

# APPLICABLE VAT RATE ON HEAT PUMP INSTALLATIONS

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The purpose of this technical bulletin is to advise members of changes to the VAT rate announced in the Chancellor's Spring Statement of 23<sup>rd</sup> March 2022.

## 1. BACKGROUND

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In July 2014 HMRC introduced a scheme for applying a reduced rate of VAT of 5% on energy saving materials and heating equipment. It followed on from the enhanced capital allowances list of previous years whereby heating equipment which featured on that list could have a 5% VAT rate applied when the products were installed in domestic situations. The move was designed to encourage the uptake of energy efficient heating systems such as heat pumps in retrofit applications.

In October 2019 the rules were subtly changed to incorporate a "60% test" that must be applied for the reduced rate to be used if certain social policy conditions are not met.

The Spring Statement of 23<sup>rd</sup> March 2022 has reversed that 2019 ruling as from 1<sup>st</sup> April 2022 meaning that the social conditions and 60% requirements no longer apply at all. This has been implemented to incentivize homeowners to install energy saving heating materials as part of a wider package of Government measures targeted at improving energy efficiency and driving the decarbonisation of heat agenda.

The zero rating applies to installations of these products and therefore cannot be applied by sellers of equipment only.

At this moment in time the zero rating can only be used by contractors in Great Britain as the EU need to agree to this move for Northern Ireland. HMRC assured us that they are working on this being a UK wide initiative as soon as possible.

## 2. VAT NOTICE 708/6 – CONFUSION OVER DEFINITIONS<sup>1</sup>

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In February 2021 an amendment to clause 2.17 Air source heat pumps was made to correct a mistake where air source heat pumps of the split air conditioning type had been specifically ruled out from the scheme. There remained a large element of confusion across the sector, however, and the issue persisted. After extensive talks between the BESA and HMRC the guidance has been updated to clarify the applicability rules and allow air source reverse cycle heat pump air conditioners in the same way it applies for monoblock heat pumps.

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<sup>1</sup> <https://www.gov.uk/guidance/vat-on-energy-saving-materials-and-heating-equipment-notice-7086>

The new text published on 6<sup>th</sup> April reads:

### 2.18 Air source heat pumps

Air source heat pumps use the air as a source of heat. They absorb heat from the outside or surrounding air and transfer that into useable heat in the home for space or water heating.

Fixed air source heat pumps can be reversed so that they can draw heat from inside a building, thus providing cooling during the summer as well indoor heating for colder periods of the year.

Only air source heat pumps that are permanently fixed and are not portable or moveable qualify as energy-saving materials.

HMRC's understanding is that most air conditioning units are air source heat pumps. However, in cases of doubt, deciding whether any particular product is to be treated as an air source heat pump will depend on the facts of the case.

## 3. IN CONCLUSION

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**The defining factor for VAT to be applied as zero rated in relation to paragraph 2.17 is that the air source heat pump can be used to *heat* the home.**

**In summary, provided the heat pump uses air as the heat source to heat the home it will qualify as an energy saving material, irrespective of whether it can also cool or not.**

**Official VAT Notice 708/6 as of 6th April 2022 can be found here:**

**<https://www.gov.uk/guidance/vat-on-energy-saving-materials-and-heating-equipment-notice-7086>**

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