

**Northern Ireland Sustainable Energy Programme
(formerly known as the Energy Efficiency Levy Programme)**

**Consultation on the detailed operational
arrangements and the revised Framework
Document**



July 2009

1.0 Introduction and Consultation Questions

- 1.1 The purpose of this consultation is to invite comments on the detailed operating arrangements for the Northern Ireland Sustainable Energy Programme (NISEP), formerly known as the Northern Ireland Energy Efficiency Levy (EEL) Programme, as set out in the attached Framework Document (Appendix 1).
- 1.2 This follows on from the full consultation on the review of the EEL and the subsequent conclusions paper published in March 2009 and is part of the Utility Regulator's development of our decision regarding proposal 7 in the conclusions paper: "Greater clarity in the Framework Document". Our decision in relation to proposal 7 stated that we would make incremental changes to the Framework Document by September 2009 and fully revise the document by September 2010. This paper therefore seeks views on the attached Framework Document which will apply to the NISEP schemes to be run in 2010/2011 and therefore is due to be in place by September 2009. The Framework Document will then undergo further development in advance of further opening of the scheme to competition.
- 1.3 In particular, views are sought in response to the following questions:
- Question 1 Respondents are asked to comment on the level of detail contained in the attached Framework Document. Are there any points which need to be clarified in order to facilitate the smooth operation of schemes for the year commencing April 2010?
- Question 2 Respondents are asked to comment on whether or not they agree with the proposal to carry out a further round of consultation on the types of organization permitted to bid for funding, before the second wave of opening up the NISEP to competition begins?
- Question 3 Respondents are asked to comment on whether or not they agree with the stated purpose of the target setting and incentive mechanism and the list of criteria for a good incentive mechanism as presented in Table 1 of this consultation document?
- Question 4 Respondents are asked to comment on whether or not they agree with the target setting and incentives mechanism as set out in sections 3.9 and 3.10 of the attached Framework Document and

as detailed in section 3.0 of this consultation document?
(If respondents feel that they have ideas for a mechanism which better meets the criteria set in Table 1 they are asked to submit their ideas.)

Question 5 Respondents are asked to list any topics/issues which they would like to be further considered when preparing the Framework Document for September 2010 and beyond.

2.0 Context and Strategic Intent

- 2.1 Since its inception in 1997/8 the EEL Programme (now the NISEP) has represented an important element of the Utility Regulator's response to its duty to protect customers and its duty to have regard for the environment. The importance of the Programme has increased over the years as issues such as fuel poverty and fuel security and environmental sustainability have increased in importance. The strategic objectives of the Programme are to contribute to
- a. the achievement of efficiency in the use of energy,
 - b. the achievement of socially and environmentally sustainable long term energy supplies,
 - c. the achievement of the above at best value to consumers while also having due regard for vulnerable customers.
- 2.2 Within this strategic framework the Utility Regulator acknowledges that it is often more difficult and expensive to deliver energy savings to vulnerable customer groups than for example to the commercial sector. Therefore, given the importance of ensuring that vulnerable customers continue to benefit from the NISEP, the Utility Regulator has retained an 80% ring-fence in the funding to be directed to schemes for vulnerable groups.
- 2.3 The Utility Regulator continually strives to find new and innovative ways to incentivize and encourage the delivery of cost effective energy savings through the Programme and considers that (within the ring-fence provisions) overall cost effectiveness of the energy savings is very important. However for completeness we acknowledge that over time energy savings may become more difficult to achieve in light of the "low hanging fruit effect," i.e. once all the most cost effective measures have been installed we must then consider the next most cost effective measures and so on. The Utility Regulator will continue to monitor overall cost effectiveness of the Programme between now and the next review.

- 2.4 The EEL was reviewed in 2006 at which time the Utility Regulator promised a further review in 2009. In March 2009 the Utility Regulator set out its conclusions on the reform of the then EEL Programme. The full conclusions paper is available on our web site (www.niaur.gov.uk/uploads/publications/EEL_Decision_Paper_March_2009.pdf) and the main conclusions are set out in Section 1.1 of the proposed Framework Document which is attached as Appendix 1 of this paper. For ease of reference they include:
- opening up the Programme to competition from bidders other than licensed electricity suppliers (opening up to take place in two phases starting with licensed gas suppliers);
 - allowing funding for renewables and innovative measures;
 - a cautious approach to the level of funding available; and
 - the reform of the target setting and incentive mechanism.

3.0 Changes to Framework Document for 2010/2011 Schemes

- 3.1 As part of the March conclusions paper, the Utility Regulator recognized the importance of appropriate consultation. Therefore the Utility Regulator has decided to consult on the attached Framework Document which contains all the detailed rules for operating schemes in the year commencing March 2010 and also contains further detail on the rules to be incorporated beyond 2010.

