

EXPLANATORY MEMORANDUM TO

THE VALUE ADDED TAX (INSTALLATION OF ENERGY-SAVING MATERIALS) ORDER 2022

2022 No. 361

1. Introduction

- 1.1 This explanatory memorandum has been prepared by HM Revenue and Customs (HMRC) on behalf of HM Treasury and is laid before the House of Commons by Command of Her Majesty.
- 1.2 This memorandum contains information for the Select Committee on Statutory Instruments.

2. Purpose of the instrument.

- 2.1 The intention of the statutory instrument is to reverse legislation that was introduced in 2019, and which narrowed the scope of the previous Value Added Tax (VAT) relief for energy-saving materials (ESMs), and to introduce a temporary zero rate of VAT for the installation of ESMs from 1 April 2022 to 31 March 2027 in Great Britain.

3. Matters of special interest to Parliament

Matters of special interest to the Select Committee on Statutory Instruments.

- 3.1 The 21-day rule is breached on this occasion. The reason for this is to accelerate take-up and prevent loss of investment for businesses as a longer delay between announcement and implementation would potentially have an adverse effect on the ESMs market. Businesses or consumers may delay entering contracts and cause a temporary stalling effect in the market which could result in supply bottlenecks further down the line.
- 3.2 This relief is intended to reverse the restrictions imposed by our previous membership of the European Union and encourage the take up of installations of ESMs in residential accommodation. This is an important element of the government's aim to increase energy efficiency in the United Kingdom (UK).

4. Extent and Territorial Application

- 4.1 The territorial extent of this instrument is the United Kingdom.
- 4.2 The territorial application of this instrument is the United Kingdom.

5. European Convention on Human Rights

- 5.1 The Financial Secretary to the Treasury, the Rt Hon. Lucy Frazer has made the following statement regarding Human Rights:

“In my view the provisions of the Value Added Tax (Installation of Energy-Saving Materials) are compatible with the convention rights.”

6. Legislative Context

- 6.1 The legislation will permanently reverse, in Great Britain, the legislative changes that the United Kingdom was required to make to narrow the scope of the relief in 2019 following the Court of Justice of the European Union (CJEU) ruling in European Commission v United Kingdom C-161/14. It also introduces a temporary zero-rate of VAT for the installation of qualifying ESMs in residential accommodation from 1 April 2022 to 31 March 2027. A sunset clause in the legislation will result in the automatic reversion to the reduced rate after five years unless the government introduces further legislation to extend the end-date.

7. Policy background

What is being done and why?

What did any law do before the changes to be made by this instrument?

- 7.1 The United Kingdom was required to implement legislative changes in 2019 to comply with infraction proceedings brought by the European Commission and which were upheld by the Court of Justice of the European Union in Case C-161/14 (European Commission v United Kingdom 2015). Consequently, reduced rating of installations of ESMs was limited to supplies that met certain social conditions or where the cost of the materials did not exceed 60% of the total value of the supply. If these conditions did not apply businesses were required to apportion their supplies and account for VAT at the reduced rate on the service element and the standard rate on the goods element. The UK was also required to exclude wind and water turbines from the list of qualifying ESMs.

Why is it being changed?

- 7.2 As the UK is no longer in the European Union the government is, in Great Britain, permanently reversing the 2019 changes along with introducing a five-year zero rate to the installation of ESMs in residential properties.
- 7.3 Businesses have requested the reversal of the 2019 changes following UK withdrawal from the EU to incentivise the take-up of ESMs in line with the government's net zero objectives.

What will it now do?

- 7.4 These changes will result in all installations of qualifying ESMs in Great Britain being covered by the zero-rate for a period of 5 years. Wind and water turbines will also be permanently added to the list of qualifying ESMs. The zero rate will be replaced with the reduced rate once the 5-year period ends, unless the government lays further legislation to extend the end date.

8. European Union Withdrawal and Future Relationship

- 8.1 This instrument is not being made under the European Union (Withdrawal) Act 2018 but relates to the withdrawal of the United Kingdom from the European Union (EU). This is because the UK is reversing legislation that was brought in as a result of EU infraction proceedings, which were upheld by the CJEU.

9. Consolidation

- 9.1 This instrument makes amendments to Schedule 7A and introduces a new Group in Schedule 8 to the VAT Act 1994. There are no plans to consolidate the legislation at this time.

10. Consultation outcome

- 10.1 To prevent the possible loss of investment on installations of qualifying ESMs, the government has chosen to introduce this measure on 1 April 2022. It has not been possible to consult in the time available.

11. Guidance

- 11.1 HMRC will update its guidance shortly after this measure is introduced.

12. Impact

- 12.1 The impact on business, charities or voluntary bodies is beneficial for those businesses that install ESMs in Great Britain, as they will no longer need to consider the social policy conditions or perform calculations to determine whether or not the installation qualifies for the relief. They will also, for a period of five years, no longer be required to charge and account for VAT on their supplies but will still be able to recover input tax in relation to these supplies. In so far as this VAT relief is passed on to consumers, it should boost demand for the installation of ESMs and benefit individuals and organisations that purchase the installation of ESMs in a residential property.
- 12.2 There is no, or no significant, impact on the public sector as this instrument will only impact residential installations of qualifying ESMs.
- 12.3 A Tax Information and Impact Note covering this instrument will be published on the website at <https://www.gov.uk/government/collections/tax-information-and-impact-notes-tiins>.

13. Regulating small business

- 13.1 This instrument applies to activities that are undertaken by small businesses.
- 13.2 No specific action is proposed to minimise regulatory burdens on small businesses (employing up to 50 people).
- 13.3 The basis for the final decision on what action to take to assist small businesses was that the changes reduce the administration associated with the relief for installed ESMs.

14. Monitoring & review

- 14.1 HMRC will monitor the effectiveness and application of this relief through normal audit activity and regular communication with affected taxpayer groups.
- 14.2 The instrument does not include a statutory review clause because it does not relate to a qualifying activity as specified by section 29 of the Small Business, Enterprise and Employment Act 2015.

15. Contact

- 15.1 Joseph Lennox at HM Revenue and Customs Telephone: 03000 566175 or email: Joseph.Lennox@hmrc.gov.uk can be contacted with any queries regarding the instrument.
- 15.2 Ian Broadhurst, Deputy Director, VAT Reliefs, Deductions and Financial Services, Indirect Tax Directorate, at HM Revenue and Customs can confirm that this Explanatory Memorandum meets the required standard.
- 15.3 Rt. Hon Lucy Frazer at HM Treasury can confirm that this Explanatory Memorandum meets the required standard.