allocated, as the devolved administrations consider appropriate.”

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154 WIT-180025

155 INQ-50008

3.5 In Northern Ireland’s own “Managing Public Money Northern Ireland”, issued by DFP/DoF, the concepts are defined as follows:

**“Departmental expenditure limits (DEL):** provision planned and managed over three years, with some scope (subject to DFP agreement and rules) for carrying forward unspent provision into future years. Usually comprises most of each department’s resource budget. Includes limits on near-cash expenditure and on the cost of administration.

**Annually managed expenditure (AME):** expenditure which is not as readily controlled as DEL is but which must be budgeted for each year, including social security expenditure.

Both DEL and AME may include capital and resource provision.”<sup>156</sup>

3.6 The vast bulk of AME funding goes towards welfare and pensions expenditure and interest on debts. For other programmes to end up funded through AME, rather than DEL, is an exception rather than the rule, and it is a decision specifically reserved for HMT to make.

3.7 In contrast, Ministers may allocate the DEL funds provided to their departments at their discretion in support of Government programmes and their priorities, provided that they stay within the relevant DEL limits set by HMT.<sup>157</sup>

3.8 The ‘HMT Consolidated Budgeting Guidance’, an annual HMT publication designed to set out the applicable budgeting rules (and guidance as to their application) for a given year, sets out the criteria that are applied by HMT in determining whether spending can be classified as AME. The March 2010 version,<sup>158</sup> setting out the guidance for financial year 2010-11, described the position in this way:<sup>159</sup>

“Criteria for Treatment in DEL or AME

1.33 All programmes are in DEL unless the Chief Secretary has determined that they should be in AME. The Chief Secretary may agree to put programmes into AME if:

- They are demand-led or exceptionally volatile in a way that could not be controlled by the department and where the programmes are so large that departments could not be expected to absorb the effects of volatility in their DELs; or
- For other reasons they are not suitable for inclusion in firm three year plans set in the spending review. For example: Lottery spending is the product of the hypothecated tax on the National Lottery and may not be reprioritised elsewhere. Certain levy-funded bodies, which serve particular industries, are in AME – see Appendix 4 to this chapter.

1.34 Not all departments have AME programmes.

1.35 The Treasury regularly reviews whether programmes in AME are still suitable for AME treatment. Where appropriate programmes are moved into DEL.”

156 WIT-35242

157 WIT-180025

158 INQ-51727 to INQ-51868

159 INQ-51739

## AME

- 3.9 AME expenditure is subject to a different management process from DEL budgets in order to reflect its different nature, and there are different rules that apply as to how it can be used.
- 3.10 AME is managed through a forecasting process reviewed twice annually and money cannot be recycled from one AME project to another or recycled to increase the DEL. AME generally also cannot be used to fund administration or civil service staff costs, all of which have to be met from a Department's DEL.<sup>160</sup>
- 3.11 The same HMT Consolidated Budgeting Guidance from 2010-11 explains<sup>161</sup> what is expected of Departments that are in receipt of AME funding:

### “Management of AME Programmes

1.40 The management of AME programmes serves the same ends as the management of DEL programmes, but the system for managing AME programmes is different. AME programmes are often demand-led or otherwise volatile programmes when it would be unreasonable to expect departments alone to bear the risks associated with variations in demand or spending. The volatility of many AME programmes means that careful management is important.

1.41 Departments are reminded that with AME programmes also, just as with DEL, they need to:

- Put in place processes to monitor spending in year, to identify longer-term trends in spending, and to provide robust projections of future spending. Early identification of changes in AME spending are needed to allow risks to be managed effectively;
- Review AME programmes regularly to ensure that they are helping to achieve Government objectives effectively and efficiently. Departments should discuss with the Treasury proposals for optimising AME spending programmes;
- Agree with HM Treasury prior to implementation any change which would increase AME spending – this includes both policy reforms and any administrative changes which impact on expenditure, for example measures to promote take-up;
- Consider carefully the impact of DEL spending on AME spending and vice versa, both within and across departments. For example, DEL usually includes the cost of administering AME programmes and the quality of administration can have a significant impact on AME expenditure. And some DEL and AME programmes are complementary;
- If a proposed DEL spending change has extra costs for AME spending, then the proposal needs to be cleared with the Treasury before being implemented;
- Consider with the Treasury what steps should be taken to support fiscal discipline and value for money if spending on AME programmes rises above expectation. As noted below, where the actions/inaction of a Department increase AME, they

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160 INQ-51738 to INQ-51741

161 INQ-51739 to INQ-51740

are assumed to fund the increases in AME by reductions in their DEL budgets, or by identifying firm savings in AME; and

- Monitor spending in Resource AME and ensure that they take steps where appropriate to prevent undue increases in spending that affects the Surplus on the Current Budget.”

3.12 The same HMT Consolidated Budgeting Guidance indicated,<sup>162</sup> though the position would be articulated differently by HMT over time, that the fact AME annual spending did not stay within forecast was not considered a breach of a spending limit in the way it would for a DEL budget. It also did not carry an automatic penalty from HMT if an AME forecast was breached. This position was no doubt to reflect the different nature of AME spending; demand-led or exceptionally volatile.

3.13 At the same time, the guidance did explain<sup>163</sup> that unforeseen changes in AME spending may indicate poor financial management by Departments, and held out the potential that the additional spending beyond AME forecasts may have to be offset, for instance, through DEL in the following year.

#### AME funding for devolved administrations

3.14 UK Government funding for the devolved administrations’ budgets is normally determined within spending reviews alongside spending settlements for UK Government Departments and in accordance with the policies set out in HMT’s SFP.<sup>164</sup> The 2010 SFP recorded that the majority of each devolved administration’s spending would be allocated in spending reviews by applying the Barnett Formula (a combination of a comparative population share, a V.A.T. adjustment and comparability of the allocation) but confirmed that there were a number of exceptions in respect of which that formula was not appropriate. Such exceptions included some DEL programmes and **all** (the Inquiry’s emphasis) AME items.<sup>165</sup>

3.15 Section 5.3 of the 2010 SFP stated that the devolved administrations would not normally need to find offsetting savings from elsewhere in their budgets when AME forecasts changed at planning stage or during the financial year to cover increases; such increases would normally be met by HMT. However, increases in AME programme spending arising from policy decisions taken by the respective devolved administrations would have to be met from their respective budgets. Such decisions would generally involve action or inaction on the part of the devolved administration leading to breach of parity with relevant UK spending. The 2010 SFP, as noted above, recorded that:

“Increases in Annually Managed Expenditure programme spending, which arise from policy decisions taken by the respective devolved administrations, will be met from their respective budgets.”<sup>166</sup>

3.16 This wording became even more explicit by the time of the equivalent direction in the HMT 2015 Statement of Funding Policy which read as follows:

162 INQ-51744

163 INQ-51744

164 INQ-50001 to INQ-50060

165 INQ-50017

166 INQ-50017

“Where a devolved administration wishes to offer more generous terms for an AME programme, then the excess over that implied by adopting broadly similar criteria to the relevant UK government department or body (and therefore broadly comparable costs) for that programme must be met from within their DEL budgets.”<sup>167</sup>

- 3.17 Most public expenditure in NI tends to be DEL and is provided through the block grant by means of which the NI Executive receives approximately 3% of the UK Government budget for public services. The block grant is adjusted each year in accordance with the population-based Barnett Formula. As already referred to above, the Inquiry notes that the HMT 2010 SFP specifically provided at section 5 that the application of the Barnett Formula was inappropriate for *all* (the Inquiry’s emphasis) AME items of devolved administration spending.<sup>168</sup> The Inquiry notes that the wording of the 2010 letter from the Chief Secretary of the Treasury offering funds for the RHI referred to a “population-based share” rather than the Barnett Formula.<sup>169</sup>
- 3.18 As discussed in more detail later, the Inquiry did hear evidence suggesting that there was a view held by some in the administration in Northern Ireland that the more AME money that came in the better. While in principle there is nothing wrong with a desire to have as much money available for the devolved administration as possible, it must be remembered that all taxpayers’ money has the same value. Paragraph 1.39 of the HMT Consolidated Budgeting Guidance from 2010-11<sup>170</sup> is instructive in this regard:

“1.39 AME programmes are spending like any other. They impact on the fiscal framework in the same way as DEL spending. They need taxes to be raised to finance them. So careful monitoring and management is just as important as it is with DEL. And the nature of certain AME programmes means that some aspects of management, e.g. forecasting, are more important than with most DEL programmes.”

### DECC’s GB RHI AME funding

- 3.19 Prior to the RHI scheme, nearly all energy schemes had been funded by levies on consumer bills and so did not impact on departmental budgets and were not subject to the same direct involvement of HMT in setting rules for their use. For a number of reasons, it had been decided to fund the RHI scheme directly out of tax and this raised concerns in DECC.
- 3.20 The Inquiry had access to correspondence between DECC and HMT from 2009,<sup>171</sup> wherein the basis of DECC’s request for the RHI to be classified as AME was set out. DECC at that time was a new Department and it had a relatively small DEL budget and sought the agreement of HMT to treat the GB RHI expenditure as AME on the ground that, in accordance with HMT guidance, such funding was appropriate in respect of “large, demand-led expenditure which was difficult to forecast.”<sup>172</sup> DECC was concerned that the uncertainties of an RHI scheme produced a risk to its DEL budget which was already committed to other programmes. Officials pointed out the need for flexibility and stated that the decision on classification of funding was “crucial to the development of the policy”, emphasising that the renewable heat market was “small,

167 INQ-50074

168 INQ-50017

169 DFE-257518 to DFE-257527; DFE-257522

170 INQ-51739

171 WIT-180058 to WIT-180081

172 WIT-180058

undeveloped and prone to large variations in demand as a result of changes in economic conditions, weather and fuel prices.”<sup>173</sup>

3.21 HMT in turn was not prepared to bear the full risk either, as is clear from the outcome of its discussions with DECC. The DECC business case seeking AME funding status for RHI, and the HMT analysis of it, bears careful scrutiny for the detailed consideration that was undertaken, and the indication that collaborative monitoring was envisaged between DECC and HMT.<sup>174</sup> In a letter from the Chief Secretary to the Treasury dated 6 January 2010,<sup>175</sup> although agreeing to AME classification, HMT sought to ensure that DECC took a measure of responsibility for the risk of overspend by requiring the inclusion of strong cost controls.<sup>176</sup>

3.22 DECC undertook to ensure that there were appropriate mechanisms in place to control the overall costs. Such controls were of fundamental importance since the scheme would be a world first, incentive-based with volatile, unpredictable demand and funded with public money. The 6 January 2010 HMT letter to DECC referred to above, which confirmed that the GB RHI could be budgeted through AME, required that the funding would be subject to a number of specific conditions, which included:

- (i) A charging arrangement to ensure that DECC faced real financial incentives to prevent overspends. DECC agreed that any RHI AME overspending in one year would be repaid out of the AME budget in future years and, as a further incentive, DECC would be required to fund a proportion of any such repayment from their wider DEL budget;
- (ii) DECC would be expected to give HMT regular, detailed updates on cost drivers and compliance activity under the scheme; and
- (iii) Given the long period between regular reviews of support, there had to be legislative scope for an emergency review should levels of spend through the scheme rise significantly above forecast.<sup>177</sup>

3.23 Following a 12-week DECC GB RHI consultation in February 2010, the feedback from which was overwhelmingly supportive, detailed proposals were published in March and a commitment to renewable heat was included in the 2010 Spending Review.<sup>178</sup>

3.24 The 2010 settlement letter issued to DECC by HMT following the 2010 Spending Review specifically stated that:

“Spending through the Renewable Heat Incentive will be budgeted through AME, but a condition of this treatment is that DECC will need to contribute towards any overspend above the Spending Review forecast...in order to provide sufficient incentive to manage spending to forecast and to take on a fair share of the fiscal risk.”<sup>179</sup>

173 WIT-180058 to WIT-180059

174 WIT-180060 to WIT-180080

175 WIT-180082 to WIT-180083

176 WIT-180026

177 WIT-180082 to WIT-180089

178 INQ-20375 to INQ-20461; DFE-15270 to DFE-15359; INQ-51210 to INQ-51315

179 WIT-180050 DFE-257518 to DFE-257527

### NI RHI's AME funding

3.25 On 20 October 2010 Danny Alexander, then Chief Secretary to the Treasury, wrote to the then First and deputy First Ministers of the NI Executive setting out the Northern Ireland Executive's funding allocation arising from the 2010 Spending Review.<sup>180</sup> The direct quotation from that letter, as far as it relates to RHI, reads as follows:

“If NIE choose to introduce an NI Renewable Heat Incentive Scheme then AME funding of £2/4/7/12 million will be available over the SR period (2011/2012 – 2014/2015) based on a population-based share of the GB scheme. ***NIE officials should inform my officials of their intentions to feed into AME forecasts.***”<sup>181</sup>  
(the Inquiry's emphasis)

3.26 No further information was provided. The Inquiry found no evidence that the devolved administration in Northern Ireland, or DETI in particular, was informed of the background behind why the potential NI RHI scheme was to be funded by AME. DETI had no knowledge of the detailed discussions that had taken place between HMT and DECC over the issue, or the nature of the formal parameters of the RHI funding that had been communicated by HMT to DECC.

3.27 In a written response to a series of questions addressed to HMT by the Inquiry, the Director of HMT's Public Services Group, with responsibility for the relationship with the NI Executive, advised that: “As heat is a devolved policy area, the NIE had full autonomy over scheme design.”<sup>182</sup> However, as noted above, the 2010 edition of the SFP confirmed at paragraph 5.3 that the devolved administrations would not normally need to find off-setting savings from elsewhere within their budgets when forecasts changed at planning stage or during the financial year to cover expenditure upon AME items, the exception being expenditure which arises from decisions taken by the respective devolved administrations which would have to be met from their respective budgets.<sup>183</sup>

3.28 A further response to the Inquiry from HMT stated that it was standard practice for Departments to be expected to manage their AME spend and continued:

“Where the spending department has levers to control the spend, the Treasury may expect the department to use those to control spending and, where the department fails to (or indeed takes action that would increase spending), the department would be expected to meet the costs from within its DEL budget.”<sup>184</sup>

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180 DFE-257518 to DFE-257527

181 DFE-257522

182 WIT-180027

183 INQ-50017

184 WIT-180048

## Findings

11. Neither the content of HMT’s confirmation letter to DECC of 6 January 2010 nor the details of the earlier funding negotiations with DECC were communicated to the relevant NI Departments, whether in the NI Settlement Letter of 20 October 2010 or otherwise.
12. No information was given to either DFP or DETI about the exchanges that had taken place between HMT and DECC with regard to the unusual nature of the form of AME funding for the RHI scheme or to the conditions that had been imposed on DECC in response to the request for funding in that form. That was of particular significance bearing in mind that the budget capped on population share was an unusual form of AME. Indeed, applying a cap to an AME budget was essentially a contradiction in terms given the unpredictable nature of the schemes in respect of which AME funding was usually considered appropriate. Most significant of all was the omission by HMT, the source of the funding, to formally provide the devolved legislature with details of the “risk sharing” agreement reached with DECC that overspending might have an impact on the DEL budget. The only source of such information for DETI was to be the Parker and Patel emails in 2011 (which are dealt with later in this chapter). While certain relevant policy decisions were subsequently taken by DETI, such as the omission to provide budget cost controls and tiering, the Inquiry finds that, when the funding was originally notified, HMT ought to have clearly informed DETI of the basic structure of the particular form of AME funding including the “risk sharing” element that had been agreed with DECC. Such clear notification would have provided DETI with an added impetus to ensure it had the necessary ‘levers’.
13. The Inquiry notes that the differences in HMT’s communications to DECC and to DETI continued. The spending settlement letter to DECC in respect of the 2015-16 financial year specified that:

**“Spending through the RHI will be budgeted through AME but a condition of the treatment is that DECC will need to contribute towards any overspend above the Spending Review forecast...”<sup>185</sup>**

The Inquiry finds that no such warning was included in the equivalent NI 2013 spending round letter, which did not even make a reference to RHI.<sup>186</sup> HMT provided AME cover for the RHI overspend in 2015-16 without qualification.

185 WIT-180050

186 DOF-59030 to DOF-59036



## The communication of the funding message

- 3.29 During the course of the Inquiry’s work it became evident that there was a long chain of communications involved in discussions about funding issues in Northern Ireland. The Inquiry was told that pursuant to a long-standing protocol or convention, all communications between HMT and DFP/DoF should be between the devolved administration spending team in HMT and the Central Expenditure Division (CED) in DFP/DoF. Onward communication from CED should be through the Supply Team in DFP/DoF, whose role should be to inform the relevant Finance Division in the spending Departments, which, in turn, should liaise with the relevant Department’s policy/spending divisions.
- 3.30 Breach of the protocol was treated as a serious matter and was illustrated by the DETI Finance Director, Trevor Cooper, who told the Inquiry that he received a telephone “roasting” from Stuart Stevenson in DFP as a result of DETI failing to observe the protocol when it engaged directly with HMT over RHI funding.<sup>187</sup>
- 3.31 DFP CED (from May 2016, DoF CED) was responsible for the planning and management of public expenditure in Northern Ireland, including the provision of biannual forecasts of AME spending to the Office of Budget Responsibility (OBR) and liaison with HMT. In her oral evidence to the Inquiry, Joanne McBurney, a grade 5 accountant and head of CED in the Public Spending Directorate (PSD) of DFP/DoF from September 2014, described the RHI funding as coming “out of the blue” in respect of which the initial reaction would have been to welcome any additional funding for investment in Northern Ireland.<sup>188</sup> She accepted that AME with annual caps, as outlined in the 20 October 2010 letter from the Chief Secretary to the Treasury, would be unusual and she was not aware of any other specific AME funding that was similarly subjected to a cap in this way.<sup>189</sup>
- 3.32 Given the volatile and unpredictable demand-led feature of schemes for which AME was generally felt appropriate, some witnesses told the Inquiry that a capping mechanism would almost amount to a contradiction in terms. It was certainly unusual in NI experience and should have alerted DFP officials to make inquiries of HMT as to the circumstances in which it was to apply in this case. However, Ms McBurney thought that the need to keep “in budget” was something which Departments would regard as normal practice. She considered that once DETI had been informed of the cap, the onus was on that Department to manage within that limit and to comply with other public spending guidance such as Managing Public Money NI and the Consolidated Budgeting Guidance.<sup>190</sup> The CED responsibility was to query DETI if any of the AME forecasts they provided exceeded the relevant cap and, as far as Ms McBurney was aware, the AME forecasts provided by DETI did not exceed the caps from the inception of the scheme up to and including 2014-15.<sup>191</sup>
- 3.33 Agnes Lennon, who was a grade 7 in CED when the funding was initially provided for RHI and responsible for AME forecasts, felt that the concept of “a population-based share” was “a slight anomaly” and “a little unusual” since it was calculated and capped as a population share of the

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187 TRA-04176 to TRA-04177

188 TRA-03261

189 TRA-03290; WIT-42251

190 WIT-42262

191 WIT-42253

DECC spend.<sup>192</sup> She explained that although they had experience of the potential for a DEL impact arising from breaking ‘parity’ and deviating in the type of service provided, in the case of the RHI scheme the DEL impact related to any overspend above the unusual population-share cap. She recalled that after receiving the October 2010 HMT settlement letter she had spoken to both Keith Jarret of the HMT NI Spending Team and to Jon Parker of the HMT Energy Team and subsequently discussed the matter with the DETI Supply Officer.<sup>193</sup> She concluded that, in keeping with all AME funding, expenditure needed to be carefully and properly managed and controlled. As a consequence of her contacts with HMT, Ms Lennon was certain that she emphasised to DFP Supply that the allocation for the NI RHI scheme was capped. She considered that, in the circumstances, it was the responsibility of DETI to devise an appropriate scheme with cost controls firmly in place.<sup>194</sup>

## Attempts to clarify the funding arrangements

### The April 2011 Parker email

- 3.34 In early 2011 a very important email exchange relating to the proposed funding took place. Alison Clydesdale of DETI was, in 2011, the grade 7 head of Sustainable Energy Branch, reporting to Fiona Hepper the then head of Energy Division. Ms Clydesdale had taken over responsibility for renewable heat within DETI from July 2009.<sup>195</sup> Ms Clydesdale, emailed Rosalind Leeming of DECC on 4 March 2011 to update her on the progress on the LCM for the 2011 Energy Act amendment to facilitate the introduction of an NI RHI scheme and asking if she could have early sight of DECC’s proposals for the GB RHI scheme (NI already having opted to proceed separately from the GB RHI).
- 3.35 In the course of her reply on 11 March Ms Leeming, having identified an error in DETI’s LCM instructions over how funding would be provided, confirmed that DECC had previously abandoned the proposal to adopt levy-based funding as had been used previously on most energy incentive schemes, adding that “...funding has been made available for the GB and prospective NI scheme through standard AME spending.”<sup>196</sup> Ms Clydesdale responded on the same day acknowledging the error in the DETI drafting and indicating that “we have accepted the AME funding – indeed we had a call from Treasury on it yesterday”.<sup>197</sup>
- 3.36 Following at least one telephone conversation on the subject, and in answer to a request for further information from Ms Clydesdale, Mr Parker of HMT, on 15 April 2011, confirmed to DETI that HMT had an agreement with DECC to cover spending commitments up to 20 years for installations installed within the Spending Review (SR) period, and indicated that similar terms would apply to an NI scheme. He set out the escalating funding profile that had been allocated to DECC for each of the financial years within the spending review period and advised that the NI share would be 2.98% of DECC’s RHI budget, which the NI scheme would need to follow “as much as possible.”<sup>198</sup> However, he then proceeded to point out the following:

192 WIT-44634

193 WIT-44634 to WIT-44635

194 WIT-44663

195 WIT-12521

196 DFE-60267 to DFE-60268

197 DFE-60267

198 DFE-62063

“The other key point it is necessary to let you know is that the DECC RHI spending is not being treated as standard AME, where the Exchequer takes on all risks of overspend. Instead, there is a risk-sharing arrangement whereby should RHI spending in one year exceed the SR profile, then DECC would need to repay this in future years. They can do this through announcing changes to the SR that will bring cost savings relative to the SR profile in future years. However, a small proportion of any required future savings (still to be determined, but likely to be of the order of 5%) will have to be funded through contributions from DECC’s DEL. Again, these rules would be applied in equivalent fashion to NI.”<sup>199</sup>

- 3.37 The Inquiry notes that Mr Parker was emailing as joint head of the Energy Policy Team in HMT and not as a member of the HMT NI Spending Team (though members of the HMT NI Spending Team were copied in). However, he had clearly been of assistance to Ms Clydesdale, who found his reply most helpful and who passed on the Parker email to Ms Hepper, the head of Energy Division, and to the DETI finance team with a question about the involvement of DFP.<sup>200</sup>
- 3.38 Ms Clydesdale passed on this exchange to, and sought advice from, Ms Brankin in Finance Division of DETI, who was aware of the HMT 20 October 2010 settlement confirming the availability of AME funding for an NI RHI scheme that she described as her first experience of “gift funding” for which it had not been necessary to bid.<sup>201</sup>
- 3.39 Ms Brankin informed Ms Clydesdale on 15 April 2011 that she had now received confirmation from DFP of the annual AME allocations for Energy Division totalling £25 million over the four financial years from 2011-12 to 2014-15 as noted above.<sup>202</sup> Ms Brankin explained that she discussed the non-standard nature of the AME funding with her head of Finance Division, Trevor Cooper, because she had no prior experience of it. Mr Cooper advised Ms Brankin that it would be necessary to speak to Stuart Stevenson, DETI’s DFP Supply Officer.<sup>203</sup>

### The 3 May 2011 Brankin warning

- 3.40 On 3 May 2011 Ms Brankin emailed Ms Clydesdale confirming Energy Division’s AME but also now pointing out that she had since spoken to Mr Stevenson, the DFP supply officer for DETI, about the NI RHI AME allocation. Ms Brankin informed Ms Clydesdale “RHI AME funding is not being treated as standard AME” and that one of the effects would be that “if you overspend in any year, DETI’s budget will be reduced by the amount of overspend in future years”. She explained that “your RHI budget allocation is being treated the same as DEL allocations.”<sup>204</sup>
- 3.41 According to Ms Brankin, Mr Stevenson advised that it would be best to treat the budget “the same as DEL allocations.”<sup>205</sup> The effect of this was said to be that underspends in any year would be lost while overspends would be taken out of DETI’s budget for future years. She advised her Energy Division colleagues that this treatment of AME should be taken into account when drawing up any proposals and made the following request:

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199 WIT-00843

200 WIT-00842 to WIT-00843

201 WIT-00842; TRA-01642 to TRA-01643

202 WIT-00841

203 WIT-24030

204 WIT-00840 to WIT-00841

205 WIT-00840

“Please copy Finance into your draft proposals which would need to address the controls that you would put in place to prevent significant under/over spending. These proposals will also require DFP approval.”<sup>206</sup>

3.42 Ms Brankin explained in her oral evidence that the reference to “Finance” in this advice had been to the Accountability and Casework Branch of Finance Division that also reported to Mr Cooper.<sup>207</sup>

3.43 Ms Brankin had also reminded Ms Clydesdale of the problems of budget control that had been encountered in relation to the Reconnect Scheme, albeit that was a domestic grant-based scheme.<sup>208</sup>

3.44 On the following day, 4 May 2011, Ms Clydesdale passed on Ms Brankin’s communication to Mr Hutchinson, copying in Ms Hepper, and Mr Connolly. Ms Clydesdale described it as a “significant challenge” and informed him that DFP would require evidence of “...our ability to control the scheme in order to minimise over/under spending in any one year.”<sup>209</sup> She referred to the Reconnect Scheme stating:

“From a finance perspective grant is the riskiest route financially as it is hard to control the number of applications especially at the end of the programme. But from the policy side I expect we will need some element of front-loaded grant to stimulate demand.”<sup>210</sup>

3.45 The Inquiry notes the perception of problems with the administration of Reconnect. The most recent evidence from DfE suggests this was not about breaching the budget, so is likely to have been about the difficulties in forecasting and managing described by Ms Clydesdale.<sup>211</sup>

3.46 Ms Clydesdale also advised her colleagues in her 4 May email that it was necessary for CEPA to be asked to factor in the information from Ms Brankin as a risk factor in the economic appraisal that they were preparing, noting that no relevant reference had been included in the draft already received.<sup>212</sup> However, this requirement does not seem to have been passed to CEPA, who appear to have based their reports upon the working assumption that the figures making up £25 million over 4 years, possibly followed by some continuing funding to 2020, were effectively capped on a ‘first come first served’ basis.<sup>213</sup>

3.47 Ms Clydesdale told the Inquiry in oral evidence that she believed that Ms Brankin was telling her that, as the funding was being treated as DEL, there was a need to control it within each relevant year. She said that she had discussed the matter with Ms Brankin and that they agreed that a tariff-based scheme would technically be more predictable, based on a metered quarterly basis, as well as easy to predict and monitor. She explained that any unpredictable increase in the number of applicants could be controlled by:

“...putting in a control to either stop applications coming in or to delay them. Bernie and I were discussing in-year budget management, and it was the nice,

206 WIT-00841

207 TRA-03207 to TRA-03209

208 WIT-24027

209 WIT-00840

210 WIT-00840

211 WIT-24136 to WIT-24137; WIT-12771

212 WIT-00840

213 TRA-01248 to TRA-01253

predictable, smooth pattern of an RHI tariff-based, quarterly, metered data [sic] seemed attractive.”<sup>214</sup>

- 3.48 Ms Clydesdale also mentioned in her Inquiry witness statement that in June 2011, although she had by then moved to a new role, she was still asked to provide comments on the DETI RHI public consultation document, which included a draft copy of the proposed NI RHI regulations.<sup>215</sup> However, she does not appear to have made any representation or comment upon the obvious absence of any administrative or statutory power of suspension of the scheme or control of the budget.
- 3.49 On 27 May 2011, on the front page of the first submission from Ms Hepper to the Minister and her SpAd after the 2011 email exchanges, Ms Hepper informed the Minister that “HMT has advised that £25 million of AME is available over the spending period should Northern Ireland choose to introduce a RHI”, but no reference was made to the qualifications, risks and consequential necessary steps confirmed by the earlier email exchanges.<sup>216</sup>
- 3.50 When questioned about this omission by Inquiry Counsel, Ms Hepper said “...I think we have obviously been aware of the qualification on it but we keep using that as shorthand.”<sup>217</sup> When asked whether the funding could have been more accurately described she said:
- “I certainly think it wouldn’t have been unhelpful to have been a little more explicit, but it’s with hindsight, absolutely. In writing it at the time we probably made an assumption that people knew there was a qualification there which does not reflect with hindsight.”<sup>218</sup>
- 3.51 Ms Hepper also told the Inquiry in her oral evidence that she was “pretty sure” that she had told Minister Foster of the unusual nature of the funding and that she was “pretty sure” that the Minister would have seen that in some budgetary documents. In the course of questioning by the Inquiry Counsel as to whether she had a specific recollection of informing the Minister, Ms Hepper said “Not a specific recollection, no, but I would be fairly sure that she would have been informed. But I can’t point to something in particular.”<sup>219</sup>
- 3.52 For her part, the former Minister has denied that she was ever aware that the funding was qualified before the autumn of 2015. She told the Inquiry that she had never encountered AME funding with DEL consequences and that she was not familiar with the HMT Statement of Funding Policy.<sup>220</sup>
- 3.53 Dr Crawford, who also denied being informed of the important qualifications or additional risks,<sup>221</sup> said that if the Minister had been so informed, she undoubtedly would have asked to see the correspondence.<sup>222</sup>

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214 TRA-00996

215 WIT-12523

216 DFE-29342

217 TRA-01848

218 TRA-01849

219 TRA-01849 to TRA-01850

220 TRA-07785 to TRA-07791

221 TRA-07651

222 TRA-07652

### The June 2011 Patel warning

- 3.54 Further efforts were made to clarify the funding situation by Mr Hutchinson engaging with DECC's Akhil Patel on 8 June 2011. In addition to questions about the availability of funding beyond 2015 (and the answer's potential effect on the length the scheme could stay open to new applicants) and about funding rising with inflation, Mr Hutchinson asked, given the funding was AME, whether unspent money from one year could be rolled over into the next. Further, and importantly, Mr Hutchinson asked Mr Patel: "how will you manage against overspend in your budget – i.e. could the scheme close temporarily if it was oversubscribed?"<sup>223</sup>
- 3.55 Mr Patel replied on 8 June 2011<sup>224</sup> and confirmed that any overspend that could not be met out of the following year's AME budget would have to be taken from the DEL budget. In view of the "large financial risk" this represented, Mr Patel informed Mr Hutchinson that the DECC policy team were developing a system of "tariff degression" that could be deployed at key points to ensure that the risk of overspending could be managed.<sup>225</sup> He provided his contact details and invited Mr Hutchinson to contact him to discuss the issues further as required.
- 3.56 Mr Hutchinson told the Inquiry that he did not know why the information about the funding qualifications had not been "front and centre" in the communications with CEPA.<sup>226</sup> Ms Hepper confirmed in oral evidence that after that June 2011 exchange it was clear that any overspend would come out of the DEL budget and that represented a significant financial risk.<sup>227</sup> She was uncertain as to what happened to the Patel email:

"I'm pretty sure that it was drawn to my attention, and I'm not sure if I discussed it with my line manager or whether the team discussed it with finance; I genuinely don't know."<sup>228</sup>

### Confusion over the nature of the RHI funding

- 3.57 The Inquiry notes witnesses' varying degrees of understanding of the funding arrangements for the NI RHI.
- 3.58 Ms Clydesdale, who engaged with HMT's Jon Parker and DETI Finance's Ms Brankin in April and May 2011, described her understanding as "crystal" – it was not standard AME and any overspend would come from the NI Block.<sup>229</sup> She engaged with Mr Hutchinson and Ms Hepper about it. Mr Hutchinson later engaged with Mr Patel as discussed above.
- 3.59 In October 2011, Joanne McCutcheon (who in May 2011 had succeeded Ms Clydesdale as the head of what became Energy Division's Renewable Heat Branch, the new home for officials working on the NI RHI, and who reported directly to Ms Hepper, the then head of Energy Division) approached DETI Finance's Ms Brankin about the potential to re-profile the £2 million from the 2011-12 financial year through one of the biannual AME forecasting exercises, that was otherwise going to go unspent (as the RHI was not up and running at that point).<sup>230</sup>

223 WIT-16381 to WIT-16382

224 WIT-16380 to WIT-16382

225 WIT-16380

226 TRA-01591 to TRA-01592

227 TRA-01858

228 TRA-01859

229 PWC-04475

230 DFE-463387

3.60 Ms Brankin replied on the same day, attaching to her response the April 2011 email exchange between Ms Clydesdale and Mr Parker, and her own May 2011 email warning to Ms Clydesdale. Ms Brankin had also copied Ms Hepper into her reply, as well as some of her own finance officials. Her reply contained the following emphatic warning:

“However, as I advised Alison earlier (see attachment), RHI spending is not being treated as standard AME. This means that your RHI NI budget allocation is being treated the same as DEL allocations. If you underspend in any year, that part of your budget is lost to the department, but you may wish to reduce budgets to prevent building underspending in to your outturn. If you overspend in any year DETI’s DEL budget will be reduced by the amount of overspend in future years which is a position that we would not want to be in. Therefore, you should not increase AME expenditure in any year.”<sup>231</sup>

3.61 Ms McCutcheon forwarded Ms Brankin’s email to Sandra Thompson.<sup>232</sup> She was a Staff Officer in Energy Division’s Energy Co-Ordination Branch who assisted Energy Division officials with financial matters. Ms Thompson was to discuss the question of the potential £2 million RHI underspend with Ms Hepper the next day.

3.62 Ms Hepper was asked about the 5% penalty for potential RHI overspends mentioned in the Parker April 2011 email. She told the Inquiry in oral evidence:

“Well, the other thing was that Jon Parker was in the energy team in DECC, [sic] and we got useful information from them, but then it had to move into the devolved budgets team, and that was most definitely DFP engaging with them, and they never came back to confirm that it would only be a 5% DEL. So we just always assumed if you went over by any amount that you were liable for the whole amount.”<sup>233</sup>

3.63 Mr Connolly, the DETI economist who advised Energy Division on the RHI, said that he did not recall seeing the Parker email exchange. He explained that he had been absent from work for three weeks and only returned on 8 May 2011, some four days after being copied in to the email chain starting with Ms Clydesdale’s email of 4 April to Mr Parker.<sup>234</sup> Mr Connolly told the Inquiry that he was not familiar with the distinction between AME and DEL funding.<sup>235</sup> No one appears to have brought that distinction to his attention, notwithstanding the clear warning in the emails about the need for cost controls.<sup>236</sup> He also informed the Inquiry that he had not been made aware of the exchange between Mr Hutchinson and Mr Patel of 6 June 2011 nor told that the funding represented a “large financial risk”.<sup>237</sup>

3.64 DFP CED’s Ms Lennon maintained that “complexity did not exist in the straightforward capped allocation” and it would not have been “in order for HMT to interfere and discuss cost controls” with a devolved administration.<sup>238</sup> She found the April 2011 Parker email “irritating” as being a direct communication with HMT outside the usual protocol.<sup>239</sup> However, Ms Lennon has

231 DFE-463386

232 DFE-463386

233 TRA-01857

234 TRA-03392

235 TRA-03394

236 TRA-03395

237 TRA-03409

238 WIT-44663

239 WIT-44664

described the ‘key message’ from DFP to DETI as being “DO NOT OVERSPEND this capped AME allocation as it will have a DEL impact.”<sup>240</sup>

3.65 Whilst Ms Lennon was clear in her recollection, and the Inquiry accepts her evidence, the Inquiry has been unable to identify a clear and objective communication chain ensuring that a message in such stark terms was passed from DFP to DETI.

3.66 Her colleagues in DFP, Mr Brennan, then head of CED, and Mr Stevenson, then DFP’s DETI Supply Officer, do not appear to have fully understood the potential risks implicit in the NI funding in the event of an overspend.<sup>241</sup> In the event, they did not seek any further clarification from colleagues or HMT. In his written evidence, Mr Brennan confirmed that, prior to the RHI scheme, he could not recollect any other funding proposal with a similar AME limit and associated DEL penalty and that he had not appreciated that the actual scheme funding had an implication beyond the AME profile initially agreed by DETI.<sup>242</sup> Mr Brennan was copied into Ms Clydesdale’s reply to HMT’s Jon Parker on 15 April 2011,<sup>243</sup> along with members of the HMT NI Spending Team. As a consequence of Ms Clydesdale copying him in, Mr Brennan forwarded her email to Mr Stevenson, Ms McBurney and Ms Lennon asking:

“Do you know what DETI are up to? We just need to be sure about what commitments they might be entering into and the possible wider consequences for the NI Executive – especially if the DETI actual spend deviates from forecast and the Centre has to pick up the pressure (even if it all remains in AME).”<sup>244</sup>

3.67 Mr Stevenson forwarded the Parker email to DETI Finance Director Trevor Cooper and appears to have spoken to him about it.<sup>245</sup> Mr Stevenson could not remember the conversation he appears to have had with Mr Cooper, and could not remember going back to Mr Brennan, though he thought it highly unlikely he would not have done so in some way, given Mr Brennan had asked him for information as to what DETI was doing.<sup>246</sup> Mr Stevenson did have further conversations with DETI’s Ms Brankin about RHI in advance of her 3 May 2011 email to Ms Clydesdale warning that the RHI funding should be treated like DEL.

3.68 In the course of giving oral evidence to the Inquiry, David Sterling, Permanent Secretary of DETI between October 2009 and June 2014, agreed that he was not aware of any other projects that were similarly funded. He added that, at the time he was Permanent Secretary at DETI he knew that whilst this was an unusual funding arrangement and that it was AME, nonetheless it was capped and it really needed to be treated as if it was conventional DEL, because exceeding that budget cap would have consequences. However, he also accepted that into 2014-15 officials entertained the misconception that the funding was conventional AME and that exceeding the budget would not lead to any impact on the DEL budget.<sup>247</sup>

3.69 Nevertheless, it appears quite clear to the Inquiry that there was awareness of a *risk* (the Inquiry’s emphasis) of some degree to the DETI DEL budget and that, given the novelty of the scheme and the unpredictability of demand, careful consideration of some form of budget

240 WIT-44664  
 241 TRA-01739 to TRA-01742  
 242 WIT-43218 to WIT-43219  
 243 WIT-30248  
 244 WIT-30248  
 245 DFE-143685  
 246 TRA-02777 to TRA-02780  
 247 TRA-06773



control was essential. What is less clear is how the documentation relating to this, and a clarity of understanding about it, at least among some officials, was lost over time. It is also unclear why the unusual nature of the funding, and its potential consequences, together with the heightened need for budget protection, were not specifically brought to the attention of those being asked to approve the NI RHI scheme, such as the members of the Casework Committee and, more importantly, the DETI Minister.

- 3.70 It appears that the relevant email exchanges were placed in a TRIM (an electronic file management system) folder under the label ‘RHI Funding’ but in separate chains and not in such a way that a civil servant colleague could easily recover the whole chain without searching through all the contents. The records of who accessed TRIM indicate that Ms McCay, who temporarily filled the gap at grade 7 level for 6 weeks in May and June 2014, between the departure of Ms McCutcheon and the arrival of Mr Stuart Wightman, did later retrieve all the emails, although in both her written and oral evidence to the Inquiry she maintained that she was not told of the April 2011 Parker email chain and that her general understanding was that the funding was AME outside the DEL budget.<sup>248</sup>
- 3.71 In later evidence to the Inquiry it became clear that the information did not survive the 2013-14 staff changeover in any unified, objective and easily identifiable form. Thus, the funding position was ‘clarified’ in the First Day Brief for the new Permanent Secretary, Dr McCormick, who replaced Mr Sterling in June 2014 as follows:
- “Funding stream for grant payments is Annually Managed Expenditure (AME) directly from HMT with no separate bidding process.”<sup>249</sup>
- 3.72 There were no words of qualification or caution as to the funding being subject to a cap, with DEL implications if the cap were exceeded, or of the clear consequential need for some type of cost control. The same inaccurate sentence was incorporated into the briefing for the new Deputy Secretary, Chris Stewart, who took over the Policy Group from Mr Thomson in August 2014.<sup>250</sup>
- 3.73 Mr Wightman, who became head of the new Energy Efficiency Branch (which included RHI) in July 2014, did recover the Parker email in September 2014 as part of his work on obtaining DFP approval for the introduction of the domestic RHI scheme, but, according to his evidence, without understanding its full significance at that time.<sup>251</sup>
- 3.74 The Inquiry was not provided with any clear objective evidence that an accurate description of the funding arrangements and risks ever reached any Minister before late 2015/early 2016.
- 3.75 The loss of this vital information seems to have been an example of the price paid as a result of there being no effective project management ensuring an objective record of progress and continuity of relevant knowledge and experience.

### Early confusion over permitted use of RHI funding

- 3.76 The evidence considered by the Inquiry also suggests that there was an initial confusion over how the funding that HMT was making available for renewable heat could be used.

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248 TRA-05509; WIT-13034

249 TRA-07058; DFE-415609

250 WIT-12311

251 TRA-06966 to TRA-06971

3.77 In the context of tendering for economic consultancy during an email exchange between Carmel McConville (DETI Strategic Planning & Economics) and Ms Clydesdale (into which Mr Connolly and Ms Hepper were copied) Ms Clydesdale, on 29 October 2010, wrote:

“Options – when I spoke with Sam we agreed that since the funding was only being made available for an RHI that this essentially meant that our other options could not proceed....The previous study has identified various options (such as grant support, industrial sector support only etc.) but there is no funding for these as the HMT funding is ring fenced for us to deliver an RHI. Do you mean for us to look at these other options in the EA or do you mean to look at various options for delivering the RHI only – I’m hoping it’s this second point.”<sup>252</sup>

3.78 Ms McConville responded that, while it made sense to only consider the option relating to the RHI scheme, the appraisal might need a small paragraph to explain why that was the case. She wrote:

“This may include why this money has been ring fenced and what are the rules governing the funding. Carrying on from this the appraisal should then look at the various options for delivering the RHI.”<sup>253</sup>

Paragraph 3 of the terms of reference subsequently issued to potential candidates to perform the economic appraisal exercise then included the following wording:

“This funding has been provided by HMT and is only available for a Renewable Heat Incentive. This is to ensure that Northern Ireland is not disadvantaged compared to the rest of the United Kingdom. The economic appraisal needs to therefore identify the most cost-effective option for implementing the policy of a renewable heat incentive.”<sup>254</sup>

3.79 However, as can be seen in the CEPA section, because the economic analysis was showing that the Challenge Fund “might have been an attractive route”, Ms Clydesdale sought further clarification from HMT regarding the possible use of the funding for a grant scheme instead.<sup>255</sup> The answer came back from HMT’s Jon Parker on 15 April 2011 that:

“This funding does have to be used for renewable heat, but if NIE decide you would like to use it for a grant scheme or some such then this would be permissible as long as the cost of NIE spend is constrained to the AME consequential.”<sup>256</sup>

### The risk of continuing confusion over RHI funding

3.80 The Inquiry notes that, in practice, some aspects of the way the funding was treated by DFP and HMT could have reinforced misconceptions about the unusual nature of the RHI AME arrangements.

3.81 Firstly, contrary to what had been said about the inability to carry forward any purported underspend, £1.8 million from the £2 million funding allocation in 2011-12 was subsequently moved forward to 2012-13 and confirmed by DFP through the budgetary process. Ms Brankin offered the explanation that this was a re-profiling exercise for the start of the scheme and not

252 DFE-186598

253 DFE-186597

254 DFE-186531

255 TRA-00950

256 WIT-12774

a carry forward of an underspend. Whether this is correct or not, the fact it occurred would appear inconsistent with how the funding was supposed to operate.

- 3.82 Secondly, as explained later in this Report, the ease with which additional AME funding was provided in 2015-16, when the AME profile for that financial year had been considerably exceeded, led to false reassurance among DETI officials (already lacking in their understanding of the true nature of the RHI funding) that subsequent overspends would also be treated as standard AME.

### Inherent uncertainty about future RHI budget allocations

- 3.83 As described earlier in this chapter, it was highly unusual for AME funding to be capped at all, let alone on the basis of a population share, yet this was how DETI's initial RHI budget allocation for the years 2011-12 to 2014-15 was set. It was also assumed to be the basis for the subsequent 2015-16 allocation in correspondence between DETI Minister Foster and DECC Minister Barker at the end of 2013/early 2014.<sup>257</sup> This suggested that Northern Ireland would receive a population share based on the £430 million cap set for the GB RHI scheme. As it turned out, HMT in error never actually set a cap in Northern Ireland for 2015-16 as discussed in more detail elsewhere in this Report.

- 3.84 For allocations in the period from 2016-17 onwards the Inquiry saw some evidence of DETI officials considering the risk that might result from any reduction in DECC's budget. In March 2015 Mr Hughes, who worked on RHI under Mr Wightman in Energy Division's Energy Efficiency Branch from July 2014, had received a copy of DECC's November 2014 RHI forecasts which set out three different estimates for 'low', 'central' and 'high' cases.<sup>258</sup>

- 3.85 In May 2015 Mr Hughes wrote back to DECC saying:

"If uptake of the GB RHI scheme (per/head of population [sic]) isn't as high as the NI scheme, we are concerned that DECC AME [sic] might submit a reduced AME profile which would lead to consequential reduction in DETI allocation under the agreed formula."<sup>259</sup>

In this same email, he suggested that DECC might submit its 'high' forecast rather than the 'central' one and transfer any additional consequential funding to Northern Ireland. DECC did not do this and told Mr Hughes that he would need to pick this up with HMT directly.

- 3.86 Mr Wightman also understood the risk. He told the Inquiry in oral evidence that in March 2015 he was aware that "no matter what we do, our profile is determined on what DECC's profile is."<sup>260</sup> However, the Inquiry saw no further evidence of this risk being evaluated or communicated. In December 2015, as discussed elsewhere in this Report, the risk then materialised when, following a sharp reduction in applications and tariff levels in the GB scheme during 2015, DECC reduced its forecast spend for the period to 2019-20 by about a third and HMT reflected this in a similar reduction for Northern Ireland's RHI allocation for this period.

