

Digital services taxes: the permanent interim

International Tax

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Six years on, digital services taxes are becoming increasingly fragmented, creating new compliance challenges for businesses operating across international markets.

Key Points

What is the issue?

Digital services taxes (DSTs) were introduced as interim measures pending global reform. With that reform yet to materialise, they have proliferated and diverged, increasingly shaped by national rules, trade pressures and political negotiations.

What does it mean to me?

Affected businesses face fragmented compliance requirements, unresolved double taxation and increasingly uncertain scope boundaries. As DSTs expand and

technology develops, a broader range of businesses may find themselves within scope.

What can I take away?

Businesses should retest the scope of DSTs against current business models, document uncertain positions, review revenue-allocation methods and establish clear processes for monitoring developments and responding to changing policy.

The expectation when digital services taxes (DSTs) were first introduced was that a multilateral solution under OECD's Pillar One would be reached to reallocate taxing rights between jurisdictions and allow unilateral DSTs to be withdrawn.

In our June 2020 article for Tax Adviser, 'International Ambitions', we cautioned that existing DSTs might be around for longer than first intended. At that time the UK, along with Austria, France, Italy and Turkey, had implemented DSTs, while other jurisdictions were considering their own measures. The OECD was still pursuing an ambitious timetable for reaching consensus, targeting the end of 2020.

Six years later, Pillar One has still not entered into effect and its future remains uncertain. Many jurisdictions nevertheless continue to present DSTs as interim measures, to be withdrawn if an appropriate multilateral solution is implemented.

The question in 2026 is no longer whether DSTs will survive, but what they have become.

Trade and fiscal pressures are pulling jurisdictions in opposite directions, encouraging retrenchment in some countries while prompting expansion elsewhere, particularly as developing economies adopt broader measures that blur the boundaries between DSTs and existing indirect taxes. At the same time, rapid technological change is making the original definitions of taxable activities more difficult to apply in practice. Taken together, these forces suggest that the next debate will be less about repeal than redesign.

Politics and trade

DSTs began as a response to a perceived defect in the international corporate tax framework. They are now increasingly entangled with trade policy, economic

security and strategic autonomy.

US objections have hardened. A February 2025 presidential memorandum directed the US Trade Representative to consider renewed or new Section 301 investigations into foreign DSTs and contemplated tariffs and other responsive measures. In June 2026, the US government went further by threatening a 100% tariff on goods from countries imposing DSTs on US companies. The implications are therefore no longer confined to tax policy but extend into market access and trade negotiations. This has brought what was previously a specialist international tax question onto the board agenda.

Whether a country retains or withdraws its tax may now depend as much on trade negotiations as on the merits of its original policy rationale. Canada provides a clear example: in June 2025, after the US suspended trade negotiations over Canada's DST, the Canadian government announced that it would rescind the tax to support the resumption of negotiations, just hours before the first payment deadline. Several taxpayers had already registered and paid the tax, creating complexity for those seeking refunds.

Domestic political incentives, however, point in the other direction. DSTs raise visible revenues and are presented by governments as ensuring that large digital businesses contribute tax in markets where they derive value from users, making withdrawal politically difficult even where external pressure is significant.

In the UK, HM Treasury's Digital Services Tax Review Report (published in November 2025) stated that the DST raised £808 million in 2024-25, compared with £380 million in 2021-22. While the review continues to describe the tax as interim, it notably does not identify a clear timetable for withdrawal, and any withdrawal is likely to be politically sensitive given the UK's current fiscal position.

Even where political or trade pressures lead governments to withdraw a DST, this does not eliminate the underlying policy objectives or fiscal incentives. Governments facing pressure to repeal may therefore look to alternative ways of increasing tax revenues, such as greater enforcement activity and increased scrutiny of cross-border transactions. For taxpayers, repeal might not reduce uncertainty but simply shift it into different areas of the tax system.

Proliferation continues

Political pressure has not, however, produced a consistent retreat from digital taxation. Poland has proposed introducing a DST from 1 January 2027, and Australia has recently introduced a digital advertising levy, illustrating how domestic revenue concerns and political incentives can outweigh the risk of trade retaliation.

