



TAX POLICY CENTER
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A PRIMER ON DIGITAL SERVICE TAXES AND THE OECD'S TWO PILLARS

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The digital economy, globalization, and tax competition have upended the traditional taxation of multinationals. In recent years, many countries have worked together under the auspices of the Organisation for Economic Cooperation and Development (OECD) to create a new international tax system, some also implementing new taxes specifically designed to tax multinationals in the new digital age. This brief provides an overview of those efforts and where the United States and US multinationals stand.

Countries have relied on various principles to tax multinationals and determine the income subject to taxation. Historically, most countries have taxed income reported by companies in their jurisdictions. But the rise of globalization and the digital economy have created new opportunities for firms to avoid taxes and shift profit, weakening the ties between where economic activity occurs and where income is reported.

In response, the Organisation for Economic Cooperation and Development (OECD) launched in 2013 coordinated efforts to curb profit-shifting and tax competition between countries by implementing a new international tax system centered around creating new rules for allocating the taxable income of multinationals across countries (Pillar 1) and a global minimum tax of 15 percent (Pillar 2). Although there hasn't been a lot of progress on Pillar 1 in the last few years, Pillar 2 has been implemented by most developed economies since early 2024—except for the US.

Since 2019, as countries wait for the new Pillar 1 rules to be adopted and implemented, some have introduced new taxes on digital services, often citing traditional tax systems as inadequate to tax companies in the digital economy.

Although the US spearheaded the BEPS efforts, it hasn't aligned the way it taxes US multinationals with Pillar 2 rules. In early 2025, the White House condemned the "Global Tax Deal" and ordered an investigation into some of its "discriminatory and extraterritorial tax measures."¹

Another executive order targeted digital service taxes and considered investigations into whether the taxes unfairly target US multinationals. The order indicated that the administration could impose tariffs and other actions “to mitigate the harm to the United States” if the foreign taxes are “discriminatory, disproportionate, or designed to transfer significant funds or intellectual property from American companies to the foreign government or its favored domestic entities.”²

New tariffs introduced by the administration in early April add more uncertainty in the future of international taxation. Some countries may change the rules of their digital service taxes or implement new ones as retaliation.

This explainer discusses the taxation of multinationals, digital service taxes, and the OECD’s two pillars.

HOW COUNTRIES TAX MULTINATIONALS

Historically, corporate income taxation has followed three main approaches:

1. **Residence-based (worldwide) system.** This taxes corporations based on their headquarters' location, regardless of where income is generated.
2. **Source-based (territorial) system.** This taxes income where goods and services are produced.
3. **Destination-based system.** This taxes income based on where goods and services are sold.

The United States operated under a *worldwide* tax system until 2017, with a key caveat: Foreign income was only taxed upon repatriation to the US. The Tax Cuts and Jobs Act of 2017 moved the US toward a *territorial* system but still imposes some US tax on foreign profits. In comparison, most countries have traditionally adopted a territorial system, taxing income generated by productive assets in their jurisdiction.

Base Erosion and Profit Shifting Efforts

The base erosion and profit shifting (BEPS) initiative, launched by the OECD in 2013, aimed to combat tax avoidance and profit shifting by large multinationals. These efforts were spurred by the rapid rise and influence of multinational profits, especially since the early 2000s. In 1990, multinationals made up an estimated 5 percent of total corporate profits and shifted an estimated 10 percent of those profits to lower-tax jurisdictions, or tax havens. By 2019, multinational profits made up close to 20 percent of corporate profits, and more than 35 percent of those profits were shifted to tax havens.³

In our modern economy, where many income generating assets are intangible and can be located anywhere, territorial tax systems have become uniquely vulnerable to tax avoidance as companies could move assets in tax havens and shift profits. The TCJA moved the US toward a territorial tax system but included a minimum tax on foreign income, the Global Intangible Low-Taxed Income (GILTI) regime. The GILTI regime was influential in shaping BEPS efforts which culminated with the OECD action plan centered around two pillars.

Digital Service Taxes

Digital Service Taxes are relatively new—France was one of the first countries to levy one in 2019—often stemming from the difficulty of taxing large tech multinationals. Digital service taxes follow destination-based principles by taxing income based on where services are sold. They differ from traditional corporate taxes because they are levied on the revenues of multinationals generated within a taxing jurisdiction. Although they primarily target tech companies, digital service taxes may apply to any large multinational that generates revenues from digital services.

