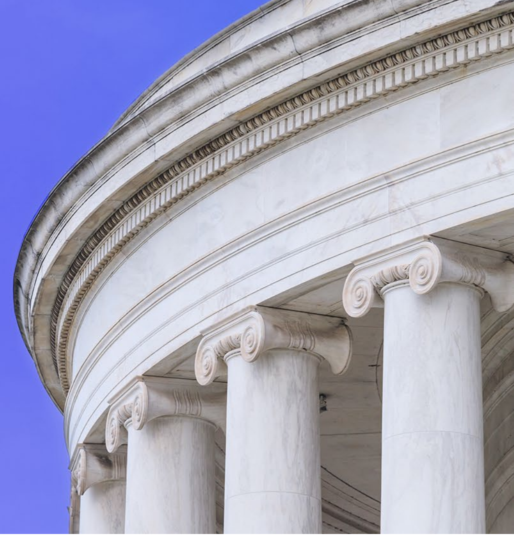
What's News in Tax

Analysis that matters from Washington National Tax

January 20, 2026



Transfer Pricing and International 2026 Tax Considerations

by the Washington National Tax International and Transfer Pricing groups

As we look ahead to the new year, what key international tax and transfer pricing challenges should companies have on their watch lists? The following issues and developments are certain to make the cut:

- Pillar Two: "side-by-side package" and transfer pricing considerations
- Planning in light of the One Big Beautiful Bill Act
- Reducing the impact of tariffs
- Public country-by-country reporting
- Planning for upcoming OECD initiatives
- Planning for evolving business models and new technology
- Transfer pricing controversy
- Corporate alternative minimum tax
- Key upcoming changes in the transfer pricing compliance landscape

2025 was a rollercoaster year in the world of international tax and transfer pricing—and 2026 already promises to be equally dynamic. On January 5, 2026, the OECD released its side-by-side (SbS) package for its Pillar Two (global minimum tax) rules, introducing safe harbors that exempt U.S.-headquartered multinational entities (MNEs) from most Pillar Two requirements. Pillar Two will remain a concern for U.S. MNEs, as the qualified domestic minimum top-up tax (QDMTT) continues to apply to many foreign subsidiaries of U.S. MNEs from 2024 onward. On the positive side, the SbS system presents new tax planning opportunities for U.S. MNEs, particularly in light of the 2025 One Big Beautiful Bill Act (OB3).

Other key issues on the 2026 horizon include ongoing tariff concerns and uncertainties related to the impact of IRS workforce reductions. The OECD is also developing new guidance for global mobility and intragroup services. In addition, most MNEs will publish their first public country-by-country (CbC) reports in 2026.

All these developments have significant implications for international tax and transfer pricing, and should factor into how MNEs plan for the future.

Pillar Two: Side-by-Side Package and Transfer Pricing Considerations

The SbS package represents the most significant change to Pillar Two since the original global anti-base erosion (GloBE) model rules were released in 2021. The package includes three core components:

1. **Side-by-Side System:** Provides a SbS Safe Harbor and ultimate parent entity (UPE) safe harbor excluding MNEs parented in eligible jurisdictions from certain Pillar Two rules. Notably, U.S.-parented groups will benefit from an exclusion from the income inclusion rule (IIR) and undertaxed profit rule (UTPR), though they will remain subject to qualified domestic minimum top-up taxes (QDMTTs).
2. **Substance-Based Tax Incentives:** Establishes a substance-based tax incentive (SBTI) safe harbor, which offers additional protection for certain qualified tax incentives (QTIs).
3. **Material Simplifications**: Includes an extension of the transitional country-by-country reporting safe harbor and introduces a new, permanent simplified effective tax rate (ETR) safe harbor.

A more detailed summary of the SbS package is available in this KPMG Overview of Pillar Two side-by-side package. A key takeaway is that, from 2026 onwards, U.S. MNEs should no longer be concerned about the potential application of top-up tax under the undertaxed profits rule (UTPR) to any low-taxed profits that could arise from leveraging foreign-derived intangible income (FDII)—now referred to as foreign-derived deduction eligible income (FDDEI).