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257 WIT-18705 to WIT-18713

258 DFE-145735

259 DFE-277206 to DFE-277207

260 TRA-10367

## Findings

14. DETI Energy Division officials working on RHI were clearly warned by DETI Finance in May 2011 that the RHI funding was not being treated as standard AME, and that the approach to adopt to it was to treat it like DEL. This was in the context of HMT speaking of DEL penalties. The design of the RHI scheme should have included proper consideration of the controls necessary to reflect this position of heightened financial risk.
15. The important information about the unusual funding arrangements, and consequent heightened risks, should have been passed to CEPA, who appear to have based their reports upon the assumption that the funding allocations were effectively capped on a “first come, first served” basis. The Inquiry was not furnished with any evidence that Ms Clydesdale’s direction of 4 May 2011 to Mr Hutchinson – that, as regards her exchanges with Ms Brankin as to the nature of the funding, “you will need to ask CEPA to factor this in as a risk factor in the economic appraisal” – was effected.<sup>261</sup>
16. In late June 2011, about two months after she ceased work on renewable heat and moved to work on a variety of other energy-related matters, Ms Clydesdale, in company with all grade 7s in Energy Division, was circulated with a draft of the RHI consultation documents. She told the Inquiry that she thought that the reviews and monitoring referred to in the documents would be followed by costs controls at a later point in a phased process. Despite the fact that her conversation with Ms Brankin had confirmed the need to treat the funding as DEL with a need to control annual expenditure, and that her own email of 4 May 2011 had recorded that the HMT funding presented a “significant challenge” and “DFP will require evidence of our ability to control the scheme in order to minimise over/under spending in any one year”, she told the Inquiry she did not take any note of the fact that the consultation documents did not refer to any such proposals.<sup>262</sup> While the Inquiry appreciates that, by this stage, she was engaged in different work and received the documents as part of a general circulation, the Inquiry finds that her omission to do so was unfortunate.
17. Ms Hepper, the head of Energy Division, was clearly told that RHI AME was to be treated like DEL and there can be absolutely no doubt that both she and Mr Cooper, Head of Finance, were fully informed in 2011 as to the unusual nature of the AME funding and the risk of an impact on the DEL budget of any overspend.
18. The officials in Energy Division working on RHI should have formally brought the unusual nature of the RHI funding, and the heightened risks it carried, to the attention of the DETI Minister, the DETI Casework Committee considering the RHI scheme, and the DFP Supply officials considering the RHI business case.

261 WIT-12771

262 TRA-00997; TRA-00992; TRA-01016

**19. No reference was subsequently made, for example in the ministerial submission from Ms Hepper of 8 June 2011, to the qualifications and risks confirmed by the April and May 2011 email exchanges.<sup>263</sup> Ms Hepper told the Inquiry that simply limiting the funding to AME was a form of “shorthand” and it was assumed that the Minister was aware of the qualifications. While Ms Hepper did go on to say that she was “pretty sure” that the officials had informed the Minister of the qualifications to this unusual type of AME funding, Ms Foster told the Inquiry that, to the best of her recollection, she was never made aware that the funding was qualified prior to the autumn of 2015, when she was in her new role at DFP. What is clear is that the information contained in the Parker email exchange was never included in any formal submission to the Minister, as it should have been. In the course of her evidence to the Inquiry Ms Hepper accepted that omission to have been “unhelpful.”<sup>264</sup>**

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263 DFE-29388

264 TRA-01849



## Chapter 4 – The Renewable Heat Team: resources and lack of project management

4.1 It quickly became evident to the Inquiry that one of the central themes that permeated all aspects of the story of Northern Ireland’s RHI scheme was the capacity of DETI to develop and operate a scheme of this kind. The scheme was destined to last some 20 years-plus, and, given that was so, the mechanisms that were, or ought to have been, put in place to properly manage the scheme, when resources were scarce and staff would inevitably change, was an important consideration for the Inquiry. These issues are examined in this chapter.

### Resources

4.2 Concerns about resources, in terms of the time, people and expertise needed to develop initiatives on renewable heat, were present amongst some officials involved with the development and delivery of the RHI scheme in Northern Ireland from an early stage. The Inquiry heard evidence from many witnesses about the pressure on resources in Northern Ireland, particularly in relation to staffing levels, and how these pressures affected what work was done and how it was delivered.

4.3 In a submission in September 2008 to her then Minister, Ms Foster, concerning the next stage of policy development on renewable heat, Ms Pyper advised against attempting to include Northern Ireland in the 2008 Energy Act, which paved the way for the GB RHI. However, while suggesting that “it would be useful to use the greater resource that BERR has”, there was no reference made in the submission to serious resource concerns about developing an independent NI RHI scheme. The serious resource concerns had been documented by Ms Martin in an earlier draft of the September submission, but, they were, significantly, omitted from the final version sent to the Minister. The earlier draft had contained the following paragraphs, which the Minister did not get to see:<sup>265</sup>

“18. DETI cannot hope to develop this area of work with current resources, but will come under increasing pressure to say what it is doing in response to announcements from the EU and BERR in this area.

19. To help deal with lack of resource at least on renewable heat, we are working to develop contacts in BERR so that they will remember that this issue is transferred to Northern Ireland and keep us informed, although this can be time-consuming of itself. We are also trying to be creative in moving this area forward by creating a stake-holder group to make recommendations about what is needed to develop renewable heat in Northern Ireland.”<sup>266</sup>

Further to the omission of these paragraphs from the submission, Ms Pyper requested follow-up advice in relation to this issue from her colleague Ms Martin and this was duly supplied on 8 November 2008. Ms Martin informed Ms Pyper that DECC (which had taken over renewable heat from BERR in October 2008) had committed significant resources to the area of renewable heat, led by a grade 5 with policy responsibility and 20 staff.<sup>267</sup> They were shortly to be

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265 DFE-25263 to DFE-25268

266 DFE-25306

267 DFE-25683 to DFE-25686

augmented by six grade 7 officials. Ms Martin commented at paragraph 10 of her advice: “I know we cannot expect anything like this type of resource.”<sup>268</sup>

- 4.4 In a subsequent submission to the Minister on 30 April 2009 Ms Pyper did touch upon the issue of resources, stating at paragraph 19:

“Development of renewable heat in Northern Ireland would require significant policy and legislative resources (including for a Bill team in 2010/11) over the short-medium term if we are to have any impact in the 2020 timeframe.”<sup>269</sup>

She also referred to DECC and the relevant Department in Scotland having committed significant resources, adding in respect of DETI that:

“The Department has limited resources and expertise to devote to managing work in this new policy area. As a result significant consultancy support will be needed to provide the evidence base and economic analysis required to underpin a Renewable Heat Bill starting in 2010/11.”<sup>270</sup>

- 4.5 In response to a Section 21 notice from the Inquiry, Ms Pyper was unable to recollect the actual reasons why in the final version of her 22 September 2008 submission she had removed the two paragraphs drafted by Ms Martin with regard to resources, speculating that the submission was on the long side or that she had felt that it was not appropriate to deal with operational issues in strategic advice.<sup>271</sup> She did confirm that, subsequent to Ms Martin’s further review of resources in November 2008, she had raised her concerns with her line manager, Mr Thomson, then Deputy Secretary and Head of DETI’s Policy Group and that, in late 2009, she instigated a full divisional workload review resulting in a comprehensive memo to Mr Thomson on 15 January 2010 detailing the resource situation for each work area across Energy Division.<sup>272</sup>
- 4.6 After delivery of the final report from the consultants AECOM/Pöyry in July 2010 confirming the potential for development of renewable heat and the need for Government financial support, Ms Hepper, Ms Pyper’s successor as Director of Energy Division, formed the view that the subsequent work could not be managed appropriately without a level of resource which was focused more directly on renewable heat.<sup>273</sup> Ms Hepper herself had less than a year of experience in post with no prior energy background, although she had already led a division elsewhere in DETI. At that time the Energy Division comprised three branches: the Energy Markets Branch, Energy Co-ordination Branch and the Sustainable Energy Branch, the latter being re-named the Renewable Heat Branch in May 2011 and the place where policy work on renewable heat was developed.
- 4.7 The renewable heat team, such as it was, included the grade 7, Alison Clydesdale, who also worked on seven or eight other policy areas. Her job thus required frequent prioritisation of work, sometimes on a daily basis. Ms Clydesdale was replaced in May 2011 by Joanne McCutcheon.

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268 DFE-25685

269 DFE-26828 to DFE-26834

270 DFE-26832

271 WIT-09965

272 WIT-09966

273 WIT-15027



Whereas Ms Clydesdale worked 28-32 hours per week,<sup>274</sup> Ms McCutcheon worked 24 hours a week during term time only.<sup>275</sup>

- 4.8 Peter Hutchinson re-joined DETI in July 2009 as a deputy principal; he had previously worked in DETI between July 2005 and June 2008. He worked full time. From June 2010, until he left DETI in May 2014, he worked on renewable heat, reporting initially to Alison Clydesdale and then, from May, 2011, to Joanne McCutcheon. He had no renewable energy or economic background, although he was soon heavily involved with the commissioning and delivery of the consultancy work by AECOM/Pöyry. He attended some training courses but, essentially, 'learned on the job' as he worked full time on the RHI scheme, soon reaching the point where most submissions were drafted by him although submitted in Ms Hepper's name.<sup>276</sup>
- 4.9 The Inquiry acknowledges that the evidence confirmed that the vast bulk of the work involved in the creation of the non-domestic RHI scheme seems to have been performed by Mr Hutchinson, which was reflected in a special bonus form in relation to him dated 2 February 2012.<sup>277</sup> During the development process, the foregoing individuals constituted the core staff working on the NI RHI scheme.
- 4.10 The GB RHI scheme, by December 2013, was resourced by 77 people including three senior civil servants and six grade 6 policy officials, albeit this was to support a scheme covering England, Wales and Scotland.
- 4.11 However, in Northern Ireland lack of adequate resources proved to be a perennial problem adversely affecting the optimal development and management of the RHI scheme. Mr Thomson confirmed in oral evidence that DETI was aware from an early stage of the staff resource devoted to the GB scheme, a level of staff that could never have been expected in Northern Ireland.<sup>278</sup> The Inquiry found no evidence to indicate that staffing levels were discussed in any detail between officials from the respective jurisdictions. Mr Thomson agreed that, at the time of the introduction of the scheme, DETI was "badly under-resourced" with 13 key objectives for DETI in the Programme for Government which had to be prioritised.<sup>279</sup> He recalled that there had been a moratorium on NICS recruitment in the time of recession and austerity after the 2010 general election. These resource pressures within DETI continued throughout the life of the NI scheme and were acknowledged by Dr McCormick who noted in respect of his period as DETI Permanent Secretary from the middle of 2014 onwards that: "We were facing a situation of constraint and reduction ..."<sup>280</sup> Nevertheless the decision was taken to proceed with a Northern Ireland RHI scheme.
- 4.12 Mr Thomson also noted in evidence that, when departmental restructuring took place in 2010-11, Energy Division had been the most stretched in terms of resources and he was aware in 2012-13 that the whole Department had resource problems. At the same time there were competing pressures within the Department and a wide-ranging policy agenda. For example, he recalled discussions in 2010 with Minister Foster about whether to proceed with all the objectives in the Strategic Energy Framework, which included the targets for producing

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274 WIT-12515

275 PWC-04547

276 TRA-01472 to TRA-01475; WIT-06033 to WIT-06034; TRA-01977

277 DFE-430499 to DFE-430500

278 TRA-05658 to TRA-05659

279 TRA-05642 to TRA-05643

280 TRA-12078

renewable heat, and it was agreed to pursue all the objectives.<sup>281</sup> Mr Thomson was referred by the Inquiry to the 10 October 2010 letter from HM Treasury that included the offer of £25 million for the period up to 2015 for an RHI scheme and asked whether such an attractive offer influenced the decision to proceed with a renewable heat incentive in spite of the Department's limited resources.<sup>282</sup> He agreed that this 'ring fenced' funding, outside the NI block grant, offered by HMT was an "attractive" and a "significant" offer,<sup>283</sup> although he also made the point that much of Energy Division's workload was dictated by EU directives and EU targets.<sup>284</sup> He also accepted that Ms Hepper had contacted him on a number of occasions between 2010 and 2013 asking for further resources.

4.13 The risk of "inadequate resources" was thought at the time that the scheme was developed in 2012 to be sufficient for it to be recorded as a specific risk on the scheme's risk register, with business implications of this risk identified as including inadequate monitoring and auditing, failure to fully implement scheme and delays in launch date.<sup>285</sup> Unfortunately, as discussed in further detail later in this Report, that risk register was never updated from its first inception.<sup>286</sup>

4.14 Mr Thomson's assurance statement to the Permanent Secretary for the period ended 30 September 2012 included the statement:

"The biggest current risk to achieving the PfG (Programme for Government) and departmental objectives is staffing constraints."<sup>287</sup>

4.15 Ms Hepper stated that whilst she was in post as Director of Energy Division up until November 2013, quite apart from her supervision of the work on renewable heat, she had responsibility for an extensive, diverse and complex portfolio of other energy matters. Overall she estimated that she spent a maximum of 10% of her time on renewable heat.<sup>288</sup> She was apparently unaware at the time that project management disciplines had been applied to the GB RHI scheme.<sup>289</sup> She accepted in evidence to the Inquiry that DETI's resources were limited, especially in contrast to the resources available to DECC, and that staff had to work extremely hard. Long hours were worked for sustained periods, including evenings and weekends. She raised the issue of staffing resources on a number of occasions in discussions with her line manager, Mr Thomson, and the then Permanent Secretary, Mr Sterling, alerting both of them to mounting pressures and the volume of work across the Division.<sup>290</sup> In the course of her evidence to the Inquiry Ms Hepper observed that re-prioritisation took place on an "almost daily basis."<sup>291</sup>

4.16 The Inquiry also saw evidence that, some two years later, the pressure on resources continued. On 30 April 2015 Mr Mills, then Head of Energy Division and Ms Hepper's successor, sent a six-monthly assurance statement to Mr Stewart, then the Deputy Secretary and his line manager, which contained the following:

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281 TRA-05641 to TRA-05643

282 TRA-05643

283 TRA-05637 to TRA-05643

284 TRA-05639

285 DFE-398623; TRA-05646 to TRA-05648

286 TRA-05644 to TRA-05647

287 DFE-265835 to DFE-265837

288 WIT-16637

289 WIT-16654

290 WIT-15028 to WIT-15029

291 TRA-01787

“The Domestic RHI Scheme was launched by the Minister on 9 December 2014. The Business Case for the scheme included an initial additional admin resource of one SO (year 1) and a further additional resource (1SO & 1AO) in years 2 and 3 as the number of RHI applications and payments build up. To date no additional staff resource has been provided for administering the Domestic RHI Scheme. This has meant that site checks/visits for assurance purposes have had to be reduced and processing of applications is taking longer. The temporary re-location of one SO within the Division has helped however this has ended and a permanent resource is required urgently.”<sup>292</sup>

- 4.17 At that point, Mr Mills was particularly exercised about the fact that a commitment had been made to provide additional staff for the implementation of the domestic RHI scheme but that these new staff were not provided and the commitment to provide additional staff was withdrawn. His evidence was that this: “extra, un-resourced work arising from implementation of the domestic scheme effectively reduced resources to clear [sic] with RHI in totality.”<sup>293</sup> As well as indicating the effect this had on dealing with RHI generally, Mr Mills used this episode as an example of how, at that particular time, there was difficulty in obtaining additional resource.
- 4.18 Mr Mills’ written evidence to the Inquiry also stated that Energy Division was generally over-committed in terms of resources and that he did not have sufficient resources, for instance, to fundamentally review the non-domestic RHI scheme.<sup>294</sup> Similarly, in his oral evidence, he said that the division was under-resourced and that RHI was “the worst example” of this. Mr Mills said that – at least with hindsight – he did not see how one could say anything other than that the resources devoted to RHI were “clearly inadequate”; although he also candidly accepted that he did not appreciate the risk which lack of resources gave rise to at that time.<sup>295</sup>
- 4.19 Minister Foster recorded in her written evidence that, “Energy was a small team with limited resources.”<sup>296</sup> Nevertheless, the perception amongst officials seems to have been that they just had to get on with it.<sup>297</sup>
- 4.20 For his part, Mr Sterling told the Inquiry that he had been conscious that Energy Division was overstretched and under pressure and that there were requests for additional resources.<sup>298</sup> He explained that DETI’s Resources Group, comprising himself, Mr Thomson and Colin Lewis, had done a lot of work to find additional resources. With hindsight, he expressed the wish that he had been “more inquisitive” about seeking assistance from the Strategic Investment Board in establishing effective programme and project management. Mr Sterling said that none of the officials had spoken to him directly about the problems but he considered the officials concerned to have been “hard working” and perhaps reluctant to ask for such help.<sup>299</sup> They were proud of what they achieved with a ‘can do’ outlook. He could not remember any instance of advising a Minister that something could not be achieved because of lack of resources or

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292 DFE-312463 to DFE-312464, also annexed to Mr Mill’s first witness statement to the Inquiry at WIT-14889 to WIT-14890. Although Mr Mills later agreed to amend the wording of another part of this assurance statement, the portion quoted above remained unchanged.

293 WIT-14541; and see TRA-09509 to TRA-09510 and TRA-09515 to TRA-09516

294 WIT-14534

295 TRA-09507 to TRA-09510

296 WIT-20585

297 TRA-04850

298 TRA-06060

299 TRA-06066 to TRA-06072

expertise; an alternative being to advise that it was very difficult and to try an alternative that would take significantly longer.

- 4.21 Minister Foster also confirmed in evidence that she raised her concern about DETI’s apparent lack of resources a number of times with the Permanent Secretary, Mr Sterling, as well as referring it to Sir Malcolm McKibbin, then Head of the Civil Service, and his predecessor, Sir Bruce Robinson, during their annual appraisals of the Permanent Secretary. She observed that the Energy Division of DETI was constantly having to ‘fire-fight’ and re-prioritise the workload.<sup>300</sup> She told the Inquiry that:

“I do think that the officials worked long hours, probably longer hours than some of their colleagues in other parts of the Civil Service...You can’t expect officials to keep working long hours all the time or there will be a consequence to that.”<sup>301</sup>

- 4.22 Sir Malcolm McKibbin agreed that the evidence as to lack of resources was not satisfactory but he thought that “people hadn’t fully realised the need for additional expertise in the energy field.”<sup>302</sup> He expressed the view that when taking on a project such as RHI “there has to be a candid discussion between senior members of the Department and the Minister on the issues of risk and capacity.” He recalled conversations with both Mr Sterling and Minister Foster about the resource pressure in Energy Division, but these were more with regard to a possible increase in workload from EU directives without any specific mention of RHI.<sup>303</sup>

- 4.23 This issue was also addressed in some detail in the evidence of Mr Sterling’s successor (from June 2014) as Permanent Secretary in DETI, Dr McCormick. In his oral evidence, albeit with the benefit of hindsight, he told the Inquiry that, “I think it’s impossible to defend the resourcing levels.”<sup>304</sup> However he also took the view that it would not have taken a vast level of resource to have identified some of the difficulties with the non-domestic RHI scheme. He considered that under-resourcing was a contributory factor to the difficulties with the scheme and that better resourcing would have reduced the risk materially in relation to some of the things which went wrong with the RHI scheme.<sup>305</sup> He also indicated that he was not getting a clear message about lack of resources in this particular area at the relevant time, speculating that more resources might have been able to be found if it was realised that this was essential.<sup>306</sup> Dr McCormick also recognised that the resourcing issue was about quality and expertise as well as simply staff numbers.<sup>307</sup>

- 4.24 Dr McCormick’s deputy on the policy side, Chris Stewart, gave evidence to similar effect. In his written evidence he said that resources in Energy Division were stretched.<sup>308</sup> In his oral evidence to the Inquiry he explained that, although he had not previously been of this view, having reflected on the evidence which he had seen in the course of the Inquiry up to that point, he now took the view that resources in Energy Division had been inadequate.<sup>309</sup> He

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300 WIT-20595 to WIT-20596

301 TRA-08523

302 TRA-16783

303 TRA-16784

304 TRA-12055

305 TRA-12055; TRA-12067; TRA-12097

306 TRA-12075 to TRA-12078

307 TRA-12076

308 WIT-11527

309 TRA-11523

also now considered that resources in the RHI team had been inadequate<sup>310</sup> although, as other witnesses did, he emphasised the resource constraints under which the Department as a whole was operating at the time<sup>311</sup> and that he was not conscious of the level of risk being carried by reason of resources being inadequate at the relevant time.<sup>312</sup> Notwithstanding this, his evidence was that what had been done to try to address resource pressures “was modest and was patently not enough.”<sup>313</sup>

4.25 Mr Stewart also explained to the Inquiry his view that there had been a “great deal of evidence of mistakes being made by small teams working under pressure”, with the logical conclusion being that:

“Had there been greater resource, less pressure on teams, then, quite probably, there would’ve been fewer errors and we might at least have had a better chance of not being where we are today.”<sup>314</sup>

### Lack of project management

4.26 Another subject on which the Inquiry heard extensive evidence was that of project management and whether, at successive stages of its existence, the RHI scheme could or should have been organised using project management practices and disciplines.

4.27 In GB the RHI scheme had a clearly defined governance structure managed within DECC according to ‘PRINCE’ project management principles. PRINCE (Projects in Controlled Environments) is a process-based method for effective project management. The principles underlying PRINCE, and indeed of all good project management methods, have been developed to assist in the planning, execution, control and completion of a project.

4.28 While widely used on capital and IT projects, PRINCE and other project management methods are flexible and capable of being adapted to the particular circumstances of any project, from the simplest to the most complex. In order to determine whether project management is appropriate, a ‘project’ is generally defined as a specific activity, different from ‘business as usual,’ that often involves change and innovation such as a new building, the development of a new product, or the introduction of a new initiative or process.

4.29 In government, ‘PRINCE’ project management principles are one of a number of methodologies used for managing projects. All good project methods contain at their core some fundamental elements. A suitably qualified team should be assembled; project objectives defined and a budget established. There should be a bespoke project plan, with mechanisms to ensure that the plan may be adjusted and/or refined to take account of and manage relevant contextual changes over time. Also essential is a clear and easily accessible system for the collection and storage of records and information. An appropriate formal structure would establish a Senior Responsible Officer (SRO) at Senior Civil Service level, a Project Board, a Project Manager, a Project Team, a Risk Register (to be updated as necessary), an Issues Log and a Benefits Realisation Plan.

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310 TRA-11524

311 TRA-11525

312 TRA-11529

313 TRA-11526 to TRA-11527

314 TRA-11524

- 4.30 In respect of the GB RHI scheme there was an overarching Heat Reform Programme Management Board; project processes were the subject of formal consideration; and, an RHI Project Board met monthly to consider the reciprocal working arrangement with Ofgem. A Risk Register was in place, a monthly risk review meeting was convened in advance of RHI Project Board meetings and risks could be escalated as necessary. The Heat Reform Programme and RHI Project Boards had formal terms of reference and monthly meetings of the Project Board were minuted.<sup>315</sup>
- 4.31 In Northern Ireland, central guidance on good practice in project management was available within the NICS on the Central Procurement Directorate website and was circulated across Departments in 2009.<sup>316</sup> One of the key recommendations contained in paragraph 1.34 of the DETI Corporate Plan initiated in April 2010 was that:
- “Project management techniques should be applied to the initiation, development and implementation of all major pieces of work with project teams drawn from across the department and its NDPBs.”<sup>317</sup>
- 4.32 In contrast to that objective, some six years later, when reporting on the closure of the RHI scheme, the Department for the Economy (the new name for DETI from May 2016) Internal Audit report of August 2016 recorded that a recognised structured programme/project framework would have been beneficial...there should have been a programme oversight board providing a challenge role on delivery of outcomes; a project plan with milestones and key decision points;...a project budget with project risks; key actions, dates and an assurance mechanism.<sup>318</sup>
- 4.33 Ms Hepper told the Inquiry that, during her time as Director of Energy, she did not consider the application of a formal project management structure to the RHI scheme was practicable in the context of the number of other projects that also required attention and the limited resources available.<sup>319</sup> In her evidence she stated that the focus was “on delivering the Scheme” and the general approach seems to have emphasised delivery, i.e. “Get on with it.”<sup>320</sup>
- 4.34 In her written evidence Ms Hepper has also said that no formal decision was taken by DETI about whether or not to use formal PRINCE methodology. She has said that she explained to Mr Thomson how the scheme was to be managed on a proportionate basis in view of the lack of resources. She was unable to say whether that explanation had involved a specific decision not to employ any formal methodology, PRINCE or otherwise.<sup>321</sup>
- 4.35 Ms Hepper nevertheless told the Inquiry that the key “overarching principles” of project management were in place: “*de facto*” members of the team included herself as the “Senior Responsible Owner,” Ms McCutcheon as the “Project Director”, and Mr Hutchinson as the “Project Manager”; that she regularly met the team and they operated in a “proportionate way.”
- 4.36 This may be contrasted with what Mr Hutchinson said in oral evidence, namely that he did not recognise the description of him by Ms Hepper as being the Project Manager although he

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315 WIT-175019 to WIT-175020

316 WIT-03282

317 DFE-262383

318 DFE-216657 to DFE-216659

319 WIT-15041; TRA-05330 to TRA-05331

320 WIT-15041

321 WIT-15041 to WIT-15044; WIT-16651; TRA-02385 to TRA-02386; TRA-05328 to TRA-05342

accepted that it was possible that he was regarded as a ‘manager’.<sup>322</sup> He attended a general training course in “Practical Project Management”, although that was in 2013 or 2014, after the NI RHI scheme regulations had been developed and implemented, and he told the Inquiry that he did not have any practical experience of the procedures. Subsequent to his service in DETI he said that he had encountered some relevant procedures in the Department of Education, including the benefits of a Project Initiation Document, Project Manager, Project Board, risk and document logs and key actions. None of these arrangements were applied or effectively implemented in respect of the RHI scheme either at the start or at any of the key phases of implementation.<sup>323</sup>

- 4.37 In the course of his evidence to the Inquiry Mr Hutchinson agreed that, given the extent of the funding made available, the unpredictability of demand, the novelty of the project and the financial risks in relation to the RHI scheme, there could be “no question” about whether a formal management procedure would be followed today and that “it should have been then”.<sup>324</sup>
- 4.38 Mr Thomson, told the Inquiry that the lack of project management was a “corporate failing.”<sup>325</sup> Dr McCormick also adopted, to use his words, “a clear position” in his evidence to the Inquiry that there should have been formal project management structures in relation to the RHI scheme and he considered that project management was one of the things which would have prevented things going wrong.<sup>326</sup>
- 4.39 Again, Mr Stewart’s evidence was to similar effect. He said that “the absence of project management for RHI has been well remarked on and acknowledged”;<sup>327</sup> that it ought to have been employed in relation to the RHI scheme;<sup>328</sup> and that, in following the evidence to the Inquiry, he had seen that “time and again, it was shown just where project management could’ve made a difference.”<sup>329</sup> Indeed, he told the Inquiry that one of the lessons which has been learned from the RHI scheme right across the Northern Ireland Civil Service is that: “unless there’s an obvious reason for not adopting a project management approach, then it really ought to be the default.”<sup>330</sup>

## The possibility of a Gateway Review in 2012

- 4.40 The evidence provided to the Inquiry indicates that Sandra Thompson of DETI’s Energy Co-ordination team, raised the question in May 2012 of subjecting the RHI to the Gateway procedure.<sup>331</sup> This provides for a series of independent peer reviews at key decisions or stages in the lifecycle of a project reflecting the commencement, delivery and closure of the project. The purpose is to ensure, as far as possible, that important decisions are reviewed and necessary arrangements are in place before proceeding to the next stage, for example, whether there are adequate resources available to develop and manage the project or initiative.

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322 TRA-01486 to TRA-01487; TRA-05329 to TRA-05330

323 WIT-06034; TRA-01472 to TRA-01478

324 TRA-01483 to TRA-01486

325 TRA-05691

326 TRA-12054 to TRA-12056

327 TRA-11513

328 TRA-11516

329 TRA-11517

330 TRA-11518

331 DFE-37393 to DFE-37395

- 4.41 Typically in the NICS the Department Assurance Co-ordinator (DAC) meets the Senior Responsible Officer (SRO) and the project team to make arrangements for a Gateway Review and the review/project team would hold an evidence-based review if required. That initial meeting would typically last 1-2 hours and the review would take 2-3 days. If the full Gateway Review process is considered to be not readily applicable, due to the characteristics of the project, a more flexible assurance review, known as a Project Assessment Review (PAR) is available managed by Central Procurement Directorate (CPD).
- 4.42 In the context of a Department with a “can do” commitment to delivery, involved in a new and highly unpredictable scheme, driven by a need to secure funding for Northern Ireland with what was believed to be a ministerial ‘preferred direction of travel’, such an independent assessment at a number of key stages of the RHI would have ensured an impartial check as to whether the project continued to be fit for purpose.
- 4.43 The apparently limited interpretation that Ms Hepper placed upon the need for formal project management, may be evidenced by a comment made by her on 16 May 2012 in the course of an email exchange with Ms McCutcheon about the question in Ms Thompson’s email of potentially applying Gateway to the RHI scheme. Ms Hepper advised that such a procedure was unnecessary for RHI, writing that:
- “I don’t think we need Gateway for RHI. We have the project finished and moving into implementation”
- and
- “so probably too late in any case.”<sup>332</sup>
- 4.44 Mr Thomson told the Inquiry that the project, involving a sizeable sum of public money, should have gone through Gateway.<sup>333</sup> He believed that, in accordance with NIGEAE, the Gateway process, should have been applied and would have added value to the project.<sup>334</sup>
- 4.45 Mr Sterling told the Inquiry that, had he been a party to the discussions about the issue at the time, he would have challenged the view that a Gateway review was not needed because the scheme was ‘up and running’ and would have advised that serious consideration should be given to such a possibility.<sup>335</sup>
- 4.46 In his evidence, Dr McCormick indicated that “an appropriate governance process” now “increasingly needs to include Gateway reviews, which were conspicuous by their absence in this case.”<sup>336</sup> Although he was not the Permanent Secretary at the time when the RHI scheme was developed and introduced, Dr McCormick’s evidence was also to the effect that DETI “absolutely” should have undertaken a Gateway Review even as early as 2011, at the stage of policy development for the scheme, to ask whether the Department was capable of taking it on.<sup>337</sup>

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332 DFE-37393 to DFE-37395

333 TRA-05674

334 DOF-60171 to DOF-60355; TRA-05666 to TRA-05674; TRA-05691

335 TRA-06088 to TRA-06092

336 TRA-12026 to TRA-12027

337 TRA-12097 to TRA-12098; TRA-12058



## Risk management of the RHI scheme

- 4.47 The routines of identifying, tracking and acting to reduce risk are a core component of project management. A document known as a ‘Risk Register’ is used to record risks as they change over time and enables all the people responsible for a project to have a shared understanding of risk and what needs to be done and by whom to reduce it. As noted earlier, the GB RHI scheme had a risk register that was reviewed monthly at its RHI Project Board.
- 4.48 In Northern Ireland, the RHI scheme Risk Register was produced in March 2012, at the time of the consideration of the scheme by the Casework Committee, and was drafted by Mr Hutchinson.<sup>338</sup> Ms Hepper in the course of her evidence explained that it had been reviewed on a quarterly basis in the course of her meetings with Ms McCutcheon and Mr Hutchinson.<sup>339</sup> However, the Inquiry was not provided with any contemporaneous documentary evidence to confirm that it was reviewed on a quarterly basis; and no further written update, additions or amendments relating to risk were recorded.
- 4.49 Even when the later CEPA report of June 2013 indicated that the target set for renewable heat in Northern Ireland was no longer going to be met, no update was made to the Risk Register to reflect this. No signatures were added to the front sheet to confirm consideration upon any particular occasion. Ms Hepper told the Inquiry that it should have been signed off at “head of branch level” by Ms McCutcheon, by herself or Mr Hutchinson simply to signal that it had been reviewed.<sup>340</sup> In summary, while discussions about risk may have taken place within Energy Division, the actual RHI scheme Risk Register first created in 2012 was never updated.

## The prospect of a joint DETI-Ofgem Project Board

- 4.50 In December 2011, Ofgem provided DETI with a study into the feasibility of Ofgem taking on the administration of the NI RHI. At paragraph 6 of the Feasibility Study, Ofgem recorded that DETI had expressed some concerns around the need for controls to be developed to ensure that the costs of the NI RHI scheme remained within budget. In the Feasibility Study Ofgem also proposed that a joint DETI-Ofgem administration board should be established to oversee the development of the NI RHI scheme, make decisions around key issues that might arise and manage the contingency fund.<sup>341</sup> The Study also suggested that the board could help guard against the risk of administrative failures, a precaution that had been included in the Risk Register attached at Appendix 5 to the Study with a risk assessment as “High”.<sup>342</sup>
- 4.51 The Feasibility Study proposed that, after the development phase, the board would continue as an operational board to monitor scheme operations and review scheme expenditure, uptake, technologies and capacities of installations. The Feasibility Study described the proposed board in the following terms:

“The purpose of the joint NI RHI Administration Board is to take decisions regarding development and delivery of the project, monitor key risks and issues and act as a change control mechanism for covering any items previously out of scope. We envisage that this Board will initially meet fortnightly throughout the development

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338 DFE-79909 to DFE-79921

339 TRA-02363 to TRA-02365

340 TRA-02364

341 DFE-79801

342 DFE-79921

stage before moving to a monthly cycle once the scheme had been established. At this time we should aim to have a face-to-face meeting at least quarterly with the Senior Responsible Owners from both organisations.”<sup>343</sup>

As discussed earlier in this chapter, such a board had been created in relation to the GB RHI scheme.

- 4.52 The idea for such a board was discussed when Ofgem’s Ms McArthur, the author of the Feasibility Study, and Mr Harnack, the Director of New Scheme Development, met Ms Hepper, Ms McCutcheon and Mr Hutchinson in Belfast on 2 November 2011.<sup>344</sup> Ms Hepper and Mr Harnack were suggested as joint chairs.<sup>345</sup> Ms McArthur told the Inquiry that it was a joint responsibility of both organisations to set this up.<sup>346</sup> However, as discussed later in this Report, despite the undertakings given later in 2012 by Energy Division officials to the Casework Committee and incorporated into the DFP business case, such a board was not set up.
- 4.53 As to why this may have occurred, Mr Hutchinson suggested in oral evidence that the lack of resources in DETI, together with the slow initial uptake on the scheme, might have contributed to the failure to set up the board. He also acknowledged that a board would have been a benefit even though there was relatively frequent contact between DETI and Ofgem.<sup>347</sup>
- 4.54 Another rationale for not setting up the joint board which was put forward by DETI officials was that regular meetings of such a body were not really needed, with informal teleconferences being seen as a practical alternative. The Inquiry notes that these informal contacts were not regular and that, after the scheme became operational, no formal or agreed minutes were kept of DETI-Ofgem meetings or teleconferences until November 2015. With regard to Ofgem, Chris Poulton, who in 2014 became the Managing Director of E-Serve – the arm within Ofgem that administered the RHI – accepted that this was an administrative oversight and that, while there were emails and conversations, one or other of the bodies should have kept formal objective records.<sup>348</sup>
- 4.55 Dr Ward of Ofgem agreed that the omission to set up a joint DETI-Ofgem Project Board was a missed opportunity and he told the Inquiry that he had never seen an explanation as to why the board had not come into being. In his view it would have been a useful and helpful mechanism, which would have encouraged dialogue at working level and escalation of issues at senior level and quarterly review. He also acknowledged that the absence of a joint board might have been to blame for the absence of joint risk and issues registers for the scheme.<sup>349</sup> Dermot Nolan, Ofgem’s Chief Executive, (up to 31 January 2020) also accepted in his evidence to the Inquiry, that the omission to establish such a board was a failing.<sup>350</sup>
- 4.56 Dr Ward accepted that he had not enquired as to why the joint DETI-Ofgem Project Board had not been set up and he had not asked whether anyone else had made such an enquiry. He also accepted that it was not until April/May 2014 that a monthly telephone conference was

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343 DFE-79800

344 OFG-124012 to OFG-124013

345 DFE-79800 to DFE-79801

346 TRA-03728

347 TRA-02021 to TRA-02022

348 WIT-282545; TRA-09725 to TRA-09726; TRA-09743

349 TRA-06556

350 TRA-14850

instituted with DETI.<sup>351</sup> When asked why he had not alerted DETI to the significant differences between DECC and DETI with regard to project management, board meetings, reviews etc. Dr Ward told the Inquiry that his focus was on the GB scheme and “it never came up.”<sup>352</sup>

## Handovers and continuing lack of project management 2014-15

- 4.57 One of the other key issues which has emerged in relation to management of the NI RHI scheme, and which spans the themes of resources and project management which are discussed in this chapter, is that of staff handover. As is discussed in further detail later in this Report, there was an unprecedented change, at virtually every level, in the officials responsible for the RHI scheme in late 2013 to mid-2014. Consequently, the Inquiry has had to consider carefully the adequacy and effectiveness of the arrangements for relevant and important knowledge to be passed between officials where personnel move on; and the implications of a lack of any formal arrangements in respect of handover.
- 4.58 Among those involved directly with the scheme, reliance seems to have been placed, to some degree, upon largely informal contacts such as the ability to visit each other’s offices for conversations. According to Alison Clydesdale, there was no agreed policy covering staff handovers and the procedures varied over different divisions. She was unsure as to whether she provided any formal handover file to Ms McCutcheon. However, she emphasised that she was “available to discuss any issues” in her office located in the same corridor and that: “RHI issues could be discussed at Grade 7 level” at monthly Head of Branch meetings.<sup>353</sup>
- 4.59 Mr Sterling gave evidence that during 40 years of service he had never encountered two similar handovers. He stated that, as a result, issues which some people considered important subsequently were not considered important by others.<sup>354</sup>
- 4.60 Ms McCay, a deputy principal in Energy Division, who was temporarily promoted to act up as the RHI team grade 7 for seven weeks in the summer of 2014 following the departure of Ms McCutcheon, read and made notes on a hard copy of Mr Hutchinson’s handover note which she passed to Mr Hughes. Mr Hutchinson’s handover note is dealt with in greater detail in chapter 18 of this Report. In her written evidence Ms McCay told the Inquiry that:
- “Project Management documentation had not been developed for the Scheme i.e. a risk register, decision log, issues log, project plan etc. Had this been done there should have been a full record of key information relating to the project, including the nature of the funding arrangement, its budget, the assumptions and modelling underpinning its design, important dates and milestones and important action points. As it was there was a handover note with references to some information and links to some key documentation.”<sup>355</sup>
- 4.61 Mr Wightman, who took over responsibility for the RHI scheme, as grade 7 Head of Energy Efficiency Branch in June 2014, told the Inquiry that the lack of effective project arrangements for both non-domestic and domestic schemes was a key omission, as was the absence of a monitoring committee. For a programme on the scale of the non-domestic scheme he would

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351 TRA-06558 to TRA-06560

352 TRA-06567 to TRA-06568

353 WIT-12528; TRA-01018 to TRA-01019

354 TRA-07053 to TRA-07054

355 WIT-13027

have expected an effective programme of management in place in line with PRINCE, with an Oversight Board and key milestones such as a review of tariffs and an application for DFP reapproval. Such a programme would have also had a decision log, live risk register and issues log.<sup>356</sup>

- 4.62 Mr Wightman said that he had not queried the lack of project management arrangements during his induction because he was assured that the non-domestic scheme was established and being administered by Ofgem on DETI's behalf. Consequently the scheme, as he understood it at that point, would take up very little time.<sup>357</sup>
- 4.63 Mr Mills, who succeeded Ms Hepper in 2014 as Head of Energy Division and who holds a qualification in PRINCE 2, told the Inquiry that he should have raised the issue of lack of project management but that the prevailing culture did not encourage it but rather favoured an approach of "get on and get things done and deliver."<sup>358</sup> He said that the relevant software was not available for certain project management techniques, that there was a lack of resources, a culture that emphasised delivery and that there was no project/programme office in the Department.<sup>359</sup> According to Ms McCay, Mr Mills mentioned to her that he had been told that RHI "could look after itself" until replacements were in post.<sup>360</sup>
- 4.64 Again, Dr McCormick, in his evidence to the Inquiry, accepted that there were failings in this area. His view was that all of the staff dealing with RHI moving within a short timescale was clearly unacceptable and "the baton was, in fact, dropped"; but that there was no recognised system within the NICS in relation to this and it was a systems issue where the buck ultimately stopped with him, with project management being the right corrective measure.<sup>361</sup>

### The role of the Permanent Secretary in respect of project management

- 4.65 As noted at the start of this section on project management, guidance was available within the NICS on good practice in project management dating from at least 2009. However it appears that it was not normal practice during the period 2011-2016 for the Permanent Secretary or either of the Deputy Secretaries in DETI to consider systematically whether projects should be managed on the basis of PRINCE or any comparable methodology, and there was no central area in DETI which ensured that the guidance was consulted and put into practice.<sup>362</sup>
- 4.66 Mr Sterling, the DETI Permanent Secretary until 2014, told the Inquiry:

"I see my role as a senior civil servant as being first and foremost to help Ministers do that which they want done. And I would say that it is always our responsibility to deliver the outcomes they're seeking to the maximum extent possible within the resources and policy framework that we have."

He added:

"I would always advise staff, 'You don't say no to a Minister.' What you would say is, 'Look, this is going to be very difficult for whatever reason. Maybe there is another

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356 WIT-17033 to WIT-17034

357 WIT-17034; TRA-06869 to TRA-06872

358 TRA-09495

359 TRA-07122 to TRA-07126

360 WIT-13021

361 TRA-12039 to TRA-12044

362 TRA-06067 to TRA-06068; TRA-11517 to TRA-11519; TRA-11581 to TRA-11582

way we can get the outcome you're looking for, or is this something that we can do but it is going to take a bit longer?"

He accepted that he had never informed a Minister that the Department did not have the resources or the expertise to take on a particular project.<sup>363</sup>

- 4.67 Mr Sterling had also told the Northern Ireland Assembly's Public Accounts Committee (PAC) on 30 November 2016 that, with hindsight, he would have to accept that project management methodology should probably have been used with respect to the RHI scheme and would have reduced the risks but that whether to use PRINCE "would not have been a decision of mine." He explained to the Assembly's Public Accounts Committee (PAC) that the decision would have been taken "in the energy division" and he "was not conscious of what considerations were applied to it at the time."<sup>364</sup>
- 4.68 Mr Sterling further told the PAC inquiry that it was not mandatory to use applications such as PRINCE when developing projects or programmes, but he also accepted in his evidence to this Inquiry that DETI officials were familiar with PRINCE and that its use was well-established and visible. He considered that it was a tool that could have reduced the risks and brought benefits to the development and implementation of the NI RHI and that both formal project management and Gateway arrangements should have been in place for projects of such scale, complexity and risk. Mr Sterling also told the PAC that when he left DETI in July 2014 the scheme was "not terribly visible on my radar" and appeared to be underperforming.<sup>365</sup>
- 4.69 In terms of his approach overall, Mr Sterling told this Inquiry that, as the head of a Department, his role was very much to ensure that there was an internal control framework which would ensure that different schemes or projects would be delivered as free from risk as possible. He accepted that the Department should have invested more in project management and that there should have been a programme management approach to the suite of projects contained in the Strategic Energy Framework.<sup>366</sup> He wished that he had sought more resources for that purpose such as the expertise which could have been available from the Strategic Investment Board (SIB).<sup>367</sup>
- 4.70 In practice Mr Sterling relied upon the six-monthly risk assurance statements and the departmental Operating Plan together with informal contacts with the officials involved. He emphasised that RHI was only one of approximately 30 actions which flowed from the Strategic Energy Framework and that RHI was the only project that produced problems.<sup>368</sup> However, Mr Sterling was unable to recall any other scheme which had, at that time, the combination of features specific to the RHI of being demand-driven and incentivised, volatile, unpredictable, grounded upon variable assumptions and funded in a highly unusual way.<sup>369</sup>
- 4.71 Ultimately, Mr Sterling was unable to say why some form of project management had not been utilised and he stated that, in his view, RHI "was a project too far for us."<sup>370</sup> Mr Stewart told the Inquiry that he agreed with that assessment.<sup>371</sup>

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363 TRA-06088

364 PAC-06186

365 PAC-06185

366 TRA-06792 to TRA-06793

367 TRA-06066; TRA-06072 to TRA-06073; TRA-06730 to TRA-06731; TRA-06763; TRA-06799 to TRA-06800

368 TRA-06810 to TRA-06811

369 TRA-06062 to TRA-06063

370 TRA-06730

371 TRA-11530

- 4.72 In summary, Mr Sterling accepted that there should have been a greater investment in project management and that Strategic Investment Board expertise might have been consulted.<sup>372</sup> Mr Sterling emphasised to the Inquiry that his role was to ensure an internal control framework was in place and that, while it was novel, the RHI scheme was not so novel that he thought “I need to get personally involved in this.”<sup>373</sup>
- 4.73 Dr McCormick, who succeeded Mr Sterling as DETI Permanent Secretary in July 2014, told the PAC that:

“The fundamental point is that it was not managed as a project. There should have been a project manager, a senior responsible owner and all the routine dimensions of a PRINCE-based procedure. That was not done. It is not clear why it was not done, but a lot of things that have gone wrong flow from the absence of those straightforward aspects of governance.”<sup>374</sup>

In his written evidence to this Inquiry, Dr McCormick said:

“Much more systematic and rigorous project management would have been appropriate throughout the project and might have mitigated the problems that arose.”<sup>375</sup>

### Were the problems of project management limited to the RHI?

- 4.74 The Inquiry notes that previous DETI projects had attracted the attention of the Northern Ireland Audit Office (NIAO) and the PAC with regard to similar problems as emerged in relation to the NI RHI scheme. It is obviously not the purpose of this Inquiry, nor this Report, to conduct any form of investigation into those earlier projects or the reasons for their falling into difficulty. However, in light of the (at times) striking similarity of some of the themes which have emerged from earlier inquiries into these previous failures, some discussion of them is appropriate by way of context.
- 4.75 The Bytel Project was a cross-border broadband initiative aimed at the provision of high-speed broadband connectivity between Belfast, Craigavon, Armagh, Dundalk and Dublin. Departmental responsibility lay with the Department of Finance and Personnel in Northern Ireland and the Department of Public Expenditure and Reform in Ireland. DETI and the equivalent Department in the Republic were appointed as Joint Implementing Agents for the project. As a cross-border project, effective co-operation was required between the Departments in Northern Ireland and the Republic of Ireland and the Special EU Programmes Body (SEUPB). However, from the outset there were serious failings in the handling of the project, with a catalogue of mismanagement, poor communication and inadequate response to warnings. As a result, the project delivered very poor value for money. The Bytel Project was the subject of a report from the Comptroller and Auditor General, Mr Kieran Donnelly, which was published by the Northern Ireland Audit Office on 3 March 2015.<sup>376</sup> It was also considered by the PAC.
- 4.76 Significant conclusions drawn by the PAC in the Executive Summary of its report on the Bytel Project, published in July 2015, included the following:

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372 TRA-06066; TRA-06072 to TRA-06073; TRA-06730 to TRA-06731; TRA-06799 to TRA-06800

373 TRA-06061 to TRA-06062

374 PAC-03644

375 WIT-10539

376 INQ-90001 to INQ-90107

“9. The assessment and appraisal of the project was seriously flawed, and it is likely that with due diligence and more robust probing of the proposal, the Project would not have had funding approved.

10. The Department admits that it did not have sufficient technical expertise to understand the Project. The failure to re-appraise the Project when it changed significantly was a fundamental shortcoming which contributed significantly to the problems which followed. This was a critical lost opportunity to re-assess costs and to ensure that the level of grant payable was reduced accordingly.

