VAT focus

Is VAT due on the 'free' supply of digital platforms?

Speed read

News that the Italian authorities are assessing Meta for VAT on the supply of Facebook has thrown into the spotlight the issue of whether VAT is due on the supply of 'free' digital services. It is arguable that there is the requisite link between such supplies and non-monetary consideration in the form of user data. There are undoubtedly difficulties in determining the taxable amount but cases on 'free' banking services and a parallel claim against Meta in the Competition Appeal Tribunal indicate that methodologies are available. Although a legal pathway is possible, this will ultimately be determined by a policy choice on how to address the value of harvesting data.

Valentina Sloane KC
Monckton Chambers
Valentina Sloane KC of Monckton Chambers is a leading barrister in EU, procurement, tax and duties law. The directories have consistently recommended Valentina as an outstanding practitioner. Email: vsloane@monckton.com; tel: 020 7405 7211.

When consumers use a 'free' social media platform, are they providing non-monetary consideration in the form of their data? Is VAT due on the supply of the platform and if so, what is the taxable amount?

The issue of whether free digital services are taxable transactions has assumed prominence in light of media headlines that Italian tax authorities are pursuing Facebook-owner Meta for alleged unpaid VAT of €870m. The basis for the alleged liability is that 'free' membership on Meta platforms comes in return for access to user data and should be classified as an exchange of services, therefore subject to VAT.

The idea has been canvassed before. The VAT Committee considered the issue in Working Paper No. 958 (30 October 2018) (see bit.ly/WP958). Germany asked whether the supply of IT services without any monetary consideration by an IT provider in exchange for the right to use the data of its clients, and the users' granting to the IT provider of the permission to use that data, constitute taxable transactions subject to VAT. If they were taxable, Germany wanted to know how the taxable amount for the services supplied should be calculated. The VAT Committee noted that IT providers use the data obtained for commercial purposes. In most cases, the IT provider sells the data for advertising purposes. The sale of the data constitutes a very important part of the turnover of these IT providers. Therefore, there is an exchange of an asset with economic value (the data) for an IT service.

So, what are the issues and how clear-cut are the conclusions?

Whether there is a B2B barter transaction with a taxable supply of data in exchange for a taxable supply of platform services

The VAT Committee first considered and dismissed the idea that the individual is making a taxable supply of data. On the basis of case law such as *Slaby* (Joined Cases C-180/10 and C-181/10), *Urfahr* (Case C-219/12) and *SPÖ* (Case C-267/08), the individual's provision of data does not constitute an economic activity. The individual provides data as the price to be paid for the use of the platform, not as a source of income. The data is within the 'personal sphere'.

The VAT Committee's analysis makes sense in the case of individuals using platforms such as Facebook for personal purposes but what of business platforms, such as LinkedIn? The same analysis surely applies. An accountant or lawyer posting articles on LinkedIn may well be doing so in order to obtain income, but the income is neither paid by the platform nor paid as consideration for the supply of the article. The creator hopes to obtain income from the business opportunities which prominence on the platform can create. Those are discrete taxable transactions with third parties, for other supplies (namely legal or accountancy services). The creation of the article is a marketing cost to the creator, not a taxable supply to a third party.

For this reason, it is inapt to describe the use of a platform in exchange for data as a 'barter transaction' in the VAT sense of a 'barter' being a B2B exchange of taxable transactions. However, that leaves open the separate issue of whether the IT platform is making a B2C taxable transaction in return for non-monetary consideration in the form of the individual's data. The IT platform provider is undoubtedly engaged in an economic activity. The question, therefore, is whether the platform is supplied for non-monetary consideration.

Whether there is a B2C supply of platform services in return for non-monetary consideration: the legal argument

The VAT Committee considered the legal principles on reciprocal performance. On the basis of case law such as *Tolsma* (Case C-16/93), *Český rozhlas* (Case C-11/15), *EC v Finland* (Case C246/08) and *Bastova* (Case C-432/15), the VAT Committee considered there is no direct link between the service provided by the platform and the value of the data provided by the individual. The Committee relied, in particular, on the fact that the data received varies in quantity and quality from one user to the other, individuals can provide false data (such as fake email addresses), the provider has no control over the amount of data provided to it and the IT provider does not offer different levels of service depending on the amount of quality of data provided to them. The Committee also considered that there is no obligation to provide a certain amount of data periodically to remain connected to the service.

There is certainly plenty of scope for argument on these issues.

First, the VAT Committee's factual assumptions appear simplistic. The collection of valuable data by platforms is far more sophisticated, extensive and subtle than the collection of a (perhaps fake) email address. The terms and conditions of many platforms oblige individuals to consent to the use of their data as a condition of use of the platform. The harvesting of data is complex and vast (see, for example, the sources listed in 'What you don't know about how Facebook uses your data', *New York Times*, 11 April 2018). The result is that *whenever* the individual uses the platform, he or she is consensually, automatically and necessarily creating and supplying data which is of value to the platform (and third parties to whom the data is sold) by virtue of what they click on, how long they pause to look at content etc. To this extent, factually, there is an immediate and direct reciprocal link between the use of the platform and the provision of data. Also, arguably, there is a broad correlation between the supply of data and the service

provided by the platform, in the sense that the greater the use of the platform, the greater the supply of data.