Although less fundamental, the simplified ETR safe harbor includes specific guidance on the treatment of transfer pricing adjustments. This guidance is intended to ensure that transfer pricing adjustments do not result in income and taxes being recognized in different periods, which could lead to unintended top-up tax—a scenario that seems to arise under the full GloBE rules. The guidance also notes that these clarifications may be incorporated in the full GloBE rules through future guidance.

Planning in Light of OB3

On July 4, 2025, the U.S. president signed into law OB3, which generally makes permanent the key international tax provisions of the 2017 Tax Cuts and Jobs Act (TCJA), with the following key updates:

- **Foreign-Derived Intangible Income, Now Foreign-Derived Deduction Eligible Income**

  While the effective tax rate will rise from 13.125% to 14% in 2026, changes to the definition of deduction eligible income and the elimination of the carveout for a deemed tangible asset return will generally result in a broader base (i.e., more eligible income). This means that many MNEs will be able to claim larger FDDEI deductions starting in 2026 than they could under current law. Because research and development (R&D) and interest will not be allocated to FDDEI, MNEs that develop intangible property in the United States are expected to see the greatest benefits from these changes. MNEs could consider restructuring (e.g., moving intangible property to the United States) to increase FDDEI or increasing FDDEI-related intercompany charges.

- ### Limitation on Interest Deductibility

OB3 permanently restores the favorable treatment of depreciation, amortization, and depletion expense in determining a taxpayer's adjusted taxable income (ATI) for purposes of establishing the limitation on interest expense under section 163(j).[1] For tax years beginning after December 31, 2024, depreciation, amortization, and depletion will be added back to the calculation of ATI, allowing more interest to be deducted. OB3 also introduces two unfavorable changes that take effect in 2026 and will generally have the effect of reducing the amount of interest expense that is deductible compared to 2025. First, global intangible low-taxed income, subpart F income, and the section 78 gross-up will not be includible in ATI, potentially reducing ATI. Second, post-2026, OB3 treats electively capitalized interest expense as "interest" for purposes of determining the limitation, reducing the ability of companies to use voluntary capitalization to mitigate the impact of section 163(j). These changes may alter the tax impact of related party debt and could have knock-on effects on other tax provisions.

- ### Base Erosion and Anti-Abuse Tax (BEAT)

The BEAT rate is scheduled to increase slightly from 10% to 10.5% in 2026. As under current law, certain general business credits (such as the research credit) will be usable without increasing BEAT liability. MNEs should consider the knock-on impact of other OB3 provisions (for example, changes to immediate expensing of domestic research, bonus depreciation, and potentially increased interest deductions) on their BEAT position. Transfer pricing techniques will, therefore, continue to be important tools to help companies manage their BEAT exposure, including establishing eligibility for the BEAT services cost method (SCM) exception under section 59A(d)(5). In addition, companies may consider tax accounting methods that could reduce exposure or change the character of payments that would otherwise be base erosion payments, such as capitalizing payments to foreign related parties.

- ### Global Intangible Low-Taxed Income (GILTI)

The effective tax rate will increase to 12.6% (approximately 14% when accounting for the effect of foreign tax credits) in 2026, and the base will widen to now include the net deemed tangible income return (NDTIR), essentially capturing all net pro rata CFC tested income.

MNEs are finding that, due to the complexity of the U.S. tax system, the full effect of OB3 changes can only be determined through comprehensive modelling, as the impact of changes can be both positive and negative. For example, beneficial FDDEI planning may expose taxpayers to BEAT or the corporate alternative minimum tax.

Reducing the Impact of Tariffs

As the U.S. administration's stance on tariffs continues to evolve, MNEs are increasingly assessing the impact of tariffs on their transfer pricing results and exploring opportunities for tariff mitigation. These strategies may include transfer pricing-focused approaches, such as reducing intercompany pricing of goods to lower the customs value, as well as more customs-focused strategies like the use of the "First Sale."