11. The pressures within DETI to meet grant expenditure targets within tight deadlines overtook the need to ensure that grant claims were properly scrutinised. The Committee is convinced that DETI’s main concern in approving grant claims for the Project was to ensure that available EU funding was spent. The Department’s primary responsibility was to scrutinise claims properly to ensure that they were valid. The Committee concludes that DETI failed fundamentally to meet this responsibility.”<sup>377</sup>

A detailed review of the project was unacceptably delayed. Paragraphs 6 and 7 of the PAC report<sup>378</sup> are of particular significance in relation to what later occurred with the RHI scheme. Those paragraphs read as follows:

“6. The failings are similar to those reported by the Committee in 2012 in relation to the Bioscience and Technology Institute. This was another DETI Project from around the same time as the Bytel Project. The Committee is very concerned that poor project management and disregard for value of money appear to have been endemic within the Department at that time.

7. The Committee notes the assurances from both DETI and SEUPB that improvements in systems and processes in recent years should substantially reduce the risk of similar failings in future. However, DETI provided unsubstantiated assurance over many years in relation to the Bytel Project. Important as systems and processes are, it is vital that these work in practice. It is clear that this case only came under proper scrutiny because of the allegations made by whistle blowers. It is essential that the culture within DETI is changed and that the Department must recognise the need to take decisive and prompt action to address problems such as those which arose in the Bytel case.”<sup>379</sup>

- 4.77 The Bioscience and Technology Institute Limited (BTI) was established in 1998 with the primary objective of providing biotechnology incubator facilities through the development of a specialised building at Belfast City Hospital. The Company was funded by a combination of public funds and debt. It was the Company’s original expectation that Belfast City Hospital would provide a site in its grounds, free of charge, on which BTI would construct business premises.
- 4.78 In the event, the premises were not built at that location and, in 2001, the Company acquired the Harbourgate Building, in respect of which it paid a “finder’s fee” of £100,000 to a firm of Belfast Solicitors. Investigations revealed that the finder’s fee was subsequently disbursed to

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377 INQ-90114

378 INQ-90108 to INQ-90126

379 INQ-90113 to INQ-90114

others. The Institute effectively never operated, as the Harbourgate Building was unsuitable and would have required to be upgraded at a cost of potentially £4 million. The project was therefore never adequately funded or managed from the outset.

4.79 Invest NI and DETI decision making and monitoring in respect of the BTI project did not follow the processes that had been established within the organisations for the assessment, approval, consideration and approval of material changes, payment of grant, or monitoring of the project. Guidelines which were in place for processes such as project appraisal and approval, project monitoring and payment of claims were not always applied.

4.80 Recommendation 14 of the Public Accounts Committee Report (of May 2012)<sup>380</sup> on the BTI project noted that:

“There is a particular responsibility on top management to encourage a culture of compliance with good practice throughout their organisation. The Committee recommends that both DETI and Invest NI now ensure that the lessons on leadership and management culture arising from the Report are assimilated within their respective organisations.”<sup>381</sup>

4.81 In a paper for the DETI Senior Management Team in November 2012 Mr Sterling noted a number of specific issues in the case including the fact that the BTI project was not adequately monitored and that records were not kept to explain each decision.<sup>382</sup> At paragraph 5 of the paper Mr Sterling recorded that it appeared that there had been a culture 10 to 12 years previously that had enabled those procedures to be circumvented and ultimately lead to the substantial loss to the public purse.<sup>383</sup> At paragraph 7 he wrote “I am content that the culture within DETI is totally different to that which appears to have operated ten to twelve years ago.”<sup>384</sup> At paragraph 10 of the same document he said:

“I am also happy that as an organisation we can and should take risks in order to deliver our objectives. Risks should be recognised and managed, and decisions taken at an appropriate level commensurate with the funding and risks being proposed. This should not result in undue delay in decision making and following appropriate and proportionate process protects the individuals involved in the decision as well as the public purse.”<sup>385</sup>

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380 INQ-05114 to INQ-05324

381 INQ-05125

382 INQ-05325 to INQ-05328

383 INQ-05327

384 INQ-05328

385 INQ-05328



## Findings

20. It is questionable whether DETI should have embarked on the independent development of an NI RHI given its own accurate assessment of lack of resources.
21. The Inquiry finds that the resources available to develop this novel and complicated scheme were inadequate. The insufficiency of resources was not only in terms of staff numbers: the small team was simply not provided with the necessary knowledge or experience to carry out the necessary activities; to analyse the information it received; to make the necessary judgments; nor was there any adequate effort to access expertise in other parts of the Northern Ireland Government such as Invest NI and/or the Strategic Investment Board.
22. The Inquiry finds that there was a failure to apply appropriate project management, which was a significant failing.
23. One of the many consequences of there being no formal project management of the RHI scheme was the complete absence of any objective, easily accessible unified record. By way of examples, as discussed later in this Report, as activity to develop the scheme advanced during 2012, the lack of formal project management documentation meant that the risk mitigation measures referred to in the Casework Committee minutes (which identified nine risks and various mitigating actions, including the need regularly to review the level of subsidy)<sup>386</sup> were not captured in an easily accessible project record. Neither the conditions attached to the DFP approval of the business case,<sup>387</sup> nor the fact that DFP's approval of expenditure was limited to the end of March 2015, were captured in a readily accessible record.
24. The absence of project management also had profound consequences for the progress of the RHI scheme. Had there been a programme plan and a progress log, together with a live risk register and issues logs, the relevant Energy Branch staff would have had an ongoing indication of steps that were required to be taken and the scheme could have been managed as circumstances changed. This was a new 'flagship project', subject to volatile and unpredictable degrees of uptake that required careful, continuing review and management of risk.
25. The decision not to have a Gateway Review in 2012 was a key missed opportunity to subject the RHI scheme to independent scrutiny, especially given that the scheme represented a very real risk, being a new, volatile, demand-led programme, subject to many variable assumptions.
26. The risks of the scheme, although well identified initially, were never managed systematically. The initial scheme Risk Register was not updated or used effectively as a tool to manage and reduce risk. While risks may have been discussed informally at team meetings, no record of such discussions was kept and the Inquiry saw no evidence that the RHI scheme Risk Register was ever formally amended or updated, not even when risks began to materialise.

386 DFE-04231 to DFE-04232

387 DOF-03244 to DOF-03245

- 27. The Inquiry has had regard to the resource difficulties faced by Ms Hepper and her approach to the practical/proportionate management of the project. The lack of adequate resources may have mitigated against the institution of all aspects of the PRINCE structure, but recognised project management disciplines are adaptable and the Inquiry finds that the application of some of the relevant features should have been considered given the characteristics of the scheme. Elsewhere in the Energy Division it appears that the “Gas-to-the-West” project was being managed subject to PRINCE principles.**
- 28. Nevertheless, the Inquiry is unable to see why, even with the limited resources available in Northern Ireland, an objective project plan could not have been created, maintained and reviewed which might have been supplemented, as required, between particular individuals together with some type of oversight board holding regular meetings. As meetings of the Renewable Heat Group declined and without a joint DETI-Ofgem board the absence of some form of project board proved particularly damaging in terms of the failure to ensure continuity of knowledge and regular review.**
- 29. Ofgem and DETI failed to establish appropriate important governance arrangements, such as the joint board originally proposed by Ofgem in the feasibility study of 2011. This was a significant failure on the part of both parties.**
- 30. The absence of such a joint project board with recorded minutes of its monitoring activities is very difficult to justify in the context of a novel, demand-led, volatile scheme subject to significant variables, not least the fluctuations of fuel prices.**
- 31. The Inquiry finds that the failings in respect of project management and the RHI scheme are all the more unacceptable given that throughout the life of the scheme, DETI was actively considering failings from previous projects which raised similar issues.**

## Chapter 5 – CEPA and its reports of 2011 and 2012

5.1 Another central theme of the Inquiry’s work has been to examine the nature and adequacy of the expert reports that DETI obtained as part of developing the Northern Ireland RHI scheme. For continuity, in this chapter the Inquiry examines the CEPA reports from 2011 and 2012, before returning to the developments in DETI in 2011. The June 2013 report from CEPA, which relates to Phase 2 of the NI RHI scheme, is dealt with later in the Report.

### Appointing CEPA

5.2 As already noted, DETI needed economic expertise to help with the development of the RHI scheme and on 30 December 2010 Ms Hepper had advanced a submission to Minister Foster, copied to Dr Crawford, and the Permanent Secretary, Mr Sterling, seeking approval to put a business case to DFP for the appointment of CEPA, which had previously been selected as the external consultants to carry out the economic appraisal of an RHI for Northern Ireland.<sup>388</sup> It seems clear that timing was regarded as being of considerable importance and the Inquiry notes that the submission emphasised the need for an early decision “as DFP approval is required and the appraisal completed to ensure spend in 2011/2012 is achievable.”<sup>389</sup> This was echoed in the business case seeking appointment of the consultants, which recorded at paragraph 1.14:

“There is no possibility in deferring this assignment. DECC intend to roll-out a RHI in GB from June 2011, by deferring this project there would be a significant delay in rolling out similar policy in Northern Ireland and therefore disadvantaging the renewable heat market here. **Further to this HMT has indicated that funding for a Northern Ireland RHI is available from 2011/2012, delaying this project would also lead to this money being unspent.**”<sup>390</sup> (the Inquiry’s emphasis)

5.3 Ms Hepper explained that DETI Economics Branch did not have the skills to undertake the necessary work in-house. It was a “complex, one-off task” that required the advice of specialist heat economists and she pointed out that previous research carried out had highlighted that the GB RHI, as it then stood, could be ineffective in Northern Ireland as it did not take account of the specific local heat market.<sup>391</sup>

5.4 The terms of reference and the business case, prepared by Peter Hutchinson, a deputy principal in Energy Division, were annexed to the submission and the terms confirmed that “The DETI Minister has already indicated that a Northern Ireland RHI will be implemented if it is economically viable.”<sup>392</sup> The business case also recorded that Minister Foster had issued a press release to that effect on 20 September 2010.<sup>393</sup>

5.5 A number of objectives for the work were specified in the terms of reference including the “development and implementation of a specific Renewable Heat Incentive (RHI) for Northern Ireland” together with “An assessment of appropriate tariff levels (pence per kWh).” There was

388 DFE-58027 to DFE-58063

389 DFE-58028

390 DFE-58036

391 DFE-58030

392 DFE-58052

393 DFE-58035

also a requirement to “Identify a full list of potential options for future delivery of a Northern Ireland Renewable Heat Incentive.”<sup>394</sup> Each option was to be fully costed, the net present values (NPVs) calculated and the financial payback of each technology assessed. The potential risks in delivery of any future support scheme were to be identified and assessed and there was a requirement to include a sensitivity analysis of key assumptions.<sup>395</sup>

- 5.6 The consultancy project was to be supervised by DETI Sustainable Energy Branch in conjunction with DETI Economics Branch. CEPA was duly commissioned in January 2011<sup>396</sup> to undertake the economic appraisal of the feasibility of an NI RHI scheme. AEA Technology (AEA), which had previously advised in relation to the GB scheme, was subcontracted by CEPA,<sup>397</sup> with DETI’s knowledge and approval, to provide specialist technical advice and input in respect of the work CEPA was undertaking for DETI.<sup>398</sup> However, the contractual nexus appears at all times to have been between DETI and CEPA rather than between DETI and AEA. Mr Hutchinson, along with DETI economist, Mr Connolly, participated in meetings with CEPA, attempted to ensure that agreed guidelines were observed and commented on various draft reports.

### The 2011 CEPA reports

- 5.7 Draft reports were supplied to DETI by CEPA on 11 and 28 March 2011, with a draft final report being furnished on 31 May.<sup>399</sup> The final report was delivered to DETI on 28 June 2011.<sup>400</sup> All four documents were considered by the Inquiry, the latter two being particularly significant for the extent to which they were used or otherwise by Energy Division officials in providing advice to Minister Foster.
- 5.8 CEPA ultimately recommended consideration of both a Challenge Fund and an NI version of the GB RHI scheme.<sup>401</sup> The Challenge Fund was a system under which supporting capital funds would be awarded on a competitive basis, the rationale being to obtain the best value for money when it was not clear how much subsidy might be required to achieve a given aim.<sup>402</sup> CEPA’s 28 June report indicated that a Challenge Fund appeared better, both in terms of heat delivered per pound and funding structure for domestic customers, although CEPA recognised that there were “wider policy considerations and stakeholder acceptability issues to consider.”<sup>403</sup> In the event that DETI was unable to confirm a sufficient degree of certainty that funding would continue beyond 2015, CEPA had a clear view that only some form of Challenge Fund or capital grant scheme would be worth pursuing.<sup>404</sup> Even if such a degree of reassurance on funding was obtained, CEPA still recommended a Challenge Fund as a means of resolving genuine concerns about technology costs and uptake, although it also recommended that DETI should consult on the option of moving to an NI RHI in the long term.
- 5.9 The Challenge Fund was shown to have the potential to produce the most renewable heat, to be much less exposed to the risk of over-subsidisation and to offer the best value for money

394 DFE-58053 to DFE-58055

395 DFE-58055 to DFE-58056

396 WIT-105459

397 WIT-105466, WIT-110025; TRA-01230 to TRA-01231

398 WIT-110025; TRA-01230 to TRA-01231; TRA-01239 to TRA-01240

399 DFE-187754 to DFE-187887

400 DFE-188120 to DFE-188264

401 DFE-188125

402 DFE-188169

403 DFE-187624

404 DFE-187625

in terms of £ per kWh renewable heat, subject to concerns that a lack of awareness might mean that the most cost-effective heat deployment opportunities might not be targeted.<sup>405</sup> Table 10.3 in the 31 May draft demonstrated that a Challenge Fund, in terms of monetised benefit, would be some £26 million cheaper than the suggested NI RHI scheme.<sup>406</sup> In oral evidence Ms Hepper agreed that, in that draft, the Challenge Fund was shown to perform better than the proposed NI RHI scheme.<sup>407</sup>

- 5.10 It appears from the early exchanges with DETI about the initial drafts of the CEPA report that DETI had concerns about the length of time it would take to establish a challenge/grant scheme and the consequent possibility of putting the £2 million funding for 2011-12 at risk, even though the Inquiry notes that such a scheme would not have required a Legislative Consent Motion or the enactment of any additional enabling powers. The risk was one of losing the funds for that year, since the AME rules implied the funds could not be rolled over, although, as discussed earlier, £1.8 million of the 2011-12 funding was in fact ultimately re-profiled into 2012-13 following an application to DFP.
- 5.11 Significantly, the draft report of 31 May also recorded that none of the options considered delivered the 10% of renewable heat set as a target for Northern Ireland.<sup>408</sup> In the circumstances, it is not surprising that exchanges about the draft reports ensued between CEPA and DETI. Mr Hutchinson continued to raise questions and Ms Hepper stressed that they were “quite demanding” in their attempts to seek plausible explanations.<sup>409</sup> However, as she observed in evidence, for those without relevant knowledge or experience it was not easy to challenge the expertise which had been brought in for guidance.<sup>410</sup>
- 5.12 The Inquiry has considered a document, dated 15 June 2011, providing CEPA’s response to a number of comments raised by Mr Hutchinson on 6 June.<sup>411</sup> He had enquired about whether additional tariff options could deliver 10% renewable heat by 2020 and/or whether there was a need for a return on capital of 15% rather than 12%.<sup>412</sup> CEPA replied that the switching of the large Invista plant to biomass was now included in the model and that this meant that 10% was reached for some scenarios. CEPA also undertook to deal with the impact of different return levels in a training session on the model and agreed to modify parts of their draft regarding some tariff levels.<sup>413</sup>
- 5.13 Of particular interest is paragraph 8 of this document, in which Mr Hutchinson raised the need to be very clear why RHI was the preferred option over the Challenge Fund in the long-term funding scenario. To this, CEPA replied:

“Our recommendation is based on the assumption that DETI wants to do an RHI. The Challenge Fund option is for comparison purposes to show what could be achievable.”<sup>414</sup>

405 DFE-188193

406 DFE-187844

407 TRA-01823 to TRA-01824

408 DFE-187759

409 TRA-01817

410 TRA-01815 to TRA-01818

411 CEP-143601 to CEP-143612

412 CEP-143601

413 CEP-143593

414 CEP-143606

- 5.14 With regard to tiering, CEPA had said in its 31 May draft that it had considered tiering for the NI RHI rates, using the DECC approach, and, for the reasons it gave, concluded that tiering was not required.<sup>415</sup> Mr Hutchinson had asked for more information as to why tiering had not been proposed for Northern Ireland.<sup>416</sup> By way of reply to Mr Hutchinson’s question, CEPA stated:
- “It is also only applied when the reference technology has a sufficient load factor and the ongoing fuel cost of the new technology is greater than what it would have been had they stuck with their counterfactual technology (a positive additional fuel expense). We did not find these conditions to be fulfilled for any technology band.”<sup>417</sup>
- 5.15 As discussed previously, during the course of its analysis CEPA compared a number of options including a Challenge Fund, capital grants, the GB RHI scheme, an NI RHI scheme based on the DECC approach to NI data, and a tailored NI RHI scheme using slightly different discount rates. CEPA concluded that the Challenge Fund approach would deliver the most renewable heat of any option and, because it was competitively allocated and technology neutral, at the lowest cost.<sup>418</sup>
- 5.16 With regard to budget control, a Challenge Fund would also have provided potentially greater natural protection compared to an RHI. While this point was not specifically highlighted by CEPA, table 5.2 of its draft and final reports recorded the potential for competitively allocated subsidies, such as a Challenge Fund, to involve the bidding for subsidy until “...the pot is exhausted.”<sup>419</sup> Mr Cockburn explained in his oral evidence to the Inquiry that CEPA had a working assumption that steps would also be taken to protect the budget if an RHI was adopted,<sup>420</sup> using a ‘first come first served’ approach, and that it was “common sense that you’ve got a finite amount of money available and you commit it up to the point where there’s no more available.”<sup>421</sup>
- 5.17 However, regarding the ultimate choice of scheme, the CEPA report also concluded that there were other factors that might indicate that an RHI should be pursued over a Challenge Fund for commercial installations. An RHI scheme was said to be less expensive upfront, although it was likely to be significantly more expensive over the long term, and would have the advantage of consistency and administrative simplicity with GB as well as providing a “long-term signal for the generation...of renewable heat.”<sup>422</sup> CEPA did suggest that there could be benefits for the non-domestic scheme in terms of administrative simplicity and experience in linking up with GB but CEPA was less persuaded of the benefit of RHI schemes for domestic applicants and recommended that DETI should reserve any final decision on the inclusion of domestic consumers until the final GB approach had been clarified.<sup>423</sup>

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415 DFE-187814

416 CEP-143610

417 CEP-143610

418 DFE-188126

419 DFE-187799; DFE-188170

420 TRA-01249 to TRA-01253

421 TRA-01249; TRA-01252

422 DFE-187933

423 DFE-188128

- 5.18 In the end no clear recommendation was made in the 31 May draft final report,<sup>424</sup> or indeed in the final version of 28 June 2011.<sup>425</sup> A later internal email exchange between Mr Cockburn and Mr Morrow of CEPA in 2017 recalling the contextual circumstances is potentially revealing. In the course of that exchange it was agreed that the Challenge Fund had offered significant advantages as compared to an RHI, including the prevention of over-subsidisation, whereas DETI would have liked to benefit from discounted administration costs by engaging Ofgem, which had been retained in GB, and it, therefore, was seeking a recommendation in favour of RHI. DETI was concerned about its ability to administer a Challenge Fund given its limited resources. Both Mr Cockburn and Mr Morrow felt that the only professional recommendation they could make would be in favour of the Challenge Fund and any decision that non-monetary internal issues rendered such a fund unworkable was a matter for DETI. They agreed that this did not appear to go down well with DETI who had made it “very clear” that they wanted an NI RHI scheme.<sup>426</sup>
- 5.19 From an economic perspective, Mr Connolly was also involved in meetings and email exchanges during the production of the CEPA reports and the draft of 31 May was sent to him for review on 1 June.<sup>427</sup> Mr Connolly responded on 3 June providing some 32 paragraphs of comment under different headings.<sup>428</sup> Noting that Table 7.4 of the 31 May draft demonstrated that the Challenge Fund produced the cheapest unit of heat and Table 10.3 recorded that the Challenge Fund produced a cheaper net monetised benefit (cost) than the NI RHI scheme,<sup>429</sup> Mr Connolly concluded that it would be useful and necessary to have a preferred option finalised and fully costed prior to submission to DFP.<sup>430</sup>
- 5.20 In his evidence to the Inquiry, Mr Connolly had no recollection of being involved in negotiations with CEPA between receipt of the May and June reports and he did not pursue his recommendation after seeing the June report nor did he raise the changes in the latter with his line manager, Shane Murphy.<sup>431</sup> Mr Connolly accepted that part of his responsibilities in the ASU was to provide policy analysis and economic advice for the Energy Division. Mr Hutchinson provided him with a copy of the final CEPA report of 28 June, along with a Regulatory Impact Assessment (RIA). The RIA described the NI RHI scheme as the “preferred option” which “offers the highest potential renewable heat output at the best value.” Mr Connolly accepted that such a statement was “inaccurate” and “totally at odds” with the final CEPA report of 28 June.<sup>432</sup> If he had noticed it he would have drawn it to the attention of Mr Hutchinson.
- 5.21 Mr Connolly told the Inquiry that he felt that the choice of option had been “settled and finished” once the Minister had expressed her contentment with the submission of 8 June 2011 (sent to the Minister by Energy Division based on CEPA’s draft final report of 31 May 2011, but before receipt of the actual final report of 28 June 2011). The 8 June submission is dealt with in detail in a later chapter of this Report. As a consequence of learning of the Minister’s decision,

424 DFE-187762 to DFE-187763

425 DFE-188128 to DFE-188129

426 CEP-150707 to CEP-150708

427 DFE-158468 to DFE-158602

428 DFE-158603 to DFE-158606

429 DFE-158538; DFE-158559

430 DFE-158606

431 TRA-03472 to TRA-03486

432 TRA-03497 to TRA-03498

Mr Connolly’s concern about the potential of a Challenge Fund had become limited.<sup>433</sup> He also confirmed that he had confidence in the professional abilities of CEPA, although he conceded that he should have followed up the failure to identify a preferred option in terms of value for money, which was a requirement of step 10 of the analysis specified by the Northern Ireland Guide to Expenditure and Appraisal Evaluation (NIGEAE).<sup>434</sup>

- 5.22 Having achieved ministerial approval for the choice of scheme, on 20 July 2011 DETI issued a public consultation document on the proposed NI RHI.<sup>435</sup> This closed on 3 October 2011 and the main issues raised by consultees concerned the need for more generous tariffs; whether the banding suggestions were appropriate; and any potential adverse impact upon the then nascent gas industry. The outcome was a decision by DETI to seek a further opinion from CEPA on a limited number of specific matters set out in emails, dated 9 and 10 November 2011, from Mr Hutchinson to Ian Morrow of CEPA, which included banding of boiler sizes and tariffs.<sup>436</sup> The tasks set out in the emails were converted by CEPA into a formal RHI Extension Proposal<sup>437</sup> which was accepted by DETI on 15 December 2011.<sup>438</sup>

### The February 2012 CEPA addendum

- 5.23 On 16 February 2012 CEPA provided an addendum to the report of 28 June 2011.<sup>439</sup> It seems clear that the request for this addendum was the source of tension and some irritation for CEPA who felt that too much was being asked of it at this time for too little reward. Nevertheless, it delivered this response and recommended two new biomass bands at 0-20kW and 20-100kW (replacing the previous <45kW and >45kW).<sup>440</sup> The main effect of this change would be to increase the size and number of boilers that could attract the new higher tariff. The assumed capital cost for boilers rose from approximately £400/kW for a 20kW reference boiler to approximately £600/kW for a 50kW reference boiler for the new 20-100kW band. CEPA warned that, wherever the bands were set, there was a potential for “gaming” by consumers choosing the number and size of boilers to maximise their benefit.<sup>441</sup>
- 5.24 Tables A25 and A27 of the addendum clearly demonstrated the amount of subsidy payable in respect of 20-100kW biomass boilers to be greater than the then price of fuel.<sup>442</sup> This meant that the 20-100kW biomass tariff put forward by CEPA in the February 2012 addendum for use by DETI in the NI RHI scheme created a perverse incentive for scheme members to generate more heat than they required in order to gain profit. The fact that some biomass tariffs proposed by CEPA were higher than the then cost of fuel meant that the NI RHI scheme would require tiering, or some other form of protection that prevented scheme members from profiting from the generation of unrequired heat. The existence of the perverse incentive within the tariffs also increased the separate need for proper and effective budget protection.

433 TRA-03481

434 TRA-03493; TRA-03480 to TRA-03481

435 DFE-63726 to DFE-63837

436 CEP-46468 to CEP-46470

437 WIT-106210 to WIT-106213

438 WIT-106219

439 DFE-77896 to DFE-77939

440 DFE-77899

441 DFE-77906

442 DFE-77929 to DFE-77930



- 5.25 Quite apart from the risk of profiteering as a consequence of a perverse incentive, CEPA was aware of the risk of overcompensation arising from a significantly greater load factor, effectively hours of usage, than that assumed in its tariff calculations, in particular its 20-100kW biomass tariff calculations. However no sensitivity analysis was provided for DETI to illustrate such a risk. Although CEPA specifically considered the question of tiering in respect of the 0-20kW Ground Source Heat Pump tariff when preparing their addendum report, CEPA does not appear to have considered the issue in respect of any of the biomass tariffs. CEPA also specifically recommended that DETI should reassess biomass prices at review points to determine whether the overall tariff levels were still appropriate.<sup>443</sup>
- 5.26 In his evidence to the Inquiry, Mr Cockburn accepted that several inputs into the tariff calculation tables set out in the addendum were incorrect, that their numerical precision gave a false sense of accuracy and certainty<sup>444</sup> and that using those figures should have produced a tariff of 6.6p/kWh rather than 5.9p/kWh.<sup>445</sup> He agreed that a revised model had been created by CEPA for the 2012 addendum but confirmed that it had not been provided to DETI.<sup>446</sup> Some two weeks after submission of the addendum report Mr Hutchinson was supplied with a number of spreadsheets, but not the revised model itself, by Ian Morrow who emphatically told Mr Hutchinson in an email dated 29 February 2012 that CEPA did not take responsibility for the sheets since “it’s outside the ToR.”<sup>447</sup>
- 5.27 The addendum was supplied to Mr Connolly, the DETI economist providing advice to Sustainable Energy Branch, to consider and ‘sign off’ as value for money (VFM) in accordance with NIGEAE.<sup>448</sup> He recognised that step 4 of NIGEAE required attention to be paid to any relevant change in circumstances. He told the Inquiry that he accepted that the addendum increased the absolute lifetime cost of NI RHI subsidy spend by approximately £111 million. However, in his oral evidence Mr Connolly explained that reassessing the Net Present Value/Cost at that stage would have been “a meaningless exercise unless you’re also trying to work out how, if at all, the NPVs of all the other options have changed.”<sup>449</sup>
- 5.28 As noted earlier in this Report, his knowledge of the June 2011 ministerial decision, which he understood to be in favour of an NI RHI scheme anyway seems to have terminated any further interest that he had in alternatives like the Challenge Fund. Although he said that he had carried out a further VFM calculation in an attempt to estimate the value of the difference in “carbon saved,” he considered that changes between 2011 and 2012 in the reports with regard to banding and barrier costs were of a technical nature outside his expertise and that, as CEPA had not included any sensitivity calculations in respect of load factors, boiler efficiency or fuel prices, it was unnecessary for him to perform any such analysis.<sup>450</sup>
- 5.29 He was assured by Mr Hutchinson that there would be constant reviews which would capture any relevant developments. He did not suggest that Mr Hutchinson should revert to CEPA with regard to the significant alteration in CEPA’s calculations over a relatively short period of time,

443 CEP-116305

444 TRA-01286

445 WIT-107780 to WIT-107781

446 TRA-01352 to TRA-01355

447 DFE-317129 to DFE-317139

448 DFE-80286 to DFE-80287

449 TRA-03532

450 WIT-29080 to WIT-29081; TRA-03534 to TRA-03537; TRA-03562 to TRA-03565

particularly in the context of the huge increase of £111 million in the cost of the NI RHI scheme between the reports of June 2011 and the addendum of February 2012.<sup>451</sup> He was referred by the Inquiry to the sensitivity analysis of load factor performed by Mr Murphy for Dr McCormick in September 2016 demonstrating how an increase in load factor to 50% would result in the rate of return rising from 12% to 73%. Mr Connolly stated that this was not an exercise that was generally performed by economists in ASU and that their task was to comment on the reports of others.<sup>452</sup>

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451 TRA-03523; TRA-03552

452 TRA-03565 to TRA-03568

## Findings

32. The CEPA draft and final reports from May and June 2011 provided a clear economic analysis of the potential to incentivise renewable heat production in Northern Ireland using a number of different approaches, mainly split between grant-based schemes and schemes providing ongoing revenue payments. The evidence base provided in support of this to DETI appears to corroborate the key findings and recommendations made in CEPA's reports.
33. The findings of CEPA's reports were stark: the Challenge Fund option produced the most heat at the least cost on an economic basis.
34. In contrast to the earlier reports, the addendum from CEPA of February 2012 appears to have been produced under time and resource pressure and contained a number of substantial errors. It appears that CEPA considered DETI to have underestimated the time and resource required. Despite these pressures, whilst acknowledging the limited scope of the addendum, CEPA had a responsibility to verify the quality of the final product. Furthermore, DETI was not provided with the necessary evidence or data to be able readily to understand or reconstruct the addendum findings, particularly given DETI's level of expertise. The revised model that was used for the addendum was not provided to DETI.
35. Knowledge transfer between CEPA and DETI was less than it should have been.
36. The Inquiry notes the significant variation in the key outputs of the three different reports (the May 2011 draft final report, the June 2011 final report and the February 2012 addendum), including scheme costs which varied by hundreds of millions of pounds and variation in the levels of renewable heat projected to be achieved. None of these variations in costs were sufficiently tested through adequate sensitivity analysis as required by the NIGEAE and CEPA's terms of reference. Responsibility for this is shared by CEPA and DETI: it was CEPA's job to do it and DETI's job to check it had been done. Sensitivity analysis should have provided clarity about which factors were particularly significant in determining the level of heat produced and the costs.
37. CEPA did correctly warn more generally about uncertainties in assumptions and modelling and the need for regular review. The need for monitoring was also set out.
38. CEPA should have recognised that the February 2012 addendum recommended a commercial biomass tariff greater than the cost of fuel used for heat production thus creating the perverse incentive to produce unnecessary and excessive amounts of heat. The Inquiry notes that this failure arose despite CEPA's own spreadsheet model automatically flagging up to it that this was the case and even calculating and showing what a tiered tariff might have looked like.<sup>453</sup> While CEPA was consulted on the basis of being an expert adviser, the Inquiry finds that the difference should also have been picked up by DETI officials who recorded the relative values upon consecutive pages of the Casework Committee synopsis, discussed later in this Report.

453 This issue is addressed in more detail later in this Report.



## Chapter 6 – The ministerial submissions of 8 June and 5 July 2011 and the launch of the public consultation

### The ministerial submission of 8 June 2011

- 6.1 A submission dated 8 June 2011 was prepared by Ms Hepper for Minister Foster for the purpose of informing her of the conclusions contained in the draft final CEPA report of 31 May 2011, which was discussed in the previous chapter of this Report.<sup>454</sup> A draft Impact Assessment accompanied the submission and is also discussed further below.
- 6.2 Ms Hepper told the Inquiry that she had signed off the submission, which was probably drafted by a combination of Mr Hutchinson and Ms McCutcheon.<sup>455</sup> The Minister does not appear to have had an opportunity to consider the draft report of 31 May 2011 until it was brought to a meeting with Ms Hepper on 14 June.<sup>456</sup> When asked by Inquiry Counsel whether it would have been better to give the Minister some time to consider the detailed figures in the report before the meeting, Ms Hepper said “Well you know that’s the way we did it and it did seem to work...”<sup>457</sup>
- 6.3 The submission timing was recorded as “Immediate” in order to allow the CEPA analysis to be published as part of the imminent public consultation. Included in the “Background” section of the submission was an account of the £25 million AME funding spread over the period 2011-15 to be provided by HMT in the course of which it was said:
- “Discussions with DECC regarding funding post 2015 have revealed the following: DECC see no difficulties re funding going forward as both DECC and HMT regard RHI as a priority, flag-ship policy; plus, HMT recognise that the scheme will be open until 2020 and that significant funding post 2015 will be required. It is also the case that DETI received a pro-rata allocation of the UK funding for the period up to 2015, and HMT are aware that our scheme will complement DECC’s, will therefore also require funding in the next spending review and we need our portion of the ‘UK pot.’”<sup>458</sup>
- 6.4 As discussed in chapter 3, Ms Hepper did not explain the unusual nature of the funding in the submission, nor any potential risks to the DEL budget of overspending or refer to the consequential need for budget controls. The Inquiry noted that such information also does not appear to have been provided to CEPA by either Mr Hutchinson or Ms Hepper. With regard to potential budgetary control, at page 44 of the May 2011 draft final report CEPA recorded that funding for a capital grant scheme could control its budget as follows:
- “In a first come first served approach, potential beneficiaries would apply for subsidy. This would be awarded until the amount available was exhausted. Potentially, this subsidy could be allocated into different pots or pools for different types of beneficiary to recognise differences between groups.”<sup>459</sup>

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454 WIT-00739 to WIT-00749; complete version may be found at DFE-29387 to DFE-29405

455 TRA-01896

456 TRA-01868

457 TRA-01869

458 WIT-00740

459 DFE-187797

- 6.5 CEPA advised that an alternative way to distribute capital grants would be on a competitive basis in the form of a Challenge Fund. In either case the grants would be kept within a capped budget and would be more appropriate for a scheme in which uptake was uncertain and subject to unpredictable surges.<sup>460</sup> Such an advantage offered by a capital grant/Challenge Fund also did not appear in the submission.
- 6.6 In the course of giving evidence, Ms Hepper thought her expectation that funding for new applicants would extend to 2020 might have been based upon a conversation between Ms McCutcheon and Jo Greasley of DECC.<sup>461</sup> However this submission was dated 8 June, the same date upon which Mr Hutchinson had emailed seeking advice from DECC as to whether it would be correct to state in the consultation that the scheme would remain open to applicants to 2020 if no funding was secure after 2015. He was also enquiring how the AME classification impacted on unspent money or overspend in one year and whether funding could be “rolled over.” The answer to that email enquiry post-dated the submission to Minister Foster.<sup>462</sup>
- 6.7 In oral evidence Ms Hepper said that “our mind-set was it’s capped in each year and we’ll not be going above that.”<sup>463</sup> However, it is rather difficult to reconcile such a mind-set with the clear terms of the earlier April/May 2011 email exchange, including HMT’s Mr Parker and then Ms Clydesdale and Ms Brankin warning of the need for clear cost controls (which is dealt with in greater detail at chapter 3 of this Report).
- 6.8 The Inquiry remains unclear as to precisely what Ms Hepper and her team believed in June 2011 in relation to the effect of the cap on the annual funding, namely whether it could act as some form of cost control or whether it would simply not be exceeded in practice for some other reason. In either event, any reassurance which was felt at this point about not exceeding the annual cap is difficult to understand in the context of a scheme which was volatile, with an unpredictable demand, and in which, once accredited, applicants would become entitled to grandfathered subsidy for 20 years. Furthermore, specific warnings had been received from DETI Finance and HMT that not only should the caps not be exceeded but that any excess had a potential to impact upon the DEL budget. The Inquiry also notes in this regard that the risk of exceeding the scheme budget was specifically included as ‘risk E’ on the Scheme Risk Register, which was later forwarded to the Casework Committee considering the scheme.<sup>464</sup>
- 6.9 In her submission of 8 June Ms Hepper confirmed that, although a draft final of the CEPA report had been received on 31 May, there were a “number of issues” that still needed to be addressed before the report could be finalised.<sup>465</sup> A copy of the CEPA draft final report was not supplied with the 8 June submission nor was it supplied in advance to Dr Crawford, who did not ask to see it.<sup>466</sup> In such circumstances he could not have been in a position to ensure that the technicalities would be fully understood and communicated to the Minister.
- 6.10 Ms Hepper’s submission noted the view expressed in the CEPA report that if no funding was guaranteed for new applicants after 2015 a Challenge Fund or grant system would be preferable, but she went on to refer to several issues to be considered if such an option were

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460 DFE-187798

461 TRA-01875

462 WIT-16380 to WIT-16382

463 TRA-01875

464 WIT-07061 to WIT-07073

465 WIT-00740

466 TRA-07517

adopted. These included that such a grant-based scheme would need to be administered by the Department or a contracted third party and thus result in additional resource pressure, that it could be complicated and require applicants to have an understanding of technology and their likely heat demands, that it could encourage the selection of a limited number of technologies at the expense of diversity, and that experience suggested that such a system would not provide long-term stable support once funding came to an end.<sup>467</sup> The submission did not refer to the relative cost benefits or the overall cost-effectiveness of the Challenge Fund, the lower support cost per unit of heat or how the potential risks to funding could be much better contained by such a fund.

- 6.11 In the submission Ms Hepper explained CEPA's advice relating to an NI RHI scheme and the need to adjust the tariffs to the different pattern of fossil fuel use as compared to GB in terms of oil rather than gas.<sup>468</sup> She also pointed out the "major issue" with an NI RHI scheme would be that customers could be potentially "over incentivised" and inefficient technologies supported.<sup>469</sup> If an NI RHI scheme was the preferred option, Ms Hepper advised that such a scheme should be in place by 1 April 2012 and suggested the establishment of a renewable heat group with inter-departmental membership.<sup>470</sup>
- 6.12 One of the issues that DETI officials had raised with CEPA following the provision of the draft final report was a need to be very clear as to why RHI was the preferred option over a Challenge Fund. CEPA had responded "Our recommendation is based on the assumption that DETI wants to do an RHI. The Challenge Fund is for comparison purposes to show what could be achievable."<sup>471</sup> The Inquiry was not provided with any written or oral evidence to establish that DETI ever challenged that assumption. Indeed, although both Mr Hutchinson and Ms Hepper denied that Energy Division officials had sought from CEPA a recommendation for an RHI scheme, each was unable to point to any clear documentary rejection, or recall any specific oral rejection, of the CEPA assertion that DETI had preferred an RHI scheme.
- 6.13 In the course of reviewing the various options discussed in the report Ms Hepper advised at paragraph 24 of her submission that:
- "The NI RHI is the preferred approach and offers the highest potential renewable heat output at the best value."<sup>472</sup>
- 6.14 Ms Hepper stated in oral evidence that this only referred to a comparison with the GB RHI scheme and, in support of that interpretation, she pointed out that the submission closed with a recommendation to consider all the options. However, she accepted that the submission did not contain any indication of that limited comparison or any detailed basis for asserting that the NI RHI scheme offered either higher heat potential or better value than the GB RHI scheme. The submission listed the options at paragraph 12 as (a) - (e), in which the NI RHI scheme at (e) was dealt with quite separately from the GB RHI scheme, capital grants, renewable challenge fund and 'do nothing'.<sup>473</sup>

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467 WIT-00742 to WIT-00743

468 WIT-00744

469 WIT-00743

470 WIT-00746 to WIT-00747

471 CEP-143606

472 WIT-00744

473 TRA-01887 to TRA-01893

- 6.15 When this aspect of the submission (that “the NI RHI is the preferred approach and offers the highest potential renewable heat output at the best value”), which was repeated in the public consultation document,<sup>474</sup> was drawn to the attention of Mr Cockburn, a director of CEPA, in the course of his oral evidence to the Inquiry he expressed the view that it did not accurately reflect the CEPA draft final report of 31 May 2011.<sup>475</sup> Mr Connolly told the Inquiry that he did not recall reading Ms Hepper’s reference to the NI RHI scheme offering the highest output for the best value, although he had been copied into the submission, but he accepted that any reasonable reading of the CEPA draft final report of 31 May would not have led to such a conclusion.<sup>476</sup>
- 6.16 In his oral evidence to the Inquiry Mr Hutchinson agreed with Ms Hepper’s explanation that this sentence had been intended to be read in the context of a comparison between a bespoke NI RHI scheme and the GB RHI scheme, although he accepted that the wording of the submission “could be interpreted as misleading” and that words such as “highest” and “best” did not lend themselves easily to the articulation of a limited comparison between only two options. He agreed that it was poorly drafted, at odds with the CEPA draft final report of 31 May 2011 and open to misinterpretation,<sup>477</sup> but he firmly rejected the suggestion by Dr Crawford that there had been any deliberate intention to mislead the Minister.<sup>478</sup> Mr Thomson, the Deputy Secretary in DETI at the material time, accepted in oral evidence that the statement was “potentially misleading”.<sup>479</sup>
- 6.17 Dr Crawford told the Inquiry that he and the Minister saw this reference to an NI RHI scheme offering the highest potential heat output at the best value as a rational and “clear steer” for preferring that option to the four alternatives and not being limited to a comparison with the GB RHI scheme.<sup>480</sup>
- 6.18 The Inquiry accepts that it was appropriate for other factors to be considered, when weighing up which option to choose, including benefitting from linking to the administration of the GB RHI scheme, the stakeholders’ preference generally to follow GB, the imbalance of resources between GB and NI, the lack of HMT budget for administration costs etc. However, in order to be able to make an informed decision, the Minister should have been told in the submission that the Challenge Fund was a cost-effective alternative to the RHI scheme.
- 6.19 This essential additional information was not identified as a contra-indication to a clear preference the Inquiry considers to then have been held by a number of DETI officials, apparently believed by some officials to be shared by the Minister, for an NI RHI scheme.

## The GB Impact Assessment for the Legislative Consent Motion

- 6.20 The submission of 8 June enclosed a draft GB Impact Assessment (IA) for the 2011 UK Energy Bill, which Minister Foster ultimately signed on 14 June 2011, the date of the meeting to discuss the submission.<sup>481</sup> That document was completed using a template provided by DECC

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474 DFE-29971

475 TRA-01275 to TRA-01276

476 TRA-03424 to TRA-03426

477 TRA-01609 to TRA-01615

478 WIT-09305

479 TRA-05716 to TRA-05721

480 TRA-07634 to TRA-07635

481 WIT-00751 to WIT-00757



for DETI in the course of arrangements to obtain the LCM in order to include the enabling powers for the introduction of the RHI in Northern Ireland in the 2011 UK Energy Act. The IA recorded as a key assumption/risk that:

“Results are sensitive to assumptions on fuel prices: reductions in fossil fuel prices will increase the resource cost of renewables and vice versa.”<sup>482</sup>

That IA also included, at paragraphs 3 and 16, references to the effect that DETI had already expressed a preference for an NI RHI, based on earlier research, and that a consistent approach with GB and DECC would be beneficial. Paragraph 3 of the ‘Evidence Base’ section contained a statement that:

“DETI has already indicated that a Northern Ireland RHI is the preferred method of incentivisation however before this can be designed and delivered a full economic appraisal is required.”<sup>483</sup>

A similar statement appeared at paragraph 16.<sup>484</sup> It seems striking that these statements were included in the draft IA provided to the Minister along with the very submission in which she, as Minister, was being asked to express her own preference.

- 6.21 There are a number of other pieces of documentary evidence which suggest that, by this time, there may have been an emerging preference for an ongoing NI RHI scheme, rather than a capital grant fund type of incentivisation for renewable heat or, at least, an emerging assumption that this was likely to be the type of scheme which the Department would ultimately pursue. For instance, the Minister’s announcement in September 2010 that renewable heat would be incentivised was apparently interpreted subsequently as a commitment to introduce a scheme similar to the GB RHI scheme.<sup>485</sup>
- 6.22 Minister Foster stated that she had not expressed or even considered such a preference until she read the submission and the IA and that she did not know why a preference was expressed for an NI RHI scheme in the IA. She explained that her press release of September 2010<sup>486</sup> was drafted by officials and followed the receipt of the AECOM Pöyry report. It was also prior to the commissioning of the economic appraisal, and at a point when no consideration had been given to the various potential methods of incentivisation.<sup>487</sup>
- 6.23 At paragraph 15 of the Impact Assessment it was stated that DETI was still conducting an analysis of the various options which would be considered by the Minister, followed by a public consultation over the summer of 2011. Paragraphs 17 and 18 of the same document had recorded that early indications were that local stakeholders wished a similar scheme to the GB RHI to be implemented in Northern Ireland. Further, that any delay would leave Northern Ireland at a disadvantage in comparison to GB and could lead to local skills being lost.<sup>488</sup> However, in her oral evidence Minister Foster agreed that there had been a “direction of travel” in DETI from 2009 for a renewable heat incentive scheme.<sup>489</sup>

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482 WIT-00752

483 WIT-00753

484 WIT-00755

485 See the Minister’s speech to the Northern Ireland Assembly in March 2011 in relation to the legislative consent motion [DFE-29148 to DFE-29149]; and footnote 2 in the IA signed on 14 June 2011 [WIT-00753], in support of what was said in paragraph 3 of that IA (referred to above).

486 INQ-30183 to INQ-30184

487 WIT-20563

488 WIT-00755

489 TRA-07722

6.24 The Inquiry further notes that not only were the full projected lifetime costs of £257 million for the scheme from the CEPA draft final report of 31 May 2011 not included anywhere in the 8 June submission, but the Minister was also being asked to sign the GB IA template for the 2011 UK Energy Bill with the cost sections left blank. The Minister signed this attesting, as set out on the GB *pro forma*, that she was satisfied the impact assessment represents “a reasonable view of the likely costs, benefits and impacts of the leading options.”<sup>490</sup>

### The meeting with the Minister on 14 June 2011

6.25 Ms Hepper accepted in oral evidence that a number of significant matters should have been dealt with, or dealt with in greater detail, in the 8 June submission. She also agreed in her evidence to the Inquiry that a Challenge Fund offered a better mechanism for controlling cost than a demand-led NI RHI scheme. However, she told the Inquiry that these matters had been fully explained by her to Minister Foster and Dr Crawford, at a substantial meeting lasting 30 minutes to an hour on 14 June 2011, at which she went through the 8 June submission and showed them a copy of the draft final CEPA report of 31 May 2011.<sup>491</sup>

6.26 As recorded on the annotations on the front page of the 8 June submission, the meeting had been originally fixed for 13 June but was then rearranged for 14 June.<sup>492</sup> Ms Hepper maintained it was at that meeting that the details of HMT funding for the NI RHI scheme, the limitation of the “most heat for best value” phrase (in a comparison with the GB RHI scheme) and the relative attractions of a Challenge Fund and an RHI scheme were fully discussed, assisted by the contents of the draft final CEPA report including the relevant tables and calculations contained within it.<sup>493</sup> Dr Crawford thought that this was unlikely, since (on his evidence) he and Minister Foster would have at least asked to take copies of the relevant tables from the report if they had been discussed in the way in which Ms Hepper suggested.<sup>494</sup> As noted above, it seems that a copy of the report was not provided in advance to either the SpAd or the Minister’s Private Office.

