



## Reduced rate VAT

on domestic\* air source heat pump applications

HMRC Statutory Instrument  
2005 no. 726

### Legislation

5% VAT L001

**Value-Added Tax** *n. Abbr. VAT.* A tax on the estimated market value added to a product or material at each stage of its manufacture or distribution, ultimately passed on to the consumer.

**Did you know households are responsible for 1/4 of all emissions?** As part of ongoing efforts to reduce emissions, the Government has reduced VAT on air source heat pumps for domestic applications, to 5% on equipment and installation.

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# The Government is committed to reducing emissions of the gases responsible for global warming as part of its Climate Change Programme and the Kyoto Protocol. Households are responsible for a quarter of all emissions, so are being targeted through a reduced rate VAT on energy efficient heating systems, including air source heat pumps.

## Reducing CO<sub>2</sub> emissions

Reducing the rate of VAT on energy efficient products lowers the cost differential between air source heat pumps and conventional heating systems to the final customer. **A dedicated air source heat pump is estimated to save in excess of two tonnes of carbon emissions per year**, so the Government is applying the reduced rate VAT in this case to increase the demand for energy efficient heating systems at the expense of existing less efficient heating systems.

## Who qualifies?

VAT has been reduced on all air source heat pumps through a change to the VAT Act 1994, in Statutory Instrument 2005 No. 726 which came into force on the 7th April 2005.

The reduced rate only applies to the supply and installation of air source heat pumps to buildings that are either:

- \* **a)** residential accommodation, or
- \* **b)** intended for use solely for a relevant charitable purpose.

An indication of the types of buildings that fall into these categories is listed below. **Please note this list is not exhaustive.** Exclusions and definitions do apply to both these categories and full details are in notice 708, Buildings and Construction, section 14.2, 14.6 and 14.7 respectively.

## \* Residential accommodation

In addition to a standard residential house or flat that consists of self-contained living accommodation, the following may also be eligible:

- (a) a home or other institution providing residential accommodation for children,
- (b) a home or other institution providing residential accommodation with personal care for persons in need of personal care by reason of old age, disablement, past or present dependence on alcohol or drugs or past or present mental disorder,
- (c) a hospice,
- (d) residential accommodation for students or school pupils,
- (e) residential accommodation for members of any of the armed forces,
- (f) a monastery, nunnery or similar establishment, or
- (g) an institution which is the sole or main residence of at least 90 per cent of its residents.

## \* Intended for use solely for a relevant charitable purpose

'Relevant Charitable Purpose' means use by a charity in either or both of the following ways:

- (a) otherwise than in the course or furtherance of business
- (b) as a village hall or similarly in providing social or recreational facilities for a local community.

If you are unsure if your project would be included please contact HM Revenue and Customs Advice Service.

## How it works

The VAT advice service has indicated that the **equipment cost** and **installation cost** for a qualifying project must be on the same invoice to benefit from the reduced rate of VAT.

Therefore, the contractor will purchase an air source heat pump at the standard rate VAT (20%), but will sell to the qualifying final customer at the reduced rate VAT (5%).

The value difference in Input (purchase) and Output (sales) VAT will be detailed on the contractor's normal VAT return, and can be reclaimed accordingly. This means there is no financial implication for the contractor, and a significant cost benefit for the final customer.

If the contractor supplies an air source heat pump to a qualifying final customer but does not install it, then the standard rate VAT will apply.

## Further information

If you require more detailed information on any of the areas mentioned in this release, the following HM Revenue and Customs publications may prove useful:

- Statutory Instrument 2005 No. 726
- Notice 708, Buildings & Construction
- Regulatory Impact Assessment (RIA) – Reduced rate of VAT on Air Source Heat Pumps and Micro Combined Heat and Power Units
- Value Added Tax Act 1994, Schedule 7A.

Details of all publications are available on the HMRC website. If you require further clarification or advice we recommend you contact HMRC Advice Service on: 0845 010 9000 or visit their website: [www.hmrc.gov.uk](http://www.hmrc.gov.uk)