

**EXPLANATORY MEMORANDUM TO
THE RENEWABLE HEAT INCENTIVE REGULATIONS 2011**

2011 No. [XXXX]

and

**THE RENEWABLE HEAT INCENTIVE (AMENDMENT TO THE ENERGY ACT
2008) REGULATIONS 2011**

2011 No. [XXXX]

1. This explanatory memorandum has been prepared by the Department of Energy and Climate Change (DECC) and is laid before Parliament by Command of Her Majesty.

2. Purpose of the instrument

2.1 The first instrument, the Renewable Heat Incentive Regulations 2011 (“the RHI Regulations”), establishes a Renewable Heat Incentive (“the RHI scheme”) to facilitate and encourage the renewable generation of heat by giving subsidy payments to eligible generators of renewable heat and producers of biomethane. The RHI Regulations will give functions to the Gas and Electricity Markets Authority (“the Authority”) to administer the scheme. The key functions for the Authority include:

- Accreditation of installations eligible for the RHI scheme;
- Registration of producers of biomethane who are producing biomethane for injection into the gas network;
- Calculating and paying periodic support payments to participants;
- Publication of annual tariff rates;
- General administrative functions needed to operate the scheme, including enforcement and auditing provisions and an appeals process;
- Reporting to the Secretary of State; and
- Providing guidance to participants on the scheme criteria.

2.2 The second instrument, the Renewable Heat Incentive (Amendment to the Energy Act 2008) Regulations 2011 (“the RHI Amendment Regulations”), amends the definitions of biomass and biogas in section 100 of the Energy Act 2008 and adds biogas as a source of energy for the renewable generation of heat.

3. Matters of special interest to the Joint Committee on Statutory Instruments

3.1 None

4. Legislative Context

4.1 The Secretary of State makes both instruments in exercise of powers conferred by section 100 of the Energy Act 2008 (“the Act”). However, the RHI Regulations are made in exercise of the powers conferred by section 100 as amended by the RHI Amendment Regulations. Accordingly, although both sets of Regulations will be laid

in Parliament together and approval for both will be sought at the same time, the RHI Regulations will not be made until such time as the RHI Amendment Regulations have come into force.

4.2 This is the first time the powers conferred by section 100 of the Act are being utilised.

4.3 Further Regulations to extend the RHI scheme to the domestic sector and to include additional heat technologies are planned for 2012.

5. Territorial Extent and Application

5.1 This instrument applies to Great Britain.

5.2 In accordance with section 100(7) of the Act, the Secretary of State has obtained the Scottish Ministers consent to the making of both sets of Regulations.

6. European Convention on Human Rights

6.1 Gregory Barker, Minister of State for the Department of Energy and Climate Change, has made the following statement regarding Human Rights:

In my view the provisions of the Renewable Heat Incentive Regulations 2011 and the Renewable Heat Incentive (Amendment to the Energy Act 2008) Regulations 2011 are compatible with the Convention rights

7. Policy background

- *What is being done and why*

The RHI Regulations

7.1 The overarching objective of the RHI scheme established by the RHI Regulations is to facilitate the heat sector's contributions to the Government's legally binding target of supplying 15% of total energy consumption from renewable sources by 2020. The Regulations are intended to encourage a step change in the uptake of renewable heat technologies helping to increase renewable heat from its current level of around 1.5% to around 12%. As well as providing a direct contribution to the 2020 Renewable Energy Target, the policy is in line with longer-term energy and climate change goals (e.g. security of supply and carbon budgets).

7.2 Currently, renewable heat technologies are unable to compete financially with fossil fuel alternatives and there are a number of non-financial barriers which prevent their deployment, such as perceived risks associated with new technologies and costs of disruption associated with switching. Without government intervention, the private sector is not expected to invest in renewable heat technologies.

7.3 Renewable heat technologies have been patchily supported through grants schemes and tax rebates. Past experience and industry feedback indicates that the "stop and go" nature of grants as well as their limited funding makes grants less suitable for large scale roll-out. It was therefore concluded that legislation was required. In order to stimulate the market to deliver ambitious action on renewable heat, the RHI Regulations establish a subsidy (referred to in the RHI Regulations as a periodic support payment) based on a pence per kWh rate for renewable heat generated and used for one of the eligible purposes specified. The subsidy is to compensate generators of

renewable heat for the difference in up-front and ongoing costs between renewable and fossil fuel generated heat, providing additional compensation to overcome non-financial barriers associated with the uptake of renewable technologies, and paying a return on the up-front investment. Producers of biomethane receive a tariff calculated by reference to the costs of production and the process of injection to the gas network.

7.4 In addition to conferring functions on the Authority to administer the RHI scheme, the Regulations:

- specify the criteria with which a plant generating heat must comply in order to be eligible for the scheme;
- specify the eligible purposes for which heat will receive payment;
- stipulate biomass composition requirements for participants generating heat from solid biomass;
- stipulate feedstock requirements for biogas used to generate heat and to produce biomethane; and
- set out ongoing obligations on participants in the RHI scheme relating to general and administrative requirements with which they must comply.

7.5 The full RHI scheme will be introduced in two phases:

- In the first phase, long-term tariff support will be targeted in the non-domestic sectors, at the big heat users - the industrial, business and public sector.
- The second phase of the RHI scheme will see households moved to a long-term tariff support. Further regulations timed to align with the Green Deal which is intended to be introduced in 2012, are proposed for this purpose.

7.6 The Regulations planned for introduction in 2012 will also include additional heat technologies in the RHI scheme. These are mainly relevant to the commercial and industrial sectors.