First Sale is a powerful tool that may allow U.S. importers to reduce their duty costs. By declaring the price paid or payable in the "first or earlier" sale in the supply chain, MNEs may be able to achieve significant savings and mitigate the impact of rising tariffs. Successful First Sale application allows an importer to remove the middleman's margin and qualifying non-dutiable customs costs from the declared value, leading to reduced duties.

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[1] Unless otherwise indicated, section references are to the Internal Revenue Code of 1986, as amended (the "Code") or the applicable regulations promulgated pursuant to the Code (the "regulations").

Some MNEs are considering large-scale restructuring plans or the possibility of "unbundling" certain transactions, which may have international tax and transfer pricing implications.

Public Country-by-Country Reporting

Almost every U.S. MNE will need to publish country-level data in some form. The pressure is coming from around the world:

- The EU's public CbC reporting directive was approved in 2021 and generally takes effect for calendar year companies in 2025. MNEs with a presence in Croatia and/or Romania may, however, be subject to these requirements earlier.
- Australia's public CbC reporting rules apply to periods beginning on or after July 1, 2024.
- The Financial Accounting Standards Board (FASB) has issued new income tax disclosure rules, applicable to public business entities for annual periods beginning after December 15, 2025. These new rules generally require more detailed disclosures about income taxes paid, rate reconciliation, and other qualitative and quantitative information.

The new public CbC reporting requirements represent a major shift for MNEs. For the first time, companies will be required to publicly disclose certain tax data that, until now, was shared only with tax authorities through their non-public tax returns. As a result, MNEs will need to carefully consider how they present their tax profile to a broader audience. Some organizations may decide that publishing only the required information is insufficient, and will supplement their disclosures to tell their story in their own words. Others may choose to go beyond compliance by providing additional narrative or context to explain their data. Still others may expand further, reporting on other categories of taxes paid—such as employment taxes, indirect taxes, or tariffs—to help frame a more comprehensive picture of their overall tax contribution. Regardless of the approach adopted, MNEs will need to invest time and careful consideration to determine the best strategy.

Planning for Upcoming OECD Initiatives

To date, the OECD's work on global mobility has primarily focused on revisiting when a home office should constitute a permanent establishment. However, the OECD has indicated that a more comprehensive work program is expected in 2026. In the transfer pricing space, the issue of geographically dispersed and mobile senior executives has been identified as a potential focus area—something that MNEs with these circumstances should continue to monitor.

The OECD is also revisiting Chapter VII of the Transfer Pricing Guidelines, which addresses intragroup services, with particular attention to high-value services. There is an obvious connection between this initiative and the questions that some tax authorities are raising about globally dispersed senior executives.

The simplification and streamlining of transfer pricing rules for baseline marketing and distribution activities under Amount B has so far only been adopted by the United States and Singapore. However, there are ongoing indications that other countries, such as Mexico and South Africa, may adopt this framework, so it remains important to monitor further developments.

Finally, the OECD is kicking off a review of the Transfer Pricing Guidelines to identify areas where the rules are unclear or inconsistent. What this project looks like and what impact it may have remains to be seen.

Planning for Evolving Business Models

New technologies, such as artificial intelligence (AI), are driving significant transformations in business models across industries. The evolution of these models presents both opportunities and risks for companies. These changes offer opportunities to rethink transfer pricing structures to better align with new value chains and achieve greater tax efficiency. Conversely, applying legacy transfer pricing models without considering fundamentally different value chains may result in misalignment between value creation and transfer pricing outcomes, increasing the potential for challenges from tax authorities.

MNEs should consider undertaking a thorough analysis to understand changes in their value chains and to determine appropriate adjustments to their transfer pricing structures going forward.

Transfer Pricing Controversy

While the full impact of IRS staff reduction remains unclear, many MNEs are facing increasing transfer pricing controversy around the world, along with more aggressive positions from the IRS. Recent court decisions and ongoing litigation serve as a reminder that companies should not rely on prior settlements, expired IRS agreements, or favorable audit histories to protect against future adjustments.