Opening up to Competition

- 3.2 This revised Framework Document is set up to facilitate the first wave of opening up the NISEP to bidding from organisations other than licensed electricity suppliers, as it will specifically allow bids from licensed gas suppliers.
- 3.3 The Framework Document also contains some detail regarding the types of organisations which will be permitted to bid for funding following the second phase of opening up the Programme. The Utility Regulator however, recognises the need for further consultation and detail regarding the bidding process and the assessment of bidding criteria. Therefore, a second round of consultation will take place, specifically on the detail regarding bidding arrangements for non license holders. The Utility Regulator considers that the second round of consultation on the bidding process, the criteria and the types or organization permitted to bid for funding should take place before the second wave of opening the NISEP begins.

Target Setting and Incentives Mechanism

- 3.4 Having taken on board comments from stakeholders, the Utility Regulator recognises there may be a need for more clarity and transparency regarding the target setting and incentive mechanism. In order to develop clear thinking in relation to targets and incentives the Utility Regulator has identified the list of criteria in Table 1 to help define an effective target setting and incentive mechanism.

Table 1: Criteria for Effective Target Setting and Incentive Mechanism

An effective target setting and incentive mechanism for the NISEP Programme should deliver the following:
1. Achievement of the Programme's objectives (as stated in para.2.1).
2. Transparency and ease of use.
3. Targets which are stretching but not impossible to meet and exceed.
4. Targets which accurately reflect the types of measure put forward.
5. A return i.e. incentive payment, which encourages participation in the programme, taking into consideration: <ul style="list-style-type: none">• the levels of effort which go into effectively managing schemes,• the levels of risk associated with effectively managing schemes, and• the benefits to customers.
6. Targets and incentives which encourage programme participants to strive to deliver more cost effectiveness to customers.
7. Encourage participants to undertake schemes which involve the most difficult and hard to reach vulnerable customers.

- 3.5 Having developed the above criteria in Table 1, we consider that there is merit in seeking further comments from stakeholders on the development of the detailed incentive mechanism. Therefore, we are seeking views on whether targets should be set before or after bids are received. The advantages and disadvantages of the two types of target setting are set out in Table 2 overleaf.

Table 2: Advantages and Disadvantages of Ex-Post and Ex-ante Target Setting

<u>Ex-Post</u> <i>Setting targets after bids are received</i>	<u>Ex-ante</u> <i>Setting targets before bids are received</i>
Advantages	Advantages
<i>Targets accurately reflect the exact mix of measures proposed by scheme bidders.</i>	<i>Scheme bidders are provided with more certainty when developing schemes.</i>
<p><i>In a competitive arena scheme bidders will strive to “bid in” accurate forecast energy savings for the following reasons;</i></p> <ul style="list-style-type: none"> <i>• If bidders overstate forecast energy savings the targets will be set at a level which they will be unable to reach, thus the bidder will be unable to earn incentives.</i> <i>• If bidders understate forecast energy savings. They are unlikely to be successful in a fully competitive bidding process.</i> 	<i>May be more appropriate prior to the full opening up of the scheme as the ex-post option relies on competition to ensure scheme bidders strive for accurate forecast energy savings.</i>
Disadvantages	Disadvantages
<i>Provides less certainty and potentially more risk for bidders at the point where they decide whether or not invest in developing a bid.</i>	<i>Runs the risk that targets may be set too low or too high.</i>

- 3.6 The March conclusions paper proposed moving to an ex-post system on the basis that it would more accurately reflect the mix of measures actually proposed. However the Utility Regulator now considers that the system detailed below can go some way to achieving that whilst also delivering more

transparency to potential bidders. The Utility Regulator considers that a move to an ex-post system of target setting should be delayed until competition for schemes is well established and has been assessed. The other principles of target setting are to remain, including the requirement that participants “recycle” any incentives earned above the threshold of 8% of total project funds into fuel poverty/energy efficiency work which is additional to that already planned. The proposed new target setting mechanism will work as follows:

- a. Target cost effectiveness will be set in advance in order to provide more certainty for potential bidders.
- b. For clarity – scheme bidders will now know the target cost effectiveness in advance of putting in a bid and they will be in a better position to estimate the target energy to be saved. Target energy savings for each individual scheme will be set by dividing the target cost effectiveness by the amount of NISEP funding actually granted i.e.

$$\text{Target Energy Savings} = \text{NISEP funding} / \text{Target Cost Effectiveness}$$

e.g. if target cost effectiveness = 2 pence per KWh of energy saved and the scheme receives £100,000 of NISEP funding, the target energy saved will be 5 GWh. (2p per kWh = £20 per MWh = £20,000 GWh therefore the calculation is: 100,000/20,000=5 GWh)