THE TWO-PILLAR APPROACH

As of 2025, over 145 countries and jurisdictions have signed the OECD's Inclusive Framework, which provides guidance and actions for the implementation of the two pillars.

Pillar 1: Reallocating Taxing Rights

The main objective of Pillar 1 is to reallocate some profits to market jurisdictions where sales occur, following destination-based principles. Pillar 1 only applies to very large corporations, those with over €20 billion. A fraction of profits (25 percent above 10 percent of revenues) is reallocated using a formula derived under the BEPS framework, which includes rules to prevent double taxation. The second objective of Pillar 1 is to standardize transfer pricing administration, a key element of multinational activity and profit-shifting.

CURRENT IMPLEMENTATION STATUS

The BEPS project released a multilateral convention in 2023 for consultation. However, it requires ratification by jurisdictions accounting for at least 60 percent of the multinationals that would meet the Pillar 1 threshold. This means that without the support of the US, which represents a majority of in-scope multinationals, Pillar 1 cannot move forward.⁴

Pillar 2: Setting A Global Minimum Tax

The goal of Pillar 2 is to establish a 15 percent global minimum tax on the income of multinationals. It applies to all multinationals with at least €750 million in revenue in two of the prior four years. It follows a combination of source-based and worldwide principles to enforce the minimum tax. It first gives taxing rights to the jurisdiction where income is reported, then to the country where the parent entity is located. It also introduces a backstop measure to ensure enforcement. An innovation of Pillar 2 is to rely on financial income, which is standardized across jurisdictions. Corporations and jurisdictions can compute the effective tax rate using a standardized formula in *each jurisdiction* where a multinational operates. Under Pillar 2, a multinational which has *one or several* subsidiaries with an effective tax lower than 15 percent will be subject to a top-up tax. Countries and jurisdictions have three main tools to enforce the minimum tax.

Is the US compliant with Pillar 2?

As of March 2025, US tax law is not compliant with Pillar 2.

The GILTI regime inspired the income inclusion rule described in the text. However, two key differences remain.¹

First, the GILTI applies on blended foreign income. This means a multinational which has income in high tax countries and tax havens may pay little or no GILTI tax. Second, since 2017 the GILTI tax rate has been 10.5 percent, lower than the 15 percent minimum.

The GILTI rate is set to increase to 13.125 percent in 2026 and combined with the corporate alternative minimum tax introduced in 2022, this will bring the US closer to the Pillar 2 guidelines.

¹ There are other differences between GILTI and Pillar 2, such as deductions for investments in tangible assets and payroll.

1. **Qualifying domestic minimum top-up tax.** This domestic minimum tax on local profits can be implemented by low-tax countries to ensure alignment with the global minimum tax. Countries can implement it as a backstop measure, since some tax credits can lead to effective tax rates lower than 15 percent, even in countries with a statutory rate above 15 percent.
2. **Income inclusion rule.** This top-up tax applies to a parent company in the jurisdiction where it is incorporated when one or more of its subsidiaries pay less than a 15 percent effective rate.
3. **Undertaxed payments rule.** This rule applies when the qualifying domestic minimum top-up tax and income inclusion rule fail to impose the minimum tax. Under this rule, countries can disallow deductions or require adjustment of payments that an affiliate located in its jurisdictions pay to another affiliate of the same multinational located in a low-tax jurisdiction, when the affiliate in the low-tax jurisdiction has an effective tax rate below 15 percent. For example, if Meta's subsidiary in the Cayman Islands pays an effective tax rate of 5 percent, and the country where Meta is headquartered doesn't have an IIR that is Pillar 2 compliant, the United Kingdom could levy additional taxes on Meta's British subsidiary.