Following the Supreme Court's departure from the long-standing *Chevron* doctrine in *Loper Bright Enterprises v. Raimondo*, regulatory challenges remain a staple of transfer pricing litigation, with ongoing cases challenging the validity of regulations concerning, for example, stock-based compensation (in both the cost sharing and services contexts. Other ongoing cases involve the application of the acquisition price method for valuing platform contributions, the interaction of section 482 and the economic substance doctrine, continuing disputes over transfer pricing methods, and pricing for procurement services. The IRS's 2025 win on the CUT/CPM method debate is expected to embolden it in continuing to adopt their CPM position; however additional debate may arise regarding how to make reliable adjustments to the CPM.

We are also observing continuing controversy outside the United States about transfer pricing issues. Now is an opportune time to consider advanced pricing agreements (APAs) to obtain certainty—especially if the intercompany transaction may be considered high risk, the volume of the transaction is significant, or if MNEs want to obtain certainty on emerging issues such as which entities bear the costs of tariffs.

We expect 2026 to be an active year for audits surrounding transfer pricing issues for financial transactions globally. Simply ensuring an arm's length interest rate is not sufficient: the current environment requires a more holistic approach towards intercompany financing transactions. Tax authorities are increasingly raising questions about an entity's ability to obtain and service debt based on its own financial strength, and, in several cases, how the leverage structure of an entity aligns with or deviates from the group's capital structure (and therefore group credit rating). Intragroup cash pooling arrangements have also seen a surge in audits from various tax jurisdictions, with several tax authorities challenging the interest earned by cash-positive entities. Amid these audits, some taxpayers have successfully negotiated APAs and transaction-specific rulings in the financial transactions space.

The OECD's International Compliance Assurance Program (ICAP) may offer another avenue for companies to engage with tax authorities to obtain assurance regarding their transfer prices, thereby practically reducing audit risks. The ICAP program enables companies to potentially obtain assurance across multiple jurisdictions that their transfer prices are considered "low risk." Although the risk assessments resulting from ICAP are not binding on tax authorities, ICAP participants have reported experiencing a "halo effect" for jurisdictions and years not directly covered by the ICAP process.

Corporate Alternative Minimum Tax

The corporate alternative minimum tax (CAMT) is effective for tax years beginning in 2023. CAMT generally applies to certain large corporate taxpayers (i.e., those with over $1 billion in adjusted book income) to the extent that 15% of a taxpayer's adjusted book income (less CAMT foreign tax credits) exceeds the taxpayer's regular tax (less regular tax foreign tax credits) plus BEAT. If a taxpayer owes a CAMT liability, they generate a credit that can generally be used to offset regular tax in a future year, to the extent that the regular tax exceeds the taxpayer's tentative CAMT liability.

Although the tax base for CAMT is book income, many of the adjustments require applying tax concepts and unpacking consolidated financial statements to disaggregate transactions between taxpayers that are consolidated for book purposes but not for tax. The proposed regulations, issued in September 2024, also contain anti-abuse rules that require making section 482 adjustments to book income when controlled transactions do not clearly reflect income. While these regulations have not yet been finalized, many taxpayers choosing to early adopt the proposed regulations will need to carefully assess whether their intercompany transactions align with section 482 principles. Moreover, CAMT liability is triggered by differences between adjusted book income and tax, which suggests that transfer pricing choices may be particularly important for some clients.

In 2024, for most MNEs, the largest CAMT issue was filing the Form 4626 for 2023, as even corporations with no CAMT liability were required to do so. However, after modelling the impact of the various OB3 provisions (e.g., increased FDDEI deductions, bonus depreciation, immediate expensing of domestic research, and increased interest deductions), MNEs are discovering that for 2025 and onward, absent planning, they may be CAMT taxpayers, and perhaps even permanent CAMT taxpayers. Companies may wish to consider restructuring opportunities (e.g., to maximize the CAMT foreign tax credits) and accounting methods and elections (e.g., electing to capitalize domestic research expenditures) to reduce their CAMT liability or, just as importantly, to ensure they can utilize the credit for any CAMT liability they do pay.

Changing Transfer Pricing Compliance Requirements

Transfer pricing documentation requirements continued to evolve this year, making it essential to assess the impact on compliance for 2026 and future years.