6.27 Ms Hepper was asked if she had discussed at the meeting the full cost of the NI RHI scheme, including the “tail” of payments that would continue even if it was closed to new applicants after 2015, amounting potentially to many millions of pounds. She said that she remembered that being one of the issues discussed and that they “went through all of the funding issues, as well, before she [the Minister] made any decision.”<sup>495</sup>

6.28 Ms Hepper also told the Inquiry that she had specifically explained that the reference to the RHI scheme being the preferred option, since it offered most heat at least cost was limited to a comparison with the GB RHI scheme rather than a comparison with all of the options mentioned in the submission. She said that she “did not recall that being a point of any difficulty”, and also that the £100 million saving represented by the Challenge Fund was fully discussed in the context of the “non-monetary issues” which were addressed at the meeting.<sup>496</sup>

6.29 Ms Hepper also said that, on 14 June, she was able to inform Minister Foster of the significant changes that were likely to be made in the forthcoming final version of the CEPA report as

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490 WIT-00751

491 See Ms Hepper’s oral evidence generally as to this meeting at TRA-01872 to TRA-01896

492 WIT-00739

493 TRA-01872; TRA-01886 to TRA-01889; TRA-01892 to TRA-01893

494 TRA-07657 to TRA-07663

495 TRA-01886

496 TRA-01891

- a consequence of discussions between Mr Hutchinson and Mr Morrow, the relevant CEPA representative, between the submission on 8 June and the meeting on 14 June.<sup>497</sup> The Inquiry has carefully considered Ms Hepper’s representations about this aspect of her evidence, as well as generally in respect of what transpired at the meeting on 14 June 2011.
- 6.30 For his part, Mr Hutchinson thought that such contacts with CEPA – to clarify what might be any likely significant change in the final CEPA report – took place on 15 June or later.<sup>498</sup>
- 6.31 CEPA representatives were asked by the Inquiry to comment in detail about their engagement with DETI officials in the context of Ms Hepper’s evidence as to what would have been known by 14 June 2011 about the likely content of their final report of 28 June 2011. In light of their evidence, it seems somewhat unlikely that Ms Hepper would have been aware of, or been justifiably confident about, changes that were likely to occur in the final report as Mr Morrow appears to have been on holiday from 6 June to 21 June 2011 and would not have been a party to exchanges with either Mr Hutchinson or Ms Hepper during that time.<sup>499</sup>
- 6.32 Furthermore, the initial queries and comments from Mr Hutchinson sent to CEPA on 7 June with regard to the balance of options were not the subject of an initial reply until 15 June 2011, the day after the meeting with Minister Foster.<sup>500</sup> Discussions about remodelling were not completed until after teleconferences on 21 June and 27 June. CEPA also had no recollection of communicating to DETI about any correction of errors in the model which led to estimated lower lifetime subsidy costs for the Challenge Fund or the revised higher lifetime subsidy costs in respect of the NI RHI scheme until the final report was issued on 28 June 2011.<sup>501</sup>
- 6.33 Returning to the meeting of 14 June 2011 itself, it seems to the Inquiry that presenting the Minister in a meeting with a report of more than 100 pages containing complex and detailed calculations, which the Minister had no opportunity to read beforehand, as a basis for expanding upon an earlier submission would seem to have been asking a lot of any Minister. If she had been presented with such an abundance of technical detail Minister Foster could simply have asked for more time to read the report and consider the oral explanations. There is no suggestion that this occurred. Ms Foster has also told the Inquiry that, had she been informed as to the limited function of the assertion that the RHI scheme delivered the most heat at the least cost in the context of the consultant’s calculations that it was the Challenge Fund that did so, she would have required the submission to be redrafted.<sup>502</sup> Again, there is no suggestion that this occurred, although the Inquiry accepts that this is plainly not in itself determinative of what was or was not explained to the Minister at the meeting. The Inquiry considers that another alternative would have been to ensure that any such clarification or changes were included in a written record, minute or note of the meeting.
- 6.34 Dr Crawford told the Inquiry that if any material changes (to the position as set out in the CEPA draft report of 31 May 2011) had been revealed at the meeting on 14 June it would have been expected that they would have been incorporated in a further submission. He also said that if the tables contained in the CEPA draft report had been presented and explained there was “no way” that the Minister would have signed off the submission.<sup>503</sup>

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497 TRA-01864

498 TRA-01997 to TRA-01999; WIT-108110

499 WIT-108106 to WIT-108112

500 CEPA-113610 to CEP-113612

501 WIT-105063 to WIT-105064

502 TRA-07775 to TRA-07776

503 TRA-07659 to TRA-07660

- 6.35 Ms Hepper accepted that, with hindsight, it would have been preferable to have more clearly highlighted the specific changes from the content of the draft report of 31 May in order to focus the attention of Minister Foster and Dr Crawford when they were later sent the final CEPA report of 28 June.<sup>504</sup> The Inquiry notes that in practical terms that might not have been of much assistance, since neither of them read that final report in any event, although relevant changes could of course have been highlighted in the body of the covering submission (dealt with below).
- 6.36 Ms Hepper told the Inquiry that she suspected that Minister Foster went through the full final report “in some detail.”<sup>505</sup> Minister Foster told the Inquiry that she did not know why Ms Hepper had said that, since she “would have been aware that I wouldn’t read all the technical reports in that fashion.”<sup>506</sup>
- 6.37 In the Inquiry’s view it seems clear that the ‘misleading’ view of the NI RHI scheme derived from the 8 June 2011 submission – that, of all of the options, it provided the most renewable heat at the least cost – continued to be held by the Minister and her SpAd after the meeting on 14 June.
- 6.38 Either at or after the meeting of 14 June, Minister Foster marked “14/6 noted” on the submission. Neither she nor her Private Office made any specific responses to the recommendations in the submission either by annotation on the submission or subsequent email. In her evidence Minister Foster was unable to recall specific details of the meeting of 14 June, but having reconsidered the CEPA draft final report of 31 May 2011 she told the Inquiry that she considered it highly unlikely that Ms Hepper took her through the details it contained, given the length of the report – some 97 pages, extending to 133 pages with annexes – and the technical nature of the calculations, in the context of a 30-45 minute meeting.<sup>507</sup>
- 6.39 Minister Foster denied that she was informed of the potential for any AME overspending to have an adverse impact upon the DEL budget either in conversations with Ms Hepper or from any other source.<sup>508</sup> Further, the former Minister also told the Inquiry that she was satisfied that if the statement (as to the RHI producing the most heat at least cost) had been properly explained to her, in the context of appropriate advice about the Challenge Fund, she would have directed the submission to be redrafted.<sup>509</sup>
- 6.40 It seems clear to the Inquiry that, whatever may or may not have been said during the meeting on 14 June, the Minister and her SpAd continued to believe that the funding was standard AME and that the expert advice was that the NI RHI scheme would produce the most heat at the least cost. That she had good ground for believing the latter would have been confirmed when she was presented with further Regulatory Impact Assessments to sign in July 2011 and on 13 April 2012, drafted by Mr Hutchinson, that contained precisely the same assertion in a review of the five options of which the NI RHI and GB RHI schemes were clearly separate options.<sup>510</sup> The statement was also repeated again without qualification in the SL1 letters that were drafted for the Minister to forward to Jim McManus, ETI Committee Clerk, on 16 March 2012<sup>511</sup> and 13 April 2012.<sup>512</sup>

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504 TRA-01871

505 TRA-01868

506 TRA-07780 to TRA-07781

507 WIT-20566 to WIT-20567

508 TRA-07784 to TRA-07786

509 TRA-07775 to TRA-07776

510 DFE-70749 to DFE-70760

511 DFE-262810 to DFE-262814

512 ETI-05984 to ETI-05988

- 6.41 Continued repetition of the assertion would have been incompatible with the conclusions of CEPA in the final report of 28 June 2011, which (the Inquiry accepts) had been published on the DETI website. If Ms Hepper realised that it was necessary to, and did effectively, explain the very limited reference of the statement to the Minister, the Inquiry finds it difficult to understand how the unvarnished assertion subsequently came to be repeated in important documents.
- 6.42 Unfortunately, the Inquiry has been unable to unearth any documentary minute or memorandum of the meeting on 14 June 2011, nor has any participant before the Inquiry been able to provide any such record. As mentioned above, the ministerial response to the submission was limited to the word “noted 14/6”, handwritten on the submission<sup>513</sup> and a simple email indicating that she was content.<sup>514</sup> Thus, there is no written record capturing the view the Minister expressed on the proposed design of an incentive scheme for Northern Ireland or for an indication of her preferred option for incentivisation by either a Challenge Fund or an RHI scheme.
- 6.43 How the Minister’s response was understood also depends, of course, on what was discussed and/or decided at the meeting of 14 June and how the Minister expressed herself at that meeting (as to which the Inquiry has no clear record). However, the Minister’s response must also be considered in the context of her having signed the related Impact Assessment (IA) on 14 June 2011. In that IA it seems clear that the Northern Ireland RHI was presented as the preferred option. For instance, on the first page, which the Minister signed, in the box which requires any preferred option to be justified, it is noted that: “The Northern Ireland RHI option is consistent to the GB position and provides long-term, stable support for those wishing to invest.”<sup>515</sup> The Minister had been asked to approve and sign the IA, which was attached to the 8 June submission as an annex, to support the necessary amendment to the 2011 Energy Bill (to allow powers to be taken to implement the NI RHI scheme).<sup>516</sup> This appears consistent with an understanding that the NI RHI option was understood as being presented as the favoured option, although the Inquiry notes Ms Hepper’s evidence that she does not recall sharing any preference for any particular option with the Minister at the meeting.<sup>517</sup>
- 6.44 For completeness, it should be noted that in a subsequent submission to the Minister of 17 June 2011, which related to briefing the ETI Committee and ministerial colleagues, there is a reference back to the meeting of 14 June 2011 and that “Following consideration, you agreed that a Northern Ireland RHI should be designed and implemented”, with an explanation that the NI RHI scheme will be similar to the GB scheme.<sup>518</sup>
- 6.45 The Inquiry has carefully considered the evidence of the various relevant witnesses in relation to the meeting which was held on 14 June 2011. Its conclusions in relation to this are set out in the findings below. The Inquiry has been seriously inhibited in a full and proper consideration of the decision-making which occurred at, or as a result of, this meeting by reason of the lack of any authoritative record of what was discussed or decided, or what further explanation or analysis was provided in relation to the contents of the 8 June submission or the version of the CEPA report which was then available. The Inquiry’s ultimate view as to what Ms Hepper is likely to have communicated, or not communicated, to the Minister in the course of this

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513 WIT-00739

514 WIT-00750

515 DFE-29535

516 See the typed annotation at the top of the submission at DFE-29542

517 TRA-01872 to TRA-01873

518 DFE-29480 to DFE-29485, at DFE-29481

meeting has been reached as a result of an assessment of each witness's credibility, having had the opportunity to see and hear each of them give oral evidence, and in light of all of the surrounding evidence which might cast light on these issues as discussed in this section of the Report and elsewhere.

6.46 The Inquiry was particularly influenced by Ms Hepper's evidence to the effect that she communicated to the Minister, on 14 June, the likely significant changes which would be forthcoming in CEPA's later final report. As already noted above, by reason of the evidence on this issue from others, particularly from CEPA itself, the Inquiry concludes that it is highly unlikely that Ms Hepper would have been in a position to share this information at her meeting with the Minister. Her adherence to her position that she would have done so, when the Inquiry considers this highly unlikely in light of other objective evidence of what was likely to have been known and communicated at that time, leads the Inquiry to consider that Ms Hepper may have a misplaced confidence in the level of detail and clarity of what she communicated to the Minister and her SpAd at the meeting of 14 June. Although Ms Hepper might well believe that she communicated clearly the qualification on the endorsement of the NI RHI option and the potential risk to the DEL budget of overspend – and the Inquiry cannot rule out for certain that these matters were discussed by reason of the lack of any clear record – in the light of the full evidence the Inquiry has considered, it has taken the view that these matters were unlikely to have been discussed, or at least unlikely to have been communicated in a sufficiently clear and effective way. What happened (or did not happen) after the meeting seems to the Inquiry to be consistent with this view.

6.47 In relation to the lack of a note or record of the meeting, when questioned by Senior Counsel to the Inquiry, Ms Hepper said her experience was that it was "not unusual" for there to be no record of an exchange or meeting with the Minister and that was "certainly my current experience."<sup>519</sup> When she was then asked about whether the application of the relevant Private Office guidance/directions (which required a record of the meeting to be prepared by those who met with the Minister) had fallen into disuse her reply was as follows:

"I think that would not be an unfair reflection of what happens. And, certainly, even in the early days, I don't recall the private office ever formally asking for a minute if something didn't turn up. But, then again, private offices are busy areas and the onus was being put on divisions and directorates to do it. But I think human nature is, when things get busier and busier, you know, some of these things do fall by the wayside."<sup>520</sup>

6.48 Mr Sterling's evidence to the Inquiry was similar with regard to taking an official note when he conceded:

"Yes, I think I've already talked about the context in which we were operating in, and indeed I have, in recent times, spoken to just all [sic] the permanent secretaries. And the sort of common view is that, over a period of time, the good practice in terms of minuting meetings with Ministers largely lapsed."<sup>521</sup>

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519 TRA-05200

520 TRA-05200

521 TRA-06121

- 6.49 Minister Foster stated that she was not aware that the practice had lapsed and found the fact that it had to be “quite shocking”.<sup>522</sup> The Inquiry simply notes that the relevant paragraphs of the DETI Private Office Guidance, paragraphs 37-39, clearly placed the obligation to record a note upon the relevant “agency, branch, division etc”.<sup>523</sup> This Private Office Guidance is dealt with in greater detail later in this Report.
- 6.50 The Inquiry also notes that on 9 June, the day after her submission to the Minister but before the meeting of 14 June 2011, Ms Hepper had issued a work request to the Department’s external legal advisers, Messrs Arthur Cox Solicitors, to draft Northern Ireland Renewable Heat Incentive Regulations which were to be “based largely, in the first instance, on the GB equivalent Regulations.”<sup>524</sup> A copy of the GB regulations was attached.<sup>525</sup> Ms Hepper told the Inquiry that this was simply “parallel processing” to ensure that, in the event that an RHI scheme was chosen, there would be draft regulations to annex to the necessary consultation document.<sup>526</sup>
- 6.51 On 21 June 2011, having elected to proceed with the NI RHI, Minister Foster wrote to her then ministerial colleagues and the then chair of the ETI Committee.<sup>527</sup> The letters were each accompanied by a detailed annex setting out the approach being taken, and the reasons for it.<sup>528</sup> The letters explained that the NI tariffs were still being finalised but they would be based upon similar lines to GB, affording a 12% rate of return for all technologies barring solar thermal which would have a 6% rate of return.<sup>529</sup>

### The ministerial submission of 5 July 2011

- 6.52 As has already been discussed, the final report from CEPA was delivered on 28 June 2011 and Minister Foster was supplied with a copy, together with a further submission, on 5 July, seeking approval for the contents of the draft NI RHI consultation documents which were also provided.<sup>530</sup> The submission was timed “Desk Immediate” with the continued incomplete reference to the financial implications and a recommendation that the final CEPA report should be published, together with the public consultation document, on the DETI website.
- 6.53 In contrast to the draft report of 31 May, the final CEPA report showed that all the options were now capable of producing the targeted 10% renewable heat by 2020. However, this would only be achieved if there was an increase in the baseline or “do nothing level”, and considerable uptake, particularly with large users, would be needed outside the RHI as well.
- 6.54 The following tables contain data extracted from the CEPA final draft report of 31 May 2011 and the final report from 28 June 2011. From the first two tables it can be seen that in the May draft final report, the Challenge Fund produced more renewable heat at a slightly lower cost.<sup>531</sup> By the time of the June final report, the Challenge Fund still produced more renewable heat but now at significantly lower cost (well below half).<sup>532</sup>

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522 TRA-08271 to TRA-08272

523 DFE-416566

524 DFE-15666 to DFE-15668

525 DFE-15624 to DFE-15655

526 TRA-01897 to TRA-01898

527 DFE-29564 to DFE-29574; DFE-29553 to DFE-29563

528 DFE-29568 to DFE-29574; DFE-29557 to DFE-29563

529 DFE-29568; DFE-29557

530 DFE-29643 to DFE-29905

531 DFE-187760 to DFE-187761

532 DFE-187931 to DFE-187932

**Table 1 – CEPA Final Draft Report & Final Report Data**

Renewable Heat Produced (% of total)	May Draft	June Final	Change
Challenge Fund	8.75	11.69	+2.94
NI RHI	7.56	11.14	+3.58
Advantage/Disadvantage of CF over NIRHI	1.19	0.55	

**Table 2 – CEPA Final Draft Report & Final Report Data**

Lifetime Cost of Heat (£/kWh)	May Draft	June Final	Reduction/Increase
Challenge Fund	0.47	0.24	-0.23
NI RHI	0.50	0.57	+0.07
Advantage/Disadvantage of CF over NIRHI	0.03	0.33	

6.55 The next two tables show how the projected lifetime costs and benefits of the schemes radically changed between May and June.<sup>533</sup> On these comparisons, the Challenge Fund (including the assumed administration costs) became roughly £200 million to £250 million more attractive than the NI RHI.

**Table 3 – CEPA Final Draft Report & Final Report Data**

Lifetime Cost of Heat (£m)	May Draft	June Final	Reduction/Increase
Challenge Fund	351	212	-139
NI RHI	257	405	+148
Advantage/Disadvantage of CF over NIRHI	-94	257	

**Table 4 – CEPA Final Draft Report & Final Report Data**

Net Present Value (£m)	May Draft	June Final	Increase/Reduction
Challenge Fund	-114	-24	-90
NI RHI	-140	-242	+102
Advantage/Disadvantage of CF over NIRHI	26	218	

6.56 This clearly demonstrates how volatile the costs and benefits were to the operation of the model and the assumptions used within it. In the course of one month the Challenge Fund total costs decreased by £139 million and those of the NI RHI scheme increased by £148 million. This meant that the difference in total lifetime costs between the two schemes changed by



£287 million and that in this regard the Challenge Fund went from being more expensive than the NI RHI scheme by £94 million to being less expensive by £193 million. Big changes could also be seen for the Net Present Value/Cost which also took into account other factors, such as the savings in carbon that would result from displacing fossil fuels from the heating sector. CEPA explained in a written statement to the Inquiry that the big changes for the Challenge Fund resulted from a modelling error when compiling the May draft report in which much higher biomass fuel prices were incorrectly used in the inputs – this was rectified for the June final report, thus reducing the lifetime subsidy costs by £150 million.<sup>534</sup>

6.57 Although the 5 July 2011 submission would appear to be the first occasion on which Minister Foster and Dr Crawford received the final CEPA report, the submission did not draw their attention to any of these very significant changes between the draft final report of 31 May and the final report of 28 June and it does not seem that the Minister was given any reason to look at it in detail. The submission did not formally record any of the specific matters said by Ms Hepper to have been discussed during the 14 June meeting.

6.58 In the section of the Executive Summary of the final CEPA report headed ‘Options considered and overall assessment’ CEPA stated: “We conclude that the Challenge Fund delivers the most renewable heat, at the lowest cost, and delivers 10% under both long-term funding scenarios.”<sup>535</sup>

6.59 CEPA looked in detail at efficiency, the level of renewable heat, the overall monetisable benefit/cost of the options and concluded at section 12.2:

“The findings from the cost-benefit analysis are pretty stark in terms of net cost differences between the schemes...Given that the amount of grant is sufficient to meet the desired target, the best value for money seems to be in the grant approaches, especially the Challenge Fund.”<sup>536</sup>

6.60 The report then went on to identify other factors that might lead to a preference for an NI RHI scheme, such as administrative simplicity in being able to ‘piggy-back’ on the GB RHI scheme at a lower cost and the ability to learn from the GB experience by alignment with the GB RHI scheme rather than adopting a ‘go it alone’ policy.<sup>537</sup> The final report also drew attention to the importance of the level at which any subsidy was set, the significant uncertainty represented by the relative prices of biomass, oil and gas and, in that context, the importance of regular monitoring and review. These were factors to which a Challenge Fund would be much less exposed than a scheme with pre-set incentives, such as the non-domestic NI RHI scheme. In the case of the former, the subsidy levels would be re-set each time there was a call for bids and would be determined competitively amongst those installing the technology under current and realistic market conditions, rather than being set in advance by administrators who would effectively have to predict and/or second guess the costs and benefits as well as how such factors might be subject to change over time.<sup>538</sup>

6.61 When asked by the Inquiry, Ms Hepper said that she had not thought it necessary to raise anything from the final report with Minister Foster.<sup>539</sup> She considered that she had appraised the Minister of the extent to which the Challenge Fund was better value for money at the 14

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534 WIT-108115 to WIT-108116

535 DFE-187930

536 DFE-188025

537 DFE-188025

538 DFE-188007 to DFE-188008

539 TRA-01901

June meeting, but that there was the other side of the equation to be considered including wider energy issues, such as the gas industry.<sup>540</sup> She did not think that she should have gone back to the Minister with regard to the increased lifetime costs contained in the final report and she took comfort from the fact that neither Minister Foster nor Dr Crawford raised any further questions with herself or Peter Hutchinson after receiving the 28 June final report.<sup>541</sup>

## The July 2011 consultation

6.62 On 20 July 2011 DETI published a public consultation document entitled ‘The Development of the Northern Ireland Renewable Heat Incentive.’<sup>542</sup> In the executive summary to the consultation document Minister Foster referred to the tariffs being “grandfathered” and “guaranteed” for 20 years but did not repeat the link to the 12% rate of return.<sup>543</sup> However, paragraph 3.36 of the consultation document explained that:

“The tariffs have been designed to bridge the gap between existing heating systems and the renewable heat alternative, with consideration given to the capital cost, operating costs and the non-financial ‘hassle’ factors that are involved in replacing existing heating systems with renewable heating technologies.”<sup>544</sup>

In addition, paragraph 3.37 stated that, apart from solar thermal, the tariffs had been designed to provide a rate of return of 12% over the lifetime of the technology.<sup>545</sup>

6.63 The Inquiry notes the confusion that ensued around the concept of ‘grandfathering’. The intention of providing a particular rate of return to investors can be achieved by protecting tariff payments for the duration of the scheme if the predominant costs are from the up-front capital investment, as with solar thermal. However, when the running costs dominate and are variable, as with biomass, the target rate of return can only be achieved by varying the payments as necessary – both upwards and downwards. Ms Foster made clear in her oral evidence that her references to ‘grandfathering’ related to the rate of return, not to a fixed payment level.<sup>546</sup>

6.64 The CEPA final report of 28 June 2011 was published on the Department’s website together with the public consultation document.<sup>547</sup> Included in the supporting documentation for the consultation was a draft RIA and draft regulations.<sup>548</sup> The draft RIA prepared by Mr Hutchinson dealt with the draft regulations, which were obviously intended to implement an RHI scheme. The RIA referred to other options noted in the CEPA report but it was made clear that DETI was now consulting on an RHI scheme specific to Northern Ireland.<sup>549</sup> The proposed NI RHI scheme was described at Option 5 as offering “the highest potential renewable heat output at the best value”, a statement which was clearly incompatible with the conclusions reached by CEPA in the final June report.<sup>550</sup> While the documents noted that administration costs had been estimated at approximately 10% of the overall costs, the gross cost figures respectively for the Challenge Fund and the RHI were not provided by way of comparison in the RIA.<sup>551</sup> In effect, the public were not invited to express views on the alternative benefits offered by the Challenge Fund.

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540 TRA-01911 to TRA-01914

541 TRA-01913 to TRA-01914

542 DFE-63726 to DFE-63837

543 DFE-63733

544 DFE-63750

545 DFE-63750

546 TRA-08506 to TRA-08507

547 DFE-187925 to DFE-188067; DFE-04002 to DFE-04111

548 DFE-04049 to DFE-04098

549 DFE-04096

550 DFE-04091

551 DFE-04095

## Findings

- 39.** The Inquiry is conscious that the multitude of matters for which Minister Foster was responsible may have had a greater impact on her ability to recall the detail of a specific meeting by contrast with Ms Hepper who, being responsible for energy matters, may have had a clearer recall of detail. However, having reflected upon the evidence, the Inquiry has concluded that while Ms Hepper may believe that she did so, it is unlikely that she told the Minister that the statement “the NI RHI Scheme produced the most heat at the best value” was restricted to a comparison with the GB non-domestic RHI scheme or, at any rate, that she did so in a sufficiently clear and effective manner. Equally, it is unlikely that the potential risk to the DEL block grant set out in the earlier official-level email exchange of April 2011 (into which Ms Hepper was copied) was adequately and effectively explained by Ms Hepper to the Minister. These were points of very considerable importance. Not ensuring that the Minister clearly understood about the restricted comparison provided continuing misleading confidence about the value for money of the NI RHI scheme. Not ensuring that the Minister clearly understood the risk to the DEL block is likely to have significantly reduced the appreciation of the necessity for budget control mechanisms.
- 40.** The Inquiry also believes that the Minister and/or her SpAd should have requested and retained a copy of the draft CEPA report, whether it was properly presented at the 14 June 2011 meeting or not. Both that document and the final June report from CEPA, having been properly read and analysed by the Energy Division officials, should have been presented in an effectively summarised form in a submission to the Minister. Even though they were not presented in such a form, the Inquiry finds that Dr Crawford, the Minister’s SpAd, should at least have sought such summaries and, if necessary, read the original documents.
- 41.** In the further submission to the Minister on 5 July 2011, following receipt of the CEPA final report of 28 June 2011, Ms Hepper, Ms McCutcheon and Mr Hutchinson failed to highlight to the Minister the very significant changes that had been made to the report since the draft of 31 May.
- 42.** The Inquiry considers that, following the July 2011 submission, the fundamental difference of view (which has emerged during the course of the Inquiry) between Minister Foster and Dr Crawford with regard to consideration of expert reports and, in particular, whose responsibility it was to read and analyse technical reports attached to submissions (a matter which is dealt with later in this Report), is likely to have contributed to the failure effectively to comprehend the full implications of the CEPA reports.
- 43.** Ms Hepper also denied that energy officials had sought from CEPA a recommendation for an RHI scheme but, as with Mr Hutchinson, she was unable to point to any clear documentary rejection, or recall any specific oral rejection, of the CEPA assertion that DETI had preferred an RHI scheme. In all of the circumstances the Inquiry is satisfied that an RHI scheme was preferred by energy officials by this stage.

44. Indeed, taking into account all of the relevant evidence, the Inquiry is persuaded that, between 2009 and 2011, a clear preference emerged amongst DETI energy officials and, based upon the advice from officials, was adopted by the DETI Minister for an NI RHI scheme; a preference that by 2011 had strengthened to the point that the alternative of an overall more cost effective capital grant scheme, the Challenge Fund, was no longer seriously considered in the decision making process. Three key factors lay behind that preference: the fact that GB had opted for an RHI scheme; the belief that some cost discount could be obtained by engaging Ofgem administration services; and the need to ensure that the offered funding was spent in Northern Ireland and not returned to HMT.
45. The Inquiry found the explanation offered by Ms Hepper and Mr Hutchinson for the inclusion of the assertion in the 8 June submission – that the NI RHI scheme produced the most heat at the best value – very difficult to reconcile with the evidence. Ms Hepper and Mr Hutchinson both agreed that it was intended that the assertion was qualified in the sense that it was restricted to a comparison between the GB RHI scheme and an NI RHI scheme. If so, the Inquiry found that the failure clearly to articulate such a restriction or qualification in a submission intended to provide a helpful summary of technically complex options was a serious omission that was likely to mislead any reader. That omission was subsequently compounded by repetition of the unqualified assertion in a number of further important documents, including RIAs and SL1 letters drafted or approved by Ms Hepper and Mr Hutchinson. If that qualification or restriction had been adequately explained to Minister Foster and Dr Crawford during the meeting of 14 June there may have been an amendment of the submission but, in any event, there would more than likely have been some clarification in the subsequent documents.

## Chapter 7 – DETI’s initial engagement with Ofgem about RHI

### Ofgem’s administration of the GB RHI scheme

- 7.1 The GB RHI scheme was administered by the Gas and Electricity Markets Authority (GEMA), through its executive arm, a non-ministerial government department known as the Office of Gas and Electricity Markets (Ofgem). GEMA is the independent regulator of the gas and electricity markets in GB.<sup>552</sup> For convenience, the Inquiry proposes generally to refer to ‘Ofgem’ unless the specific context requires reference to GEMA.
- 7.2 For its funding, Ofgem recovers costs through an annualised fee from the licensed companies which it regulates. In addition to its regulatory activities, Ofgem, acting through its dedicated division known as E-Serve, had developed experience of administering a range of energy schemes in addition to the GB RHI scheme, including the Feed-in-Tariff, and Renewables Obligation, which it also administered for Northern Ireland.
- 7.3 The provisions of the Energy Act 2008 which conferred enabling powers for the GB RHI scheme provided a power to the DECC Secretary of State to make regulations, including for the administration of the scheme. The enabling power envisaged the involvement of Ofgem in the administration. The February 2010 DECC GB RHI consultation document<sup>553</sup> set out DECC’s belief that Ofgem was the best placed body to administer the GB RHI, which would include it making payments, but also dealing with audit, compliance and enforcement. In its 26 April 2010 response to the consultation the Renewables Advisory Board (RAB) expressed a number of concerns about Ofgem acting as the scheme administrator, as compared to commercial service providers.<sup>554</sup> These concerns included what RAB said was its belief that while:

“Ofgem would be well placed to act as a regulator of compliance for the scheme, and that this is entirely appropriate and in keeping with Ofgem’s more general role; for it to act as the administrator as well presents a clear conflict of interest as it would be determining complaints about its own performance.”<sup>555</sup>

Nonetheless, the subsequent 2011 GB RHI regulations conferred the administrative functions on GEMA as the ‘Authority’ to fully administer the scheme.<sup>556</sup>

### The Ofgem Feasibility Study

- 7.4 In response to the consultation on the NI RHI, in the summer of 2011, concern was also expressed that the NI RHI scheme should be managed locally<sup>557</sup> and, accordingly, it was initially proposed that the Energy Act 2011 (in which enabling powers for the NI RHI were to be provided) should appoint DETI or NIAUR as the legal administrator of the scheme, with power to transfer functions to Ofgem. That was consistent with the practice adopted in relation to NIRO and NI Renewable Energy Guarantees of Origin (REGO).

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552 [www.ofgem.gov.uk](http://www.ofgem.gov.uk)

553 INQ-20375 to INQ-20461 at INQ-20444

554 INQ-16086 to INQ-16094

555 INQ-16092

556 LEG-00316 to LEG-00318

557 DFE-382415 to DFE-382449

- 7.5 Ofgem had initially been contacted by Mr Hutchinson with regard to its potential administration of the NI RHI scheme in June 2011.<sup>558</sup> A formal request for Ofgem to submit an outline proposal was then made by Ms Hepper on 11 July, when she wrote to Ofgem stating:
- “Ofgem’s experience in developing and implementing the RHI in Great Britain will be invaluable in the administration of the Northern Ireland scheme given the many similarities in the two incentive measures.”<sup>559</sup>
- 7.6 On 10 August 2011 Ms Hepper addressed a submission first to the DETI Permanent Secretary, as Departmental Accounting Officer, for onward passage to Minister Foster and Dr Crawford, seeking approval for the appointment of Ofgem to carry out a feasibility study, at a cost in the region of £100,000, into the administration arrangements for an NI RHI scheme.<sup>560</sup> Ms Hepper advised that an appropriate delivery agent was required but that the capability needed to deliver the scheme in terms of technical expertise, people and IT systems was not available in DETI.<sup>561</sup> She further advised that such a feasibility study was an essential piece of work for the future implementation of the NI RHI scheme and provided a draft business case.<sup>562</sup> The submission also pointed out that Ofgem had a proven track record for delivery of large-scale energy projects and that it had accumulated extensive expertise in GB that could be utilised in Northern Ireland, bringing a significant saving to DETI.<sup>563</sup> Minister Foster accepted the submission’s recommendation on 11 August.<sup>564</sup>
- 7.7 The Feasibility Study started in September and on 16 December 2011 Ofgem presented DETI with a report setting out its proposed resourcing requirements in order to complete the development of the NI RHI scheme in partnership with DETI and undertake the administration of the scheme.<sup>565</sup>
- 7.8 Catherine McArthur of Ofgem, the author of the study, explained to the Inquiry that she worked with colleagues across Ofgem to produce her report. The report outlined Ofgem’s proposals to develop and implement the NI RHI scheme noting that the purpose of the study was to:
- “...provide DETI and Ofgem senior management with a detailed understanding of the delivery and ongoing administrative implications of the scheme for Ofgem. This includes an analysis of costs, delivery options, risks and enforcement requirements.”<sup>566</sup>
- 7.9 Significantly, the Feasibility Study specifically listed some 14 assumptions upon which the study was based. The assumptions, Ms McArthur explained, were about setting conditions, so that in the event that circumstances changed, the cost to DETI for Ofgem’s administration would also change.<sup>567</sup> Ms McArthur told the Inquiry that when she started in September 2011, DETI’s consultation on the NI scheme, and therefore its policy work, was still ongoing. Given the uncertainties about the final scheme which would ultimately be adopted, she was asked by

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558 DFE-313725 to DFE-313727  
559 DFE-313730 to DFE-313731  
560 DFE-143773 to DFE-143797  
561 DFE-143776  
562 DFE-143777  
563 DFE-143776  
564 DFE-30436  
565 DFE-79758 to DFE-79921  
566 DFE-79761  
567 TRA-03658

DETI in October 2011 to take the GB RHI regulations as the basis for the study:

“So, when I commenced work on the feasibility study in September 2011, DETI was still consulting on the scheme. We were expecting to have more certainty around what the final policy would be when we received the draft regulations to review, but, when we received them, they were the GB regs basically with the names changed...”<sup>568</sup>

- 7.10 When Ms McArthur and Mr Harnack, then Associate Director of Ofgem E-Serve’s New Scheme Development,<sup>569</sup> met Ms Hepper, Ms McCutcheon and Mr Hutchinson in Belfast on 2 November 2011, DETI is noted to have outlined some “local political issues” that may impact upon their final policy position, in particular “an imperative to differentiate the Northern Ireland scheme from Great Britain’s”. It appears that that had been the rationale behind the desire to introduce air source heat pumps (ASHPs) and bioliquids from scheme commencement.<sup>570</sup>

### The promised Northern Ireland specific independent risk assessment

- 7.11 Section 2.14 of the Feasibility Study was headed ‘Fraud Risk’ and confirmed that Ofgem had undertaken the study on the assumption that the level of fraud risk was the same in Northern Ireland as in GB. That risk was to be reassessed during the development stage following an independent risk assessment to identify key areas of risk including any local factors that might require a different approach to that taken in GB.<sup>571</sup>
- 7.12 Section 5.17 of the Feasibility Study agreed that Ofgem’s independent risk assessment would “inform the development of a Fraud Prevention Strategy to address the risks specific to Northern Ireland.”<sup>572</sup>
- 7.13 The Feasibility Study was updated on 1 November 2012<sup>573</sup> at the time of the scheme launch. In the updated version, at section 1.8,<sup>574</sup> it was again stated that the assumption that the level of fraud risk for the NI RHI was the same as the GB RHI would be re-assessed during the development phase following an independent risk assessment to identify key areas of risk to the NI RHI scheme, including any local factors that may require a different approach to the GB RHI. Further, at section 10.3 of the guidance published by Ofgem and DETI in November 2012 Ofgem indicated that it would develop a detailed fraud prevention strategy for the NI RHI.<sup>575</sup>
- 7.14 In the event such an independent risk assessment was not carried out and an NI RHI specific fraud prevention strategy, which took into account the differences between the GB and NI RHI Schemes, was never produced. In fact, as is discussed later in this Report, when Northern Ireland was added to a GB RHI Fraud Prevention Strategy in 2014 it erroneously said that the NI RHI scheme had the protection of tiering when it did not.
- 7.15 Dermot Nolan, Ofgem’s Chief Executive, accepted in his oral evidence to the Inquiry that an independent risk assessment of the NI RHI should have been done and that Ofgem did “get it

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568 TRA-03655

569 WIT-103823 (E-Serve’s New Scheme Development department was then the department within Ofgem responsible for developing and operating the administration of new sustainability schemes such as RHI).

570 OFG-17383 to OFG-17389 at OFG-17384

571 DFE-79778

572 DFE-79795

573 OFG-81441; OFG-81452 to OFG-81477

574 OFG-81459

575 INQ-30157

wrong” in this regard. Had such an assessment taken place, he speculated that it would have covered lack of cost controls and issues about tiering.<sup>576</sup> Mr Nolan accepted that this was “certainly a key failing.”<sup>577</sup>

- 7.16 In general, however, the Feasibility Study indicated that Ofgem could, and was in principle willing to, administer the NI RHI scheme on behalf of DETI, on the basis set out in the study. It was an important piece of work which further informed scheme development and planning within DETI and set out how Ofgem proposed to administer the scheme.

### The appointment of Ofgem as administrator

- 7.17 To develop the systems for the NI RHI, Ofgem had proposed a budget of £386,000, with a contingency of 100% to cover uncertainty arising around final scheme policy, legal and IT work.<sup>578</sup>
- 7.18 On 18 April 2012 – after the Minister had cleared the submission of 16 March 2012 giving approval to proceed with the NI RHI scheme (discussed elsewhere) – Ms Hepper submitted a business case to Minister Foster for the appointment of Ofgem to administer the NI RHI scheme and to act as an external delivery organisation on behalf of DETI.<sup>579</sup> The April 2012 submission referred to several advantages of using Ofgem for this role, including economies of scale, consistency of approach with GB, Ofgem’s sound track record and the adaptation of an existing system which would be quicker and carry less risk. It was proposed that Ofgem would be engaged via an Agency Services Agreement. The Minister recorded her approval on 24 April 2012.<sup>580</sup> However, as appears later in this Report, the relationship between DETI and Ofgem was to prove far from straightforward and became subject to non legally binding ‘Arrangements’ rather than a contractual Agency Services Agreement.
- 7.19 There were ongoing differences of opinion in relation to the costs to be paid to Ofgem during the development phase. In August 2012 an internal Ofgem email recorded DETI as “quite frankly furious” to be told of a significant increase in costs. Minuted meetings between Ofgem and DETI representatives, which had apparently recorded assurances by Ofgem that the costs would not exceed £386,000, were attributed by Ofgem to “misunderstanding” on the part of their staff. Ofgem had calculated development costs to have risen to around £700,000, including a contingency sum.<sup>581</sup> These were later revised down to £430,000, which was accepted by DETI.
- 7.20 The Inquiry notes that in an effort to reduce costs, once again, the independent risk assessment that had not been carried out during the Feasibility Study was abandoned and replaced by a proposed joint GB-NI exercise. This, it was said, yielded a saving of £5,000.<sup>582</sup> Notwithstanding this, no evidence was presented to the Inquiry that even this joint risk assessment was ever carried out.
- 7.21 Paragraph 4.30 of the December 2011 Feasibility Study had recorded that Ofgem’s approach to NI:

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576 TRA-16355

577 TRA-16357

578 Feasibility Study at DFE-79782 para 3.11 and DFE-79842 para 11.19

579 DFE-143898 to DFE-143920

580 DFE-143925 to DFE-143930

581 OFG-04738 to OFG-04739

582 OFG-04911 to OFG-04912



“...will benefit from the development work of GB RHI and provide a system that will ensure security of information, minimise fraud risks and human error and provide administrative efficiencies while providing the most cost-effective solution to meet the specific needs of the NI RHI.”<sup>583</sup>

7.22 In a January 2012 email exchange between E-Serve’s then managing director, Stuart Cook, and one of his senior managers, Bob Hull, Mr Hull went further and pointed out that:

“... a key value add ... is the benefit we provide in terms of fraud, error and ***gaming prevention and detection*** (the Inquiry’s emphasis). This is far greater value than any efficiency savings of us operating the scheme.”<sup>584</sup>

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583 DFE-79790  
584 OFG-03036

## Findings

46. **There was an early preference for Ofgem to be the NI RHI scheme administrator. The alternative of local administration was never seriously considered, even though in the responses to the public consultation some concerns were expressed about using a body based in GB, rather than in Northern Ireland, to carry out the work.**
47. **Ofgem failed to undertake the promised independent risk assessment which it had indicated on a number of occasions would be carried out; and did not establish a separate scheme risk register for Northern Ireland.**
48. **As discussed elsewhere, Ofgem failed to develop and implement the intended Fraud Prevention Strategy that addressed the risks specific to the NI RHI. Given that the GB and NI RHI schemes were not in fact the same, this failure by Ofgem left the NI RHI scheme potentially exposed to greater risk of abuse. Ofgem also failed to tell DETI that it had not carried out the intended independent risk assessment nor produced the intended fraud prevention strategy that addressed the risks specific to the NI RHI.**

## The November 2011 Ofgem legal review

- 7.23 On 11 October 2011, during the course of the Feasibility Study that it had commissioned by direct award contract in August, DETI sent Ofgem a draft of the proposed regulations grounding the NI RHI scheme.<sup>585</sup>
- 7.24 On 7 November 2011 the Ofgem legal team sent DETI a legal review of the draft NI regulations. The review consisted of 28 pages of detailed analysis, and Ofgem, in evidence to the Inquiry, placed considerable reliance on the document as evidencing the types of warnings Ofgem was giving to DETI prior to the NI RHI scheme commencing.
- 7.25 The review drew DETI’s attention to a number of issues which Ofgem had raised with DECC in relation to the GB RHI regulations but which, in Ofgem’s view, had not been addressed adequately or at all by DECC. Appendix 1 to the Ofgem legal review document contained a lengthy table of deficiencies that Ofgem raised in relation to the GB RHI regulations, replicated in the then draft Northern Ireland RHI regulations, and the appendix 2 comments were specific to NI matters.<sup>586</sup> The former included some matters of particular significance under the heading “Potential perverse outcomes”, such as: “Some participants may install additional pipework and multiple smaller (and potentially less efficient) units in order to meet eligibility for higher tariff thresholds.” A suggested solution to such a potential outcome was to consider imposing a requirement that where separate heating systems serve the same end-heat-use purpose, they should be considered to be part of the same heating system.<sup>587</sup> The document also included a reference to “gaming opportunities” with regard to the minimal restrictions imposed as to what should count as “eligible heat use”.<sup>588</sup> Ofgem advised that it had concerns about other definitions, including “process” and “heating systems”.<sup>589</sup> Under the general heading “Legal”, in the specific context of the proposed regulation 14, there was a reference to the absence of a clear definition of “heating system” from the draft NI regulations. Such a definition was seen (rightly, as it turned out) as the “key determinant” of whether multiple plants should be treated as a single installation and Ofgem warned that “DETI should add a defined term to ensure clarity. It is not acceptable for this to be clarified in the guidance.”<sup>590</sup>
- 7.26 Ofgem was seeking guidance from DETI as to whether it preferred to delay any changes to the draft NI regulations until DECC reviewed the GB regulations regarding these shared concerns or whether DETI wished to be proactive and address the issues raised, thereby establishing a more robust scheme from commencement.<sup>591</sup>
- 7.27 In her oral evidence to the Inquiry Ms Hepper stated that these suggestions had been noted at the time but explained that their approach, as a matter of policy, was to follow DECC. In this instance, that appeared to be by way of introducing a scheme in Northern Ireland which reflected the frailties in the GB RHI regulations that had been identified by Ofgem and, if DECC took action in relation to those at a later stage, following suit at that point. In this regard, Ms Hepper noted that: “We didn’t have that in terms of the number... [of staff].”<sup>592</sup> She told

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585 DFE-314352 to DFE-314407

586 DFE-314501 to DFE-314521; DFE-314522 to DFE-314526

587 DFE-314505 to DFE-314506

588 DFE-314506

589 DFE-314503

590 DFE-314514

591 DFE-314497 to DFE-314498

592 TRA-02660

the Inquiry that both Mr Harnack and Mr Hull of Ofgem knew that Northern Ireland would be “following the DECC track” in due course.<sup>593</sup>

7.28 Ms Hepper agreed that the issue of exploitation of the scheme by the use of multiple boilers had later become a major problem but observed that “at that stage DECC did not make that change, as you can see from the document, and we did have a discussion around that and it was highlighted in the guidance.”<sup>594</sup> When she was reminded that Ofgem had expressed the clear view that it was not acceptable for it to be clarified in the guidance alone, Ms Hepper simply pointed out that it was in the DECC guidance.<sup>595</sup>

7.29 Mr Sterling told the Inquiry that the decision on the one hand to delay making the changes to the draft regulations recommended in the Ofgem legal review or, on the other, to adopt a proactive approach was the type of judgment that senior civil servants should make. The decision as to which approach to adopt in this instance was not discussed with him but should, as a minimum, have been escalated to Mr Thomson.<sup>596</sup> For his part, Mr Thomson told the Inquiry that he could not recall the detail of the Ofgem legal review ever being so escalated.<sup>597</sup>

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593 TRA-02649

594 TRA-02651

595 TRA-02651

596 TRA-06703 to TRA-06704

597 TRA-05722 to TRA-05723

## Findings

- 49.** In November 2011 Ofgem provided DETI with a detailed legal review of the then draft NI RHI regulations. The NI RHI regulations would not come into force until November 2012. The legal review identified a range of potential weaknesses in the draft regulations, many of which were in keeping with potential weaknesses already present in the GB regulations which came into force in November 2011.
- 50.** Ofgem and DETI were therefore aware from the start of risks associated with certain unclear formulations in the regulations. However, as discussed later in this Report, Ofgem did not follow up with DETI, as it ought to have done, on the issues Ofgem had identified in November 2011.
- 51.** DETI itself, which received the November 2011 warnings from Ofgem, took little or no action to address the concerns. Ms Hepper agreed that there had been a series of discussions with Ofgem and that there was no written record of the significant decision, and the reasoning upon which it was based, as to what to do about the issues raised in the Ofgem legal review. The approach which DETI adopted was not to be proactive with regard to the warnings referred to by Ofgem in the legal review, including the issues of 'gaming' and 'useful heat', but simply to postpone consideration and wait to see what DECC would do.