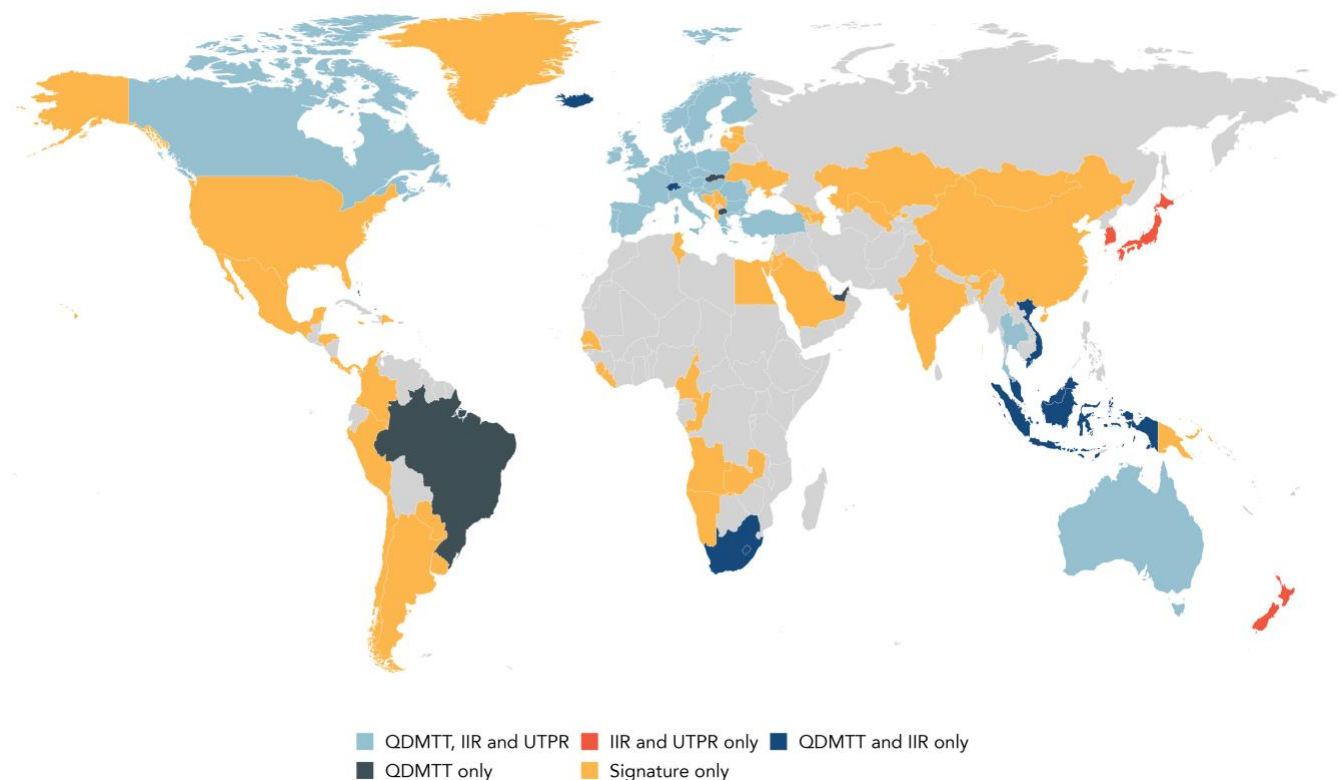
CURRENT IMPLEMENTATION STATUS

As of January 2025, over 100 countries have ratified the global tax agreement, with many beginning to implement the minimum tax. Many countries have adopted a qualifying domestic minimum top-up tax or an income inclusion rule effective as of 2024. The underpayment tax rule was set to become applicable in numerous countries, including the Australia, South Korea, most EU nations, and the UK on or after December 31, 2024.

As figure 1 highlights, most large economies, as well as developed economies, have agreed to work toward the global minimum tax and signed the Inclusive Framework. As of 2025, Australia, Canada, most European countries, Thailand, Turkey, and the UK have implemented a qualifying domestic minimum top-up tax, an income inclusion rule, and an undertaxed payment rule. South Korea and New Zealand have an income inclusion rule and an undertaxed payment rule, while Japan has adopted an income inclusion rule and the undertaxed payment rule is expected to apply in 2026.

The Build Back Better Act introduced in 2021 attempted to align the US with Pillar 2 and raise taxes on the foreign income of US multinationals but failed to be enacted into law. Further efforts to reform US international taxation have faced challenges and failed. On January 20, 2025, President Trump's executive order "The Organization for Economic Co-operation and Development (OECD) Global Tax Deal" decried the global tax agreements of the OECD and indicated that any prior commitment the US had made had no effect in the US without action by Congress.

FIGURE 1
Pillar 2 Implementation across the World
As of March 2025



Source: "PwC Online Tracker" (PwC, accessed April 25, 2025), <https://www.pwc.com/gx/en/tax/international-tax-planning/pillar-two/pwc-pillar-two-country-tracker-summary-v2.pdf> and author's research.