Secondly, the case law on the need for reciprocity and a direct link between supply and consideration is sufficiently flexible and nuanced (or, some might say, sufficiently inconsistent, unprincipled and uncertain) to allow scope for argument. In *Colchester Institute Corporation v HMRC* [2020] UKUT 368 (TCC), the Upper Tribunal stated: 'There is nothing in the case law to suggest that a link of that degree of specificity or directness must be present in order to constitute consideration. The concept of direct link is more flexible than that'. In expanding the scope of application of VAT, the courts have held that there is the required reciprocity and a direct link between supply and consideration, even where there is no consumption (*Air France-KLM* (Joined Cases C-250/14 and C-289/14)), no consent (advocate general's opinion in *Fluvius* (Case C-677/21)) and no enforceable obligation (*Town and County Factors* (Case C-498/99)).

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Thirdly, parallels can be drawn between the provision of a 'free' platform and the provision of 'free' banking services which have been found to be taxable supplies, in cases such as *First National Bank of Chicago* (Case C-172/96) and *ING Intermediate Holdings Ltd v HMRC* [2017] EWCA Civ 2111 (*ING*). In *ING*, the UK courts found that 'free' banking services were provided in exchange for depositing of funds. The clear bargain between the parties was that if a deposit was made, the depositor would receive in exchange interest together with the services. While the interest would plainly correlate to the amount deposited, there was no such relationship between the amount of funds deposited and the level of service provided. It is perfectly possible that bank customers with lower level of funds could have used more of the bank's services, such as its call centres and branches. As *ING* illustrates, there is no VAT principle that, in order for there to be reciprocity and a direct link, individuals must necessarily provide the same consideration (objectively valued) in order to obtain the same level of service from the supplier.

Whether there is a B2C supply of platform services in return for non-monetary consideration: the economic argument

A further argument was raised by the VAT Committee, not at the level of legal principle but at the level of economic policy. The Committee considered that it made sense not to consider the provision of the platform to be a taxable transaction on the basis that: 'The activity of the IT company is not to provide IT services for free but to sell data in exchange for consideration'. The Committee posited that the offering of IT services for free is not the purpose of the company. Rather, the purpose is to make a profit from sales of data. That activity is taxed at the time when the IT platform sells the data of the users to third parties.

The argument based on the *purpose* of the company, which discounts the activity of providing the platform, again appears simplistic in light of the evolution of data-banking market models. Data-banking companies are sometimes described as 'two-sided', both in the sense that: (1) the company and the consumer provide something of value to each other and (2) the company makes a B2C supply on one side and a B2B supply on its related other side. The purpose of this profit-making business model, which may entail cross-subsidisation of a loss-making B2C supply, does not provide a persuasive economic argument for taxation of one economic activity (the supply of data) but not another (the supply of the platform).

There are other, competing economic arguments both for and against taxing the provision of the IT platform. On the one hand, there is the argument that VAT is a tax on consumption and taxation of consumption of digital supplies, in exchange for data, is necessary in order to maintain fiscal neutrality and non-distortion of competition. On the other hand, it has been argued that VAT is not truly a tax on consumption, as many forms of 'free consumption' are not taxed. Rather, VAT intends not to tax production (see 'What does the EU VAT actually tax?' (Christian Amand), *International VAT Monitor*, 2022, issue 2).

Is it possible to determine the taxable amount?

The Committee noted the particular difficulties of establishing the taxable amount, but the CJEU has previously given short shrift to arguments that a taxable amount cannot be ascertained. In *First National Bank of Chicago*, the CJEU held that 'any technical difficulties which exist in determining the amount of consideration cannot by themselves justify the conclusion that no consideration exists'. It is immaterial that neither the taxable person making the supply nor the other party to the transaction know the amount of the consideration serving as the taxable amount or, therefore, the basis on which VAT will be charged (*Argos Distributors v C&E Commrs* (Case C-288/94)). In *ING*, the Court of Appeal similarly rejected the argument that the consideration for 'free' banking services could not expressed in a monetary form. In the absence of any available benchmark, it considered four methodologies and concluded that the final choice of method would depend upon the evidence available to the court.

In an interesting parallel, overlapping issues are currently arising in the Competition Appeal Tribunal, where Meta is being sued for abuse of a dominant position, including by unfair pricing (see bit.ly/CATmeta). A central part of the claim is that Facebook did not pay its users for access to, or use of, their personal data, which is 'extremely valuable' and which Facebook used to generate 'vast amounts of revenue'. The CAT has described the situation as one of barter: 'The User offers up personal data in exchange for the Facebook service; and Meta provides Facebook in exchange for the data. There is no monetary consideration, but there is consideration'. As part of the quantification of the claim, expert economists are proposing methodologies which will put forward assessments of the market price of the data and the market price that users would have been charged by Facebook for the platform in a competitive market. Tax practitioners may therefore want to keep an eye on developments in that competition litigation.

Conclusions

While the issue provides a great source of debate for legal practitioners, the issue will not be determined by competing legal analyses. Given the huge ramifications for the digital marketplace and the free economy, the choice will ultimately be a policy one. Both nationally and supra-nationally, a conversation is in train as to whether (and if so, how) taxation is an appropriate tool for addressing the value of the harvesting of user data. ■