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## Chapter 8 – State Aid

- 8.1 The introduction of an RHI scheme to Northern Ireland, as it had in GB, raised questions of compliance with European State Aid rules. Article 107 of the Treaty on the Functioning of the European Union (TFEU) provides that any aid granted by a member state or through state resources which distorts or threatens to distort competition by favouring certain undertakings is incompatible with the internal market. Article 107(3) provides for certain exceptions, including aid to facilitate certain economic activities where such aid does not adversely affect trading conditions to an extent contrary to the common interest.<sup>598</sup>
- 8.2 EU Guidelines on State Aid for Environmental Protection issued in 2008 dealt with aid for renewable energy sources at 3.1.6. The relevant forms of aid were divided into Investment Aid at 3.1.6.1 and Operating Aid at 3.1.6.2.<sup>599</sup>
- 8.3 Stephen Moore was a deputy principal employed in the State Aid Unit of DETI, whose task it was to provide advice and assistance with regard to the potential application of EU State Aid rules.
- 8.4 Mr Moore told the Inquiry that most State Aid in Northern Ireland is Investment Aid, with some Operating Aid mostly applied in the energy sector.<sup>600</sup> Aid authorised in accordance with the Guidelines may not be combined with other State Aid or other forms of Community financing if such overlapping results in aid intensity higher than that laid down in the Guidelines.<sup>601</sup>
- 8.5 Mr Moore, who is not a lawyer, emphasised in oral evidence to the Inquiry that his role was to advise on the relevant rules and procedures rather than to provide legal advice. He would refer any legal issue to the Departmental Solicitor's Office, the Government solicitors in Northern Ireland. It was the task of the relevant branch or division within DETI to prepare the draft application for State Aid approval in compliance with the rules and he would then read the draft, adopting the approach of the Commission as he understood it, to ensure correct procedures had been correctly followed in accordance with the Guidelines.<sup>602</sup>
- 8.6 When he became aware of the economic appraisal work being undertaken by CEPA, in relation to a proposed means of incentivisation of renewable heat, instituted by DETI, Mr Moore emailed Mr Hutchinson on 17 February 2011 to remind him of the need to comply with the relevant State Aid rules.<sup>603</sup> He heard nothing more until the summer of 2011, when he became aware of DETI's consultation on the RHI. At that point he took the initiative to track down DECC's State Aid application for the GB RHI scheme and, on the back of this, he spoke to and emailed Mr Hutchinson on 4 August 2011 listing all the things Energy Division needed to do to comply with the rules.<sup>604</sup>
- 8.7 There was then a discussion in which Mr Moore pointed out that the GB RHI scheme had required notification to the Commission in accordance with Article 108(3) TFEU and that,

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598 LEG-15001 to LEG-15002

599 WIT-24661 to WIT-24662

600 TRA-03992

601 WIT-24662

602 TRA-03978 to TRA-03982

603 WIT-24602

604 WIT-24603

therefore, the NI RHI scheme should follow the same course.<sup>605</sup> The EU Commission must be given sufficient time to consider an application and Mr Moore was not optimistic about obtaining State Aid approval by the date then planned for the NI RHI scheme to go live, namely 1 April 2012, since he was aware that there was generally a queue of cases, and applications for Commission approval could take six to twelve months. He told the Inquiry that he repeatedly pressed Renewable Heat Branch for progress with the process of notifying the Commission.<sup>606</sup>

8.8 Mr Moore told the Inquiry that, at all relevant times, he believed he was dealing with an application for an NI RHI scheme similar to GB and he was never made aware of the Challenge Fund as a possible alternative means of incentivisation.<sup>607</sup>

8.9 The GB RHI scheme received approval from the Commission on 28 September 2011. Regarding a topic that would later emerge as very significant, it is interesting to note that the Commission document recording the decision to grant approval for the GB RHI scheme, after referring to how tiering would operate at paragraph 22, stated at paragraph 53 as follows:

“The Commission welcomes the two-tier approach for small and medium biomass installations which indeed are likely to reduce the perverse incentives to increase heat production beyond reasonable use in order to claim the RHI tariffs.”<sup>608</sup>

8.10 Mr Moore’s evidence was that he had been aware of the employment of tiered tariffs as a means of combating the perverse incentive to maximise returns and he took this to be at least a partial answer to that risk.<sup>609</sup>

8.11 Further time passed and Mr Moore again expressed his concern about delay by email, observing in November 2011 that a decision before 1 April 2012 looked “very unlikely.”<sup>610</sup> On 19 December 2011 Mr Moore received a draft application for State Aid approval from Mr Hutchinson. The draft did not include final figures for tariffs. Mr Moore was due to be out of the office over Christmas and indicated therefore that it was unlikely that the application would be made before January.<sup>611</sup> On the same day he received an email from Ms Hepper in the following terms:

“I want this submitted before Christmas – so, if you can’t look at it now, we will proceed and pick up any points you may have if we have to add further information re the tariffs. Peter and Joanne – please proceed.”<sup>612</sup>

8.12 In the event, the DETI notification was lodged on 20 December 2011 by Mr Moore with the then Westminster Department for Business, Innovation and Skills (BIS), through which all UK and devolved administration applications for State Aid had to be channelled and, after some helpful email exchanges, it was decided to proceed by way of a two-stage process, starting with pre-notification which was submitted by BIS on 21 December.<sup>613</sup>

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605 TRA-04004 to TRA-04006

606 TRA-04006 to TRA-04007

607 TRA-03992 to TRA-03993

608 DFE-76682 to DFE-76683

609 TRA-04019 to TRA-04020

610 TRA-04023

611 TRA-04026

612 TRA-04027

613 TRA-04029



- 8.13 The annexes to the application included the CEPA Final Report from June 2011, which did not provide for tiering of tariffs in Northern Ireland, and draft NI RHI regulations, dated 4 October 2011, which did so provide at draft regulation 39(9).<sup>614</sup> The accompanying information sheet, completed by Mr Moore probably with the assistance of Mr Hutchinson, stated that: “The tariffs have been established ex-ante and there will be regular reviews. The first review is scheduled for 2014 with any changes or revisions implemented by 2015.”<sup>615</sup>
- 8.14 On 1 February 2012 it became clear that the Commission would seek some further information including, for example, details of the final tariff figures. On 20 February 2012 Mr Hutchinson sent Mr Moore the draft addendum to the State Aid application, which was designed to provide the necessary further information, together with the CEPA addendum report of February 2012. The notification paper prepared by Mr Hutchinson showed the relevant tariff for medium biomass boilers to be 5.9p/kWh and the CEPA report showed that this proposed tariff exceeded the cost of biomass fuel. Mr Moore accepted that he did not notice this fact, stating that he would not have considered it necessary to look for it and that, in any event, he did not have time; he was working on his own at the time.<sup>616</sup> Mr Moore also told the Inquiry:

“I certainly thought that energy division would’ve understood what was required, and therefore, from my risk assessment perspective, I thought this was a low-risk notification to the Commission and it didn’t contain any significant anomalies that I should be looking for.”<sup>617</sup>

It is fair to say that the EU officials provided with the material do not appear to have identified this problem either.

- 8.15 The final form of notification was submitted on 22 February 2012.<sup>618</sup> On 25 April 2012 the EU Commission forwarded three questions, which included seeking confirmation that the development of production costs as well as the tariffs and underlying costs would be the subject of scheduled reviews and that the UK authorities (i.e. the Northern Ireland authorities in this instance) would respect the annual reporting and monitoring provisions of the Guidelines. The questions were satisfactorily answered by Mr Moore and Mr Hutchinson. Some further questions were raised with regard to differences between the GB and NI schemes which were referred to Mr Hutchinson.
- 8.16 Significantly, the question<sup>619</sup> relating to the absence of tiering of tariffs in respect of medium and small biomass installations in Northern Ireland was answered by stating: “In developing tariffs DETI also considered this issue however in all cases, the subsidy rates were found to be lower than the incremental fuel expense”, thereby replicating the error based in the CEPA February 2012 addendum.<sup>620</sup> Mr Moore read these replies but did not return to the CEPA addendum for confirmation.<sup>621</sup> He told the Inquiry:

614 TRA-04037

615 TRA-04038 to TRA-04039

616 TRA-04057 to TRA-04059

617 TRA-04058

618 TRA-04063

619 DFE-78086

620 TRA-04076

621 TRA-04077

“Whenever this all came to a head and was pointed out to me by Michael Woods in Internal Audit [in 2016], it was fairly obvious to me, and immediately I was thinking to myself, ‘Well how on earth did I miss this?’ I think time is a factor in it.”<sup>622</sup>

- 8.17 A positive decision recording approval of the NI RHI scheme was received from the Commission on 12 June 2012.<sup>623</sup> The Commission recognised that the primary objective was environmental protection with a view to increasing the uptake of renewable heat in Northern Ireland to 10% by 2020 and also to support the displacement of oil as the primary heating fuel. Paragraph 24 of the Commission decision noted that the tariffs had been set based on economic advice from external consultants.<sup>624</sup> Paragraph 43 stated that the methodology followed for setting the tariffs had been the same as that used for the GB scheme, apart from the use of uniform discount rates to value costs in future years.<sup>625</sup> Tables annexed to the approval showed the tariff for medium commercial biomass installations to be 5.9p/kWh, which was higher than the cost of the fuel which was stated to be 4.39p/kWh. That tariff was lower than the equivalent GB tariff but was not tiered.<sup>626</sup> Paragraph 34 of the approval noted that, in order not to provide perverse incentives to waste heat, each reference installation was calibrated to have a specific load factor with reference to which the tariff was calculated, providing as an example a load factor of 15% – meaning that the installation would be used at full capacity for 15% of the time. If this meant that the Commission believed that the use of an assumed load factor when calculating the tariff in some way guarded against the perverse incentive it was in error, but it does not appear that such an error was ever corrected by DETI.<sup>627</sup>
- 8.18 Paragraph 39 of the approval recorded that the UK authorities intended to carry out early reviews where they became aware of significant changes in production costs to ensure against overcompensation.<sup>628</sup> At paragraph 62 the Commission recorded the need for the tariff calculation to avoid “systematic overcompensation” and at paragraph 63 noted that a discount rate of 12% applied which coincided with the rate adopted in GB and lay at the lower end of the range 8% to 22% stated to be necessary by the detailed report from the independent consultant.<sup>629</sup> Paragraph 67 recorded that, with respect to the absence of overcompensation in time, the UK authorities had confirmed that production costs would be monitored over time through scheduled reviews.
- 8.19 At paragraph 70 the Commission made an express determination that the scheme was approved “in the light of the above mentioned considerations, **including the commitment of the UK authorities to adapt the notified measure in time in order to avoid overcompensation**” (the Inquiry’s emphasis); and at paragraph 79 confirmed the conclusion of the Commission that the scheme was compatible with the internal market.<sup>630</sup>

622 TRA-04062

623 WIT-24623 to WIT-24642

624 WIT-24630

625 WIT-24631

626 WIT-24629

627 WIT-24629

628 WIT-24630

629 WIT-24633 to WIT-24634

630 WIT-24634

## Findings

- 52. Mr Moore appears to have provided unstinting support to the officials in Energy Division, despite being repeatedly provided with very late information and then being expected to provide an immediate response.**
- 53. The State Aid approval was very clearly made reliant on the need for regular review and the obligation to avoid overcompensation. In fact, no reviews of the scheme or the tariffs were carried out by the Department until 2018. Although a tiering mechanism had been introduced in 2015, that was simply as an emergency measure rather than as a consequence of a carefully conducted and analysed review.**



## Chapter 9 – The RHI Casework Committee

9.1 Before being in a position to send a Business Case to DFP in order to seek approval to introduce the RHI scheme, DETI Energy Division officials had first to present the policy internally to a DETI Casework Committee. On Friday 9 March 2012 the draft proposals for an NI RHI were brought before such a committee.<sup>631</sup>

### The purpose of the Casework Committee

9.2 The Casework Committee was intended to enable DETI to discharge a form of independent challenge and/or reassurance role on behalf of the Permanent Secretary, as Accounting Officer, by way of peer review aimed at ensuring that the policy proposals which came before it represented value for money sufficiently clearly for the policy to be made up into a business case for submission to DFP. Membership of the committee was normally at grade 5 level or above, with a grade 3 chair, and constituted by individuals who were not involved in the project under consideration.

9.3 At the Casework Committee which dealt with the proposed RHI scheme on 9 March the element of independence was supplied by three representatives, namely: Mr Cooper, then acting Senior Finance Director, who chaired the Committee; Philip Angus, then the Director of Human Resources and Central Services at DETI; and Shane Murphy, then the senior principal economist at DETI and head of the Analytical Services Unit (ASU).

9.4 Mr Cooper was a member of the Institute of Chartered Accountants in Ireland and was acting up as grade 3 Senior Finance Director at the time. Mr Cooper had produced a note on DETI Casework Committee minutes for Heads of Division in April 2009, in which he recorded that “The system has worked well and **has ensured that a strong internal challenge function is exercised when considering significant expenditure proposals**” (the Inquiry’s emphasis).<sup>632</sup>

9.5 The RHI policy paper was presented by Ms Hepper, Ms McCutcheon and Mr Hutchinson.<sup>633</sup> Also present during the committee meeting was Mr Connolly, the economist with the ASU who was assisting Energy Division with the development of the RHI policy. He was provided with the casework papers on 28 February by Mr Hutchinson, some of which he had seen before, and, on 1 March, he signed off the RHI project, in the form of the draft casework papers which he referred to as an “appraisal”, as both complying with NIGEAE principles and being value for money.<sup>634</sup>

### The Casework Committee papers

9.6 The index to the Casework Committee papers and the subsequent committee minutes show that the committee was provided with a considerable amount of documentation including the following:<sup>635</sup>

- (i) A Synopsis of Renewable Heat Incentive Scheme Project;<sup>636</sup>

631 DFE-414011 to DFE-414023

632 WIT-18843

633 DFE-382570 to DFE-382582

634 WIT-10380 to WIT-10385

635 DFE-414011 to DFE-414027

636 DFE-398064 to DFE-398080

- (ii) The AECOM/Pöyry Report;<sup>637</sup>
- (iii) The full Economic Appraisal – CEPA final report June 2011;<sup>638</sup>
- (iv) The CEPA additional analysis (the Addendum) February 2012;<sup>639</sup>
- (v) The Ofgem Feasibility Study;<sup>640</sup>
- (vi) A Risk Register;<sup>641</sup>
- (vii) The State Aid Application/Addendum to application;<sup>642</sup>
- (viii) The Strategic Outline Case provided to DFP on 22 November 2011 together with the response granting approval on 3 January 2012;<sup>643</sup> and
- (ix) Mr Connolly’s economist comments of 1 March 2012 dealing with compliance with NIGEAE and value for money.<sup>644</sup>

No draft regulations, draft regulatory impact assessment, draft business case nor any previous submissions to the Minister were included amongst the papers,<sup>645</sup> although the existence of the draft regulations was referred to in the Ofgem Feasibility Study and the State Aid application.

9.7 The covering letter of 2 March 2012<sup>646</sup> to Mr Cooper from Mr Thomson, the then grade 3 Head of DETI Policy Group and therefore a member of the DETI Top Management Team, which was copied to the other members of the Casework Committee, included the following opinion:

“I am content that the proposals outlined have been thoroughly researched, analysed and appraised and note the supportive comments from the DETI economist, specifically that the proposed scheme is the most effective way of allocating the resources provided by HMG. From the evidence available, I consider that the implementation of the RHI in Northern Ireland represents the most appropriate way for the renewable heat market to be incentivised to a level of 10% by 2020.”<sup>647</sup>

9.8 Mr Cooper told the Inquiry that he considered the letter from Mr Thomson to be simply the provision of an assurance from the grade 3 that he stood over the submitted case, but that that did not change the nature of the role of the Casework Committee, which was not obliged to accept Mr Thomson’s view.<sup>648</sup>

9.9 Despite the bulk of the papers and documents referred to above, Mr Murphy gave evidence that he only received them some seven days prior to the committee meeting, which apparently was not unusual.<sup>649</sup>

637 DFE-398081 to DFE-398254

638 DFE-398255 to DFE-398400

639 DFE-398401 to DFE-398444

640 DFE-398445 to DFE-398612

641 DFE-398613 to DFE-398625

642 DFE-398627 to DFE-398690

643 DFE-398691 to DFE-398702

644 DFE-398703

645 TRA-04204

646 DFE-398062 to DFE-398063

647 DFE-398063

648 TRA-04208 to TRA-04210

649 TRA-02445 to TRA-02446

## The Casework Committee meeting

- 9.10 Mr Murphy told the Inquiry that there had been a ‘pre-meeting’ prior to the formal Casework Committee meeting, either shortly before the meeting or earlier that day, at which it was agreed to pursue a line of questioning as to why the Challenge Fund had not been preferred.<sup>650</sup>
- 9.11 At the Casework Committee meeting, as the senior civil servant responsible for the policy, Ms Hepper provided a brief overview of the proposed project. The policy context and the various options were discussed and actions agreed.<sup>651</sup> For the purposes of the Inquiry the following matters are of particular significance.

### The funding issue

- 9.12 Ms Hepper informed the Committee that HMT had provided DETI with funding of £25 million over the next four years for the development of the renewable heat market. However, she added that HMT had advised that this funding was only to be used for the RHI scheme itself and not the administration of the scheme. Therefore, any costs of administration would have to be found by DETI from within its DEL budget.<sup>652</sup> In particular, there was no reference to the earlier Parker, Clydesdale and Brankin email exchanges of April/May 2011 outlining the significant risks and challenges associated with the funding, which are considered in greater detail in chapter 3.
- 9.13 The absence of any reference to, or discussion of, the unusual nature of the funding is surprising since the relevant emails in relation to this had been variously copied at the time to Ms Hepper, Mr Hutchinson and Mr Cooper. When questioned about the absence of any reference to the unusual nature of the funding Ms Hepper accepted that it had not featured in the paperwork for the committee.<sup>653</sup>
- 9.14 The Casework Committee mechanism was intended to provide the initial reassurance that the scheme proposal in this case would meet the requirements for DFP approval. When asked about the absence of any reference in the minutes to potential impact upon the DEL budget Mr Cooper agreed that it was not expressly mentioned but pointed out that included under the heading “Risk Management” was the risk of insufficient budget resulting from higher than expected uptake. That risk was to be mitigated by liaison with Ofgem, and DETI had been liaising with DECC about future finance for existing commitments. He told the Inquiry that the fact that there were consequences to overspending was “...actually described in terms of, ‘You’re required to stay within your budget here. You can’t overspend here.’”<sup>654</sup> The Inquiry notes that such a phrase was not included in the final signed minutes<sup>655</sup> and that Mr Cooper had removed the word “overspend” from an earlier draft.<sup>656</sup>

### The Challenge Fund and administrative costs

- 9.15 According to the minutes of the Casework Committee meeting, Mr Murphy enquired as to why the Challenge Fund had not been taken forward as the preferred option rather than the RHI scheme. The Inquiry notes that neither the covering letter from Mr Thomson nor the synopsis

650 TRA-02494 to TRA-02496

651 DFE-04222 to DFE-04233

652 DFE-04222

653 TRA-01848 to TRA-01850

654 TRA-07236 to TRA-07238

655 DFE-382567 to DFE-382582

656 TRA-07237

presented to the committee from Energy Division had raised the Challenge Fund as a realistic alternative to an NI RHI scheme worthy of consideration.

- 9.16 Mr Hutchinson confirmed in the meeting that the CEPA final report of June 2011 had suggested that a Challenge Fund option could produce the most renewable heat at the lowest cost but that a number of very influential factors had been taken into account by Energy Division in reaching the decision to proceed with the RHI option. These included affordability of administration, the reliability of the Challenge Fund assumptions, the ability to meet targets over set timescales, risk, consistency with GB and the example of the NIRO.<sup>657</sup>
- 9.17 Mr Murphy gave evidence to the Inquiry that, during the Casework Committee discussion, he had noted down his impression that HMT funding had been restricted to an NI RHI scheme.<sup>658</sup> The Inquiry notes that such an impression was clearly not consistent with the email from Jon Parker of HMT in April 2011.<sup>659</sup>
- 9.18 As noted above, Ms Hepper had confirmed to the Casework Committee that HMT would not pay administration costs<sup>660</sup> and the Casework Committee minutes record that the presenting officials advised that “the costs of running a Challenge Fund were considered to be prohibitive.” The committee was also told that a Challenge Fund “dealing with commercial applications and involving complex evaluation metrics” could be expected to be at least as costly, if not more so, than the Reconnect Scheme (the previous DETI renewable energy grant scheme operated between 2006 and 2008 that had been for domestic customers only and operated on a first come first served basis, and discussed previously in chapter 2 of this Report). The Casework Committee was told that Reconnect demonstrated administration costs of some 14% of the total expenditure of the grant scheme, and consequently administration costs of running a Challenge Fund could equate to potentially £3.5 million over the first four years.<sup>661</sup> However, the Inquiry notes that the presenting officials do not appear to have carried out any detailed analysis of the potential administration costs of a Challenge Fund. In addition, the 28 June 2011 CEPA report had analysed the issue of administration costs and suggested that for any scheme (Challenge Fund or RHI) the administration costs would be around 10% of total spend, and that CEPA had utilised that figure in its calculations.<sup>662</sup> Further, the Inquiry’s investigation established that the presented administration costs for Reconnect were not an accurate comparator to use because the figures included substantial marketing costs.<sup>663</sup>
- 9.19 No one appears to have appreciated or to have made the case, or certainly did not document in the Casework Committee minutes, that the CEPA report had demonstrated that any additional administrative costs of a Challenge Fund, as compared to those of an NI RHI scheme, would be easily absorbed in the overall comparative lifetime costs in favour of the former. To the layman, opting for a scheme that was hundreds of millions of pounds more costly overall in order to save a couple of million pounds in administration costs might appear to be an enormous false economy.

657 TRA-03391 to TRA-03393

658 TRA-02413 to TRA-02414

659 DFE-62062 to DFE-62063

660 DFE-04222

661 DFE-04225

662 DFE-398335 to DFE-398336; DFE-398351

663 WIT-24135 to WIT-24139



- 9.20 As already noted (in chapter 3) the funding that was already available for the RHI scheme could not be used for the administration costs. The Inquiry notes that, in 2012, there were tremendous austerity pressures on spending, which would have made even small increases in administration budgets difficult. Nevertheless, DETI officials did not even appear to explore the trade-offs and how these could be managed to realise the potential savings offered by the Challenge Fund.
- 9.21 Ms Hepper sent a letter to the Top Management Team on 15 March 2012 bidding for the administration costs of RHI,<sup>664</sup> which was effective in obtaining approval of the budget she requested. No similar letter seems to have been considered with regard to obtaining a budget for the administration of a potential Challenge Fund. When such a possibility was raised with Mr Connolly by the Inquiry’s Counsel, he accepted that a similar letter could have been written using the argument that preferring the RHI scheme to a Challenge Fund represented a substantial false economy.<sup>665</sup>
- 9.22 In the course of his evidence to the Inquiry Mr Murphy described the fact that administration costs for an RHI scheme were not to be covered by HMT as being for him, a “stop/go” factor, so that once it was established that such costs were not to be covered, he saw little purpose or weight to be given to other reasons for preferring an RHI scheme.<sup>666</sup> For Mr Murphy the other reasons were only “balance of advantage and convenience factors.”<sup>667</sup> However, in the same context, Mr Murphy accepted that he had not noted down or raised with the committee the obvious substantial overall saving represented by the Challenge Fund.<sup>668</sup> He said in evidence that he recognised “in my head”<sup>669</sup> that the overall cost of the RHI scheme was at least £200 million more expensive. As a result, the rejection of the Challenge Fund on the basis of higher administration costs would have represented a false economy.
- 9.23 The Inquiry also notes that, by the time the RHI scheme actually went live in December 2012, the estimates for the RHI administration costs had increased by around 16%<sup>670</sup> and as a result Ms Hepper and Mr Cooper were involved in a significant dispute which had to be escalated to the Permanent Secretary for resolution. Mr Cooper made the case that this increase was a material change to a major factor discussed at the Casework Committee and might now require further consideration by the committee and Ms Hepper disagreed.<sup>671</sup> This further suggests that the evidence base for comparing the administration costs of a Challenge Fund and the RHI scheme was not well founded.
- 9.24 On the other hand, at the time of the Casework Committee meeting, Mr Angus did not perceive administration costs to be terminal in the same way as Mr Murphy. He considered he would have weighed up the six different issues said to affect the Challenge Fund, of which administration cost was one, and was not sure he would have given any one greater weight than another at the time of the meeting, though, in his oral evidence to the Inquiry, he did appreciate: “the fact that, if you don’t have the money to find the staff to administer a scheme, then it is a bit of a show stopper.”<sup>672</sup>

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664 DFE-62230 to DFE-62233

665 TRA-03586 to TRA-03590

666 TRA-02419 to TRA-02420

667 TRA-02419 to TRA-02420

668 TRA-02458 to TRA-02460

669 TRA-02490

670 DFE-144168 to DFE-144169

671 TRA-04136; TRA-04139

672 TRA-02618

- 9.25 Ms Hepper herself also did not regard administrative costs as a single determining factor. She told the Inquiry in oral evidence that her principal reasons for preferring an RHI scheme over a Challenge Fund were consistency with GB: managing the risk of installations not producing heat and previous experience with NIRO.<sup>673</sup>
- 9.26 The Inquiry was informed that the Casework Committee only considered “shovel ready” policy proposals and did not have the power to choose between policies.<sup>674</sup> As Mr Murphy put it in evidence, the Energy Division had come to the meeting with “all their ducks lined up.”<sup>675</sup> However, inherent in the committee’s challenge/reassurance role, if it were to have any real significance, must have been that it did have the power to refuse to approve a “shovel ready” policy and to send it back pending informed investigation of whether it did in fact represent value for money in public expenditure terms.<sup>676</sup> Mr Murphy said that once the issues over not progressing the Challenge Fund were explained (and the explanations satisfied him at the time) then there was no good reason to block the RHI from progressing.<sup>677</sup>
- 9.27 In the course of giving evidence, Mr Angus referred to “a momentum”<sup>678</sup> in relation to an RHI scheme, in that this was the proposal that was brought to casework (as opposed to the RHI scheme and the Challenge Fund being brought to casework for the Casework Committee members to choose whichever they preferred).
- 9.28 In one of his written statements, Mr Cooper also noted that the RHI scheme had progressed to a much more advanced stage than the Challenge Fund and, at the time of the Casework Committee meeting, there was an obvious disadvantage surrounding the length of time that it would have taken to get a Challenge Fund up and running.<sup>679</sup> That does not appear to have been an argument that was recorded in the minutes but it may reflect the delivery attitude (to “get on with it”) that appears to have motivated much of the Department’s activity.

### **Inaccurate scheme costs information provided by the presenting officials**

- 9.29 The Inquiry notes that the net present costs (NPC) of the NI RHI were quoted at paragraph 50 of The Synopsis of the Renewable Heat Incentive Scheme Project provided to the Casework Committee, by using the June 2011 CEPA final report figure of £242 million, which took no account of the increase in scheme subsidy costs from £334 million to £445 million as recorded in the CEPA February 2012 addendum. This reliance on a potentially redundant NPC was not spotted at the time, but when pointed out by Inquiry Counsel, both Mr Murphy and Mr Angus stated that the committee should not have been invited to approve a policy on the basis of inaccurate information.<sup>680</sup> Further evidence of incorrect or incomplete information in the casework papers emerged with both Mr Angus and Mr Murphy confirming that they had not been told that the Minister had received and approved Ms Hepper’s submission in favour of an NI RHI scheme in June 2011 based on a completely different set of tariffs and costs.<sup>681</sup>

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673 TRA-02341 to TRA-02342

674 WIT-19575

675 WIT-19562; TRA-02440

676 WIT-19545

677 TRA-02440

678 TRA-02608

679 WIT-27314

680 TRA-02632 to TRA-02634

681 TRA-02558 to TRA-02559; TRA-02622

### The proposed scheme tariffs

- 9.30 In answer to an enquiry from Mr Cooper as to how the tariffs had been designed, Mr Hutchinson explained to the Casework Committee that tariffs would vary, depending upon the type and size of technology, to ensure financial support was targeted for a specific installation and to avoid overcompensation. He explained that the scheme would be open for new installations until 31 March 2020 and, since the tariffs were “grandfathered”, the final payments would be made in 2040.<sup>682</sup>
- 9.31 The minutes do not refer to any discussion of the risk of overcompensation or the perverse incentive and there does not appear to have been any discussion as to why no tiering of the tariff for the biomass boilers had been adopted in Northern Ireland despite the fact that biomass fuel cost was clearly shown to be less than the proposed subsidy (being set out upon consecutive pages of the synopsis as well as the CEPA documentation). Such an omission may be considered surprising since Mr Murphy’s written statement to the Inquiry confirmed that he had read the CEPA footnote stating the opposite.<sup>683</sup> The table at paragraph 19 of the synopsis recorded the cost of biomass as 4.39 p/kWh and paragraph 22 demonstrated this to be cheaper than the proposed subsidy for boilers between 20kW and 100kW at 5.9 p/kWh.<sup>684</sup> However, it is also the case that this was one of a number of different tariffs for different technologies, and at a time before the launch of the scheme, and before uptake was actually known. The Casework Committee was also expressly told by Energy Division in its synopsis, at paragraph 22 and footnote 9<sup>685</sup> (having set out the proposed biomass tariffs and the GB equivalents that included tiering), that:

“Tiering is used to ensure the technology is not ‘over-used’ just to receive an incentive. It works by dropping the paid tariff after the technology reaches its optimum use for the year; this is deemed at 1314kWhrs [sic] (15% of annual hours). After this level is reached the tier 2 tariff is paid. Tiering is not included in the NI scheme because in each instance the subsidy rate is lower than the incremental fuel cost.”

The final sentence in footnote 9 was incorrect, but it could have led the reader of the synopsis to understand that the matter had been considered and a reasoned decision taken that tiering was not necessary. In turn, this may have made it more difficult for the attention of the committee members to be drawn to the fact that the fuel cost was also documented to be lower than the proposed subsidy.

### Proposed scheme protections

- 9.32 The risk of subsidy levels proposed for the RHI being either too high or too low was discussed. That risk was proposed to be managed through regular, planned reviews of subsidy levels. Ms Hepper explained to the Casework Committee that the RHI would have scheduled reviews “built-in” to the scheme to allow DETI to ensure that the scheme remained fit for purpose and value for money.<sup>686</sup> Both Ms Hepper and Mr Hutchinson told the committee that a first

682 DFE-04226 to DFE-04227

683 WIT-19552 to WIT-19553

684 DFE-398068; DFE-398070

685 DFE-398070

686 DFE-179470

scheduled review would take place in 2014,<sup>687</sup> with Mr Hutchinson explaining that any proposed changes would be implemented in 2015.<sup>688</sup> Ms Hepper also advised the committee that the Department had “included an option to hold emergency reviews” should the need arise.<sup>689</sup>

- 9.33 Nobody appears to have questioned the basis upon which the scheme incorporated such scheduled ‘built-in’ or emergency reviews, or whether they were to be included in the draft regulations. It seems that Energy Division officials were not asked to provide any further detail as to where such an option had been “included” or how it would operate, nor did they furnish any further explanation.
- 9.34 Mr Cooper told the Inquiry that he accepted on trust the assurances from Ms Hepper and Mr Hutchinson that there would be regular reviews and monitoring. While he did not associate the words ‘built-in’ or ‘in-built’ with a statutory or regulatory framework, he was aware that similar undertakings were recorded in the synopsis and risk register.<sup>690</sup>
- 9.35 The committee was also informed that a monitoring board would be created.<sup>691</sup> As has been noted elsewhere in this Report, no such board came into existence. In his evidence to the Inquiry, Mr Hutchinson agreed that such a board would have been helpful, but he was unable to say why it had not been created.<sup>692</sup>
- 9.36 Mr Hutchinson also informed the committee that, if necessary, the scheme could be closed to new applications mid-year if applications were higher than expected and budgets risked being overspent.<sup>693</sup> He told the Inquiry that this was intended as a reference to using the normal procedure of public consultation followed by amending legislation, although he accepted that at the time he would not have known how long such a procedure would have taken.<sup>694</sup> It is difficult to understand how that could be reconciled with the obviously expeditious assurance of “mid-year” closure, but if that was the intended mechanism it should certainly have been clarified for the committee.
- 9.37 The draft regulations, which contained no power to close or otherwise suspend the scheme, do not appear to have been separately included with the documentation provided for the committee meeting as a discrete appendix. It is possible that a copy of the draft regulations may have been annexed to the State Aid papers. However there was evidence which suggested that the annexed document may have been the 2011 enabling Act rather than the draft regulations.
- 9.38 Mr Cooper told the Inquiry that if the explanation provided to the Inquiry by Mr Hutchinson as to what he meant had been provided to the committee (namely that closure of the scheme mid-year was to be by way of legislative amendment), he would have said “That doesn’t work!”<sup>695</sup> He told the Inquiry that he had no detailed experience of legislation.<sup>696</sup> However, he did not ask Mr Hutchinson to explain the mechanism for closure to which he referred, despite having been

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687 DFE-179466; DFE-179470

688 DFE-179470

689 DFE-179466

690 TRA-04213 to TRA-04218

691 WIT-06795 to WIT-06796; DFE-179472

692 TRA-02023

693 DFE-179472; WIT-08683

694 TRA-02162 to TRA-02164

695 TRA-04230

696 TRA-04213

copied in to the email of 3 May 2011 from Ms Brankin advising that, in view of the nature of the funding, details of proposed controls to prevent significant under/over spending would be required in order to obtain DFP approval.<sup>697</sup> Mr Cooper told the Inquiry that he simply accepted the assurance that there was an emergency “big red button” to stop the scheme. He accepted that he had not picked up that no such emergency provision had been included in the DETI risk register.<sup>698</sup>

- 9.39 Mr Connolly said in evidence that it seemed obvious to him that DETI would just tell Ofgem to refuse further applications when an annual budget had been breached.<sup>699</sup> He was clearly unaware that the proposed regulations would provide that, if eligible, an installation had to be accredited and that, once accredited, a participant would be entitled to subsidy. He did not ask any questions as to how costs were to be controlled and he accepted Mr Hutchinson’s assurance that “the scheme could be stopped mid-year.”<sup>700</sup> In the course of his evidence Mr Connolly accepted that he should have raised such enquiries.<sup>701</sup>
- 9.40 Mr Murphy also told the Inquiry that he was “upset” when he later learned the real nature and duration of the procedure needed to introduce controls.<sup>702</sup> In evidence to the Inquiry Mr Murphy also said that he believed at the time that there would be some mechanism, not necessarily statutory, which would allow changes in tariffs to be effected.<sup>703</sup> However, he does not appear to have raised an enquiry during the casework discussion itself as to what that mechanism might have been.

### The RHI Risk Register

- 9.41 The Risk Register, a copy of which was included in the committee documentation, was opened on 1 March 2012 and was described as a “dynamic document” that required any newly identified risks to be added and any risks no longer considered to be appropriate to be removed as the scheme progressed.<sup>704</sup> The register was to be held by the ‘project manager’, who was to be responsible for its upkeep.<sup>705</sup> The register included the identification of the following particularly relevant risks:
- (i) Incorrect tariff levels set either too high or too low, one indicator of which was said to be “Higher than expected uptake or overspending on profiled budget (indicating that tariffs are over generous).” The register recorded that external consultants had advised on determining tariff levels and there were to be planned reviews so that tariffs could be revised depending on market conditions.<sup>706</sup>
  - (ii) Insufficient budget secured for RHI payments or for administration of the scheme. The indicators were specified as “Tariffs set at too high/generous a level leading to a higher than expected uptake” and “External circumstances making the tariffs more generous” including “reduction in renewable heating costs.” Actions required included ongoing

697 TRA-04224

698 TRA-04222 to TRA-04224

699 TRA-03397 to TRA-03398

700 TRA-03397 to TRA-03399

701 TRA-03399

702 TRA-02467

703 TRA-02465 to TRA-02466

704 DFE-398613 to DFE-398625

705 DFE-398615

706 DFE-398620

engagement with key industry stakeholders, liaison with the administrator and planned reviews.<sup>707</sup>

- (iii) The risk of inadequate resources “to deliver the project/separate key functions including staff.” The risk indicators included the following: the fact that there was a “small team”; that the scheme involved “complex and technical issues”; and that there were “Varied requirements i.e. policy development, legislation, resource management, programme management, liaison with Ofgem, liaison with stakeholders etc.”<sup>708</sup> Actions required to manage this risk fully included “Clear programme management structures, monitoring of progress...” and the need for “additional resource.” The impact and likelihood of this risk was specified as “high” and the need for resources noted to be “immediate.”<sup>709</sup>

9.42 Further risks appearing in the register included low uptake, harm to other sectors such as the gas market, failure of renewable heat supply, failure to meet EU and Executive targets, failure to qualify for State Aid, failure in administration and instances of fraud.<sup>710</sup> However, despite the clear identification of a number of risks that were to play a fundamental role in the development of the RHI scheme, there is no objective evidence that the register ever appears to have been further used in the way it was intended. Indeed the deputy principal, Mr Hughes, who joined DETI on 30 June 2014 and effectively took over responsibility for the day-to-day running of the scheme from that time, reporting to Mr Wightman, said that he had not seen the document prior to the Inquiry.<sup>711</sup>

### Project management

9.43 In a written statement to the Inquiry Mr Cooper stated that the committee had sought assurances from Energy Division about the need for robust project management arrangements.<sup>712</sup> The only reference to project management in the casework minutes related to the governance and management of Ofgem management arrangements with a note that Mr Cooper had asked “what controls would be in place for the project management aspect of the contract with Ofgem?” It seems that Ms McCutcheon advised that discussions had taken place with Ofgem.<sup>713</sup> In a subsequent email Ms Hepper expanded upon the proposed details of the Agency Services Agreement. It does not appear that any questions were raised with regard to the potential application of project management principles to DETI’s own administration of the RHI scheme.

### The decision of the Casework Committee

9.44 Ultimately, as reflected in the final version of the minutes of the Casework Committee of 30 March 2012, the Casework Committee confirmed they “were content to approve the RHI and RHPP schemes to proceed to DFP”, conditional upon a number of agreed actions being completed by the Energy Division officials.<sup>714</sup> The matters to be dealt with were set out in the minutes.<sup>715</sup>

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707 DFE-398620  
 708 DFE-398623  
 709 DFE-398623  
 710 DFE-398622 to DFE-398624  
 711 TRA-05863 to TRA-05864  
 712 WIT-27313  
 713 DFE-382578  
 714 DFE-179464 to DFE-179476  
 715 DFE-179476

- 9.45 As a matter of fairness to the members of the Casework Committee, it is of note that they did require (at the initial request of Mr Angus, but with which his committee colleagues agreed) an addition to the draft minutes specifically to record an action required of the presenting officials that “the business case to DFP (and the Minister) should explicitly address the reasons why the RHI is favoured over the Challenge Fund.”<sup>716</sup> This was so even though the presenting officials had not included any reference to the Challenge Fund in the synopsis they initially presented to the Casework Committee.

## Findings

54. The synopsis provided for the Casework Committee, upon which the members of the committee were bound to focus, was incomplete and contained inaccurate information in some key respects. In addition, the evidence base for comparing the administration costs of the Challenge Fund and the RHI scheme was not well founded. The Inquiry agrees with Mr Angus that the committee should not have been invited to approve a policy on the basis of inaccurate or incomplete information. The Inquiry accepts that additional information was available in the further documentation supplied to the committee but, as suggested above, it is obviously important that the relevant matters were clearly and accurately set out in the synopsis itself, which was designed to summarise the key issues for consideration by the committee.<sup>717</sup>
55. The incomplete and inaccurate information that was provided to the Casework Committee did disclose a significant difference (over £200 million) between the overall cost of the Challenge Fund and the preferred RHI. Given that the committee was concerned to understand why the RHI was preferred in the context of the Challenge Fund option being said to produce the most renewable heat at the lowest cost, the minutes should have clearly set out how much more expensive the chosen policy was over what appeared to be a viable alternative, and detailed why the committee accepted the reasons put forward by Energy Division for preferring the RHI.
56. Ms Hepper accepted that no comparison of the costs of administration of a Challenge Fund as an alternative to an RHI scheme was placed before the committee.<sup>718</sup> In the course of evidence, reference was made to the generally constrained financial circumstances that existed at the time when the Casework Committee was considering these issues and the difficulty in persuading HMT to reconsider any decision not to provide the costs of administration out of AME funds that it was providing. If the committee considered that (what was said to be) the unaffordable cost of the administration of the Challenge Fund meant that a much more expensive policy (in overall terms) was to proceed, then this should have been clearly recorded in the casework minutes. The Inquiry finds it difficult to understand why the committee would not have drawn specific attention to the overall cost disparity as disclosed in the material, and required that the reasons for proceeding in spite of that disparity be specifically drawn to the Minister's attention.
57. Inherent in the committee's challenge/reassurance role must have been that it did have the power to refuse to approve a "shovel ready" policy and to send it back pending informed investigation of whether it did in fact represent value for money in public expenditure terms. However, as Mr Murphy pointed out, the "shovel ready" approach encouraged the assumption by the Casework Committee that the material put before it was accurate.<sup>719</sup> In the case of the RHI scheme there had been a lot of development including a public consultation and State Aid application. Mr Murphy told the Inquiry that the committee did not have a strong reason to reject the proposal and his own view was that the lack of administrative funding took the Challenge Fund "off

717 TRA-02632

718 TRA-02321

719 TRA-02459 to TRA-02460



the table”.<sup>720</sup> In the course of giving oral evidence, Mr Angus noted that the proposal was presented by Energy Division officials, based on what was said to be CEPA’s position as “This is the option that seems to be preferred” reflecting “a momentum” in favour of an NI RHI scheme, although, in his view, not for any reason other than the Energy Division officials felt it was the best option.<sup>721</sup>

58. A fundamental error in the synopsis provided to the Casework Committee was the statement from Energy Division officials that tiering of tariffs was not included in the NI RHI scheme because in each instance the subsidy rate was lower than the incremental fuel cost. This statement was made to the Casework Committee despite the fact that the synopsis also included information that showed the price of biomass fuel to be less than the comparative price of oil, and, more importantly, less than the proposed subsidy. While the primary responsibility for the fundamental error lay with the expert consultants, CEPA, Energy Division officials, having decided to recommend the RHI scheme for approval, and in the light of the risk of overcompensation which had been identified, should have identified this error and not repeated it to the Casework Committee.
59. The Inquiry can understand, in the circumstances, that it may have been difficult for the Casework Committee members (who had not been engaged with the consultants, had not developed the policy and who were reading a lot of information about a new scheme over a short period of time, including a synopsis that specifically told them tiering was not necessary in the NI RHI scheme) to notice the error.
60. The evidence available to the Inquiry indicates that the Casework Committee sought and received a number of assurances from Energy Division officials about the RHI scheme, which the members of the committee took at face value. However, some of those assurances were without substance. In addition, some assurances were given to the committee, but the action thereafter required to make good on the assurance was not taken. The Inquiry finds that there was no effective mechanism for ensuring that the assurances given to the Casework Committee were subsequently honoured.
61. Further, the evidence available to the Inquiry indicates that the Casework Committee did identify steps that the presenting officials needed to take following the grant of approval by the committee. The Inquiry notes there was also no effective mechanism for ensuring those steps were actually taken.
62. Mr Hutchinson had claimed to the Casework Committee that “if necessary the scheme could be closed to new applicants mid-year if applications were higher than expected and budgets risked being overspent.”<sup>722</sup> He did not explain the mechanism by which this budget protection was said to be available. He should have done. In addition, while the Casework Committee panel was entitled to operate on the assumption that what it was being told was accurate, the issue of budget protection was sufficiently important that the committee should have sought and obtained confirmation of the mechanism by which this budget protection was said to have been available.

720 TRA-02542 to TRA-02543

721 TRA-02608

722 DFE-179472

63. The Energy Division presenting officials should have known, arising from the April 2011 email exchanges between Ms Clydesdale and Mr Parker,<sup>723</sup> that the funding for the RHI was a form of AME that carried a potential DEL consequence. As a result, Energy Division had received an instruction from DETI Finance in May 2011<sup>724</sup> to treat RHI as if it was funded through DEL, and to avoid any overspends. The fact that RHI was funded through AME, but had potential DEL consequences and was to be treated as DEL, should have been specifically brought to the attention of the Casework Committee by the Energy Division presenting officials. Had it been, it is likely that there may have been greater testing of the controls which the presenting officials asserted would be in place. The chair of the Casework Committee had also been copied into the April/May 2011 emails in his role as Finance Director. It was unfortunate that he did not remember about them during the 2012 casework process.
64. It seems that even the final draft of the Casework Committee minutes may not have recorded all relevant exchanges. Mr Cooper told the Inquiry that, in the casework meeting, he had raised with Ms Hepper the issue as to whether, given its novelty and complexity (both technical and economic), the scheme should ever have been accepted as suitable for an already overstretched Department to develop and operate. He told the Inquiry that he had queried whether the scheme was appropriate at all for DETI and why it had not been outsourced to a more specialised body such as Invest NI. He also said that he asked why it had been decided not to combine with the GB-based scheme using appropriately adjusted NI rates. Mr Cooper told the Inquiry that he received a complicated explanation based on legislation and legal reasons. These were all important points, which should have been recorded in the minutes of the Casework Committee if they were discussed at the meeting as Mr Cooper contends they were. Mr Cooper said that, with hindsight, he wished that he had ensured that these exchanges had been included in the minutes.<sup>725</sup>
65. The presentation of the RHI policy to the Casework Committee (responsibility for which lies with the Energy Division presenting officials) was incomplete, included errors, and failed to identify a number of potential risks; those problems went undetected. Further, a number of assurances sought by the committee, and given by the presenting officials, were not subsequently honoured. Consequently, the Inquiry considers that the casework process did not fulfil its purpose as an effective challenge and assurance mechanism.