7.7 The European Commission are in the process of assessing this RHI scheme for the purpose of providing state aids approval. The RHI Regulations will not be made until the scheme has received state aids clearance.

The RHI Amendment Regulations 2011

7.8 The definition of biogas in section 100 (3) of the Energy Act 2008 would only have allowed for support for the production of biogas made through anaerobic digestion. This instrument will enable the RHI scheme to support the production of biogas produced by a range of methods including gasification and pyrolysis. Biogas was not included in the sources of energy and technologies listed in section 100(4) of the Energy Act 2008. This instrument will enable support for the generation of renewable generation of heat using biogas.

7.9 The definition of biomass in section 100 (3) of the Energy Act 2008 would have allowed for the burning of “peat” as a biomass fuel source. This instrument seeks to rectify this in line with the approach already taken for biomass electricity generation in the Renewables Obligation Order 2009.

- **Consolidation**

7.10 None

8. Consultation outcome

8.1 The RHI scheme proposals were subject to a twelve week consultation by the previous administration in February 2010. The consultation proposals were published on the DECC website alongside a number of government commissioned studies and independent analyses, all of which provided evidence to support the proposals. The consultation received over 650 responses. Feedback was overwhelmingly supportive of the policy proposals. As the first incentive of its kind worldwide it generated considerable interest from the public, manufacturers and installers, as well as the international community.

8.2 Commitment to renewable heat was made in the 2010 Spending Review, where an allocation of £860m over the spending review period was provided for the RHI.

8.3 In order to maximise value for money in achieving the required uptake the Coalition Government reassessed the RHI proposals put forward under the previous Administration and decided to:

- a) maintain the scheme for the non domestic sector with some adjustments since the February 2010 consultation in order to improve value for money; and
- b) delay the introduction of the scheme for the domestic sector until 2012.

8.4 This phased approach will allow further consideration of the most cost effective way of increasing renewable heat deployment at the domestic scale while maintaining a policy which sets out a path towards seeking to deliver a 12% target for renewable heat by 2020. Although this is less favourable for the small scale industries, the renewables industry and trade associations understand the rationale behind this and have been supportive of the decision. DECC has communicated the changes from the original proposals to stakeholders to the Devolved Administrations of Scotland and Wales and the Authority.

8.5 The detailed arrangements and policy decisions including scheme administration, tariff levels, enforcement and appeals and eligibility criteria were published in March 2011. Draft text for the Regulations was also published on the DECC website for comment. Meetings were arranged with specific stakeholders to critique the proposed text, including a stakeholder workshop organised by DECC in April 2011 to discuss some of the more technical areas. The final RHI Regulations reflect comments and suggestions received through informal stakeholder feedback.

9. Guidance

9.1 The Authority will provide detailed guidance for potential participants in the RHI scheme in a variety of formats for the start of the scheme.

10. Impact

RHI Regulations

10.1 The RHI is a voluntary subsidy scheme. The impact on business, charities or voluntary bodies is only applicable if they are owners of eligible renewable heat

installations and apply for the RHI. The Department expects that the design of the tariff structure, which focuses higher support levels at the smaller scale will encourage uptake in the small firms segment. Small firms are also expected to benefit from business and job creation opportunities generated from increased demand for renewable technologies. Currently, a significant proportion of the firms which carry out domestic and other small scale installations are small firms.

10.2 The impact on the public sector is an increase of up to £5m per annum in the Authority's administrative expenditure resulting from development of systems and ongoing scheme administration.

10.3 HM Treasury will be providing funds for tariff payments directly to the Authority and have committed to covering these costs. For the first projection period – to 2020:

- The in year subsidy cost (cost to the Government) is £1.4bn
- The cumulative subsidy cost to 2020 is £5.4bn) – subject to confirmation in the next Spending Review period.

10.4 An Impact Assessment is attached to this memorandum and will be published alongside the Explanatory Memorandum on www.legislation.gov.uk.

RHI Amendment Regulations

10.5 The impact on business, charities or voluntary bodies is nil.

10.6 The impact on the public sector is nil.

10.7 No impact assessment has been prepared for this instrument.

11. Regulating small business

11.1 The legislation applies to small business.

11.2 To minimise the impact on small business employing up to 20 people, the approach taken is to exempt participants under 1 MWth from sustainability reporting requirements for biomass and measurement of fossil fuel contamination. Small and Medium sized Enterprises (SMEs) represent a significant component of the renewables industry. The Department's consultation on the RHI scheme indicates small businesses will have a total installed capacity below 1 MW so will be unaffected by these obligations.

11.3 The basis for the final decision on what action to take to assist small business is to seek to provide support levels that enable industry to deliver renewable heat. The Department expects the RHI to lead to an expansion of the renewables industry and its associated supply chains creating opportunities for existing SMEs to grow and new start-up businesses.

12. Monitoring & review

12.1 The instrument aims to increase renewable heat from its current level of around 1.5% to around 12%. The RHI scheme differentiates support levels by technology, size and consumer groups. In doing so the scheme will seek to incentivise uptake across a range of technologies and sectors while also minimising the costs to society and avoiding the creation of perverse incentives (e.g. over-generation of heat). The

Department will conduct periodic reviews of the scheme, timed to coincide with reviews of the Renewables Obligation and Feed in Tariff where possible. At scheme reviews the Department will reassess the costs of technologies and whether the target rate of return is still appropriate and consider revision of tariff levels accordingly. Scheme reviews will also consider the treatment of technologies not currently supported, whether it is appropriate to allow those technologies to access the scheme and, if so, consider appropriate tariffs.

13. Contact

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