National regimes are also being revised: Italy abolished its €5.5 million domestic revenue threshold, meaning that once the global €750 million threshold is met, a single taxable transaction in Italy could trigger a liability and associated compliance obligations.

At EU level, the debate has re-emerged in the context of financing the 2028-34 Multiannual Financial Framework. A recent European Parliament briefing considers several possibilities, including a temporary EU-wide DST, coordination or replacement of national regimes and a hybrid framework capable of evolving alongside an eventual Pillar One solution (see tinyurl.com/3thj55d8).

The potential revenues for governments are significant. The briefing estimates that an EU digital levy could generate between €20.6 billion and €42.9 billion annually, equivalent to approximately 10% to 22% of today's EU budget.

Around 70% of this estimated base comes from business-to-consumer (B2C) e-commerce, illustrating how far the policy discussion has moved beyond the architecture of the original DST. The Commission's 2018 proposal focused on online advertising, digital intermediation and sales of user-generated data, whereas the 2026 modelling covers a considerably wider range of activities, including B2C e-commerce, cloud services and digital media. However, the briefing uses B2C e-commerce as a proxy because comparable EU-wide information on intermediary-service revenues is unavailable. The modelling should not be read as a settled legislative proposal.

Accordingly, the direction of travel seems not to be towards repeal but towards further expansion and adjustment, shaped by continuing political pressure and the absence of an effective global solution.

Divergence, not convergence

In 2020, we identified material differences between emerging DST regimes. France and Italy broadly followed the EU model, while Turkey's DST was drafted more

widely. A group falling outside the UK regime could not assume that it would reach the same conclusion elsewhere.

That divergence has become entrenched. Even within the EU, national regimes differ in rates, thresholds, taxable activities and reporting requirements. The European Parliament briefing concludes that this fragmentation creates legal uncertainty and additional compliance costs for businesses operating across multiple jurisdictions.

The proliferation is also increasingly visible outside the established European regimes. Across Africa, digital businesses may face overlapping VAT, DST and withholding tax regimes, often with broad definitions and low or no registration thresholds. Some Latin American jurisdictions similarly use significant economic presence or source-based rules to tax remote digital activity. These measures are not simply replicas of the early European DSTs. They widen the compliance map and increase the risk that the same revenue is taxed under more than one instrument.

While some regimes apply only to non-resident businesses, others make no distinction based on residence, which can lead domestically focused taxpayers to view the tax as disproportionately burdensome.

DST therefore no longer describes one recognisable tax. It describes a family of revenue-based measures that vary by policy objective, taxable base and target sector.

The receipts remain modest as a share of total tax revenues but are sufficiently material for governments to defend. According to the Parliamentary briefing, France collected approximately €756 million in 2024, equivalent to around 0.9% of its corporation tax receipts, while Italy collected approximately €455 million, equivalent to around 0.8%. The briefing describes revenues from established national DST regimes as relatively stable and manageable to administer, although evidence on longer-term administrative costs remains limited.

Fragmentation is therefore becoming a more established feature of the international tax landscape, rather than a purely transitional issue.

Existing definitions are being tested

The more fundamental challenge is that concepts which appeared reasonably stable in 2019 may no longer effectively describe the digital economy.

The UK tax applies to revenues from social media services, search engines and online marketplaces. The original premise was that these were identifiable categories of activity through which user participation created value. However, AI developments are now testing those boundaries.

A search service may now return a generated answer rather than a list of indexed links, while a conversational interface may retrieve information, synthesise it and complete a task within the same user journey. Depending on the facts, the service could resemble search, content generation, software or intermediation, and its revenues may combine advertising, subscriptions and commissions. This raises a practical question about how existing DST categories should apply to rapidly developing technologies.

At the same time, these categories are reaching beyond the technology companies that dominated the original debate into a much broader range of sectors. In practice, marketplace concepts can extend to hotel franchise arrangements where a central platform facilitates bookings between guests and independently operated hotels. DST has also affected the automotive and manufacturing sectors as business models become increasingly digital. Importantly, this expansion is not necessarily driven by changes to the rules themselves. As companies develop new digital revenue streams and place greater emphasis on user participation and data, they may come within the scope of existing DST regimes.