723 WIT-00842; WIT-00843

724 WIT-00840; WIT-00841

725 TRA-04118 to TRA-04121

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## Chapter 10 – The submission of 16 March 2012

- 10.1 On 16 March 2012, post the Casework Committee meeting where approval to proceed with a business case to DFP had been secured, Ms Hepper sent<sup>726</sup> a further submission to Minister Foster and Dr Crawford seeking approval to proceed with the introduction of the NI RHI scheme and the associated Renewable Heat Premium Payments (RHPP), which was the interim grant scheme established prior to the introduction of the domestic RHI. The submission attached a draft SL1 letter to be sent to the ETI Committee, and a draft Regulatory Impact Assessment (RIA) for the Minister to consider and sign.
- 10.2 In between the provision of the submission and it being signed off, Energy Division officials sent, on 22 March 2012, to DFP the RHI business case for approval.<sup>727</sup> DECC, on 26 March 2012,<sup>728</sup> published its interim cost control consultation. Neither of these developments was drawn to the Minister’s attention before she signed off the submission.
- 10.3 Paragraph 28 of the submission<sup>729</sup> informed the Minister that the Casework Committee was content with the proposals for an RHI and RHPP subject to a number of matters that were then set out, mostly relating to scheme administration and administration costs. The Minister was not told in the submission that the Casework Committee had required that Energy Division officials ensure that “the business case to DFP (and the Minister) should explicitly address the reasons why the RHI is favoured over the Challenge Fund option.” Philip Angus had required this insertion when providing his comments on the draft Casework Committee minutes on 14 March 2012, two days before the submission was lodged.<sup>730</sup> There was no reference in the submission to the Challenge Fund, or a comparison with an NI RHI scheme in terms of overall cost.
- 10.4 The submission set out the proposed new tariff structure,<sup>731</sup> which included the proposed tariff for biomass boilers between 20kW and 100kW at 5.9p/kwh. The proposed tariff structure table, once again, had the erroneous footnote explaining that tiering of the tariff was not included in Northern Ireland because in each instance the subsidy rate was lower than the incremental biomass fuel cost.<sup>732</sup> Reviews were once more described as “built-in” to the scheme to allow DETI to ensure that the scheme remained fit for purpose and value for money for the duration.
- 10.5 The Minister was also informed in paragraph 8<sup>733</sup> of the submission that only “useful heat” would be deemed eligible and this was explained as meaning heat that would otherwise be provided by fossil fuels. She was told that this would exclude deliberately wasting or dumping heat with the sole purpose of claiming incentive payments. The Inquiry notes however that, contrary to the recommendations contained in the Ofgem Legal Review of November 2011, no such definition of “useful heat” was included in the NI RHI 2012 Regulations when they came to be made.<sup>734</sup> The submission also proposed, in paragraph 26, that Ofgem should be appointed to administer the scheme.<sup>735</sup>

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726 DFE-31773 to DFE-31799

727 DFE-82632

728 INQ-22023 to INQ-22037

729 DFE-31781

730 DFE-80619 to DFE-80626

731 DFE-31777

732 DFE-31777

733 DFE-31776

734 WIT-01237 to WIT-01264

735 DFE-31781

- 10.6 The Minister has stated to the Inquiry that she was not provided, alongside the submission, with a copy of the CEPA addendum of February 2012, the synopsis prepared for the Casework Committee, the draft minutes of the Casework Committee, or the business case subsequently submitted to DFP by DETI on 22 March.<sup>736</sup>
- 10.7 The submission was signed off by the Minister on 11 April 2012,<sup>737</sup> and the accompanying Regulatory Impact Assessment was signed by her on 13 April 2012.<sup>738</sup> The draft RIA that the Minister signed detailed a number of risks and uncertainties anticipated by Energy Division officials as potentially arising in the course of implementing an RHI scheme in Northern Ireland. These included: the risk of subsidies proposed for the RHI being too high or too low (which was said to be mitigated by regular planned reviews); the risk of low take-up; the risk of failure to implement the targets set by the EU Directive; the risk of insufficient budget resulting from higher than expected uptake (said to be mitigated by ongoing engagement with Ofgem to assess uptake levels and expected spend against profiled budget); the risk of a refusal of State Aid; the risk of fraud (to counteract which Energy Division officials claimed to have put in place a number of measures); and the risk of administrative failure (to mitigate which DETI undertook to establish a joint project team with Ofgem as the scheme was implemented).<sup>739</sup> The Minister would have been left in no doubt as to the nature and extent of the risks and the proposed mitigation; indeed she signed the document that specified these risks.<sup>740</sup>
- 10.8 Despite providing reasonably comprehensive information about the risk categories, the RIA document contained only limited information about the funding available and no quantitative information about the projected lifetime subsidy costs. It did provide some quantification of the administration costs and of the lifetime carbon saving benefits.
- 10.9 Notwithstanding this lack of information, Minister Foster signed it declaring:

“I have read the Regulatory Impact Assessment and I am satisfied that the benefits justify the costs.”<sup>741</sup>

In her oral evidence to the Inquiry, Minister Foster agreed with Inquiry Counsel that, when signing the March 2012 RIA, she did not know what the subsidy spend over the entire period was going to be, although she did understand that the total cost of the scheme was going to be a lot more than £25 million. She agreed that she should have had a clearer understanding of what the scheme costs were.<sup>742</sup> In further questioning by the Panel, Minister Foster accepted that the decision-making had been effectively delegated by the Treasury to her and that she needed to make the relevant judgment about the use of public money, although that was not possible without important information about the costs being available to her.<sup>743</sup>

736 WIT-20576 to WIT-20577

737 DFE-143880

738 DFE-70760

739 DFE-04250 to DFE-04252

740 DFE-70749 to DFE-70760

741 DFE-70760

742 TRA-08209 to TRA-08210; TRA-08216

743 TRA-08219

## Findings

- 66.** Once again the erroneous statement appeared, this time in a ministerial submission, reflecting a direct quotation from the CEPA final report, explaining that tiering of the tariffs was not included in Northern Ireland because in each instance the subsidy rate was lower than the incremental fuel cost.
- 67.** The Inquiry notes that despite a submission to her assuring the Minister that payments would only be made for “useful heat” such a condition was not laid down in the 2012 regulations.
- 68.** The Minister should have been informed at this point, 16 March 2012, that the predicted lifetime subsidy costs of the scheme had risen from £334 million to £445 million between CEPA’s final report of June 2011 and the addendum in February 2012.
- 69.** The “false economy” of the decision to prioritise the potential saving of a few million pounds in administrative costs associated with the RHI scheme over the potential saving of £200 million to £300 million in subsidy spend with a Challenge Fund, was not drawn to the attention of the Minister; it should have been.
- 70.** The Minister and/or her SpAd should have asked more questions and sought further reassurance in relation to at least some of the matters identified in the submission of 12 March 2012 and the associated Regulatory Impact Assessment. For example, they might have questioned how the reviews of the scheme were to be “built in” and they might have enquired as to the form of any “budget control” that might be required.
- 71.** Minister Foster should not have signed an RIA document in which she was declaring that the benefits justified the costs without being provided with or seeking all of the necessary information about the lifetime costs.



## Chapter 11 – The Business Case for the approval of DFP

### The Business Case

- 11.1 On 22 March 2012 a Business Case relating to the proposal for an NI RHI scheme was forwarded from DETI to DFP for approval. The covering email<sup>744</sup> from DETI Finance’s Accountability and Casework Branch referred to the earlier Strategic Outline Business Case that had been approved in autumn 2011 subject to a number of areas that were to be addressed. It referred the reader to where the Business Case addressed those issues; details and costs in respect of administration, the potential risk of EU infraction fines, risks involved in developing and implementing the proposal and details of how the scheme was to be managed.<sup>745</sup> The covering email also confirmed that the proposal had been approved by DETI Casework Committee and DETI economists.<sup>746</sup>
- 11.2 DETI was required to complete and submit a short DFP Business Case *pro forma* and to tick an option as to whether the case was “standard”; “novel”; “contentious”; or “setting a precedent”.<sup>747</sup> Mr Hutchinson, who completed the *pro forma*; marked it as “standard”. He could not recall whether or not there was a discussion with Ms McCutcheon and Ms Hepper about this but agreed it would not have been an issue that was dwelt on.<sup>748</sup> Mike Brennan from DFP, who in 2012 was the head of Central Expenditure Division (CED) within its Public Spending Directorate, said in his oral evidence that at the time he would have ticked the “novel” box and with the benefit of hindsight would have ticked all three “non-standard” boxes.<sup>749</sup>
- 11.3 A large volume of documentation was supplied to DFP, along with the Business Case, in excess of 700 pages, including the AECOM/Pöyry and CEPA reports, the Ofgem Feasibility Study of December 2011, the EU State Aid notification papers of December 2011 and February 2012, the draft scheme risk register and various relevant calculations. Much of the material contained in the Business Case had been put before the DETI Casework Committee. The Inquiry considers the following incomplete, incorrect or misleading aspects of the Business Case to have been of particular significance.
- (i) Funding by HMT was described in paragraph 2.7 of the Business Case as incremental over the budget period 2011-15.<sup>750</sup> No reference was made to the fact this was AME funding, nor that it had been the subject of the suggestion of DEL penalties by HMT in April 2011, nor of the fact DETI Finance had, in May 2011, warned that although it was AME funding it should be treated like DEL. Nor was there any reference to budget controls – see in this regard the Jon Parker, Ms Clydesdale and Ms Brankin emails of April and May 2011 referred to in chapter 3.
  - (ii) DFP was informed, in sections 7 and 8 of the Business Case that DETI had considered a number of options, the most appropriate of which were seen as either an NI RHI

744 DFE 82632

745 DFE-82657

746 DFE-82632

747 DFE-83337 to DFE-83339

748 TRA-02173 to TRA-02174

749 TRA-01211

750 DFE-82641

scheme or a Challenge Fund.<sup>751</sup> The administrative costs of running a Challenge Fund were described in paragraph 8.5 as prohibitive compared to the potential costs of administering an NI RHI scheme.<sup>752</sup> In section 9, on the monetary costs and benefits, no information or calculation was provided with regard to the projected administration costs or to the lifetime comparative costs of both options which could have illustrated the potential for cost-effective overall savings represented by the Challenge Fund. The actual Net Present Cost (NPC) of the scheme was wrongly quoted as £242 million, which came from the CEPA final report of June 2011, rather than taking account of the addendum in February 2012, which included much higher tariffs and subsidy costs that alone had risen by £111 million since the June 2011 final report.<sup>753</sup>

- (iii) In section 10 of the Business Case, dealing with ‘Risks’, the risk of ‘over-subsidising’ was clearly recognised but it was pointed out in section 10.4 that:

“The tariffs have been developed by CEPA and AEA Technologies, subject to a public consultation and then subsequently reviewed by CEPA and AEA. Departmental Economists have also assessed the tariffs and assumptions behind the calculations and have deemed them appropriate.”<sup>754</sup>

DETI Economist Mr Connolly was asked about the accuracy of the last sentence of the above quotation by Inquiry Counsel. He replied by stating that it was not an accurate characterisation of what he had done and that he had not assessed any of the technical assumptions. He agreed that it was a potentially misleading statement.<sup>755</sup>

- (iv) No consideration appears to have been given to the protection afforded by the ‘first come, first served’ approach of the Challenge Fund with regard to keeping within an annual budget – once the allocation for any period was used, no further awards would be made.
- (v) There appears to have been no guidance provided about whether a Challenge Fund could be introduced more or less expeditiously than the RHI scheme. No new legislation would have been needed for this since the Department could already introduce grant schemes with its existing powers, but arrangements for administration by DETI would have been needed in place of what Ofgem was going to do for the RHI scheme.
- (vi) The Business Case, at paragraph 2.31 on internal page 17, again showed a tariff of 5.9p/kWh for biomass boilers between 20kW and 100kW (or the medium biomass tariff)<sup>756</sup> and, two pages previously on internal page 15, stated the cost of biomass to be 4.39p/kWh.<sup>757</sup> At page 17 the same erroneous footnote appeared once more:

“Tiering is used to ensure the technology is not ‘over-used’ just to receive an incentive. It works by dropping the paid tariff after the technology reaches its optimum use for a year; this is deemed at 1314h (15% of annual hours). After this level is reached the tier 2 tariff is paid. Tiering is not included in

751 DFE-82706

752 DFE-82706

753 DFE-82711; DFE-00581

754 DFE-82712

755 TRA-03617 to TRA-03618

756 DFE-82649

757 DFE-82647



the NI scheme because in each instance the subsidy rate is lower than the incremental fuel cost.”<sup>758</sup>

- (vii) At paragraph 7.53 the business case confirmed that: “There will be scheduled reviews in-built into the Northern Ireland RHI”<sup>759</sup> and, at paragraph 10.4, that it was currently proposed the first review was scheduled to start in January 2014, with any changes or revisions implemented by 1 April 2015.<sup>760</sup> The term “in-built” was not explained, nor does it appear that it was queried by DFP. Comparisons were drawn with the NIRO but the Inquiry notes that reviews were put on a statutory basis in the NIRO regulations, a useful precedent that does not appear to have been highlighted in the documentation or discussions surrounding the RHI Business Case.
- (viii) DFP was also informed that an inter-departmental Renewable Heat Strategy Group would monitor the progress of the RHI.<sup>761</sup> Although this could not have been known at the time of the Business Case being submitted (and, therefore, does not represent an omission in the Business Case *per se*), it seems that the work of that group was ‘paused’ in 2013 because of a lack of resources and not revived thereafter.

## DFP consideration of the Business Case

- 11.4 Based on evidence provided to the Inquiry, there was only limited scrutiny of the Business Case carried out by DFP. The main documented evidence available to the Inquiry stems from work done by Rachel McAfee, an economist within DFP’s Economic Appraisal Branch, who, in the limited time available to her, appears to have considered the proposal and highlighted a number of points in her very short summary to colleagues. Two of these points – relating to the need for formal review of the scheme and for its reapproval by DFP in 2015 – were adopted as conditions in the final approval letter of 27 April 2012.<sup>762</sup>
- 11.5 None of the fundamental errors or omissions in the Business Case (as outlined above) were identified by DFP, which may reflect an inherent lack of challenge in the process, perhaps, as evidenced by Mr Stevenson, the then grade 7 DFP Supply Officer responsible for engagement with DETI, who told the Inquiry:

“For our system to work at pace, we need to trust the information that would come to us.”<sup>763</sup>

## The DFP approval

- 11.6 On 27 April 2012 one of Mr Stevenson’s team, Ronnie McAteer, wrote to DETI indicating that DFP were content to approve the proposal on the basis that arrangements were put in place for scheduled reviews by DETI, the first of which was noted to start in 2014, and that any decision to continue the scheme beyond 2015 would require further/separate DFP approval.<sup>764</sup> Despite DFP’s own knowledge, which it had from at least 2011, that the NI RHI’s capped funding was not standard AME, no condition was imposed requiring any mechanism of budgetary cost control.

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758 DFE-82649

759 DFE-82703

760 DFE-82712

761 DFE-82658

762 DOF-03239 to DOF-03240

763 TRA-03096

764 DFE-171221 to DFE-171223

- 11.7 The DFP approval letter was emailed by Mr McAteer to Iain McFarlane, then head of DETI's Finance's Accountability and Casework Branch.<sup>765</sup> Mr Cooper, who had chaired the Casework Committee, and who at the time was 'acting up' as the grade 3 Senior Finance Director, was unsure in his evidence as to whether he saw the approval letter.<sup>766</sup> Mr Cooper told the Inquiry that conditions were attached to every approval but, given the resources that DETI Finance Division had, it was impossible to check that every condition had been properly managed by the divisions, who had ultimate responsibility for this.<sup>767</sup>
- 11.8 Despite DFP's clear conditions for the approval – requirement for review of the scheme and for reapproval of spend beyond March 2015 – no formal system of review was established by DETI and no formal record or minute was created to ensure continuity of knowledge of these important conditions, other than placing the DFP approval letter in TRIM. Neither of the above conditions were ultimately fulfilled on time, if at all, during the period for which the scheme was open. The Inquiry was later to hear from Mr Hughes, who took up his post in Energy Division at the end of June 2014, that according to the NICS record-keeping system at the time, the Business Case and the approval letter were not stored together.<sup>768</sup> This was contrary to the principles of project management and a common sense need to have a formal system to ensure continuity of knowledge.
- 11.9 The non-domestic scheme was not flagged in Energy Division records as requiring reapproval. Mr Mills, who became head of Energy Division in January 2014, later told the Inquiry that he forgot about the need for reapproval, something that he recalled was mentioned to him by Ms McCutcheon and Mr Hutchinson at a meeting in March 2014.<sup>769</sup> He also stated that it was incongruous to seek reapproval in March 2015 for a scheme that to him appeared permanent until 2020 in the implementing regulations.<sup>770</sup> This fallacy may well have led to the need to re-apply for DFP approval in March 2015 being overlooked. This confusion clearly shows the importance of a formal record keeping system rather than a reliance on word-of-mouth communications.

### Submission to the Minister on receipt of DFP approval

- 11.10 The DETI Financial Procedures Manual<sup>771</sup> required both Casework Committee and DFP approval to be obtained before seeking ministerial approval for projects over £1 million. Section 6.5 of the manual provided as follows with regard to seeking ministerial approval after DFP approval has been obtained:

"All projects over £1 million require Ministerial approval after DFP approval has been obtained. The Casework Committee minutes, casework papers and appraisal documents should be sent to Private Office along with the Ministerial Submission. It is the responsibility of the Operating Division to prepare the Ministerial Submission."<sup>772</sup>

765 DFE-171221 to DFE-171223

766 TRA-15645 to TRA-15646

767 TRA-15648

768 TRA-05846 to TRA-05847

769 TRA-07144

770 TRA-09597

771 DFE-423435 to DFE-423656

772 DFE-423488

No such submission was sent to the Minister. Consequently, the Minister did not receive the Casework Committee minutes or the Business Case, nor did she receive the DFP approval letter in order to see its conditional nature.

## Findings

- 72.** Given the novel nature of the scheme, the unpredictability and volatility of demand, the unusual form of funding and the fact that accreditation entitled applicants to 20 years of subsidy, the Inquiry finds that DETI should not have submitted the Business Case to DFP with a *pro forma* claiming it to be a “standard” business case. The Inquiry considers that one of the other available options – such as “novel”, “contentious” or “setting a precedent” – would have been more appropriate and should have been chosen.
- 73.** The Inquiry finds that, in the circumstances, the DFP officials concerned should also have recognised that the Business Case that it received from DETI was not “standard” and should have drawn that to the attention of DETI.
- 74.** A large volume of documentation was supplied to DFP with the Business Case. This practice of providing so many lengthy documents may have been seen as a well-intentioned means of informing recipients. The Inquiry has seen that this approach to the quantity of documents did not equate to quality of information or advice, and only very few of those receiving such large packs of documents ever read even a fraction of them. Important information was obscured by the sheer volume of data, and a series of errors went unrecognised and important messages missed.
- 75.** Insufficient challenge was applied by DFP to the information provided and even basic numerical checks were not carried out. Too much reliance was placed on assurances from DETI, which had itself not uncovered the many errors or areas of misunderstanding in the Business Case.
- 76.** DETI did not have proper procedures in place to ensure that the DFP approval conditions were observed. DFP had no procedure in place to monitor compliance with its conditions.
- 77.** The Inquiry finds that, in order to comply with DETI’s own financial procedures, the relevant DETI Energy Division officials ought to have sent a submission to the Minister after receiving DFP approval. That submission should have included the Casework Committee minutes, the Business Case sent to DFP, and the DFP approval letter. Had that happened, the Minister would then have been apprised of the structure of the RHI scheme in much greater detail, as well as the fact that approval had been granted subject to conditions.

## Chapter 12 – Ofgem cost control warnings (June 2012)

### The 26 June Ofgem warning

- 12.1 In June 2012 DECC published the results of its consultation, commenced in March, some three to four months after passage of the GB RHI regulations, as to the need for some form of interim cost control for the GB RHI scheme. The relevant GB amendment regulations were duly made at the end of July.
- 12.2 During a teleconference, which took place on 26 June 2012 between a number of Ofgem employees and Ms McCutcheon and Mr Hutchinson of DETI, Ofgem referred to the concerns that they had expressed in the November 2011 legal review document and to the forthcoming amendment to permit interim cost control in GB with regard to the draft NI regulations.
- 12.3 As the NI regulations were intended to reflect those in force in GB, Ofgem felt that it would be advisable to wait for the GB amendments and adopt those considered relevant, including any form of interim cost control, thereby avoiding any risk that it had been considered necessary to guard against in GB. Ofgem offered to put DETI in touch with the DECC officials who were concerned in the imminent amendment to the GB regulations.
- 12.4 Draft minutes of the teleconference of 26 June 2012, which Ofgem sent to Ms McCutcheon and Mr Hutchinson of DETI on the 29 June 2012, recorded that Ofgem were told by the DETI officials that they had a commitment to their Minister to bring the NI RHI regulations into force by the end of September 2012 and this could not be put back to dovetail into GB legislative updates and that there might also be a risk of putting funding in jeopardy. They were also informed that DETI intended to have a Phase 2 update to the regulations in the summer of 2013 when they would reproduce the amendments which DECC were to consult on in the summer.<sup>773</sup> It was only on this latter point that DETI sought an amendment to the minutes of the teleconference of 26 June, to reflect that although they would be making amendments to the NI RHI regulations in the summer of 2013 (to align with DECC's planned changes in January 2013), the main objective of the amendments was to bring in Phase 2 of the NI RHI.<sup>774</sup> Mr Hutchinson told the Inquiry that they preferred to get their scheme up and running and make changes in the future – to stop everything was just not “a feasible option for us.”<sup>775</sup>
- 12.5 The Inquiry believes that Mr Hutchinson, who had read and was familiar with the GB RHI consultation documents, recognised the legal implications of Ofgem's advice, namely that it would be advisable to wait to see whether DECC decided that an amendment to its legislation was justified in order to protect its budget. However he also thought that Ofgem understood DETI's position from an administration standpoint with a commitment to their Minister to “get the scheme launched”.<sup>776</sup>
- 12.6 The Inquiry notes that since DETI did not make a Technical Standards Directive application to the European Commission until 25 July 2012 the NI RHI regulations could not, in any event, have been brought into force until 25 October to take account of the necessary three month

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773 OFG-03517 to OFG-03519

774 OFG-00633 to OFG-00636

775 TRA-02211

776 TRA-02210

“standstill”. Marcus Porter, a lawyer within Ofgem’s legal department, participated in the teleconference on 26 June and he was adamant in an internal email of 29 June that the Ofgem minutes of the teleconference should have “hammered home” the significance of Ofgem’s concerns regarding the course that DETI was proposing to adopt.<sup>777</sup> The recommendation to adopt some form of cost control was stimulated by the risk arising from the absence thereof from the current DETI draft regulations. Mr Hutchinson accepted that the minute reflected the clear recommendation made by Ofgem.<sup>778</sup>

## Ms Hepper’s claim to have passed on the Ofgem warning to Minister Foster

- 12.7 Ms Hepper was not present during the 26 June teleconference, but she was informed of its contents by Mr Hutchinson and Ms McCutcheon. Ms Hepper told the Inquiry that, at the time, they were conscious of slippage in launching the scheme as originally hoped in April or June.<sup>779</sup> By the date of the teleconference they had obtained State Aid clearance and an SL1 letter had gone to the ETI Committee of the NI Assembly on 22 June, in anticipation of a committee meeting before the July break, with a view to launching the NI RHI in September or October. She said that she was satisfied that Minister Foster was aware of and content with the commitment to bring the regulations into force by the end of September or as soon as possible thereafter.<sup>780</sup>
- 12.8 Ms Hepper explained that incorporating an amendment for interim cost control would have had to be put out to consultation for an 8 to 12 week period, the responses analysed, the amended regulations resubmitted to the EU for the three month standstill period and a further SL1 submitted to the ETI Committee, with the launch of the scheme being postponed to February or March of 2013.<sup>781</sup> She also explained how, by not incorporating interim cost controls from the outset of the NI RHI scheme, DETI was in fact “doing the same as” DECC which had launched their scheme, and run it for several months, without such controls.<sup>782</sup>
- 12.9 Ms Hepper said that when her team raised the Ofgem advice with her she appreciated that it had come from the Ofgem legal advisers and that was sufficiently important to raise it further up the line. Accordingly, she discussed the options with her superior, Mr Thomson, who agreed that she should bring the matter to the attention of the Minister.<sup>783</sup> Mr Thomson told the Inquiry that he could recall the issue and a discussion with Ms Hepper. However, he was unable to recall whether he had advised that they needed to talk to the Minister or, if so, whether a submission was necessary. He did say that taking such a matter to the Minister would generally have been done by way of a submission. Mr Thomson told the Inquiry that it would have been better to have advanced a written submission incorporating a copy of DECC’s public consultation documents relating to the GB interim cost control mechanism.<sup>784</sup>

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777 WIT-104767

778 TRA-02205

779 TRA-02356

780 TRA-02685

781 TRA-02686 to TRA-02688

782 TRA-02696 to TRA-02697

783 TRA-02689 to TRA-02691

784 TRA-05743 to TRA-05747

- 12.10 Ms Hepper was unable to recall clearly whether her conversation with Minister Foster was by telephone or face-to-face, although she thought that it had probably been the former.<sup>785</sup> Ms Hepper said that she outlined the details of the issue to the Minister explaining what the Ofgem representatives had said. She said that she had a clear recollection of not downplaying the material in any way, that she provided all the information about what DECC was doing in terms of interim cost control and that the advice came from Ofgem lawyers. She also said she described the stage which the NI scheme had reached and the likely delay that would flow from the Ofgem recommendation. She said that she had emphasised that DECC were bringing in the interim cost controls as a “failsafe” procedure, a bit of “belt and braces,” and that Ofgem had known that the GB scheme had been operating for some ten months without the amendment.<sup>786</sup> The Inquiry notes that the GB regulations had only been in operation for some four months before the initiation of the consultation to bring in interim cost control, which was implemented in July 2012. Ms Hepper said that the Minister was content that the NI RHI scheme should proceed without amendment on receiving an assurance that DETI would be consulting on cost controls during the following spring or summer.<sup>787</sup>
- 12.11 In contrast, Minister Foster told the Inquiry that she had no recollection of any such telephone call or meeting.<sup>788</sup> She said that the information confirmed a fundamental change to the GB RHI scheme in that a form of cost control had been the subject of consultation and was to be put into effect despite the low uptake of applications.<sup>789</sup> The Minister said that she would have required a formal submission had the information been clearly set out and there was “no way” that she would have taken a decision without having spoken to Dr Crawford.<sup>790</sup> She could only assume that, if any communication had taken place, it had been significantly downplayed.<sup>791</sup>
- 12.12 For his part, in his evidence to the Inquiry Dr Crawford was adamant that he had not been involved in any meeting or phone call with the Minister and Ms Hepper about cost control warnings from Ofgem. He was also not prepared to accept that there could have been a telephone conversation between Ms Hepper and the Minister, because had there been such a call about a “critical energy issue” the Minister would have spoken to him about it afterwards. He was adamant that a “critical issue” like this would have had to be followed up by a submission to the Minister.<sup>792</sup>
- 12.13 Ms Hepper told the Inquiry that the reason that there was not a written submission in respect of the conversation was that, as she had agreed with Mr Thomson, she wanted to get the matter raised as quickly as possible because the ETI Committee was sitting on the paperwork in relation to the SL1.<sup>793</sup> At another point in her oral evidence she accepted that “it was the working practices of the time that prevailed.”<sup>794</sup>

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785 TRA-02695

786 TRA-02696

787 TRA-02696

788 TRA-08242 to TRA-08244

789 TRA-08261

790 TRA-08239

791 TRA-08262

792 TRA-08042 to TRA-08044

793 TRA-02694 to TRA-02695

794 TRA-05201

## Findings

78. The Inquiry was not persuaded by the explanation put forward by Ms Hepper that, because DECC had not included an interim budget control in their original legislation, DETI, in omitting to do so in Northern Ireland, was simply doing what DECC did.<sup>795</sup> The practical approach should have been to take into account the reasons that DECC felt it necessary to amend its scheme almost immediately after it was launched, as detailed in the March 2012 DECC interim cost control public consultation document, and to ensure that the NI RHI scheme took the benefit of this experience. This would have been consistent with the argument put forward by the DETI presenting officials at the March 2012 DETI Casework Committee meeting in favour of an NI RHI scheme, namely consistency of approach with GB which would assist policy development in the future in Northern Ireland.<sup>796</sup>
79. The Inquiry gave very careful consideration to the two accounts given by Ms Hepper and Minister Foster with regard to the conversation said to have taken place subsequent to the Ofgem warning of June 2012. The Inquiry has taken into account the effect of hindsight as well as the requirement to be fair to both Ms Hepper and the Minister. Ms Hepper was unable to recall whether the conversation had been face to face or by telephone. On the other hand, the acceptance by Mr Thomson that she did speak to him about contacting the Minister, although he did not remember a meeting, was consistent with some form of conversation having taken place. However, apart from that fact, Mr Thomson's evidence was not particularly supportive. The Minister did not have a clear recollection. It was a conversation which was of particular significance in that Ms Hepper had been copied in to the 3 May 2011 email exchange advising of the need to include adequate controls in RHI budgetary expenditure because of the potential implication for the DEL budget. The 26 June 2012 warning was being given by the administrator of the GB RHI scheme in respect of which interim cost controls were being proposed a short time after the scheme came into operation, a public consultation had taken place and controls were shortly to be implemented. DECC had formed the view that such interim controls were necessary in order to safeguard public funds. If the conversation between Ms Hepper and the Minister did take place the Inquiry finds that the warning was not highlighted as Ms Hepper maintained. It is the view of the Inquiry that if such a warning were being raised with the Minister it should have been the subject of a careful minute or record setting out the advice that Ms Hepper had provided to the Minister and the Minister's response thereto. This would have provided objective evidence of a significant policy decision by a Minister of the Northern Ireland Executive and the grounds upon which such a decision had been reached. From Ms Hepper's own point of view such a record would have provided objective evidence confirming the circumstances of the decision.

795 TRA-02696 to TRA-02697

796 WIT-00902



80. Whether or not the June 2012 conversation between Ms Hepper and Mrs Foster did take place, and whether or not Ms Hepper downplayed the warning from Ofgem with regard to the advisability of waiting for the outcome of the GB RHI cost control consultation, this important development about the introduction of an interim cost control for the GB RHI should have been the subject of a formal submission, especially as it had been considered important enough for Ms Hepper to seek the advice of the Deputy Secretary, Mr Thomson.
81. Ultimately, the Inquiry found that the absence of any such submission/minute/record was significant evidence in support of the conclusion that the warning had not been highlighted by Ms Hepper. If it had been highlighted, the Inquiry is satisfied that the Minister and/or her SpAd, if he had been present, should have then ensured that there was an appropriate minute or record; and that Energy Division officials would have wished there to have been such a record in order to demonstrate that any additional risk had been assumed by the Minister upon an informed basis.
82. The need for expediency and early delivery of a novel and volatile scheme cannot be used retrospectively to justify or explain the absence of a record of a conversation in which the Minister was said to have been referred to the emphatic warning from Ofgem. The absence of any written record was said to reflect the normal, but what the Inquiry considers unacceptable, practice of the time.
83. The failure to record what the Inquiry was told were interactions with the Minister over the June 2012 Ofgem warnings must be seen in the context of previous warnings about financial risks received by the relevant DETI officials engaged on the NI RHI scheme. Key messages appear to have been lost and not escalated to the Minister. The messages contained in the Parker, Clydesdale and Brankin email exchanges of April and May of the previous year were still highly relevant but had disappeared from view. So too with the messages from the 8 June 2011 email exchange between Mr Patel of DECC and Mr Hutchinson advising of the “large financial risk” posed by the nature of the funding.<sup>797</sup> This risk had persuaded DECC to proceed with interim cost controls and, ultimately, degeneration. Quite apart from the obvious practical danger of such details being left to the recollection of the respective individuals it seems to the Inquiry that the omission to put forward a relevant submission and keep a minute or record of the advice given and decision made placed Ms Hepper in breach of the requirements contained in paragraphs 13 to 18 and 37 to 39 of the then operative DETI Private Office Guidance.



## Chapter 13 – ETI Committee – consideration of RHI proposals

### The ETI Committee and its purpose

- 13.1 The Committee for Enterprise, Trade and Investment (ETI Committee) was a statutory committee of the Northern Ireland Assembly established in accordance with paragraphs 8 and 9 of Strand 1 of the Belfast Agreement, section 29 of the Northern Ireland Act 1998 and under Assembly Standing Order 48. The ETI Committee had a scrutiny, policy development and consultation role with respect to DETI and had a role in the initiation of legislation.
- 13.2 The Committee had power to:
- a. consider and advise on departmental budgets and Annual Plans in the context of the overall budget allocation;
  - b. approve relevant secondary legislation and take the Committee stage of relevant primary legislation;
  - c. call for persons and papers;
  - d. initiate inquiries and make reports; and
  - e. consider and advise on matters brought to the Committee by the Minister for Enterprise, Trade and Investment.
- 13.3 Statutory Rules (SR), including regulations implementing and governing the existence of schemes such as the NI RHI, must be laid before the relevant statutory committee. Such rules proposed by DETI are referred to and considered by the ETI Committee, which was created by a resolution of the NI Assembly in May 2011.<sup>798</sup> The functions of the ETI Committee are, in accordance with section 29(1)(a)(ii) of the Northern Ireland Act 1998, to “advise and assist” the Minister for Enterprise, Trade and Investment “with respect to matters within his responsibilities as a Minister.”<sup>799</sup> It consisted of 11 members drawn from all parties represented in the Assembly.<sup>800</sup>
- 13.4 The regulations relating to the NI RHI scheme were subject to a procedure in accordance with which the ETI Committee will, in most cases, provide a recommendation to the Assembly as to whether it should or should not approve the rules. Regulations are not the subject of detailed consideration and debate by the Assembly and, therefore, the careful and effective scrutiny by the ETI Committee is of particular importance.
- 13.5 Prior to receiving the text of the relevant regulations, the Committee is supplied with a document known as an SL1 letter, which is prepared by the relevant Department to assist the Committee and sets out the underlying policy. In addition, in order to inform the decision whether to recommend regulations, a Committee may take into account submissions made by interested parties and oral briefings from departmental officials. An officer of the Assembly known as the Examiner of Statutory Rules will advise the Committee with regard to technical issues, but not on the objectives or merits of the policy as contained in the relevant SR/regulations.<sup>801</sup>

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798 WIT-134010

799 WIT-134010

800 TRA-02954

801 WIT-134011

## The SL1 for the NI RHI scheme

- 13.6 The subordinate legislation document (SL1) provided by DETI in support of the proposed RHI regulations, dated 13 April 2012, consisted of five pages signed by Ms Hepper.<sup>802</sup> The function of the SL1 document is to set out the policy underlying statutory rules/regulations.
- 13.7 It referred to the CEPA economic appraisal, which had considered various options, and to the outcome of the public consultation. Five options were described to the ETI Committee including the Challenge Fund. However all the comments relating to that option were relatively adverse and, in particular, the administrative costs were said to be prohibitive as far as DETI was concerned. No reference was made to the significant overall economic advantage offered by that option as opposed to the incentive scheme, or to the protection that it offered against potential overspending.
- 13.8 In fact, the section dealing with the specifically tailored NI RHI scheme opened with the (by now familiar) inaccurate statement that “The NI RHI option offers the highest potential renewable heat output at the best value.” The Committee was informed of the available £25 million of HMT funding but no reference was made to the associated risk to the DEL budget of overspend.

## The ETI Committee’s consideration of the NI RHI scheme proposal

- 13.9 The ETI Committee, chaired at the time by Alban Maginness MLA, first considered the SL1 for the proposed RHI regulations 2012 on 19 April 2012, when it was resolved to seek further information from DETI relating to payments to participants, tariff levels, calculation of tariffs, a summary of consultation results and incentives for domestic installations.<sup>803</sup> DETI’s response was considered at a meeting on 17 May when it was decided to await the outcome of an exchange with the EU Commission and to organise an oral briefing from DETI.<sup>804</sup>
- 13.10 On 24 May the ETI Committee received an oral briefing from Ms McCutcheon and Mr Hutchinson, which included a general discussion of the initial phase of the non-domestic RHI scheme and the proposed second phase that would include introduction of a domestic RHI scheme. They were also briefed about tariff levels, although DETI was only able to produce ‘indicative’ tariff figures as part of what the officials described as a “parallel process” seeking to obtain both EU Commission and ETI approval before the Assembly’s summer recess. The ETI Committee indicated that it was not willing to agree the SL1 without sight of the final tariff figures.<sup>805</sup>
- 13.11 On 5 July 2012 the DETI Minister notified the ETI Committee that EU approval had been received. It was then agreed, at a meeting on the same day, to receive a further oral briefing from DETI and that the views of Action Renewables would be sought. Action Renewables is an organisation originally set up by DETI to aid with the development of renewable policy, but which is now an independent body with charitable status.
- 13.12 On 13 September the ETI Committee received a further briefing from Ms Hepper, Ms McCutcheon and Mr Hutchinson. The Committee expressed concerns about monitoring and review but was assured by the officials that the electronic system used to operate the scheme would produce weekly and monthly statistics and that figures relating to energy use and cost

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802 ETI-05984 to ETI-05988

803 WIT-134551

804 WIT-134551

805 WIT-134551 to WIT-134552

would be published quarterly on the DETI website. The DETI officials described the project as “a living scheme we will keep under active review.”<sup>806</sup>

- 13.13 The ETI Committee also considered the response from Action Renewables, which was supportive of the proposals. Nevertheless, the response contained the following portentous warning regarding the banding of the tariffs:

“The significant drop in biomass support, from 5.9 to 1.5p/kWh at the 100kWth level, will create distortion in the market. It will lead to applicants installing boilers with a smaller capacity than is required, at the 100kW level and supplementing their heat from oil generation, as it will be the most remunerative way of exploiting the scheme.”<sup>807</sup>

- 13.14 By September 2012 Mr Patsy McGlone had taken over as chair of the ETI Committee. He considered that the control of any such distortion would be an operational matter for DETI, but confirmed that no further action was taken by the ETI Committee to explore this or to ensure that it was being addressed by DETI, although he too gave evidence to the Inquiry that the ETI Committee had been assured by DETI that the operation of the scheme would be kept under “active review”.<sup>808</sup>

- 13.15 Mr McGlone did also come back to this concern on the part of Action Renewables in his speech to the Assembly on 22 October 2012 in support of a motion to approve the 2012 NI RHI regulations. In the presence of the DETI Minister he indicated that it was something about which DETI might wish to consult and that the ETI Committee had been assured by DETI officials that the scheme would have “scheduled reviews built in to ensure that it remained fit for purpose and provided value for money.”<sup>809</sup> He said “Clearly the Committee will pay particular attention to the reviews”, but he told the Inquiry that the function of the ETI Committee was scrutiny and that it was not a management body for DETI.<sup>810</sup> He did not recall any mention at the ETI Committee’s briefing meeting with Ms Hepper, Ms McCutcheon and Mr Hutchinson on 13 September 2012, of the warnings raised by Ofgem relating to potential shortcomings in the GB and NI regulations, the need for effective cost controls and, in particular, the advice to await the outcome of the GB proposals to adopt interim cost controls. Mr McGlone conceded that the ETI Committee did not preserve the Action Renewables’ warning in a file for future reference. In retrospect he said that he wished there had been further probing of the description of the reviews as “built in”.<sup>811</sup>

- 13.16 Mr McGlone drew the attention of the Inquiry to the lack of resources available to the ETI Committee:

“...where you have four members of staff servicing the needs of a Committee which covers virtually every aspect of the economy...who are helping you to wade... through all that stuff. ...the Clerk that we had was very good at his job and, if we just had a few more resources and a few more personnel to help us do our job, it would make things a whole lot easier.”<sup>812</sup>

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806 WIT-134552

807 WIT-134011

808 WIT-134554

809 TRA-03035 to TRA-03037

810 TRA-03037 to TRA-03038

811 TRA-03017 to TRA-03040

812 TRA-14639 to TRA-14640

- 13.17 Mr McGlone highlighted the difference between a Department and the ETI Committee, with the former having “400” members of staff while “we’re sitting with 4 good members of staff.” He emphasised how fundamental it was for the ETI Committee to have a free flow of comprehensive and open information.<sup>813</sup> With hindsight, he considered that the evidence presented to the ETI Committee by DETI presented “a very poor picture” compared to that which had emerged before the Inquiry.<sup>814</sup>
- 13.18 The Inquiry notes the frustration expressed in evidence by Mr McGlone about the unsatisfactory practice that often left the ETI Committee without the timely and relevant information that was needed by it to carry out its statutory functions to hold the Department to account and challenge policy proposals. Mr McGlone told the Inquiry that the ETI Committee was “utterly reliant” upon the professionalism of the department officials concerned and, in a written statement, he emphasised that the ETI Committee depended upon being supplied by DETI with all the relevant facts and information.<sup>815</sup>

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813 TRA-14711 to TRA-14713

814 TRA-02956

815 TRA-02959 to TRA-02962

## Findings

- 84. In relation to briefings linked to the NI RHI SL1, the ETI Committee was provided by DETI Energy Division officials with incomplete and inaccurate information about the RHI scheme; among other omissions, information was not included about risks that DETI had been made aware of by Ofgem.**
- 85. The ETI Committee expressed a number of concerns and received third party advice about a number of risks (for example, information from Action Renewables); nevertheless they accepted the assurances provided by DETI and did not follow up on these concerns or check that DETI was delivering what had been promised.**
- 86. The Inquiry finds that the ETI Committee was not provided with sufficient/adequate information to permit the ETI Committee to effectively discharge its scrutiny function.**





## Chapter 14 – The development of the NI RHI regulations and the launch of the NI RHI scheme

### Developing the NI RHI regulations

- 14.1 Following a competitive tender in the first quarter of 2011 the private law firm of Arthur Cox solicitors was appointed to provide legal advice to DETI on energy matters in Northern Ireland.<sup>816</sup> Arthur Cox had expertise in that area and was able to utilise it in providing general advice to DETI about a number of policy areas. However, in relation to the proposed NI RHI scheme the principal task required of Arthur Cox by DETI was to draft the NI Renewable Heat Incentive regulations based on the equivalent regulations in GB, subject only to any changes that were specifically required for the Northern Ireland jurisdiction.<sup>817</sup>
- 14.2 Mr Bissett, who was in charge of the relevant legal team at Arthur Cox, told the Inquiry that, at the first RHI-related meeting with DETI officials in May 2011, he was told that any NI RHI regulations would have to stick very closely to or mirror those in GB in order to benefit from a discount in administration costs from Ofgem.
- 14.3 The DETI team at that meeting was led by Ms Clydesdale and included Ms McCutcheon and Mr Hutchinson.<sup>818</sup> Arthur Cox had not been involved in the policy development described earlier in this Report. They were informed that any diversion from the GB regulations would result in an additional charge by Ofgem, who were to administer the scheme, so they should limit any amendment(s) to details that were relevant to Northern Ireland and to references to relevant Northern Ireland legislation. The DETI team gave specific instructions that DETI would be responsible for any policy diversion from the GB scheme.<sup>819</sup> They were provided with the then current draft of the GB RHI regulations which had been prepared in March 2011.<sup>820</sup> Mr Bissett was informed by Ms Clydesdale of the options being considered by DETI, namely a Challenge Fund or an NI RHI and that new regulations would be required if the latter scheme were to be adopted.<sup>821</sup>
- 14.4 DETI also sought assistance from the Northern Ireland Government Legal Service’s Departmental Solicitor’s Office (DSO). On 15 August 2011 Mr Hutchinson emailed Paul McGinn at DSO, copying in Mr McGinn’s DSO colleague Nicola Wheeler, as well as DETI’s Ms Hepper, Ms McCutcheon, and Susan Stewart. Mr Hutchinson provided a general history of the NI scheme to that point and sought confirmation that DSO was content with an enclosed draft of the proposed NI RHI regulations. He also indicated that it would be helpful to have assistance from DSO with regard to facilitating the process of bringing the regulations into force.
- 14.5 The draft had been prepared by Arthur Cox and the Inquiry notes that its schedule of tariffs included the GB provision relating to tiering of the tariff for medium biomass boilers.<sup>822</sup> The DSO was not asked to advise on any particular issues or specific provisions within the draft.

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816 WIT-28212

817 WIT-28213

818 TRA-02867 to TRA-02868

819 TRA-02871 to TRA-02872

820 TRA-02874

821 WIT-28223 to WIT-28224; DFE-15374

822 WIT-01006 to WIT-01046

The core expertise of DSO lies in the field of public law.<sup>823</sup> Advising as to merits or policy content, such as methods of cost control, was not part of its responsibility given its limited resources.