Notes: Data collected in April 2025. Yellow countries and territories have signed the Inclusive Framework but haven't yet implemented any of the Pillar 2 tools. Light blue countries have implemented all three main tools (Norway has announced an undertaxed payment rule (UTPR) will take into effect later in 2025). Red countries have implemented the income inclusion rule (IRR) and UTPR but not the qualifying domestic minimum top-up tax (we classify Japan as having a UTPR, but it will only apply on and after April 1, 2026). Navy countries have implemented an income inclusion rule and qualifying domestic minimum top-up tax (QDMTT) but not the UTPR. Grey countries have only implemented a QDMTT top-up tax.

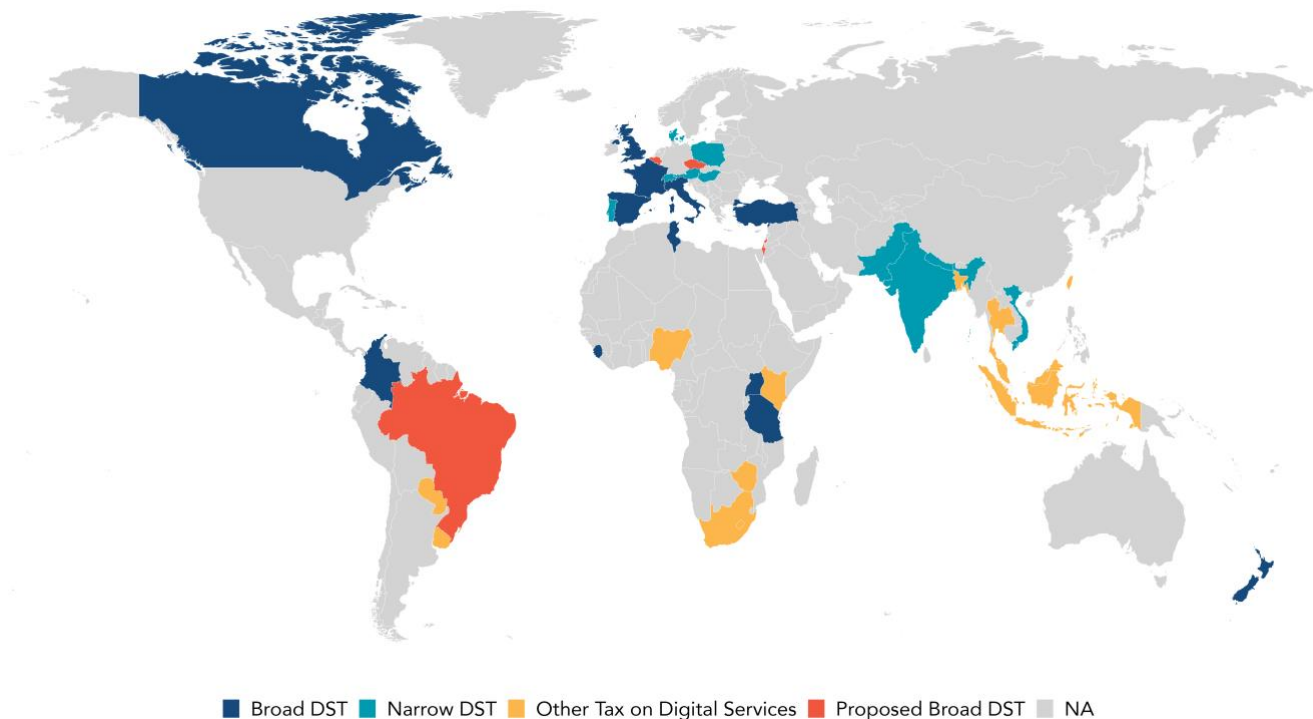
DIGITAL SERVICE TAXES

Digital service taxes vary in which digital-service activity they target. Some countries like France have designed digital service taxes that apply broadly to companies with digital services, like digital advertising, social media, digital interface, or data transmission. Other countries have designed digital service taxes that have a narrower base. For example, Portugal has a 1.5 percent tax on revenues generated from video-sharing platforms and subscription TV streaming services.

How Large Are Digital Service Taxes?

Digital service taxes often apply to large multinationals that generate revenues above a threshold. Digital service tax rates typically range from 1 to 5 percent. For example, France imposes a 3 percent tax on French revenues by multinationals with global revenues above €750 million dollars and at least €25 million in revenues in France. The French digital service tax is also restricted to companies that meet the “French digital presence” determined by the proportion users or advertisers in France. This ensures the tax aligns with local economic activity.

FIGURE 2
Digital Services Taxes around the World
As of March 2025



Are US multinationals targeted by Pillar 2 and digital service taxes?