- c. Schemes will be grouped into categories as shown in Table 3 below. Note that there are ring-fence provisions in the framework document aimed at ensuring a wide variety of schemes – 80% priority (subdivided into 34% whole house solutions and 46% other measures), 10% innovative non priority and 10% other non priority. These ring-fencing arrangements remain and the groups specified in Table 3 are for the purpose of target setting on a scheme by scheme basis only.
- d. In order to meet the criteria set out in Table 1 and allow applicants to earn a reasonable level of incentive payments for all types of schemes, the target cost effectiveness figures for the categories within the priority group will be doubled to give ‘revised cost effectiveness’ figures. The ‘revised target cost effectiveness’ figures, shown in Table 4 will be used for target setting purposes.

Table 3: Scheme Categories for Target Setting

Priority Group Schemes
<i>Priority Domestic – individual measures</i>
<i>Priority Domestic – whole house solutions</i>
Non Priority Group Schemes
<i>Non Priority Domestic – established, whole house solutions</i>
<i>Non Priority Domestic – established, individual measures</i>
<i>Non Priority Domestic – renewable biomass boilers</i>
<i>Non Priority Domestic – renewable solar thermal</i>
<i>Non Priority Domestic – innovative technology /hard to treat, whole house solutions</i>
<i>Non Priority Domestic – innovative technology /hard to treat, individual measures</i>
<i>Non Priority Domestic – innovative technology /hard to treat, insulation only (including interior or exterior solid wall insulation)</i>
<i>Non Priority Commercial – established technology</i>
<i>Non Priority Commercial – innovative</i>

- 3.6 Table 3 clarifies the detail in relation to the statement in the March conclusions paper that schemes should be grouped before targets are set. The March paper did not set out what the groups should be. The Utility Regulator believes that the above groups provide a good basis for ensuring that the targets accurately reflect the types of measures actually taken.
- 3.7 Table 4 below sets out the proposed cost effectiveness targets for each category, and the revised cost effectiveness targets i.e. with the figures doubled for priority group schemes, which will be used for target setting for schemes to be undertaken in 2010/2011. Further detail is contained in Section 3.9 of the revised Framework Document.

Table 4: Target Cost Effectiveness for 2010/2011 Schemes

Category	Target Cost Effectiveness (p/kWh)	Multiplier Factor	Revised Target Cost Effectiveness
Priority Domestic Individual Measures	0.982	2.0	1.964
Priority Domestic Whole House Solutions	3.682	2.0	7.364
Non Priority Domestic Whole House Solutions	0.624	1.0	0.624
Non Priority Domestic Established Individual Measures	0.329	1.0	0.329
Non Priority Domestic Renewable Biomass Boilers	2.243	1.0	2.243
Non Priority Domestic Renewable Solar Thermal	9.754	1.0	9.754
Non Priority Domestic Innovative Individual Measures	0.329	1.0	0.329
Non Priority Domestic Hard to Treat Whole House Solutions	2.796	1.0	2.796
Non Priority Domestic Hard to Treat Insulation Only (including solid or exterior wall insulation)	6.363	1.0	6.363
Non Priority Commercial Established Technology	0.276	1.0	0.276
Non Priority Commercial Innovative Technology	0.276	1.0	0.276

- 3.8 The March conclusions paper stated that the new level for incentive payments would be £1,000 per GWh of target exceeded. This will be the case for non priority group schemes, however, for priority group schemes the Utility Regulator has decided to increase the level of incentive payment earned to £2,000. This to acknowledge the generally greater degree of complexity involved in undertaking schemes for vulnerable customers, for example: the difficulty in identifying properties to participate in a scheme, benefit checks, heating system installations, inspections and grant administration etc.. More detail on the incentive payments is contained in Section 3.10 of the attached Framework Document.
- 3.9 The Utility Regulator, in conjunction with the Programme Administrator, may further refine the proposed target setting and incentive mechanism for 2010/11 NISEP schemes following the consultation and analysis of responses received.

4.0 Conclusions and Next Steps

- 4.1 Respondents should send their responses to the questions listed in Section 1 and any other comments on the attached Framework Document to:

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In order to have the Framework Document finalized in time for the 'call for schemes' in September 2009, **responses to this consultation must be received by Friday 21st August 2009 at the latest.** (Please note that due to the tight timescale for having the Framework Document ready, we will be unable to grant any extensions to the consultation period.)

- 4.2 Following this consultation the Framework Document will be finalised and placed on our website in September 2009. In September 2009 the Utility Regulator also intends to issue a call for schemes inviting bids for funding for the year commencing April 2010. Applications for funding should be based on the September 09 Framework Document, and completed bids should be received no later than 2 January 2010. Bidders will be informed whether or not they are successful in February 2010.