

April 17, 2026

Reproduced with permission from Tax Management International Journal, 4/17/2026. Copyright © 2026 by Bloomberg Industry Group, Inc. (800-372-1033) <http://www.bloombergindustry.com>

Don't Let Your IP Transfer Pricing Catch You Off Guard



Jayme Reynolds, Thomas Bettge, Madeline Mitchell, Saurabh Dhanuka, and Serene Tan
KPMG

The digital economy is creating unprecedented market opportunities while reshaping tax risks for fast-growing companies.

Consider a technology company entering a high-growth phase and seeking additional venture capital. Founded in Europe, it retains legal ownership of its intellectual property there. As the business scales, the company decides to relocate its C-suite and expand its research and development footprint in the US—a scenario that is increasingly common for companies in the technology space.

Digital tools, cloud platforms, global mobility, and advances in AI have made it easier than ever for companies to grow quickly, expand operations across borders, and hire talent anywhere. But this flexibility comes at a price.

Fast forward several years. The company is preparing for an acquisition but due diligence uncovers a problem: legal ownership of the IP no longer aligns with where the underlying IP value is being created. The immediate implications may seem manageable—purchase price adjustments or indemnities in connection with the pending acquisition—but they rarely stop there.

Left unaddressed, this issue doesn't disappear—it compounds quietly, often resurfacing when the stakes are much higher. As the business becomes profitable, the same misalignment under a tax audit can translate into a much more substantial tax exposure.

Legal Form vs. Economic Substance

At the heart of the issue, there is a disconnect between legal form and economic substance. In this case, the legal ownership of the IP isn't aligned with where the activities that create intangible value reside. Economic and operational substance have become a focal point for tax authorities worldwide. Structures that allocate profits to entities with limited operational contribution beyond contractual assumption of risks and responsibilities are increasingly challenged.

In its 2015 Final Report for Actions 8-10: “Aligning Transfer Pricing Outcomes with Value Creation,” the Organization for Economic Cooperation and Development [formally introduced](#) a Development,

* [Jayme Reynolds](#) is a managing director in the Washington National Tax (WNT)—Tax Controversy and Dispute Resolution group at KPMG. [Thomas Bettge](#) is a managing director, [Madeline Mitchell](#) is a manager, [Saurabh Dhanuka](#) is a partner, and [Serene Tan](#) is a senior manager in the WNT—Economic and Valuation Services group.

Enhancement, Maintenance, Protection and Exploitation framework to align transfer pricing outcomes with value creation. DEMPE focuses on the functions performed, assets owned, or risks assumed to determine the appropriate compensation in intercompany transactions, rather than relying solely on legal ownership.

Many tax authorities globally have since adopted the DEMPE framework as a tool to identify which entities within a multinational enterprise group perform the value-creating functions for the intangible assets and are therefore entitled to the associated profits or losses.

The US hasn't formally adopted DEMPE in its transfer pricing regulations, but the IRS increasingly has applied DEMPE-like principles in transfer pricing audits and disputes, scrutinizing profit split allocations, challenging assumptions around shared intangibles and management control, and placing greater emphasis on an expectation of detailed documentation of functions, risks, and economic analyses.

Companies most exposed to associated tax risks include fast-growing companies, companies with outdated tax structures, and both acquisition targets and acquirers. Misalignment of legal and economic substance typically happens when companies rapidly expand. For example, they may rush to set up entities quickly to meet operational needs without considering whether the existing IP ownership or compensation structures need to be changed, potentially leaving residual intangible returns in entities or jurisdictions without DEMPE functions.

Similar risks can arise when leadership is relocated across jurisdictions to meet business needs, resulting in a migration of DEMPE functions from the entity that contractually owns the IP, without addressing the potential tax implications.

These challenges are especially relevant in Europe, where countries including Denmark, the Netherlands, Spain, and Germany are actively fostering tech innovation and start-ups. As these companies grow, many look to the US to scale, drawn by larger markets, investor opportunities, and access to global talent. The transition—from European incubation to US scaling—can create the very misalignment between legal ownership of the IP and the location of value creation discussed earlier.

‘Wait and See’ Pitfalls

Overlooking this misalignment can be costly. By the time an IP transfer is contemplated, or a transfer pricing audit arises, valuations may have skyrocketed. At higher valuations, such moves can have significant cash tax implications and operational challenges, requiring changes on a much larger scale.

The consequences affect stakeholders across the board. Treasury teams may face cash flow pressures if revenue streams must move across jurisdictions. Legal counsel may need to grapple with legacy intercompany agreements and implement new ones while managing heightened risks of dispute. Investors and financial statement auditors, meanwhile, will be concerned with how misalignment affects reported earnings, valuation, and financial disclosures.

Tax authorities will have their own priorities. In the earlier example with the European company, a European tax authority will be sensitive to any erosion of taxable income tied to the legacy IP, while the IRS in the US will likely want to ensure that the US entity is appropriately compensated for its share of the IP going forward.

A transfer pricing audit often can be a lengthy and resource-intensive process, with huge tax adjustments and penalties at stake, not to mention the reputational impact that comes with media publicity in high-profile cases. Recent cases underscore just how steep the financial stakes can be. Tax authorities across

the US and Europe, for instance, have challenged profit allocations they view as misaligned with value-creating functions, with adjustments in larger cases running into the billions.

The increased scrutiny from tax authorities into transfer pricing isn't going away anytime soon. Globally, tax authorities are stepping up. The UK's HMRC reported a record [£3.4 billion](#) in tax revenue in 2024-2025 from transfer pricing audits. The Australian Taxation Office continues to expand funding and capabilities of its Tax Avoidance Taskforce, securing a [\\$4.3 billion](#) additional tax revenue in FY24-FY25.

Throughout the EU, scrutiny of transfer pricing, and particularly DEMPE alignment, is high. In the US, despite cuts to IRS resources, IP-related issues remain a focus, with the IRS's [rethinking](#) of periodic adjustments giving examiners a super-powered new tool to address valuation issues years after the fact.

A Path Forward

The good news is that misalignment can be managed—if addressed early. Start by reviewing where your IP resides, where your value-creating functions take place, and whether your intercompany agreements truly reflect economic reality. These preemptive steps can prevent costly surprises as your business scales.

For situations where DEMPE misalignment already exists, all is not lost. Acting proactively can still save significant resources, yield better outcomes, and take substantial tax uncertainty off the table for prior years. Mutual agreement procedures offer a government-to-government mechanism to resolve existing cross-border disputes and avoid double taxation. Advance pricing agreements offer an opportunity to seek certainty and reduce audit risks preemptively or retroactively. Considering these tools early is key to managing any exposure.

IP misalignment isn't just a small problem that will go away—it's a fundamental risk that should be nipped in the bud. Aligning IP ownership with where value is created should be a top priority, not an afterthought. Careful planning today ensures your IP structure drives growth, not complications.

This article does not necessarily reflect the opinion of Bloomberg Industry Group, Inc., the publisher of Bloomberg Law, Bloomberg Tax, and Bloomberg Government, or its owners.

The information in this article is not intended to be “written advice concerning one or more Federal tax matters” subject to the requirements of section 10.37(a)(2) of Treasury Department Circular 230. The information contained herein is of a general nature and based on authorities that are subject to change. Applicability of the information to specific situations should be determined through consultation with your tax adviser. This article represents the views of the authors only, and does not necessarily represent the views or professional advice of KPMG LLP.