Pillar 2 and digital service taxes apply to all multinationals that meet the revenue thresholds. However, US multinationals are particularly exposed because of the following:

1. **Their size and influence.** In January 2025, they represented almost two-thirds of the world's largest 100 companies.¹
2. **Their dominance in the tech sector.** In February 2025, 34 of the 50 largest tech companies by market capitalization were US companies.²

¹ “US Corporations Dominate Global Stock Markets – Europe and Asia Lag Far Behind,” EY, January 3, 2025, https://www.ey.com/en_ch/newsroom/2025/01/us-corporations-dominate-global-stock-markets-europe-and-asia-lag-far-behind.

² “Largest Tech Companies by Market Cap,” Companies Market Cap, accessed April 15, 2025, <https://companiesmarketcap.com/tech/largest-tech-companies-by-market-cap/>.

Source: VAT Calc online tracker (<https://www.vatcalc.com/global/digital-services-taxes-dst-global-tracker/>) and author's research.

Notes: Data was collected in March 2025. We define broad digital service tax that apply to several categories of digital services. Narrow digital service taxes apply to one or two categories of digital service (e.g., streaming, or digital advertising). Other tax on digital services highlights countries which have specifically adapted their tax system to capture revenues from digital services rather than implement a digital service tax. Several countries are discussing implementing a digital service tax, but we did not include them if they did not have specific legislation or detailed proposals.

Digital Service Taxes around the World

By early 2025, only a handful of countries (see figure 2) had implemented broad DSTs, defined as taxes that apply broadly to digital services, such as France (adopted in 2019), Italy (2020), Turkey (2020), the UK (2020), Spain (2021), or Canada (2024). Some countries like Brazil have proposed a broad digital service tax but haven't implemented it yet. Revenues from broad digital service taxes are not trivial—the digital service tax in France and the UK generated over €400 million in revenue in 2021. However, they still represent a very small fraction of total tax revenues, about 0.1 percent in most countries.⁵

A handful of countries like India, Poland, Portugal, Switzerland, or Vietnam have implemented narrow and targeted digital service taxes. India had implemented a broad digital service tax in 2021 but repealed it in 2024. Other countries have chosen a more traditional routes than a digital service tax to levy taxes on the consumption of digital services. For example, the Philippines and Thailand have started to levy a value-added tax on digital services that were previously excluded.

Most governments with digital service taxes agreed to repeal the tax upon the adoption of Pillar 1. On February 21, 2025, President Trump's executive order "Defending American Companies and Innovators from Overseas Extortion and Unfair Fines and Penalties" designated digital service taxes by Austria, Canada, France, Italy, Spain, Turkey, and the UK to be investigated as "extraterritorial" and "unfair" for US companies.

CONCLUSION

The landscape of international taxation is rapidly evolving as nations compete for investment and navigate both domestic and international political pressures. Many countries are facing rising debt levels and an urgent need to increase tax revenues. The growth of profit shifting has enabled many multinational corporations to pay lower effective tax rates than domestic firms, reinforcing public perceptions that large companies do not contribute their fair share.

OECD's Inclusive Framework was developed to address profit-shifting concerns. However, with the framework's Pillar 1 unlikely to be implemented in the near future, more countries may adopt digital services taxes as an alternative. While the rollout of Pillar 2 is progressing, the future of UTPRs—a key enforcement mechanism—remains uncertain due to opposition from the current US administration. In response, some countries may delay or cancel their implementation.

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NOTES

- ¹ “The Organization for Economic Co-operation and Development (OECD) Global Tax Deal (Global Tax Deal),” White House, January 20, 2025, <https://www.whitehouse.gov/presidential-actions/2025/01/the-organization-for-economic-co-operation-and-development-oecd-global-tax-deal-global-tax-deal/>.
- ² The executive order singled out digital service taxes in Austria, Canada, France, Italy, Spain, Turkey, and the UK. See “Defending American Companies and Innovators From Overseas Extortion and Unfair Fines and Penalties,” White House, February 21, 2025, <https://www.whitehouse.gov/presidential-actions/2025/02/defending-american-companies-and-innovators-from-overseas-extortion-and-unfair-fines-and-penalties/>.
- ³ Estimates are from Wier and Zucman (2022).
- ⁴ “Background to Pillar 1,” OECD Pillars, last updated July 11, 2023, https://oecdpillars.com/pillar_one/pillar-one-summary-2/.
- ⁵ Figures on total digital service tax revenue and share of total tax revenues are from Borders and colleagues (2023), who use official reports from governments.

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