Germany introduced changes to transfer pricing documentation requirements effective January 1, 2025. Changes included a shortened submission deadline of 30 days for transfer pricing documentation and a mandatory submission requirement during tax audits for all open fiscal years before January 1, 2025. The transfer pricing documentation should include a new transaction matrix containing, for each related-party transaction, the nature, parties, and jurisdictions involved; the volume and remuneration thereof; and the transfer pricing method applied, among other pieces of information. In addition, effective January 1, 2025, Germany implemented stricter documentation requirements for extraordinary business transactions for which documentation must now be proactively documented within six months following the fiscal year. Germany also introduced a new obligation for taxpayers to proactively correct tax returns when transfer pricing errors are identified.

Chile published Law 21.713, which introduced amendments related to transfer pricing from November 1, 2024. These amendments include the concept of the arm's length principle in line with OECD guidelines and reinforcement of the concepts of functions, assets, and risks assumed by the parties. Further, the amendments explicitly state to taxpayers the need to maintain supporting information when an analyzed party is foreign.

New Zealand's Inland Revenue published its 2024 compliance focus guide for multinational enterprises, which includes a transfer pricing governance checklist. This checklist stresses the importance of comprehensive documentation that covers all cross-border, related-party transactions. The documentation should be developed with input from local management or the finance team and kept current to reflect changes in business functions, assets, and risks.

The **UAE** Federal Tax Authority (FTA) released a tax guide that includes transfer pricing thresholds for related-party disclosures for financial years starting on or after June 1, 2023, and onward. For instance, a disclosure is required only when the market value or financial statement value of related party transactions exceeds AED40 million plus individual transaction thresholds. Further, any transfer pricing adjustments that reduce taxable income will require preapproval from the FTA. In addition, the Ministerial Decision No. 301 of 2024 on tax groups for tax periods beginning on or after January 1, 2025, requires a tax group, in certain scenarios, to calculate the taxable income attributable to one or more of its members on an arm's length basis and to disclose this information in its transfer pricing schedule.

Costa Rica's tax authority issued final guidance in July 2025, effective August 4, 2025, requiring specific taxpayers to submit an annual transfer pricing information return beginning with the 2024 fiscal year. In the final guidance, the submission deadline of the return for the 2024 fiscal year was extended on a one time basis to November 30, 2025, while returns for subsequent years must be filed within six months following the end of the taxpayer's authorized fiscal period.

Malaysia issued transfer pricing guidelines effective for assessment years 2023 and onward. The guidelines include revised thresholds for the preparation of full or minimum contemporaneous transfer pricing documentation, exemptions to such preparation, and availability of a simplified approach for low value-adding intragroup services. Taxpayers should prepare full contemporaneous transfer pricing documentation if they generated gross business income of more than RM30 million in total and engaged in cross-border controlled transactions totaling RMA10 million or more annually; or if they received or provided controlled financial assistance of more than RM50 million annually.

Denmark introduced new transfer pricing rules that significantly reduce documentation burdens for qualifying taxpayers. Effective for the income year 2025, the amendments raise thresholds for limited documentation eligibility and exempt certain controlled transactions from reporting requirements. Additionally, companies with controlled transactions below DKK5 million and intra-group receivables or debts below DKK50 million are exempt from documentation obligations. The new rules also remove the Danish tax agency's authority to request auditor statements and introduces an automatic extension for transfer pricing documentation deadlines when a corporate tax return extension is granted.

Taiwan's Ministry of Finance clarified that profit-seeking enterprises engaged in controlled transactions during the 2024 fiscal year should prepare a transfer pricing report when filing their 2024 income tax return. However, enterprises that meet certain specified conditions may opt to submit substitute documentation instead.

Conclusion

There is much to consider in the realm of international tax and transfer pricing as 2026 begins. While we expect to see more changes in 2026, many key tax initiatives, such as the Pillar Two side-by-side agreement, have advanced to a point where now is an opportune time for MNEs to evaluate and pursue tax planning opportunities for the future.

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