

VAT: guidance on changes to energy-saving materials

Q1. What is this guidance about?

A1. This guidance provides an overview of changes to amend the scope of the reduced rate for the installation of energy saving materials.

Q2. Why are these changes being made?

A2. This measure amends the scope of the relief to ensure consistency with a Court of Justice of the European Union (CJEU) ruling (Case C-161/14).

Q3. When do the changes take effect?

A3. The changes will affect supplies made on or after 1 October 2019 except for supplies paid for before that date or made pursuant to a contract entered into before that date.

Q4. What are the changes?

A4. The changes are best categorised into three parts.

(i) The reduced rate of 5% will no longer be available for the installation of wind or water turbines.

(ii) The reduced rate will remain fully available (except on wind and water turbines) on supplies of services of installing ESMs in residential accommodation:

- to a “qualifying person”, where the residential accommodation is the qualifying person’s sole or main residence (note: a “qualifying person” is defined in legislation as a person who is aged 60 or over, or is in receipt of certain benefits); or
- to a “relevant housing association” as defined in legislation; or

- where the residential accommodation is a building or part of a building used solely for a “relevant residential purpose” as defined in legislation.

(iii) Otherwise, the reduced rate will remain available (except on wind and water turbines) provided that the open market value of the supply of the ESMs does not exceed 60% of the cost (excluding VAT) of the total value of the supply of installing the energy saving materials to the customer. If the value of the energy saving materials exceeds 60%, then only the labour cost element will qualify for the reduced rate (with the supply of the materials standard rated).

Q5. What is meant by the “open market value of the supply of materials” and the “cost of the total supply”?

A5. The open market value of the supply of materials is the price that an installer of ESMs would have to pay (excluding VAT) to purchase the materials on the open market. In practice, this will normally be the price the installer pays their own supplier for the materials. The inclusion of the term “open market value” has been included to guard against the artificial undervaluation of materials.

The cost of the total supply is the total charge (excluding VAT) made to the customer (i.e. the total value of the supply of installing the energy-saving materials).

Example: A business installs insulation into a residential property. The business (the installer) is charged £400 (excluding VAT) for the insulation material, and charges their customer £1,000 (excluding VAT) for the installation. Since the value of the materials (the insulation) is only 40% of the cost of the total supply to the customer, the installer can

charge the reduced rate of 5% on the total supply i.e. 5% of £1,000 = £50.

Q6. Why are water turbines and wind turbines being withdrawn from the relief?

A6. The ruling by the CJEU has clarified that installation of wind and water turbines to generate electricity is not within the permitted items for reduced VAT rates as set out in the EU framework.

Q7. Why do these changes need to be made given the UK will be leaving the EU?

A7. During the implementation period, the UK will no longer be an EU Member State but market access will continue on current terms.

Common rules will remain in place until the end of the period, meaning that business will trade on the same terms as now. For VAT and excise, this will effectively mean maintaining the status quo.

While there may be flexibility in the future, during the implementation period the UK should adhere to EU VAT and excise rules and so it is required to comply with the CJEU judgment.

Q8. Why do only people aged 60 years or over, or those on certain benefits qualify for the full relief on the installation of energy saving materials?

A8. The EU VAT framework allows the reduced rate of VAT to apply to supplies of the installation of energy saving materials in housing where it is installed as part of social policy – for those in social need. This is how the UK has determined its social policy criteria.

Q9. Why is the reduced rate only available on ESMs when the value does not exceed 60% of cost of the total supply?

A9. The EU VAT framework allows the reduced rate to apply to the whole installation except where the cost of the goods element is 'significant'. 60% is judged to strike the right balance in terms of complying with EU law and minimising any adverse impacts on UK businesses.

Q10. Will the changes require legislative change?

A10. Yes, the changes will be introduced by affirmative Statutory Instrument.

Q11. Has HMRC previously consulted on the changes?

A11. Yes, HMRC originally published a consultation document on 9 December 2015, together with the draft legislation. This consultation is therefore a short technical consultation on the proposed legislation that, subject to Parliamentary approval, will be implemented with effect from 1 October 2019.

Q12. Where can I find further guidance on ESMs?

A12. Further guidance is available in VAT Notice 708/6: energy saving materials and VENS AV3000. These can be accessed via the gov.uk website.