- 14.6 Ms Wheeler became the solicitor primarily concerned on behalf of DSO and she understood that her role would be to check the legal implications for the Northern Ireland jurisdiction, while assistance with policy advice would be a matter for Arthur Cox, which had the relevant energy expertise.<sup>824</sup> She made it clear in her response of 3 October 2011 to Mr Hutchinson, enclosing her notes on the draft regulations, that she could not comment on the technical nature of the document as she did not have the requisite experience. She was merely checking the drafting to ensure that the conventions commonly used in Northern Ireland were applied and that Northern Ireland legislative definitions and references were correct.<sup>825</sup>
- 14.7 On 15 May 2012 Ms Wheeler provided some advice on the use of the term “Authority” in the regulations and she was sent a further draft by Mr Hutchinson in October that he explained had been produced in conjunction with Arthur Cox and Ofgem.<sup>826</sup> The Inquiry notes that the draft schedule of tariffs now contained a single tariff of 5.9p/kWh for medium biomass boilers, which was not subject to tiering.<sup>827</sup>
- 14.8 During the development of the various drafts of the regulations DETI passed on to Arthur Cox comments and suggestions from the legal department of Ofgem and the DSO. These were then incorporated by Arthur Cox. Arthur Cox was told that in the light of Ofgem’s role in administering the scheme their comments should be incorporated and that DSO would have the final sign-off on the form that the regulations were to take.<sup>828</sup> Mr Bissett told the Inquiry that Arthur Cox was not furnished with a copy of the Ofgem legal review document of 26 November 2011 until March 2012.<sup>829</sup> Mr Bissett was told that DETI wanted to “follow behind GB not lead GB” and that there was no scope to move away from GB. His task was simply to review any item that applied specifically to Northern Ireland and advise whether it could be quickly completed.<sup>830</sup>
- 14.9 Mr Bissett told the Inquiry that his firm produced a number of drafts of the regulations incorporating amendments to the GB regulations and the comments from Ofgem and DSO.<sup>831</sup> He believed that the first draft they prepared and supplied to DETI in early July 2011 was to be published as part of the documentation for the DETI public consultation in July 2011. That draft followed the GB regulations by including tiering of tariffs (regulation 37(9) and Schedule 3 of the GB Regulations of 2011). He later discovered that the Arthur Cox draft had not been used for the consultation. Instead a draft compiled by Mr Hutchinson had been published which did not include the tiering provision (or tiering of the tariffs in the draft tariff schedule). That provision was also absent from a further draft in October 2011, again compiled by Mr Hutchinson. The tiering provision was also removed by Energy Division from an Arthur Cox draft of 18 May 2012.<sup>832</sup> Upon that occasion Mr Bissett received an email from Susan Stewart of DETI

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823 WIT-28617 to WIT-28619

824 TRA-02810 to TRA-02812

825 WIT-01185 to WIT-01236

826 DSO-01047 to DSO-01048; DSO-00690 to DSO-00727

827 DSO-00721

828 WIT-28220

829 TRA-02884 to TRA-02885; DFE-66112

830 TRA-02895

831 WIT-28217

832 TRA-02875 to TRA-02878

informing him that the tariffs and banding provisions should be treated as “restricted” and were not to be disseminated.<sup>833</sup> Mr Bissett told the Inquiry that, prior to Ms Stewart’s email, the Arthur Cox team had not been informed of these developments and that no discussion had taken place about the use of the DETI drafts or the omission of the tiering provisions.<sup>834</sup>

- 14.10 In March 2012 Ms Hepper emailed Jim McManus, Clerk to the ETI Committee, informing the Committee of the intention to bring the draft regulations into force.<sup>835</sup> The SL1 was sent to Mr McManus on 13 April and the Minister signed the relevant Regulatory Impact Assessment on the same date.<sup>836</sup> On 18 April Ms Hepper sent a submission to the Minister, her SpAd and the Permanent Secretary seeking approval for the appointment of Ofgem as the administrator of the scheme, which was endorsed by the Minister on 24 April.<sup>837</sup>
- 14.11 Mr Bissett told the Inquiry that he did not see a copy of the GB RHI amendment regulations of July 2012 until September 2012, nor was he told of the warning from Ofgem delivered during the 26 June 2012 teleconference (discussed in chapter 12 of this Report). Upon seeing the GB RHI amendment regulations, he noticed the interim cost control provision and assumed that the provisions had not been seen by DETI and he sent them a copy by email, dated 11 September, asking whether, in keeping with the established policy of consistency with GB, the changes should be incorporated into the draft NI RHI regulations.<sup>838</sup> It appears that he then received an email from Ms Stewart informing him that DETI was being pressed on finalising these regulations as soon as possible and asking him to attend a meeting to discuss various RHI issues.<sup>839</sup>
- 14.12 The meeting took place on 18 September 2012 at DETI’s offices at Netherleigh, Belfast and Mr Bissett told the Inquiry that the GB RHI amendment was the first item he discussed. He said that he was told, as far as he can recollect by Mr Hutchinson, that, because it was an interim measure and DETI knew that DECC was going to consult on a long-term measure for cost control, they wanted to await the outcome of that consultation and, in the meantime, skip the step of having interim cost controls. He was told that DETI intended to introduce permanent cost controls as part of Phase 2 of the RHI scheme. Mr Bissett told the Inquiry that this struck him as a “plausible” reason which he accepted, although he was surprised in that it seemed contrary to the approach based on following and benefitting from GB and DECC experience, which had been the requirement for the past 18 months.<sup>840</sup>
- 14.13 Ms Wheeler at DSO was asked to check a further draft of the proposed regulations in October 2012, which she did, once more confirming that commenting upon the technical nature of the provisions was outside her remit.<sup>841</sup> She was not provided with the July 2012 GB RHI Amendment Regulations, which contained an interim system of cost control and which had been the subject of discussion between Ofgem and DETI, and between Arthur Cox and DETI. She told the Inquiry that, had she been so provided, she would have pointed out that any significant deviation from GB would have required a “very good reason.” She added that,

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833 DFE-17570 to DFE-17571

834 TRA-02880

835 DFE-70014 to DFE-70019

836 ETI-05984 to ETI-05988; DFE-67455 to DFE-67466

837 DFE-143899 to DFE-143920; DFE-32178 to DFE-32180

838 TRA-02913 to TRA-02914; DFE-67951

839 DFE-19648

840 TRA-02914 to TRA-02918

841 DSO-00690; DSO-00777 to DSO-00778

normally, she would ask a client Department for the most up-to-date legislation and in any event check the legislation website herself. She regretted that she had not done so in this case.<sup>842</sup>

- 14.14 Mr Bissett emphasised that throughout all of his work for DETI on the NI RHI scheme the timescales were very short and everything had to be done very quickly, often at “breakneck” speed.<sup>843</sup>

### The November 2012 launch of the NI RHI scheme

- 14.15 On 17 October 2012 Ms McCutcheon lodged a submission with the DETI Private Office relating to the Assembly Motion that the Minister needed to move for the approval of the NI RHI regulations.<sup>844</sup> The Minister was informed that all approvals were in place for the NI RHI, that the draft NI RHI regulations had already been laid at the Assembly on 9 October 2012, and that the Minister was to present the draft NI RHI regulations for affirmative resolution to the Assembly on 22 October 2012.
- 14.16 Along with the submission the Minister was provided (as a series of annexes to the submission) with draft speeches, a briefing document on questions and answers on the NI RHI, the draft NI RHI regulations and the Explanatory Memorandum, and a draft press release. Paragraph 3 of the submission explained that Ms McCutcheon and Mr Hutchinson would be in attendance at the Assembly to provide briefing for the Minister on the NI RHI regulations and on any wider energy issues that might arise during the debate.
- 14.17 The submission, and its accompanying documents, did not contain any reference to Ofgem’s warnings about the NI RHI regulations replicating flaws from GB. Nor was there any mention of the issue of budget control, in any form. For instance, the questions and answers briefing document prepared for the Minister did not pose any question about the GB RHI interim budget control introduced in GB in July 2012, nor consequently suggest any corresponding answer as to why DETI’s draft NI RHI regulations did not have any such or similar mechanism. If some Assembly Member had known of those GB developments, and posed questions on the floor of the Assembly during the debate, the Minister would not have had the answer in the material with which she was briefed.
- 14.18 As it turned out, when the Minister did move the draft NI RHI regulations for approval before the Assembly on 22 October 2012 no such question was posed. All those who spoke in the Assembly debate broadly welcomed the proposals and the Assembly approved the draft NI RHI regulations.
- 14.19 The Minister herself admitted in her oral evidence to the Inquiry that she did not believe that she had actually read the draft NI RHI regulations by the time she was moving the Assembly motion, rather that she would probably have read the accompanying explanatory note.<sup>845</sup>
- 14.20 The Inquiry considers that the decision by Ms Hepper and her team not to adopt relevant developments from GB, but to await the outcome of the development of a more permanent form of budget control, was certainly a high-risk strategy in light of the well-reasoned DECC consultation document of March 2012 dealing with interim budget control, the warning from

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842 TRA-02844 to TRA-02845

843 TRA-02918 to TRA-02919

844 DFE-33111 to DFE-33166

845 TRA-07874

Ofgem in June 2012, and the GB RHI amendment regulations of July 2012, none of which, as discussed earlier in this Report, featured in a submission to the Minister at any stage.

- 14.21 Minister Foster accepted in her evidence to the Inquiry that her approach had been that the NI RHI scheme should proceed “as soon as possible” because it was lagging behind its GB equivalent and it had a budget available.<sup>846</sup> She stated that she trusted the combination of DETI officials, including departmental economists, and Ofgem to put into effect robust measures of cost control to ensure that budgets were not exceeded.<sup>847</sup> There had been some slippage of the anticipated commencement of the NI RHI scheme from April to October 2012 and the Minister was aware of DETI’s limited resources but, even in that context, she emphasised in her evidence to the Inquiry that she would not have anticipated that officials would ignore warnings or proceed with a scheme that was inherently flawed. Minister Foster would have expected the Ofgem warnings to have been “clearly and straightforwardly” brought to her attention in a formal submission, which she could have brought to the attention of her SpAd, so as to enable her to reach a properly informed decision as to whether the scheme was fit for purpose.<sup>848</sup>
- 14.22 Equally, Minister Foster accepted in her oral evidence that she could have been more curious. She could have asked for a follow-up note or submission on the back of a conversation with an official and that does not appear to have happened in this case, most probably because she did not feel the subject required it.<sup>849</sup> As discussed previously, she had no recollection of the telephone conversation that Ms Hepper said had taken place in June 2012 or of being clearly told about the Ofgem legal review of November 2011, or the warning about GB’s intention to adopt interim cost control.<sup>850</sup>
- 14.23 The NI RHI regulations duly came into force on 1 November 2012.<sup>851</sup> They established a system under which applications to benefit from subsidy were to be made after installation and, if properly made, **must be accredited** (the Inquiry’s emphasis). They created an unpredictable, volatile, demand-led scheme in which demand might increase with little or no warning. Nevertheless, the NI RHI regulations did not include any budgetary cost controls or tiering of subsidies. There was no statutory obligation to review the scheme and no emergency stop mechanism. There was no definition of “useful heat”. Nor was there any definition of a “heating system” that would serve to exclude multiple, small separate boilers being used in the same space/area to take advantage of the most lucrative tariff in a scheme in which DETI was subject to a statutory obligation to pay participants once an installation was accredited.
- 14.24 When the NI RHI scheme launched on 1 November 2012 the Arrangements for the administration of the scheme between DETI and Ofgem had still not been finalised. The Arrangements were not in fact executed until 28 December 2012. The development of the Arrangements is discussed in the next chapter.
- 14.25 In December 2012 Ms Hepper confirmed to the DETI Top Management Team and the RHI Casework Committee that Ofgem had revised upwards its annual administrative costs forecasts, and the revised total operating costs of administering the NI RHI scheme during the first four years would be in the region of £870,000, assuming an uptake in NI of 3-5% of the GB RHI

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846 WIT-20580

847 WIT-20579

848 WIT-20580

849 TRA-07829 to TRA-07830

850 TRA-08238 to TRA-08263

851 LEG-00001 to LEG-00035

scheme.<sup>852</sup> This was an increase of some 16% from the forecast operating costs that had been set out in the December 2011 Feasibility Study, and advised to the Casework Committee. Ofgem had previously also required DETI to underwrite a legal contingency fund of £1 million per year during the operation of the scheme.<sup>853</sup>

- 14.26 Ms McCutcheon and Mr Hutchinson had responsibility for management of the relationship with Ofgem in order to ensure service was delivered and within the agreed budget. During the initial operation of the scheme they received a weekly spreadsheet with information provided by Ofgem including data on applications/accreditations, the type of technology, and eligibility standards. On a monthly basis, information was provided indicating the submitted heat data from meter readings and the payments required but, as discussed in chapter 45 of this Report, crucially this did not include sufficient data about ownership and location of applicants to monitor and analyse the scheme for exploitation issues, like multiple boilers.<sup>854</sup>

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852 DFE-144168 to DFE-144169; WIT-09187 to WIT-09189

853 WIT-09158 to WIT-09159

854 WIT-06092 to WIT-06093

## Findings

87. Drafting of the regulations was divided between three organisations: DETI and two sets of legal advisers, Arthur Cox and the Departmental Solicitor's Office. Advice and comments had also been provided by Ofgem. DETI's poor co-ordination and management of communication between those involved created a significant risk of important information falling between the cracks.
88. Arthur Cox, the external solicitors, had included a provision for tiering of tariffs as part of their wider remit to mirror the GB scheme. They were not informed that this provision had been removed from their draft by DETI officials until 18 May 2012. This was not discussed with Arthur Cox; it ought to have been.
89. Mr Bissett of Arthur Cox told the Inquiry that he and his team did not receive a copy of the Ofgem legal review of November 2011 until March 2012. DETI ought to have provided it to Arthur Cox at an earlier stage.
90. The reasons given for decisions not to adopt important DECC GB RHI amendments appear to have been a commitment to the Minister to bring the NI RHI regulations into force by the autumn of 2012 and an associated concern about a potential adverse impact of delay upon access to HMT funding.
91. It is clear that DETI, no doubt in company with other Departments of the devolved administration, was anxious to ensure that any funds available to encourage technological development and employment in Northern Ireland should not be lost but, by way of balance, proper precautions should have been taken to ensure that such funds were effectively managed and protected.
92. The lack of resources in Northern Ireland, particularly in comparison to DECC, actually justified or enhanced the need to "mirror" GB. Successive amendments to the GB scheme from 2012 onwards had the benefit of DECC's scale and scrutiny arising from their greater resources – technical, legal, economic and otherwise.
93. The Inquiry accepts that DETI had a small RHI team, without any real degree of relevant specialist expertise, subject to serious pressure of work and lack of resources. However, a number of issues of scheme design, for example the changes referred to in the Ofgem legal review (November 2011) and DECC's interim cost control proposal (March 2012), were undoubtedly of such significance in the context of a new, volatile, unpredictable and unusually funded policy that they clearly required to be escalated to the highest level for transparent, fully informed and appropriately recorded decisions.<sup>855</sup>
94. Energy Division officials gave priority to speed. They pressed on with the scheme, putting off dealing with Ofgem's recommendations and justifying that as due to pressure from the Minister without explicitly obtaining Mrs Foster's written agreement to this approach and its associated risks.

**95. Minister Foster told the Inquiry in her oral evidence that she did not read the regulations, although she did read the explanatory notes.<sup>856</sup> The Inquiry considers that the Minister, in presenting the regulations to the Assembly and asking for their approval, should have read them herself, not least because in the Inquiry’s view to do so is a core part of a Minister’s job. If she and/or her SpAd had read the regulations, this might well have made no difference to the outcome; but if they had done so, or taken a more active interest in the development of the regulations, this would have provided an opportunity for each of them to see that, particularly with regard to the submission that she had received on 16 March 2012, there were no reviews ‘built-in’ to the regulations (as had been the case in the NIRO regulations), there was no definition of ‘useful heat’, and no form of budget control had been included.<sup>857</sup>**

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856 TRA-07874

857 DFE-31747 to DFE-31772



## Chapter 15 – Ofgem arrangements with DETI

- 15.1 At the end of the last chapter mention was made of how, at the time the NI RHI scheme was launched in November 2012, the document formally establishing the relationship between DETI and its NI RHI scheme administrator, Ofgem, had not been executed.
- 15.2 As is inevitably the case on occasions, given the number of intertwining events and issues developing at the same time, it is necessary to look back from the point reached in the overall chronological development of the NI RHI scheme to understand how a specific issue arose.

### The 18 April 2012 submission to appoint Ofgem via a contractual Agency Service Agreement

- 15.3 On 18 April 2012 Ms Hepper sent the then DETI Permanent Secretary and Accounting Officer, Mr Sterling, a submission in respect of the appointment of Ofgem to administer the NI RHI scheme.<sup>858</sup>
- 15.4 The submission attached the business case for the appointment, which already contained an approval obtained from the Central Procurement Directorate (CPD), the directorate within DFP that assisted with Government procurement matters. The business case referred to a Direct Award Contract and an Agency Services Agreement with Ofgem.
- 15.5 The submission itself referred throughout to a “contract” with Ofgem and “formal contractual arrangements with Ofgem”, which were to be via an Agency Services Agreement. Ofgem would then be treated by DETI as an External Delivery Organisation.
- 15.6 The submission sought Accounting Officer approval of the business case and his authorisation for the appointment of Ofgem. Mr Sterling provided the required approval and authorisation on the same date.<sup>859</sup> As mentioned earlier in the Report, the business case submission was then provided to the Minister’s Private Office on 18 April and approved by Dr Crawford on 23 April.<sup>860</sup> Minister Foster confirmed that she was “content” with the submission on 24 April 2012.<sup>861</sup>

### Ofgem’s different roles under the GB and NI RHI regulations

- 15.7 The mechanism by which the relationship between DETI and Ofgem was created differed from that between DECC and Ofgem in respect of the GB RHI scheme. Paragraph 2.1 of the explanatory memorandum accompanying the equivalent 2011 GB RHI regulations explained that the GB RHI regulations conferred functions directly on the Gas and Electricity Markets Authority (GEMA) to administer the GB RHI scheme. The GB RHI regulations referred to GEMA (Ofgem for our purposes) as “the Authority”.<sup>862</sup> The regulations then set out the role, powers and responsibilities that Ofgem had.

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858 DFE-315740 to DFE-315761

859 DFE-143926 DFE-143926

860 DFE-143926

861 DFE-143926

862 LEG-00987

- 15.8 In contrast, although the explanatory memorandum accompanying (and published with) the 2012 NI RHI scheme regulations, said, in paragraph 2.1,<sup>863</sup> that the NI RHI regulations would give functions to Ofgem to administer the NI RHI scheme, the regulations did not in fact do that. Instead, the 2012 NI RHI regulations conferred all functions on DETI.
- 15.9 The explanatory note at the end of the 2012 NI RHI regulations (as opposed to the accompanying, and inconsistent, explanatory memorandum) stated that:
- “The Regulations confer functions on the Department in connection with the general administration of the scheme.”<sup>864</sup>
- 15.10 As discussed previously, the 2011 Energy Act was the enabling legislation which had provided DETI with the power to make regulations establishing the NI RHI scheme. Section 113 of the 2011 Energy Act had provided power to DETI to make regulations that would confer various functions on either DETI or the Northern Ireland Authority for Utility Regulations (each was referred to in section 114 as a “Northern Ireland authority”). Section 114 then provided that:
- “GEMA and an NI authority may enter into arrangements for GEMA to act on behalf of the NI authority for, or in connection with, the carrying out of any functions that may be conferred on the NI authority under, or for the purposes of, any scheme that may be established under section 113.”<sup>865</sup>
- 15.11 This meant that a different set of arrangements would be necessary to engage Ofgem to administer the NI RHI scheme. To develop these “arrangements”, between June and September 2012, there were regular teleconferences between Ofgem officials, Mr Hutchinson and Ms McCutcheon.<sup>866</sup>

## The development of the Arrangements

- 15.12 The December 2011 Feasibility Study had proposed, in paragraphs 2.5 and 2.6, that the relationship between Ofgem and NIAUR was to be set out in an Agency Services Agreement.<sup>867</sup> However, even though this was the form of a relationship it already held with the relevant authority in Northern Ireland (NIAUR) in respect of the NIRO, Ofgem adopted a different position in respect of the NI RHI scheme. As discussions ensued, Ofgem became wary of using the term “Services Agreement”, which it felt might compromise its legal obligations and status as an independent regulator. That was despite the fact that Ofgem was not acting as a regulator for the NI RHI scheme. In this regard Ms Hepper pointed out that one of the differences between the GB and NI schemes was that Ofgem did not have a statutory role in NI as it had in GB. She also explained, as the Inquiry has noted, that a service agreement was already in operation for Ofgem’s administration of another renewable energy scheme, the NIRO, on behalf of the NIAUR.<sup>868</sup>
- 15.13 What ultimately emerged from the discussions were a set of bespoke administrative Arrangements, which created a relationship significantly different from that which had been

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863 LEG-00036

864 LEG-00032

865 DFE-67516

866 WIT-06032

867 OFG-126017 to OFG-126018

868 TRA-05246

set out in the 18 April 2012 DETI submission. They were not intended to be legally binding or to give rise to any legal rights or obligations between the parties. Instead, clause 1.4 provided that:

“...both parties will endeavour to comply with the provisions of these Arrangements.”<sup>869</sup>

The clause then continued in the following terms:

“For the avoidance of doubt, nothing in these Arrangements is intended to, or will be deemed to, give rise to a relationship of agent and principal between the parties or overrides or is intended to pre-empt the ability of either party to discharge any of its powers or duties that arise as a matter of law.”<sup>870</sup>

15.14 DETI’s limited number of retained functions were stated in the Arrangements to be those contained in regulations 36(8), 47(1)(a), 50 and 51 of what was to become the 2012 NI RHI regulations, while Ofgem was to carry out all functions that were not retained.<sup>871</sup>

15.15 There remained a conceptual difference between the parties, particularly as regards DETI’s entitlement to oversight of Ofgem’s work. DETI, having given assurances to the March 2012 Casework Committee on setting key performance indicators and ensuring a right to audit Ofgem’s administration of the scheme, was insistent that these should be included in the Arrangements. This was also captured in a letter from Ms Hepper to Mr Harnack in November 2012 wherein she stated:

“As discussed this morning and previously with Joanne, it is vital that performance indicators are included at least in the covering letter to demonstrate the expected service that will be provided by Ofgem on receipt of the agreed funding.”

“...we just need to be clear about what DETI Audit will expect to see. On a high level, we will need to be able to confirm that the monies paid to you on a monthly basis to fund tariff payments for accredited installations are being transferred correctly and accurately to the appropriate installer. To confirm this, we will need sight of the records showing this money trail.”<sup>872</sup>

15.16 DETI was clear that Ofgem was acting on its behalf to provide a service. Ms Hepper summarised her view on this in her oral evidence to the Inquiry:

“We were dealing with ... a service delivery wing of Ofgem, so they were delivering a service to us that we were paying for. Therefore, we wanted to see aspects of performance and how it was being taken forward in a set of KPIs.”<sup>873</sup>

“It still to me, to this day, seems peculiar that there is a wing called E-Serve, which is a service delivery function, which sits slightly separately from their regulatory side, and, yet, they put the umbrella over the two.”<sup>874</sup>

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869 OFG-161839

870 OFG-161839

871 LEG-00020 to LEG-00028

872 OFG-09924

873 TRA-05246

874 TRA-05254

15.17 However, Ofgem sought to maintain what it considered to be the necessity of its independence and, although it agreed to provide some data regularly, fought against being subject to any performance indicators set by DETI, (see also chapter 47 of this Report). It also objected to its activities being subject to independent audit by DETI. Ofgem emphasised that its role endowed it with “ownership” of all functions that were not specifically reserved to DETI under the terms of the 2012 NI RHI regulations. This was summarised by Ofgem lawyer Marcus Porter, who stated that Ofgem had stepped:

“...into the shoes of DETI and taken over their role completely – no less than would have been the case had we been appointed directly in the legislation and there had been no mention of DETI at all.”<sup>875</sup>

15.18 Ofgem’s belief that it had now taken over the role and was “at the helm” was clearly embodied in the draft Arrangements with regard to paragraph 5.2, where it proposed a very one-sided process for dispute resolution regarding administration costs:<sup>876</sup>

“If any dispute arises as to the amount of Administration Costs payable by DETI to GEMA in relation to a given month, the same shall be referred to GEMA’s Chief Operating Officer for settlement and the adjudication of GEMA’s Chief Operating Officer shall be final.”<sup>877</sup>

15.19 The development of the administrative Arrangements therefore proved difficult and, at times, bordered on the fractious and consequently were not executed until 28 December 2012. In an email to his Ofgem colleagues on 6 November 2012 Keith Avis, the project manager, remarked:

“I appreciate that the Northern Ireland renewable heat incentive was more of a petulant teenager than the cute baby brother of the GB regs.”<sup>878</sup>

15.20 In giving oral evidence to the Inquiry, Mr Poulton, who in 2014 became Ofgem E-Serve’s Deputy Managing Director, later Managing Director, described the relationship with DETI as that of “a customer” but that there was “also a partnership element”, thereby further reflecting the ambiguities contained in the administrative Arrangements.<sup>879</sup>

15.21 Looking back at this time, DETI’s Internal Audit Service report on the scheme, issued on 4 August 2016, noted that:

“...DETI was reliant on Ofgem for the administration and control of the Scheme that had inadequate oversight arrangements in place which lacked specific assurance on the management of risks in the NI Scheme.”<sup>880</sup>

15.22 DETI Internal Audit also noted that key performance indicators were not agreed between Ofgem and the Department for the administration of the scheme.<sup>881</sup>

15.23 Price Waterhouse Coopers (PwC) recorded in January 2017 at paragraph 4.24 in their ‘Heat 1’ report analysing the failings of the NI RHI scheme, that:

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875 WIT-104774

876 OFG-215625

877 DSO-04585

878 OFG-10183 to OFG-10184

879 TRA-09652

880 DFE-05388

881 DFE-05387

“Significant weaknesses have been identified in the governance arrangements between the Department and Ofgem. While there are Administrative Arrangements in place between the Department and the Gas and Electricity Markets Authority, Ofgem’s governing body, the Administrative Arrangements do not define responsibility for key elements of service delivery by Ofgem, including the provision of management information.”<sup>882</sup>

15.24 In paragraphs 4.25 to 4.30 of the same report PwC identified what it said were the following weaknesses:

- (i) a lack of documentation relating to monthly meetings between DETI and Ofgem;
- (ii) a lack of agreed key performance indicators for work undertaken by Ofgem;
- (iii) a lack of consideration of the specific risk profile associated with the Northern Ireland scheme and the need for additional controls; and
- (iv) a lack of periodic communication between DETI and Ofgem in respect of the audit process, specifically with regard to the results of site inspections undertaken and the impact of Ofgem resource constraints.<sup>883</sup>

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882 DFE-05553

883 DFE-05553 to DFE-05554

## Findings

96. The fact DETI began with the intention to enter into a direct award contract with its scheme administrator, in the form of an Agency Services Agreement, but ended up with a form of what was said to be non legally binding administrative Arrangements reflected significant differences in how DETI and Ofgem regarded their relationship in respect of the administration of the NI RHI scheme. The effect of this conceptual difference of view would continue to be felt during Ofgem’s administration of the NI RHI scheme, (see for example chapters 45 to 48).

## Chapter 16 – Monitoring the initial operation of the NI RHI scheme

- 16.1 As previously discussed, the NI RHI scheme launched in November 2012. Initial uptake of the scheme was slow, and the first applications did not occur until February 2013. In the first six months there were 11 applications (an average of fewer than two per month) and in the first year, 56 (an average of fewer than five per month).<sup>884</sup>
- 16.2 Ms Hepper left Energy Division in November 2013. From the start of the scheme in November 2012 until Mr Hutchinson left in May 2014 there were around 100 accreditations to the non-domestic RHI scheme.<sup>885</sup>
- 16.3 During 2013 and up until the point when staff changes occurred in the spring and summer of 2014, Energy Division’s Renewable Heat Branch consisted of five people. Ms McCutcheon, who did not work full time, and Mr Hutchinson who did, were responsible for monitoring the non-domestic RHI scheme and also the development of Phase 2 of the NI RHI. Phase 2 covered both changes to the non-domestic scheme and the development of a scheme for domestic users. There were three other staff members, (two full-time equivalents) all of whom worked on the Renewable Heat Premium Payment (RHPP), the interim scheme for domestic users pending the introduction of a domestic RHI. Mr Hutchinson told the Inquiry that, in addition to his RHI duties, he also worked on the RHPP for half a day to three quarters of a day a week providing a second check on payment approvals.<sup>886</sup>
- 16.4 Despite the fact applications to the non-domestic RHI scheme were initially very low, there were a number of imperatives for DETI to monitor ongoing performance of the RHI scheme, not least the assurances given to the Casework Committee, DFP and the ETI Committee. State Aid approval had also included requirements to monitor production costs and adapt as necessary to avoid over-compensation.<sup>887</sup> In addition, the NIGEAE (the guidance under which the scheme had been approved) set out clear requirements for monitoring and evaluation (Step 9 of 10), with a requirement for there to be a monitoring plan in place for the chosen scheme.<sup>888</sup>
- 16.5 DETI received information from Ofgem on a regular basis:
- (i) Each week, Ofgem supplied a spreadsheet showing raw data derived from application forms, including the technology type of each installation, its installed capacity and the (anonymised) applicant’s estimate of the average weekly running hours. Information was also supplied as to whether and when an application was accredited.
  - (ii) Each month, Ofgem supplied to DETI a further spreadsheet with a different purpose, seeking DETI’s approval for payments to owners of accredited installations. This contained information of heat output and proposed payment against each accredited member’s code number, but no further identifying information.

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884 WIT-08442; WIT-06118

885 WIT-95150 to WIT-95151

886 TRA-04836

887 DFE-78137

888 INQ-50251 to INQ-50259

- 16.6 From the summer of 2013 onwards, initially for marketing reasons, DETI began asking Ofgem for more detailed information about applicants' locations. In the autumn of 2013, Ofgem shared with DETI the location of applicants, though only grouped by the first part of their post-code (e.g. BT34; BT47). This was included in the form of a map showing the distribution of applicants in the first (and it turns out only) annual report on the scheme from Ofgem. The map was subsequently seen by the Minister in approving an update to be sent to the ETI Committee in November 2013.<sup>889</sup>
- 16.7 Gaining more specific detail however took much longer due in large part to Ofgem's concerns about ownership of data and privacy. It was not until 2015 that information which was crucial for the detection of scheme exploitation through the use of multiple boilers, such as data relating to the names and addresses of applicants, was made available to DETI.
- 16.8 In addition to reviewing the material that he did receive from Ofgem, Mr Hutchinson maintained a summary spreadsheet in which he brought together information that he obtained from published sources about uptake in GB and similar types of information about uptake in NI, derived from the raw data supplied by Ofgem. This enabled him to track the NI uptake compared with GB uptake at a similar point in their scheme, adjusted on a *pro rata* basis. Such comparisons were used in updates to the ETI Committee.<sup>890</sup>
- 16.9 The Inquiry saw evidence that, towards the end of 2013 and particularly in early 2014, Mr Hutchinson was alert to some of the trends that emerged on the NI RHI scheme. For example, he became aware of increasing uptake of the scheme and the popularity of 99kW boilers by the end of 2013. His initial reaction however was to see this as a positive development, for as he told the Inquiry referring to 99kW boilers: "at least there's uptake in that band." The scheme at that stage, it seemed to him, was catching on and the task ahead was to achieve uptake for the other technologies and biomass boilers in other bands.<sup>891</sup>
- 16.10 It was only in late 2013/early 2014 that he started to be more conscious that there were virtually no applications for 200kW or 300kW boilers.<sup>892</sup> It was April or May 2014 before he pieced this together with other information to reach a view that action of some sort was needed.<sup>893</sup>
- 16.11 Not only was there an obligation upon DETI officials to monitor the scheme arising from the advice they had received, and consistent with assurances they had given, but under regulation 51<sup>894</sup> of the 2012 NI RHI regulations they also had an obligation to publish information about the scheme performance, the number of accredited installations, technology and capacity breakdown, the amount of heat generated and the total amount of payments. None of the DETI officials appear to have been aware of the requirements of this particular regulation, carried over from the GB RHI regulations. If they were so aware, they did not comply with its requirements.

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889 DFE-355680

890 WIT-06032; WIT-06060 to WIT-06061; WIT-06092 to WIT-06095; WIT-06116 to WIT-06120

891 TRA-04905

892 TRA-04908 to TRA-04909

893 TRA-05159

894 LEG-00027 to LEG-00028



16.12 Separate from any monitoring obligation arising directly from the NI RHI scheme, DETI also had an internal assurance process that operated on a six-monthly basis, requiring officials to identify and report problems in their work areas. In June 2013 CEPA, once again in conjunction with AEA, had provided a further report to DETI, following on from DETI's Phase 2 RHI work<sup>895</sup> (discussed elsewhere in this Report), which recorded that the desired target for the production of renewable heat (10% by 2020) was now unlikely to be reached.<sup>896</sup> However, the Energy Division six-monthly assurance statement for the period up to September 2013 did not record this potential problem in respect of the NI RHI scheme.<sup>897</sup> The same is true in respect of the following six-monthly assurance statement for March 2014.<sup>898</sup> Indeed, each of these documents, signed off by the Head of Energy Division, contained a positive tick against box 1.2 which recorded that "timely, relevant and reliable reports on progress against targets are produced and reviewed at the appropriate level to ensure that corrective action is taken as required."<sup>899</sup>

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895 DFE-349064 to DFE-349195

896 DFE-349074

897 DFE-312034 to DFE-312048

898 DFE388233 to DFE-388368

899 DFE-312035; DFE-388258



## Chapter 17 – Phase 2 of the NI RHI – the intended introduction of the domestic RHI and the expansion of the non-domestic RHI

17.1 Although not the primary focus of the Inquiry’s work, it is necessary to examine some aspects of the work relating to the domestic RHI scheme as some of the policy development and related key decisions were to have an important impact on the non-domestic RHI scheme. The following sections do not attempt to replicate the full evidence available on the domestic scheme, only to summarise those elements of particular relevance to the Inquiry’s Terms of Reference.

### RHPP and the commencement of work on Phase 2 of RHI

17.2 Almost immediately after the launch of the non-domestic scheme in November 2012 work began in earnest within the Renewable Heat Branch on Phase 2 of the NI RHI.

17.3 Phase 2 work included both the development of a domestic RHI scheme and extension of the non-domestic RHI scheme, as well as a number of other changes including the introduction of new technologies and a form of cost control intended to apply to the budget of both domestic and non-domestic NI RHI schemes.

17.4 An interim solution of grant support in the form of the RHPP scheme had been introduced in May 2012 for domestic consumers while DETI developed the non-domestic RHI scheme.<sup>900</sup> The RHPP was administered from within DETI’s Renewable Heat Branch.

### Developing the Phase 2 regulations

17.5 On 26 February 2013 a work request was sent to Arthur Cox by Mr Hutchinson regarding the development of regulations for the expansion of the non-domestic RHI scheme and the introduction of the domestic scheme.<sup>901</sup> Guidance was sought on developments in GB and the changes that had taken place with regard to the GB RHI regulations, which included the introduction of interim cost controls (which had been introduced in July 2012), and a consultation and Government response on the introduction of degression (the consultation launched in July 2012 and the DECC response was published in February 2013).

17.6 Advice and guidance was sought from Arthur Cox on recent and proposed future legislative changes in GB together with preparation of a first draft of regulations for Phase 2 of Northern Ireland’s RHI. DETI commissioned Arthur Cox to write a report reviewing the consultations carried out by DECC in relation to renewable heat, both domestic and non-domestic, and that report was issued at the end of March 2013. Mr Bissett told the Inquiry that it did seem odd to him that his firm was being asked to write a report reviewing the consultations undertaken and the legislation enacted by DECC in GB, but he assumed that the relationship between DETI and DECC was not good. Arthur Cox attempted to speak to DECC but formed the opinion that DECC were not “overly helpful”.<sup>902</sup> That appears to have been the only involvement of Arthur Cox in Phase 2 of the NI RHI domestic scheme.<sup>903</sup>

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900 TRA-02147 to TRA-02148

901 DFE-20434

902 TRA-02147 to TRA-02148

903 DFE-20434

## The June 2013 CEPA report

- 17.7 The Inquiry set out its examination of the CEPA reports from June 2011 and February 2012 in chapter 5 of this Report. In 2013 CEPA, with the assistance of AEA, was again commissioned to carry out the economic analysis for the introduction of the domestic RHI scheme<sup>904</sup> and the possible expansion of the non-domestic RHI scheme. CEPA was not asked to advise on the introduction of budget cost controls.
- 17.8 As noted elsewhere in this Report, the resulting CEPA analysis of June 2013 indicated that the 10% renewable heat by 2020 target would no longer be met by any of the options under consideration.<sup>905</sup> However, this significant information was never highlighted to the Minister despite the renewable heat target being contained within the NI Executive Programme for Government 2011-15.

## The 2013 cost control/budget control plan

- 17.9 Separately from the work CEPA was doing, budget control proposals were developed by Mr Hutchinson for both the non-domestic and domestic RHI schemes. Those proposals were set out in detail in the Phase 2 public consultation document, the Executive Summary of which included the following statement:<sup>906</sup>

“A method of cost control is to be introduced that will ensure budgets are not overspent and will hopefully remove the need for emergency reviews.”

- 17.10 The cost control proposal itself (though the Inquiry considers it may be better understood as a budget control) was found at paragraphs 4.12 to 4.16 of the consultation document:<sup>907</sup>

### “COST CONTROL

4.12 Given the introduction of tariffs for larger systems and the need to maintain confidence and consistency in the scheme DETI is proposing to introduce cost control measures that would ensure budgetary levels wouldn't be breached and to remove the need for emergency reviews or reductions in tariffs at short notice. DECC are in the process of introducing a system of tariff degression in GB whereby tariffs will automatically reduce when deployment levels reach set trigger points. DETI expect to introduce similar measures in the future but in the interim it is proposed that a simpler system is put in place.

4.13 The RHI is different in nature to the NIRO in that there is a finite budget for new installations and these budget limits cannot be breached. Whilst tariffs are designed to ensure that the budget is adhered to there is always a risk that renewable heat technologies might be deployed in greater numbers than what is forecast and payments exceed expectations. The risk of this increases as tariffs become available for larger technologies such as biomass over 1MW, biomass/bioliquids CHP and deep geothermal. Therefore DETI must retain the right to suspend the scheme if budget limits could be breached; however this will only happen at a last resort and, at this stage, is not envisioned to happen.

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904 DFE-88596 to DFE-88599

905 DFE-91772 to DFE-91773

906 DFE-97577

907 DFE-97607 to DFE-97608

4.14 In order to ensure confidence in the scheme continues DETI proposes to introduce a number of trigger points that will provide forewarning to potential applicants that the committed budget is nearing the set limit. The trigger points are set out in table below.

	<b>BUDGET LEVELS</b>	<b>ACTION</b>	<b>RATIONALE / FURTHER INFORMATION</b>
<b>TRIGGER 1</b>	50% of annual budget is committed	DETI will make a public notification of the committed budget.	So all applicants are aware of budget levels and potential DETI actions.
<b>TRIGGER 2</b>	60% of annual budget is committed	DETI will make a public notification of the committed budget and warn that the domestic RHI may need to close if the next budget trigger point is reached.	If the budget levels could be breached the domestic RHI will close first. The domestic sector contributes less overall renewable heat to the target and in general terms is less cost-effective than the non-domestic scheme.
<b>TRIGGER 3</b>	70% of annual budget is committed	DETI will make a public notification of the committed budget and will begin procedures to close the domestic RHI for the financial year.  The domestic scheme will remain open for new applications for 4 weeks after which no further applications will be accepted until the new financial year. Incomplete applications will be rejected.  Applications will re-open for the domestic scheme on 1 April.	The closure of the domestic RHI will be only until the new financial year and will not affect accredited applications.
<b>TRIGGER 4</b>	80% of annual budget is committed	DETI will make a public notification of the committed budget levels and warn that the non-domestic RHI may need to close if the next budget trigger is reached.  DETI will formally advise the administrator to prepare for closure.	When this level is reached DETI will begin processes to stop the non-domestic RHI however formal closure will not begin until the next trigger point.

	BUDGET LEVELS	ACTION	RATIONALE / FURTHER INFORMATION
<b>TRIGGER 5</b>	90% of annual budget is committed	<p>DETI will make a public notification of the committed budget and will begin procedures to close the domestic RHI for the financial year.</p> <p>The scheme will remain open for 4 weeks, with only schemes receiving full accreditation within this timescale being supported.</p>	<p>All applicants will be given 4 weeks to attain full accreditation with the administrator; this means having the system in place and ensuring the administrator has all relevant information to accredit.</p> <p>Applications that fall outside of the time period will continue to be considered by the administrator however accreditation will not be awarded until 1 April.</p>

4.15 This proposal will provide DETI with the ability to control the uptake of the scheme and ensure that budgets are not overcommitted; however it will also provide potential applicants with adequate information on the progress of the scheme and the potential for closure.

4.16 DETI welcomes views on this proposal and specifically on the proposed trigger points, actions and rationale.”

- 17.11 Of particular significance to the Inquiry’s work is the fact that the cost control as designed and set out in the consultation document applied to both the non-domestic RHI and the domestic RHI; the initial triggers acted to close the domestic scheme first, and the later triggers acted to close the non-domestic scheme.
- 17.12 In his evidence to the Inquiry Mr Hutchinson described this proposal as a “half-way house” between DECC’s interim cost control (which, while initially referred to as “interim” in DECC’s March 2012 consultation document, was subsequently described as a “stand-by” mechanism in the DECC consultation response of June 2012) and degeneration. He saw it as something that DETI could deliver itself and a pragmatic step before full degeneration would be introduced in Northern Ireland.<sup>908</sup> The 2013 proposal is discussed in greater detail in relation to budget control in chapter 51 of this Report.

### The 2013 RHI Phase 2 consultation

- 17.13 On 26 June 2013 a submission was sent to the DETI Minister<sup>909</sup> seeking approval to launch a public consultation on the Phase 2 proposals, to publish CEPA’s recent June 2013 report and to write to the Chair of the ETI Committee with an update.
- 17.14 The submission essentially offered a description of proposals as they were set out in the consultation document, namely for a domestic scheme, for expansion of the non-domestic scheme and for various actions to set standards, improve performance and introduce cost control.

908 TRA-05105 to TRA-05109

909 DFE-97307 to DFE-97359

- 17.15 The CEPA analysis was referenced in the submission but a copy was not appended. As mentioned earlier, the submission did not mention that CEPA had stated it was unlikely that Northern Ireland would reach its target of 10% renewable heat by 2020. The note to the ETI Committee recorded, as far as the non-domestic scheme was concerned, that there had by that point been 25 applications with eight accredited.<sup>910</sup>
- 17.16 Minister Foster initially approved, on 2 July 2013,<sup>911</sup> only the communication to the ETI Committee.<sup>912</sup> The Minister’s SpAd, Dr Crawford, then met with the Energy Division officials on 17 July 2013<sup>913</sup> to discuss some aspects of the consultation proposals to do with bioliquids (which were not material for the Inquiry’s purposes). However, Dr Crawford had, on 6 July 2013, already sent his cousin, Richard Crawford, a copy of the draft Phase 2 consultation document<sup>914</sup> despite it not having been approved by the Minister. Dr Crawford acknowledged he should not have sent the draft consultation document to his cousin (this aspect is discussed later in this Report). Following Dr Crawford’s meeting with the Energy Division officials the Minister subsequently approved the rest of the submission, including the launch of the Phase 2 consultation, on 18 July 2013.<sup>915</sup>
- 17.17 The consultation was launched on 22 July 2013<sup>916</sup> and closed on 14 October 2013. The Inquiry notes the following particular points in respect of the consultation exercise:
- (i) There were 50<sup>917</sup> responses to the Phase 2 consultation;
  - (ii) According to Mr Hutchinson’s statement to the Inquiry, much of the interest focused on the domestic RHI scheme with some attention to the tariffs for new technologies proposed for the non-domestic scheme; and
  - (iii) Of the small number of respondents who mentioned cost control, some confusion was noted as to how the proposals would work, but respondents were generally content.<sup>918</sup>

## The DETI response to the consultation

- 17.18 A response to the consultation was eventually published by DETI in June 2014, by which time Ms McCutcheon and Mr Hutchinson had left. The response related only to the domestic scheme.<sup>919</sup>
- 17.19 On the very first page of the response publication, the following statement was included: “The issues relating to the non-domestic scheme will be dealt with separately and a similar response document will issue in due course.”
- 17.20 The June 2014 response made no reference to the budget control mechanism that had formed part of the 2013 consultation. DETI did not introduce it through the legislation that would be required to introduce the domestic scheme.

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910 DFE-97307 to DFE-97359

911 DFE-97366; DFE-97360 to DFE-97361

912 DFE 97362 to DFE-97365

913 DFE 97456

914 WIT-266013

915 DFE-97456

916 DFE 97618 to DFE-97620; DFE-97572 to DFE-97622

917 DFE-399144; DFE-93623

918 WIT-06087

919 DFE-93261 to DFE-93276

- 17.21 As can be seen from the more detailed account of events in 2015 which appears later in this Report, it was not until 2 October 2015 that DETI eventually published a response that dealt with the cost control aspect of the July 2013 consultation.<sup>920</sup> By that point in October 2015, as will be discussed later in this Report, the RHI was essentially in crisis. Cost control was dealt with at section 2 of the October 2015 response, which referred to the proposed ‘trigger’ system. It was recorded that several public responses to the 2013 consultation had expressed concern that the trigger method of budget management might be viewed as a disincentive. At paragraph 2.3 DETI recorded that, by that point in October 2015, there had been significant increases in levels of uptake with associated increases in monthly expenditure. The paragraph continued: “Cost controls now need to be introduced to ensure future budgetary levels wouldn’t be breached and to ensure the scheme continues to provide value for money.”<sup>921</sup>
- 17.22 The proposed solution put forward was, instead, tiering for the non-domestic medium biomass tariff. Such a proposal had not formed part of the public consultation in 2013 and, although it was not fully understood by those who proposed it, would not actually operate as a budget control.

## State Aid for the Phase 2 proposals

- 17.23 For the new technologies proposed for Phase 2 of the the non-domestic scheme, it was clear in 2013 that a new State Aid approval process would be required and that this would take a number of months.
- 17.24 Ms Hepper’s ministerial submission of 26 November 2013,<sup>922</sup> which was to be her last RHI submission as head of DETI Energy Division, provided a six monthly update to the ETI Committee. The update stated at paragraph 13: “Given that the domestic RHI does not require State Aid approval, it is likely that it can be launched earlier...” DETI Energy Division officials appear initially to have held the mistaken belief that the domestic RHI scheme was different and did not require State Aid approval.<sup>923</sup> That appears to have led to the further belief, during the latter part of 2013, that the domestic scheme could be separated from, and introduced more quickly than, the remainder of the Phase 2 non-domestic proposals which did require a State Aid application.
- 17.25 However, Mr Hutchinson and Ms McCutcheon were made aware, by February 2014 at the latest, that DECC had applied for and obtained State Aid approval for the GB domestic scheme.<sup>924</sup> Mr Hutchinson was told by email on 19 February that DECC had applied for State Aid for the GB domestic RHI scheme because the scheme would cover commercial usage by landlords and energy service companies.<sup>925</sup>
- 17.26 Nonetheless it appears to the Inquiry that Ms McCutcheon and Mr Hutchinson did not use the information obtained from DECC to reconsider the need for State Aid approval for the NI domestic RHI scheme or the sequencing of the Phase 2 proposals.

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920 DFE-424818 to DFE-424823

921 DFE-424822

922 DFE-33719 to DFE-33725

923 DFE-33724

924 DFE-92096; DFE-92318

925 DFE-54573



## The prioritisation of the domestic RHI

- 17.27 Partly based on the need to prioritise its limited resources, and supported by the mistaken belief that the domestic scheme could be taken forward more quickly as it did not require a State Aid application, it appears the Phase 2 proposals started to be developed on separate time tracks.<sup>926</sup> Mr Hutchinson gave oral evidence that there was no formal decision by Minister Foster or anybody else to decouple the domestic scheme from the rest of the Phase 2 proposals.<sup>927</sup>
- 17.28 However, by September 2013, Energy Division officials had adopted the path of advancing the domestic RHI ahead of the other proposals. The first available indication of this is found in the Energy Division Corporate and Operating Plan as at 30 September 2013.<sup>928</sup>
- 17.29 The following entry was to be found in relation to Phase 2 of the RHI:
- “State aid application should be submitted by 31 December 2013, but on current evidence the approval is likely to take some months. As only some elements of Phase 2 require State Aid approval, Phase 2 will launch in two stages – the domestic scheme, which does not require approval, in early Spring 2014, with the non-domestic elements launching as soon as approval is obtained.”<sup>929</sup>
- 17.30 The submission to Minister Foster and Dr Crawford dated 26 November 2013 seeking approval of a draft six monthly update for the ETI Committee, which was referred to above, continued this theme. Ms Hepper told the Minister, at paragraph 13 of the draft document to be sent to the ETI Committee:
- “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.”<sup>930</sup>
- 17.31 The Energy Division Corporate and Operating Plan, advocating the different time tracks and prioritisation, was available to John Mills when he took up his appointment as the new head of Energy Division in January 2014. Mr Mills said that his general impression upon taking up his post with DETI in January 2014 was that the non-domestic RHI scheme was not a prominent issue and the only real concern was the perceived slow uptake. He remembered that the question that Energy Division did not want to be asked was “How much money are you giving back to the Treasury?”<sup>931</sup> His answer to that was the introduction of the domestic scheme, which he said had been the “direction of travel” priority since his arrival; a priority that he agreed he then maintained and later mistakenly and repeatedly represented as a decision that had been taken by Minister Foster.<sup>932</sup> Minister Foster had not taken any such decision; she, like the ETI Committee, had been advised of a course that had been adopted by Energy Division in late 2013 based on a mistaken belief about the State Aid position.
- 17.32 On 15 May 2014 Mr Mills advanced a submission to Minister Foster containing a six monthly update on the RHI and RHPP schemes, which was to be forwarded with her approval to the

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926 DFE-33720 to DFE-33725 (see Annex A, paragraph 13); DFE-144531 to DFE-144537; TRA-05110 to TRA-05131; WIT-02436

927 TRA-05126 to TRA-05130

928 DFE-399116 to DFE-399124

929 DFE-399122

930 DFE-33720 to DFE-33725 (see Annex A, paragraph 13)

931 TRA-07089

932 TRA-07090; TRA-07094 to TRA-07095; TRA-07184; TRA-07201 to TRA-07206

ETI Committee.<sup>933</sup> The submission referred to the Phase 2 consultation between July and October 2013 and confirmed that, subsequently, the Department had been primarily focused on finalising policy on the domestic scheme and preparing for implementation. The other elements of Phase 2 “such as new technologies in the non-domestic sector and technical changes to legislation” were now to be addressed once the domestic scheme was agreed.<sup>934</sup>

- 17.33 The Inquiry notes that Minister Foster annotated a submission that she received on 16 September 2014 from Mr Wightman, who took over as the grade 7 responsible for Renewable Heat in June 2014, seeking her approval of the business case for the domestic scheme, with the words “get this launched ASAP”, thus confirming a sense of urgency to get the domestic scheme launched.<sup>935</sup> Though, in fairness to the Minister, she, and the ETI Committee, had previously been told that it was intended to launch Phase 2 of RHI by Autumn 2013,<sup>936</sup> and then December 2013.<sup>937</sup>

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933 DFE-230084 to DFE-230090

934 DFE-230089

935 DFE-184099 to DFE-184101

936 DFE-355293 to DFE-355304

937 DFE-33518 to DFE-33519; DFE-399144; DFE-355572

## Findings

97. The Minister should have been specifically advised, in June 2013, that CEPA had said in its June 2013 report that the target of 10% of heat from renewable sources by 2020 was, by that point, unlikely to be met.
98. At no point was there a clear, reasoned decision to separate out development of the domestic scheme from other changes proposed for Phase 2 of the RHI. The separation arose from an initial misunderstanding about State Aid. The domestic scheme, was ‘de-coupled’ from other Phase 2 developments based on a mistaken belief that it could be progressed swiftly in the absence of a requirement for State Aid and then came to be the focus of work in late 2013.
99. The lack of formal record keeping and the weakness of handover procedures also contributed significantly to the later erroneous belief that there had been a decision to de-couple and prioritise the domestic scheme and that this had been made by the Minister.
100. The Inquiry finds that, by February 2014, Ms McCutcheon and Mr Hutchinson were aware that DECC had applied for State Aid in respect of the GB domestic RHI scheme, together with the reason for that application. That information should have initiated a further consideration of the decision to ‘de-couple’ and prioritise the NI domestic RHI scheme and triggered an appropriate application for State Aid in respect of the NI domestic RHI scheme.
101. The consequence of the focus on the NI domestic RHI scheme was that budgetary cost controls which had been designed to operate across both domestic and non-domestic parts of the scheme, as proposed in the Phase 2 consultation, effectively fell by the wayside.
102. Given that the RHPP was already in place and proving popular, the Inquiry considers that the focus on the domestic RHI scheme was unnecessary, especially once it became known in February 2014 that it would require a State Aid application.
103. A combination of focus on the domestic RHI scheme and the limited resources within the Energy Division meant, in practice, notwithstanding the work of Mr Hutchinson, that insufficient resource was allocated by the Department to managing, monitoring and reviewing of the non-domestic RHI scheme. This work should have been done regardless of whether the scheme was perceived as under-performing.