The rules present two related challenges: they can capture activities distant from the original policy target, while their application to emerging technologies remains uncertain.

There has been limited litigation to date, so many questions around the boundaries of taxable activity remain untested. In the UK, HM Treasury's review suggests that compliance issues have arisen mainly from differences in legal interpretation or mistakes, rather than deliberate non-compliance, indicating that future disputes may focus on how existing statutory concepts apply to evolving business models.

Practical consequences

Whether captured by design or through the widening scope of the rules, affected businesses face significant practical challenges in managing DST compliance across jurisdictions.

Data is often the main constraint. Tax authorities generally state that taxpayers are not expected to collect additional information solely for DST purposes, but groups can still struggle to attribute revenue accurately to local users where billing addresses, IP information and contractual records do not align. Where insufficient data is held, reasonable proxies may be required, introducing further judgement and inconsistency across jurisdictions.

The problem of double taxation also remains unsolved. The UK offers a 50% cross-border relief on online marketplace transactions that are subject to a foreign DST. However, this can be difficult to apply in practice because jurisdictions have different rules for locating users. Revenue treated as UK-linked for one regime may therefore not align with the foreign tax base.

Another question for businesses is who ultimately bears the cost of the DST. The UK review records changes to the pricing strategies of some in-scope groups, while the European Parliament briefing identifies possible pass-through via higher prices, commissions and fees. Businesses have been known to pass DST costs to customers not only through general pricing changes but also by itemising the charge separately on invoices. That approach raises commercial, contractual and broader tax questions. The practical challenges of DST therefore extend well beyond the tax function, requiring effective coordination across tax, finance, legal and commercial teams as the policy landscape continues to evolve.

Looking ahead

Pillar One remains stalled. The multilateral convention required to implement Amount A, which would reallocate a share of the profits of the world's largest multinational businesses to the jurisdictions where their customers and users are located, was finalised in 2023. However, this has not entered into force because the necessary political and legislative steps have not been completed.

The UN Framework Convention on International Tax Cooperation now offers a parallel institutional pathway. Negotiations are expected to continue until 2027, including work on a protocol covering income from cross-border services in an

increasingly digitalised economy. Its potential reach may be broader than Pillar One, but its eventual effect remains uncertain.

Against this backdrop, DSTs show little sign of disappearing. Instead, they are likely to continue expanding unevenly, while technological change places increasing pressure on existing scope boundaries and strengthens the case for redesign.

Four questions for tax functions

With DSTs set to remain for at least the short to medium term, there are four key questions tax functions should consider when seeking to understand the impact of these taxes on their business.

1. **Has a scope assessment been carried out since DSTs were introduced six years ago?** Products should be retested as they operate now, including any new features and activities introduced since the previous review.
 2. **How are uncertain positions being documented?** Businesses should retain evidence supporting their approach to classification and revenue attribution and, where appropriate, consider engaging with tax authorities to obtain greater certainty, particularly if a jurisdiction has specific disclosure requirements for uncertain tax treatments.
 3. **Do revenue-allocation methods remain appropriate?** Registered groups should test whether their methods still use the most accurate data reasonably available and revisit assumptions and proxies used to allocate revenue, particularly where systems or sourcing rules have changed.
 4. **Is there a process for monitoring global developments and engaging with policymakers?** Responsibility should be clear for tracking new regimes, thresholds, guidance, trade responses and consultations, and for feeding relevant changes into commercial decision-making.
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In conclusion

In 2020, we asked whether there had ever been a more challenging time for an indirect tax function. Six years later, the challenge is no longer simply keeping pace with change, but navigating regimes that are becoming more fragmented, more politically exposed and less straightforward to apply to evolving business models.

With Pillar One still uncertain, DSTs look increasingly less like interim measures and more like a lasting feature of the international tax landscape. The key question is not when they will disappear, but how businesses should manage them as their scope and strategic significance continue to evolve.