## Chapter 18 – Staff turnover and its effect on RHI

18.1 A significant problem that became apparent to the Inquiry during the course of its work was the almost wholesale changeover of relevant staff in DETI from late 2013 and the first half of 2014 and the potential effect that had on the management of the RHI. For that reason the Inquiry, in this chapter, examines that specific issue.

### Big changes in a short period of time

18.2 As noted elsewhere in this Report the NI RHI scheme was novel, demand-led, volatile and economically and technically complex. It was also intended to last for in excess of 20 years. Given the specialist and technical nature of the subject matter, it was necessary within Energy Division on a number of occasions to engage consultants to undertake key pieces of work. This was within the bounds of normal practice in DETI at the time. However, where the RHI was concerned, this approach of assigning generalist civil servants to technically complex roles, supported periodically by specialist consultants, over time placed a premium on the acquired knowledge and skills of the civil servants in the Renewable Heat Branch.

18.3 The 2010 business case proposal document for the appointment of consultants to conduct the economic appraisal of an NI RHI scheme prepared by Mr Hutchinson and approved by Ms Hepper in November 2010 contained a section 5 dealing with ‘Skills Transfer’. Paragraph 5.4 provided that:

“Due to the highly technical nature of renewable heat, specifically the economics surrounding the various technologies, the skills transfer involved in the project will not mean that future consultancy will not be required. However, the transfer of skills, knowledge and understanding during this assignment will ensure that this work can be developed further in-house and that any future consultancy will be monitored and quality assured by knowledgeable and experienced staff.”<sup>938</sup>

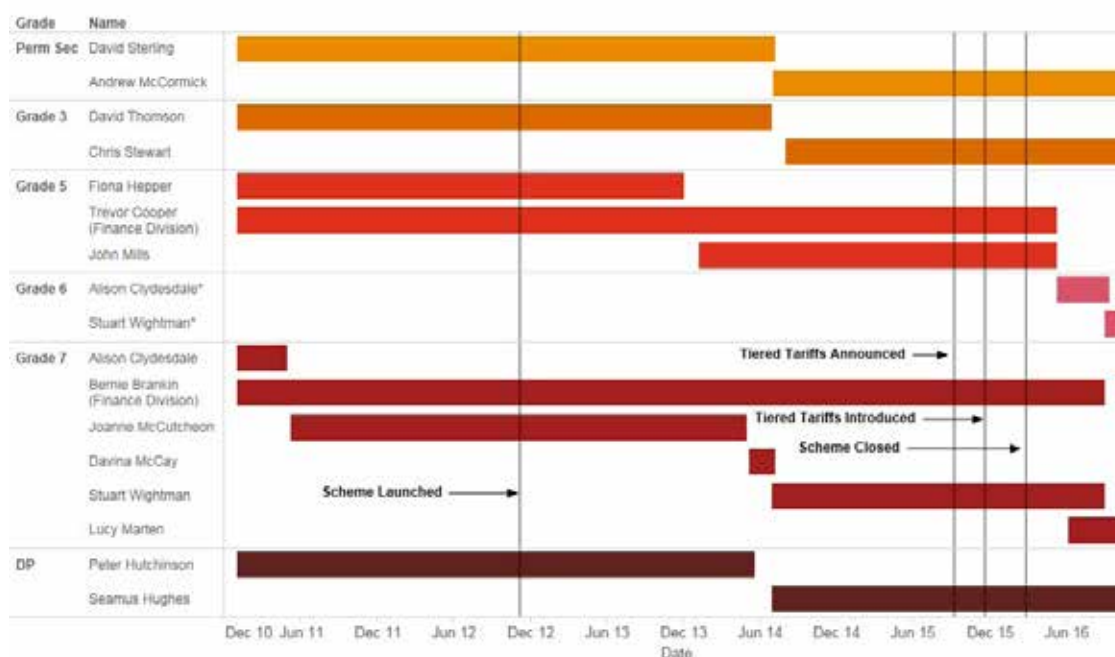
18.4 This insight appears to have been lost in 2013-14 when an unprecedented level of staff turnover was allowed to take place. Figure 3 below prepared by PwC illustrates how, other than for two relevant staff in DETI Finance Division, during the 7 to 8 months from December 2013 very significant and wide-ranging changes, from Permanent Secretary to deputy principal, took place with regard to the members of staff who had primary responsibility for the development and initial implementation of the RHI scheme.<sup>939</sup>

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938 DFE-56409

939 DFE-05633; PWC-04392

Figure 3 – Staff Changes



- The grade 5 head of Energy Division, Ms Hepper, left on promotion on 2 December 2013 (her last day in Energy Division being at the end of November). She was replaced by Mr Mills on 6 January 2014.
- The grade 7, Ms McCutcheon, left on 1 May 2014 for a career break and was succeeded in terms of responsibility for RHI by Mr Wightman on 30 June 2014. Between the departure of Ms McCutcheon and the arrival of Mr Wightman, Ms McCay acted as grade 7 on a temporary basis from 14 May to 7 July 2014.
- The deputy principal, Mr Hutchinson, left on 16 May 2014. He wanted a change of experience having been in Energy Division since July 2009.<sup>940</sup> Seamus Hughes replaced Mr Hutchinson on 30 June 2014.
- The grade 3, Mr Thomson, retired in June 2014 to be succeeded by Mr Stewart as Deputy Secretary and head of policy in August 2014.
- Mr Sterling was transferred to DFP as Permanent Secretary to be succeeded at DETI by Dr McCormick in July 2014.<sup>941</sup>

18.5 Mr Hutchinson had been in post for almost five years and had experience of the crucial early development and implementation of the NI RHI scheme together with the initiation of the relationship with Ofgem. It appears that during the early part of 2014 Ms McCutcheon tried to persuade Mr Mills to retain Mr Hutchinson for a period of time as, in her words, she saw him as “the lynchpin” in terms of knowledge and experience. She even suggested that Mr Hutchinson might be promoted to ‘act up’ in her grade 7 post pending his move so as to provide some degree of continuity.<sup>942</sup> However, she appears to have been told by Mr Mills that it was not his practice to stand in the way of people wishing to move and, instead, the grade 7 post was taken on a temporary basis by Ms McCay.<sup>943</sup> Mr Mills’ evidence was to the effect that

940 WIT-00022 to WIT-00024

941 WIT-00022 to WIT-00024

942 WIT-26003

943 PWC-04552; TRA-09545

he was aware that Mr Hutchinson was very capable and did not want to lose him; but that, although Ms McCutcheon did discuss Peter Hutchinson’s ability with him, he was not told, and did not appreciate, that if Mr Hutchinson left “there will be a disaster and the non-domestic scheme will run off the tracks.”<sup>944</sup> He also emphasised that Ms McCutcheon did not refuse Mr Hutchinson’s request to move, as his line manager, or advise him in unequivocal terms that Peter should stay.<sup>945</sup> He felt that it would be unfair to stop Mr Hutchinson’s career development in circumstances where he wanted to move on.

18.6 The Inquiry heard evidence from a number of witnesses about the staff turnover.

- Mr Thomson was unsure as to whether he knew that Ms McCutcheon and Mr Hutchinson were leaving at the same time. He said that he thought that it was an incorrect decision to let them both go as it was too small a team and, had he known about it, he would not have agreed.<sup>946</sup>
- Mr Mills agreed that the changeover had resulted in “a significant knowledge gap” and he had not appreciated the importance of Mr Hutchinson’s experience and knowledge given the potential risks arising from the non-domestic RHI scheme.<sup>947</sup>
- Mr Hughes told the Inquiry that he had not experienced such an extensive change of staff at the same time in all his 36 years of employment in the Northern Ireland Civil Service. In his written evidence Mr Hughes said he believed that that level of staff change significantly contributed to the subsequent problems.<sup>948</sup>
- Mr Wightman agreed that a changeover ranging from deputy principal to Permanent Secretary was very unusual.<sup>949</sup>
- Mr Stewart told the Inquiry that the absence of a systematic approach to handover could be “disastrous if, as in the particular circumstances of RHI, you get a very high incidence of turnover at all grades from permanent secretary to deputy principal in a fairly short period of time”.<sup>950</sup> He also said that after he joined DETI he was aware that Energy Division “had lost a lot of corporate continuity in a very short time” but that he did not take any particular actions over it because it took him some months, or even longer, to “realise just how profoundly challenging that was”.<sup>951</sup> His summary of the situation was that anyone looking at the staff turnover situation now “would recognise that it was a bad thing” and that “it was clearly suboptimal to have that amount of staff turnover in that time”, although he thought some elements of it were beyond anyone’s control.<sup>952</sup>

18.7 The new officials coming in during 2014 to run this scheme which was volatile, demand-led and unpredictable had very little, if any, relevant experience. For example, Mr Wightman’s experience was limited to capital schemes which had an identifiable beginning and end; he had never been involved in running a “live” scheme.<sup>953</sup>

944 TRA-09548

945 WIT-26002

946 TRA-06026

947 TRA-09531

948 WIT-14019

949 TRA-06877

950 TRA-11507 to TRA-11508

951 TRA-11516

952 TRA-11520

953 TRA-06846

- 18.8 Mr Hughes was completely unfamiliar with energy policy and renewable heat and he had no previous experience of an incentive driven scheme.<sup>954</sup>
- 18.9 Mr Mills had no experience of energy issues and did not receive any formal training in ‘renewables’ or any other aspects of the wide spectrum of Energy Division projects. He was concerned about handling the pressures of the role, given his personal circumstances, but says that he was reassured by Mr Sterling that his job could be done in normal hours.<sup>955</sup> Mr Sterling gave evidence that he remembered the conversation in question and that he had told Mr Mills that he reckoned that he could “manage the division without having to work the hours that Fiona was working at that time” (it apparently being accepted that Ms Hepper worked much longer than standard working hours).<sup>956</sup> He explained this by virtue of his assessment of Ms Hepper and Mr Mills’ respective management styles; and that Mr Mills might have had a “lighter touch” when it came to the way in which he worked with his grade 7s (although also emphasising that he was not suggesting that any less responsibility would have been exercised or that there was a right and wrong way to approach such management).<sup>957</sup> Given the hours worked by Ms Hepper, the limitation of resources and the wide range of complex projects for which he was to take responsibility the Inquiry considers it likely that the reassurance offered by Mr Sterling was unduly optimistic. Although Mr Sterling might well not have appreciated it at the time and (the Inquiry accepts) would have encouraged Mr Mills to take the post in good faith, with hindsight Mr Mills’ assessment that Fiona Hepper’s approach was required seems to be correct.<sup>958</sup> This chimes with other evidence the Inquiry heard from a variety of witnesses as to quite how “heavily loaded” was the Director of Energy Division post.

### The lack of any formalised or consistent handover process

- 18.10 As the Inquiry notes in detail in chapter 4 of this Report, the RHI scheme had been established without the mechanisms and objective records which, under an effective degree of project management, would have been likely to improve the prospects of preserving continuity and corporate knowledge irrespective of staff changes.
- 18.11 A number of witnesses, including Mr Thomson, told the Inquiry that the nature and extent of the “handover” from one official to his or her successor was very much a matter of discretion and not the subject of any formal rule or code.<sup>959</sup>
- 18.12 The Inquiry notes that Mr Wightman had initially been prevented in November 2013 from leaving his previous post at the Department for Regional Development (DRD) until summer 2014 for business continuity purposes. His line manager at DRD in November 2013, Mr Mills, was about to leave to take up the role of Director of the Energy Division at DETI, and Mr Wightman had to remain in DRD to complete work on water policy and to facilitate a handover with the Director for water policy.<sup>960</sup> Thus, at least in DRD at that time, two post holders with significant linked responsibilities were not permitted to move roles at the same time. When Mr Wightman eventually took up his DETI post in the Energy Efficiency Branch on

954 WIT-14019

955 WIT-14519

956 TRA-06758

957 TRA-06759

958 TRA-07073

959 TRA-06027

960 WIT-17020



30 June 2014 no significant period of introduction and familiarisation was given to him for the RHI scheme.

- 18.13 Mr Stewart confirmed that while there might be many varying examples of handover notes, there would be just as many, if not more, people simply relying on learning on the job.<sup>961</sup> He told the Inquiry that he had received the same first-day briefing pack as had been provided to Dr McCormick, which listed 53 policy issues including 17 on energy, of which RHI was the last to be mentioned at number 17.<sup>962</sup> When he took over from Mr Thomson there was no documentary or formal handover but only a couple of meetings with Mr Thomson at which RHI was not mentioned.<sup>963</sup> Mr Stewart said that he understood that his experience reflected general practice across the Northern Ireland Civil Service. There was no systematic approach and the handover process operated upon an *ad hoc* basis. As already noted earlier in this chapter, Mr Stewart accepted that such a situation could be disastrous in terms of continuity of knowledge and experience in the context of such a large staff turnover.<sup>964</sup> Dr McCormick likewise accepted in his oral evidence that there was no recognised system within the NICS for handover and that, in the context of the RHI scheme, all of the staff moving at broadly the same time was unsatisfactory.<sup>965</sup>

## Electronic record keeping

- 18.14 Mr Stewart, amongst others, was also asked about the efficacy of the TRIM system for digitally storing information. He agreed that it could store large quantities of information but added that what might be called the ‘front end’ of TRIM was a difficult and challenging interface to use. Mr Stewart expressed the view that its search capabilities were well short of what might be considered best practice by modern standards, adding that:

“With TRIM you are relying first on the container title and thereafter on the record title and, if they’re not precise enough or comprehensive enough, you’re left either taking a chance and not reading a document or, more likely, looking at it and thinking, ‘well that might be relevant I’d better read it just in case’ which is very laborious and slows down the use of TRIM in that way.”

By contrast, Mr Stewart felt that a suite of project management documents provides a core repository of information when taking up a post.<sup>966</sup>

- 18.15 Dr McCormick told the Inquiry that he was “not a big TRIM user” and avoided the system if it were possible. He said the system was difficult to use if the user does not know that the materials sought existed.<sup>967</sup> Mr Mills, on the other hand, would have usually insisted upon relevant material going into TRIM because that allowed several people to work on a document. He compared that facility to a ‘handover note’ which was a ‘one off’.<sup>968</sup> He agreed that staff must know what they were looking for in TRIM and be familiar with the correct word for which

961 TRA-11507

962 TRA-11504

963 WIT-11572

964 TRA-11507 to TRA-11508

965 TRA-12039 to TRA-12041

966 TRA-11511 to TRA-11513

967 TRA-12142 to TRA-12143

968 TRA-09562

to search.<sup>969</sup> In the course of giving oral evidence, Mr Mills repeated that the TRIM system was “great if you knew what to look for”<sup>970</sup> and added that he “wouldn’t say that knowledge transfer was a strong suit” of the system.<sup>971</sup>

- 18.16 Mr Wightman agreed that it could be “quite difficult to find stuff on TRIM”.<sup>972</sup> However, he appeared to be reasonably familiar with the system. Mr Hughes told the Inquiry that he did not have the capacity to conduct a thorough search in TRIM.<sup>973</sup>
- 18.17 The Inquiry notes the difficulties of using the TRIM system of information storage referred to by some witnesses. For example, the version of the 2011 HMT Jon Parker email chain that Mr Wightman had from TRIM<sup>974</sup> was not the one that included some of the starker warnings from Ms Brankin and Ms Clydesdale about the risks,<sup>975</sup> although both versions were in the same TRIM folder entitled ‘RHI Funding’. On the other hand, in her short time in the temporary grade 7 role, Ms McCay had found such relevant documents.<sup>976</sup>
- 18.18 The precise advantages and disadvantages of any particular information management software, which probably also vary proportionately to the training which is provided in its use, are not for the Inquiry to address in detail. The Inquiry has noted with concern, however, the apparent lack of consistency and reliability in relation to officials’ ability and/or willingness to retrieve relevant and comprehensive information from the TRIM system that would have been helpful in the course of their work on the RHI scheme.

## The January 2014 handover to Mr Mills

- 18.19 Mr Mills, who succeeded Ms Hepper as head of Energy Division, told the Inquiry that some form of personal overlap would have been helpful, although he realised at the time that such an overlap would not occur in the circumstances since she was leaving in November 2013 and he would not arrive until January 2014. He said that he agreed with Mr Sterling, who said that in his experience there was often no formal handover between senior officials.<sup>977</sup>
- 18.20 Mr Mills said that he did receive a half-day briefing from Ms Hepper in her office in November 2013.<sup>978</sup> He told the Inquiry that the impression that he received was that the non-domestic RHI scheme was underperforming and needed to be given emphasis.<sup>979</sup> During the Inquiry his attention was drawn to the evidence given by Ms Hepper that the discussion included reference to the need for DFP reapproval, early review and cost control/depression.
- 18.21 Mr Mills stated that he did not recall any such specific issues being highlighted as a significant risk. He told the Inquiry that if the need for a review starting in January 2014 had been emphasised, he would have asked Ms Hepper to put arrangements in hand or sought to identify

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969 TRA-11080 to TRA-11081

970 TRA-11080

971 TRA-11081

972 TRA-06876

973 TRA-05841 to TRA-05843

974 DFE-193406; DFE-193418 to DFE-193420

975 WIT-02716 to WIT-02720

976 TRA-05475

977 TRA-07079

978 WIT-14519

979 WIT-14522

a grade 7 himself to whom he would have given the appropriate instruction. He did not recollect any reference to the need for DFP reapproval in March 2015.<sup>980</sup>

- 18.22 Mr Mills agreed that he had subsequently been given a documentary induction pack in January 2014 consisting of some 80 pages<sup>981</sup> in which the only references to RHI were limited to pages 76 to 77.<sup>982</sup> Those pages of the pack were prepared by Ms McCutcheon and Mr Hutchinson. It contained no mention of the unusual nature of the funding, the need for early review in January 2014, the need for continuing careful monitoring, the review of the scheme and tariffs, the communication from Janette O’Hagan, the time-limit of the budget, the need to reapply for DFP approval in March 2015, or the need to consider budget control/degression. Mr Mills said that he did not recall any form of induction from Mr Thomson, his line manager, but that he did not question that at the time.<sup>983</sup>

### Mr Hutchinson’s May 2014 handover document

- 18.23 Despite the significant turnover of staff during a potentially very important time in the development of the NI RHI scheme the only handover document containing any real detail that the Inquiry has been able to identify was that written by Mr Hutchinson in May 2014. However, given the culture and practice at the time, the Inquiry understands why different individuals might have perceived its relevance in different ways.

- 18.24 The handover note<sup>984</sup> consisted of 14 pages and had sections dealing with:

- (i) Relevant staff;
- (ii) Immediate actions;
- (iii) The RHI;
- (iv) The RHPP;
- (v) Phase 2 of RHI;
- (vi) Communications; and
- (vii) The renewable heat sub-group of SEIDWG.

The section on “Immediate Actions (by end August 2014)” contained 7 bulleted actions, each with a number of sub-points. The section on RHI had sub-sections setting out an overview, useful reading/documents, key contacts, and current/emerging issues. A similar pattern was applied to the other topics covered by the handover note such as RHPP and Phase 2 of RHI.

- 18.25 Mr Mills did not recall having read Mr Hutchinson’s handover note, although it was produced at his request.<sup>985</sup> Mr Mills considered he was inhibited by time pressures and therefore would not have been going through such a document, dealing with a deputy principal’s job, in any detail. However, he said that the purpose of the handover note was to provide continuity for anyone directly involved with the scheme.<sup>986</sup> He could not confirm whether Mr Wightman and/

980 TRA-07084 to TRA-07087

981 WIT-14519

982 WIT-14700 to WIT-14701

983 TRA-07095 to TRA-07097

984 WIT-07596 to WIT-07609

985 TRA-09543

986 TRA-09554

or Mr Hughes had read the note<sup>987</sup> as, when he joined the Department, the non-domestic scheme was not considered to represent a high-risk project and there were many other issues with higher priority.<sup>988</sup>

18.26 As mentioned above, in the handover note Mr Hutchinson identified a number of “immediate actions” that he felt should be dealt with by the end of August 2014.<sup>989</sup> These included the approval and launch of the domestic RHI scheme, some further subjects to be agreed with Ofgem and a review of the non-domestic scheme including the following points: “Review biomass tariffs under 100kW” and “Consideration of tiered tariffs to prevent excessive payments.”

18.27 An important section of the document was that relating to the RHI. That section contained a sub-section entitled “Current/emerging issues”, one of which was “Tariffs”. The “Tariffs” bullet point read as follows:

“It is becoming apparent that the payments made to installations are higher than would have been expected under CEPA modelling...Ofgem (Edmund Ward) has advised on 13.05.14) that the experience in GB and NI has shown that many installations have had a higher demand (time of operation) than had been assumed in the tariff calculations; this is especially true of certain sectors. As the demand is higher than what has been assumed the tariffs can become over-generous. This issue would need to be considered as a matter of urgency...The email from Janette O’Hagan (DTI/14/0088268 (refers to TRIM reference)) us [sic] also relevant to this point, where applicants could over-use technology for financial gain...CEPA had advised in their 2011 analysis that this wouldn’t be the case...The solution would be to “tier” tariffs, where a certain tariff is provided for the first 15/20% of use and then another lower tariff is provided for the rest of the heat use. This is used in GB tariffs. Certainly this should be considered for biomass under 100kW as a matter of urgency...This has been discussed briefly with Edmund Ward and he advised that Ofgem would be able to implement without too many changes to existing systems.”<sup>990</sup>

18.28 This passage contained very significant references to high demand, over-generous tariffs, and overuse for financial gain. He stated that this needed to be considered “as a matter of urgency”, yet none of those coming after Mr Hutchinson appear to have picked up on this properly or taken any appropriate action.

18.29 Mr Hutchinson said something similar, although perhaps in shorter and less forthright terms, in a contribution for a Heads of Branch meeting scheduled for 15 May 2014 when he recorded that there was “a potential need for review of tariffs (particularly for biomass less than 99kW) given advice from Ofgem re: the use of those systems”. He suggested that “a system of tiered tariffs might be appropriate”.<sup>991</sup> That suggestion remained in the Heads of Branch records for the next three meetings, but by the meeting of 25 July 2014 (two months after Mr Hutchinson had left) it had disappeared.<sup>992</sup>

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987 TRA-09544

988 TRA-09565

989 WIT-06068 to WIT-06069; WIT-07597 to WIT-07598

990 WIT-06069 to WIT-06070

991 DFE-410161

992 DFE-410169; DFE-410177; DFE-410198

- 18.30 At around the same time as the handover note was being prepared, a new entry was added to the Renewable Heat Branch section of the May 2014 Energy Division 2014-15 Composite Divisional Plan. This plan recorded the aims and objectives of the various business areas of Energy Division, identifying key performance targets as well as risks associated with the various objectives. It was contributed to by officials from the various branches between March and May 2014, before being finalised in and around 14 May 2014. All the various versions of this divisional plan were made available to the Inquiry. As a result, the Inquiry was able to see that on or about 13 May 2014, in what became version 27 of the then draft divisional plan, a new objective was added to “monitor uptake of the non-domestic RHI.”<sup>993</sup> That new objective had a “key action” of “monitor[ing] the uptake of the non-domestic RHI and carry[ing] out policy reviews as required.” The accompanying risk was described in the following terms: “tariffs under the scheme are overly generous and lead to higher than expected uptake and excessive payments, impacting on budgets.”<sup>994</sup> Like the entry in the Heads of Branch document, these additions to the Composite Divisional Plan<sup>995</sup> were expressed in less detailed terms than the relevant part of the handover note.
- 18.31 At a later section of his handover document dealing with Phase 2 of the RHI scheme under the sub-heading “Non-Domestic key issues/papers”, Mr Hutchinson included the need to consider “Cost Control or Degression.”<sup>996</sup>
- 18.32 The handover note included a considerable volume of detailed information and reference to a substantial range of important documentation relating to the development and implementation of the RHI scheme.
- 18.33 However, the handover note did not contain any reference to a number of matters discussed earlier in this Report, such as the following:
- (i) the unusual form of the RHI funding, about which he would have been aware as a consequence of the 2011 Parker, Clydesdale and Brankin email exchanges, and his own email correspondence with Akhil Patel of DECC in June 2011,<sup>997</sup>
  - (ii) the fact that the April 2012 DFP approval of the RHI business case had been granted subject to reapproval being sought from DFP by March 2015; and
  - (iii) that DECC had confirmed in February 2014 that a State Aid application had been considered necessary for the GB domestic RHI scheme.
- 18.34 To be fair, the documentation referenced in the note included the 2012 Casework Committee synopsis and the 2012 RHI business case, each of which explained that the initial scheme budget ran up to, but not including, the year 2015-16.<sup>998</sup> In this particular regard, the note also recorded that there had been no confirmation regarding the budget for 2015-16 as well as identifying the TRIM reference for a number of documents relating to the budget, such as the 15 April 2011 email from Jon Parker of HMT mentioned earlier in this Report.<sup>999</sup> In his oral evidence to the Inquiry, when asked about these omissions from his handover note,

993 Version 26 is at DFE-377636 to DFE-377676 and version 27 is at DFE-377595 to DFE-377635

994 DFE-377626

995 DFE-377585; DFE-377544; DFE-377503

996 WIT-07605

997 DFE-05426 to DFE-05428

998 DFE-398076; DFE-00190 to DE-00191

999 WIT-07601; DFE-61975; DFE-62062 to DFE-62064

Mr Hutchinson acknowledged them but also pointed out that there was some continuity in Energy Division in the form of Mr Mills, with whom he had already discussed issues such as the need for scheme reapproval,<sup>1000</sup> and that Ms McCutcheon had given him a steer as to what should be included in the note,<sup>1001</sup> that the focus of the note was on the following three months,<sup>1002</sup> and that his clear understanding and expectation, based upon a discussion with Mr Mills before he left, was that his successors would be free to speak to him about any issues.<sup>1003</sup> Mr Hutchinson also said that he prepared two accompanying hardcopy files of relevant background material, but neither Mr Wightman nor Mr Hughes were able to recall coming across such files.<sup>1004</sup>

- 18.35 At a DETI Energy Division planning meeting on 26 June 2014 Mr Wightman met Ms McCay (who had stood in on a temporary basis as the grade 7 in Renewable Heat Branch pending Mr Wightman's arrival, and who had received a copy of Mr Hutchinson's document from him during their handover),<sup>1005</sup> and there was some discussion about Mr Wightman's duties.<sup>1006</sup>
- 18.36 Subsequent to that meeting, Ms McCay emailed a copy of Mr Hutchinson's handover note to Mr Wightman. It appears that Mr Wightman forwarded the email, and its attachment, to his personal email address, but he never got around to reading it and subsequently forgot that he had done so.<sup>1007</sup> It seems that he also had a hard copy of the document in his place of work, but only read the first three pages containing the names of relevant staff and bullet-pointed actions to be completed by the end of August 2014.<sup>1008</sup> The Inquiry notes that one of those bullet points included the need to review biomass tariffs under 100kW and consideration of tiered tariffs to prevent excessive payments. He did incorporate some of these matters, including the point about the review, in various versions of the Energy Efficiency Branch Plan for 2014-15. It seems that he then placed his hard copy in a cupboard and it was not recovered by Mr Wightman until shortly before the PAC inquiry into RHI in the autumn of 2016.<sup>1009</sup> As he told the Inquiry, the upshot was that he had no recollection of seeing or discussing the full document until that time.<sup>1010</sup>
- 18.37 Mr Hughes was provided with a hard copy of Mr Hutchinson's handover note by Ms McCay, who referred, in their handover meeting, to parts of the document.<sup>1011</sup> However, Mr Hughes maintained that it was not a detailed discussion and that Ms McCay told him that even the achievement of the first four bullet points of the 'Immediate Actions by end August 2014' page was unrealistic.<sup>1012</sup>
- 18.38 In oral evidence Mr Hughes emphasised that he felt that the assessment of what could be done, and the date by which it could be done, which was contained in the handover document

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1000 TRA-05149

1001 TRA-05159

1002 TRA-05149; TRA-05157 to TRA-05158; TRA-05163 to TRA-05164

1003 TRA-05156; TRA-05163 to TRA-05164

1004 TRA-05168 to TRA-05169; TRA-06897; TRA-09179; WIT-06112 to WIT-06113

1005 WIT-13024

1006 TRA-06885 to TRA-06886

1007 WIT-17678 to WIT-17692

1008 WIT-17031

1009 TRA-06887 to TRA-06895

1010 TRA-06892 to TRA-06893

1011 DFE-05397 to DFE-05410

1012 TRA-05810 to TRA-05811

was “entirely unrealistic”.<sup>1013</sup> Being completely new to DETI Energy Division and this branch he was not in a position to question or raise any relevant issues. He kept the handover document and looked at some of the “useful reading” referred to therein but would not have used it otherwise.<sup>1014</sup> The CEPA reports did not mean a lot to him and he did not recognise the importance of reviewing the tariffs.<sup>1015</sup>

- 18.39 He said that he had no previous experience of AME funding and that he simply did not have time to retrieve and read all the documents relating to RHI that may have been contained in the TRIM digital storage system, however helpfully indexed that might have been.<sup>1016</sup> Mr Hughes told the Inquiry that he relied on Mr Wightman for directions and that all of his time until December 2014 was taken up by prioritising the launch of the domestic scheme.<sup>1017</sup>
- 18.40 It is important that the Inquiry should recognise that Mr Hutchinson appears to have been the only official who went to some considerable lengths to ensure that a detailed handover note was provided for the benefit of those coming into the Department to work on renewable heat after he had left. He also made himself available to meet his successors, an opportunity that was taken up by Mr Hughes, although that meeting appears to have been limited to consideration of the domestic scheme. The handover document does not seem to have been considered in detail by Mr Wightman and Mr Hughes, nor indeed at all by Mr Mills who did not recall seeing or reading it, although he thought he recalled Mr Hutchinson confirming to him that it had been completed.<sup>1018</sup>

### ‘Learning on the job’

- 18.41 Although the Inquiry heard that there were many examples in the Northern Ireland Civil Service of those taking up new posts ‘learning on the job’,<sup>1019</sup> the newcomers joining Energy Division in 2014 did not enjoy any realistic prospect of doing so with respect to the non-domestic RHI scheme. Such limited resources as were available were to be devoted to running the RHPP scheme and the launch of the domestic RHI scheme.
- 18.42 Mr Wightman told the Inquiry that: “there was little time for policy”, describing his two years at DETI as a “blur” during which the work was largely reactive.<sup>1020</sup> He said that the telephone never stopped ringing, and answering telephone enquiries took up most of Mr Hughes’ time.
- 18.43 Mr Hughes described most of his work as reactive and said that he was directed to prioritise the domestic scheme and two non-domestic issues, namely the handling of Carbon Trust loans and the development of a data sharing protocol in connection with administration by Ofgem.<sup>1021</sup>

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1013 TRA-05834

1014 TRA-05812

1015 TRA-05854

1016 TRA-05831 to TRA-05834

1017 TRA-05822 to TRA-05825

1018 TRA-09543; TRA-09561 to TRA-09563

1019 See, for instance, Mr Stewart’s evidence at TRA-11507

1020 TRA-06839

1021 WIT-14018

## Findings

104. The extent of staff turnover between the autumn of 2013 and the summer of 2014 should not have been allowed to happen. This robbed the Energy Division, and in particular Renewable Heat Branch (later the Energy Efficiency Branch) of such skills and knowledge on RHI as had been acquired to that point. The level of turnover should have been escalated to top management within DETI and failure to do so clearly suggested a lack of leadership.
105. The complete absence of any formal system of handover between departing and new staff was not satisfactory. The Inquiry found it difficult to understand how this significant changeover of senior and junior staff was permitted to occur without the benefit of management structures and practices designed to ensure preservation of corporate knowledge, especially given the highly unpredictable impact of a ground-breaking incentive scheme in an immature market.
106. Given the number of staff changes, including that Joanne McCutcheon was about to leave, the Inquiry considers it a failing that Mr Mills did not properly appreciate the significance of Mr Hutchinson's experience and, probably as a result of this, did not take sufficient steps either to encourage Mr Hutchinson to remain within the branch or, more importantly, to ensure greater continuity of knowledge when he left.
107. None of the new staff received any significant training, nor was there any meaningful overlap with the staff who left. The result was a lack of continuity and loss of corporate memory.<sup>1022</sup>
108. The Inquiry finds the process in 2014 of recruiting replacement staff to work on RHI was inadequate. Whatever process was used to assess the roles to be filled, the end result was that, at that stage of the scheme, the job roles should have been looked at anew, and more effort should have been made to recruit staff with more appropriate skills and experience to match those revised roles.



## Chapter 19 – The business case for the domestic RHI

- 19.1 As mentioned previously, the Inquiry has not investigated and is not reporting on, the NI domestic RHI scheme *per se*. Rather it has looked at aspects of decision making around the domestic RHI scheme in DETI and DFP in terms of how decisions had an impact on the non-domestic RHI scheme.
- 19.2 During early 2014, work continued on developing the business case to seek approval for the introduction of the domestic RHI scheme. On 23 May 2014 Energy Division, now without Ms McCutcheon and Mr Hutchinson, submitted the domestic RHI proposals for consideration by a DETI Casework Committee.<sup>1023</sup> The proposals were again supported by a covering letter from Mr Thomson.<sup>1024</sup>

### The DETI domestic RHI Casework Committee

- 19.3 The domestic RHI Casework Committee met on 9 June 2014 and approved the proposals. Mr Cooper, who had chaired the March 2012 Casework Committee that had considered the non-domestic RHI, also sat on the domestic RHI Casework Committee. Mr Cooper had sought and received a copy of the 27 April 2012 DFP approval of the non-domestic scheme on the day of the domestic RHI Casework Committee meeting.<sup>1025</sup>

### Changes to the review required of the non-domestic RHI scheme

- 19.4 As discussed further in chapter 32 of this Report, there was a clear requirement for DETI to review the non-domestic RHI scheme. This was set out, for instance, as condition 2 of the DFP approval of 27 April 2012, which required arrangements to be put in place for scheduled reviews and noted that the first review was scheduled to start in 2014.<sup>1026</sup>
- 19.5 The Inquiry also notes that paragraph 10.10 of the business case for the introduction of the domestic RHI scheme of 15 August 2014, originally prepared by Mr Hutchinson before his departure in May 2014, then revised by Mr Wightman and approved by Mr Mills, incorrectly stated that the first formal review of the commercial non-domestic RHI scheme would begin in early 2015, rather than 2014, with changes to be implemented in 2016, rather than 2015, as indicated in earlier documents.<sup>1027</sup> The Inquiry was shown no evidence of a conscious decision being made for this and Mr Hutchinson, who had drafted the document, gave oral evidence to the effect that it may have been an error, or had been changed by someone other than him.<sup>1028</sup>
- 19.6 Whatever may have been the source of the change, it was then replicated in all future documentation regarding the review. In fact, DETI had neither carried out the review of the non-domestic RHI scheme originally scheduled for January 2014 nor the urgent review of the biomass tariffs under 100kW recommended in Mr Hutchinson's handover note of May 2014.

1023 DFE-269737 to DFE-269937

1024 WIT-13099 to WIT-13100

1025 DFE-144451 to DFE-144455

1026 DOF-03244 to DOF-03245

1027 DFE-163958; DFE-163896 to DFE-164103

1028 TRA-05145 to TRA-05150

## DFP's approval of the domestic RHI business case

- 19.7 The Inquiry looked closely at DFP's handling of the approval of the DETI domestic RHI business case because of its potential ramifications for events relating to the non-domestic RHI scheme. The Department of Finance (DoF, formerly DFP) told the Inquiry that its primary function in respect of granting approval for business cases was to assess whether the business case represented value for money.<sup>1029</sup> DETI submitted the domestic RHI business case to DFP Supply on 15 August 2014.<sup>1030</sup>
- 19.8 By this point, there was a new DFP Supply Officer responsible for DETI, Michelle Scott. Ms Scott had not been involved in the DFP approval for the non-domestic scheme in 2012. DoF informed the Inquiry that none of the DFP Supply team involved with the 2012 approval were involved with the 2014 approval of the domestic case; the handover process had not included RHI (as there was no live business case at the time); and the need to treat the domestic RHI business case as an extension of the non-domestic RHI scheme was not recognised.<sup>1031</sup>
- 19.9 The 15 August 2014 DETI covering letter to DFP in respect of the domestic RHI business case material was sent under the name of Iain McFarlane, who worked in the DETI Finance Division's Accountability and Casework Branch.<sup>1032</sup> This letter contained a number of errors, omissions and inconsistencies:
- (i) Paragraph 5 wrongly stated that "funding of £25 million is available to 2015-16 for the scheme" whereas the original £25 million offered by HMT was only to cover the period up to 2014-15. There was no clarification to explain that HMT had also committed to paying the ongoing incentives arising from accreditations to the scheme in this period, and that these 'tail payments' needed to be included in AME forecasts from 2015-16 onwards alongside estimates for payments to new scheme members.
  - (ii) Paragraph 6 implied that for the one year, 2015-16, DETI should receive a population share of DECC's £430 million award. This would have amounted to £12.9 million to cover payments to existing and new scheme members for that year, although no confirmation of this had been received from HMT, and there had been no mention of RHI in the NI Executive's July 2013 settlement letter from HMT that dealt with the single financial year 2015-16.
  - (iii) In contrast to the implication of paragraph 6, paragraph 7 summarised DETI's then current AME forecasts for the scheme, which only recorded £9.5 million for the year 2015-16 as part of a total cumulative forecast of £103 million for the years from 2014-15 to 2019-20. That same figure of £103 million was then carried over into the second page of the DFP Supply Division business case *pro forma*.<sup>1033</sup>
- None of these issues were identified by DFP Supply.
- 19.10 The letter of 15 August 2014 made no reference to the fact that DFP approval of the non-domestic RHI scheme, as set out in DFP's letter of 27 April 2012, was time-limited. This was in spite of the fact that the £103 million being referred to as available for the domestic RHI

1029 WIT-34719

1030 DFE-163895

1031 WIT-34729

1032 DFE-145074 to DFE-145075

1033 DFE-145076 to DFE-145077

scheme as far as 2019-20 (a figure said, in paragraph 9 of the letter, to render the domestic RHI scheme affordable) was in fact the AME profile for the already existing non-domestic RHI scheme. The DFP approval for the non-domestic scheme was due to expire at the end of March 2015.

- 19.11 It seems that during DFP’s 2014 consideration of the domestic RHI business case no one in DFP looked at the 27 April 2012 approval it had previously granted for the non-domestic RHI scheme. DoF accepted before the Inquiry that DFP considered the domestic RHI business case as a stand-alone case.<sup>1034</sup> DoF fully accepted before the Inquiry that it was not a stand-alone case and should not have been considered as such.<sup>1035</sup>
- 19.12 On 18 August 2015, DFP Supply Division’s Ms Scott sent the DETI domestic RHI business case to DFP Economic Appraisal Branch, which housed the DFP economists, for their comment.<sup>1036</sup> Ms Scott also delegated, within DFP Supply, the further consideration of the domestic RHI business case to her deputy principal, Angela Millar.
- 19.13 The DETI domestic RHI business case was looked at by DFP economist, Michael Houston, who enquired about the inconsistency of the funding information provided and also asked whether there was any confirmation of the funding coming to Northern Ireland and whether it had been agreed by CED that any Barnett consequential of DECC’s GB RHI funding would be allocated to DETI.<sup>1037</sup>
- 19.14 Emer Morelli, who came into post as head of DFP Supply Division in September 2014, gave oral evidence to the Inquiry on behalf of DoF in respect of DFP’s handling of the domestic RHI business case. Ms Morelli said that she could not find any evidence of DFP Supply turning to DFP CED (the then section of DFP responsible for AME and engagement with HMT) with regard to Mr Houston’s enquiries.<sup>1038</sup> DoF also accepted that, in September 2014, Supply should have engaged with CED with questions about the funding of the RHI scheme.<sup>1039</sup>
- 19.15 However, Ms Millar did ask DETI about affordability and, on 5 September 2014, DETI Accountability and Casework’s Rachel Linton sent on to DFP Supply a series of finance-related correspondence that Mr Wightman had located.<sup>1040</sup> That material included the 15 April 2011 HMT Parker email as well as the correspondence between DETI Minister Foster and DECC Minister Barker at the end of 2013 and early 2014, which culminated with Minister Barker’s letter of 7 January 2014. That DECC letter referred to the GB RHI funding of £430 million for 2015-16 and how, while DETI’s funding for 2015-16 would be derived from the figure of £430 million through the population-based share, DETI should have received notification of its RHI funding directly from HMT in the 2015-16 Spending Round. DETI’s handling of the DECC 2013 and 2014 correspondence, particularly relating to the issue of budget control, is dealt with later in this Report. It does not appear that, in September 2014, the potential significance of the HMT Parker email, or the import of the Barker letter, as to the funding position was recognised in DFP.

1034 TRA-11418

1035 TRA-11426

1036 DOF-100212

1037 DOF-100210 to DOF-100211

1038 TRA-11416

1039 TRA-11417

1040 DFE-193421 to DFE-193452

- 19.16 Following a further exchange of questions and answers between DFP Supply and DETI, approval was given by DFP for the domestic RHI scheme on 15 September 2014.<sup>1041</sup> The DFP approval letter of 15 September 2014 stated that the preferred option mirrored the approach taken in GB and “will see the introduction of a Domestic Renewable Heat Incentive Scheme at a capital cost of £103 million and a resource cost of £1.4 million.”<sup>1042</sup> The characterisation of the funding as “capital” was incorrect. The reference to £103 million did not contain any recognition that this sum referred to AME forecasting for the non-domestic RHI scheme. It also did not suggest that it was a sum that would have to cover both schemes.
- 19.17 In written evidence to the Inquiry, Ms Scott conceded that, subsequently, she could see that the consideration of the domestic RHI business case in 2014 provided an opportunity for DFP to consider the progress of the non-domestic RHI scheme to that point, as well as the funding arrangements for both schemes. Ms Scott accepted responsibility for this missed opportunity.<sup>1043</sup>
- 19.18 In response to questioning by Inquiry Counsel, Ms Morelli accepted that, had the matter been dealt with properly, at best DETI could have received a time-limited approval for the domestic RHI scheme to 31 March 2015, which would have mirrored the already existing time limit for the non-domestic RHI scheme approval.<sup>1044</sup> A realistic alternative would have been for DFP to have contacted DETI to explain that it could not give approval for the domestic RHI scheme until such times as DFP were satisfied that DETI were proceeding with the review which had also been a condition of the 2012 approval of the non-domestic RHI scheme.<sup>1045</sup> In such circumstances approval might have been given to the domestic RHI scheme conditional upon the satisfactory completion of the review of the non-domestic scheme.
- 19.19 Ultimately, Ms Morelli accepted, on behalf of DoF, that had DFP properly conducted its consideration of the DETI domestic RHI business case in the summer of 2014, the result would inevitably have meant a significant intervention in the chain of events relating to the non-domestic RHI scheme, rather than an unlimited approval of the domestic scheme for a proposed sum of money that did not really exist.<sup>1046</sup>
- 19.20 Ms Morelli confirmed to the Inquiry that DoF had already introduced changes to its systems in respect of the approval of business cases, including the introduction of a formal triage system to ensure that business cases were subject to a much more rigorous assessment at the initial stage.<sup>1047</sup>
- 19.21 Following the DFP approval, Mr Wightman sent a submission dated 16 September 2014 to the DETI Minister indicating that the launch date of the domestic scheme was considerably delayed. As discussed earlier in this Report, Minister Foster approved the submission on 29 September indicating that the scheme should be launched as soon as possible.<sup>1048</sup>
- 19.22 On 8 December 2014 Minister Foster moved the motion before the Northern Ireland Assembly seeking approval of the domestic RHI regulations. The Assembly granted approval on the same

1041 DFE-145326 to DFE-145327

1042 DFE-145326

1043 WIT-44566

1044 TRA-11444

1045 TRA-11444 to TRA-11445

1046 TRA-11447

1047 TRA-11420

1048 DFE-303067 to DFE-303069

day and the Renewable Heat Incentive Scheme Regulations (Northern Ireland) 2014 (2014 No 301) came into force on 9 December 2014.

## Findings

109. DETI should have provided a domestic RHI business case to DFP that was entirely accurate, including with regard to the funding position.
110. DFP should not have treated the domestic RHI business case as a stand-alone business case.
111. The mishandling of the approval of the domestic RHI business case by DFP in September 2014 amounted to a significant missed opportunity to break the chain of unsatisfactory events relating to the non-domestic RHI scheme.
112. The various steps and many individuals involved in the approvals process once again failed to pick up key errors, omissions and inconsistencies in the domestic RHI business case. This failure contributed to the need for the important review of the non-domestic RHI scheme being missed, to the need for reapproval of the non-domestic RHI scheme being missed and to further confusion about the available funding and its associated risks.
113. The Inquiry notes that many of these problems in DETI arose due to limited resources and the major turnover in staff that occurred during 2014, the extent of which, according to Mr Hughes, was unparalleled in his experience. The staff changeover in question is discussed in greater detail in chapter 18 of this Report.