

Transfer Pricing

# Tariff Chaos Raises Audit Risks for Transfer Pricing

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## Summary by Bloomberg AI

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- Countries are increasing their investments in audit teams, and transfer pricing examination can be an attractive place to find revenue, according to EY partner Jose Murillo.
- Tax authorities, such as those in Mexico, Australia, and India, are becoming more assertive and aggressive in audits, especially in the transfer pricing space, with a focus on intercompany loans and intangibles.
- US tariff rates have raised the specter of more audits, posing a double audit risk for companies, which have to navigate scrutiny from both customs and tax authorities, and requiring companies to factor tariffs into their transfer prices.

Transfer pricing is increasingly becoming a hot area for tax audits, raising risks for companies as they try to navigate an uncertain political and economic environment, recently exacerbated by ever-changing US tariff rates on major trading partners.

Countries are looking for revenue, especially after the pandemic and amid a brewing trade war with the US—and transfer pricing examination can be an attractive place to find it. Unlike in the US, many tax authorities are increasing their investments in audit teams.

“Fiscal pressures cause all tax authorities to be more assertive, more aggressive in audits, especially in the transfer pricing space,” EY partner Jose Murillo said. “That’s what you’re seeing across the globe.”

In Mexico, the government touted its growing TP audit revenue, with plans to double down on investment in its auditing functions, including further investment in technology such as artificial intelligence.

Paul Sutton with LCN Legal said he's seen "a demonstrable uptick in terms of the number of transfer pricing inquiries and disputes, and that's alongside a tightening of the administrative requirements in Germany."

Australia and India also continue to be aggressive in examinations, with each fostering a reputation for competent examination teams applying close scrutiny each year to a high number of companies, including their related-company transactions.

Sutton said audits have been focusing increasingly on intercompany loans and intangibles—particularly the relocation of intangibles like intellectual property.

### **Double Risk From Tariffs**

President Donald Trump's tariffs across the globe have upended the world of transfer pricing, and significantly raised the specter of more audits.

US tariff rates have been changing almost daily, requiring companies to know what their options are in each scenario—each of which involves different transfer pricing implications as well as risks.

"Our team spent a tremendous amount of time doing modeling—modeling with data that shows the overall impact for a company combined with what the intercompany impact would be," said Chris Desmond, principal, customs and international trade at PwC US.

Companies need to factor tariffs into the transfer prices they set for their related-party transactions with the goal of mitigating their impact through adjustments.

This poses a double audit risk for companies, which have to navigate scrutiny from both customs and tax authorities. Tax agencies require companies to do transfer pricing differently than customs agencies, and companies need to make sure pricing on both ends matches up. Transfer pricing for tax typically takes a more high-level view of the profits made by each entity, while customs typically focuses on the pricing of individual transactions.

Tariffs have prompted senior executives to get more involved in the nuts and bolts of transfer pricing.

"The C-suite engaging in transfer pricing and customs is not something I've heard in the same sentence for most of my career as a transfer pricing practitioner," Desmond said. "Now customs and trade is the tip of the spear, because the numbers due to tariffs are some of, if not the most, impactful numbers of a company's financial statement."

Tax heads need to understand the customs implications of their tax positions, as well.

"I see a lot more TP practitioners study up on customs, and it's been a whole expansion of TP professionals now intersecting with custom professionals and trying to figure out like, OK, what's the balance?" Mimi Song, chief operating officer at tax services firm Exactera, said.

## IRS Staffing Issues

In the US, companies are still figuring out what major changes at the IRS mean for their audit risk, despite hopes that auditing volume would plummet in the face of recent layoffs.

The agency has drastically reduced its staffing in the last year—including members of audit teams—raising questions about how much taxpayers should be worrying about future audits.

EY's Murillo said that while there is an expectation that fewer audits will happen with fewer IRS staffers, the audits that do happen will be much tougher—in part because of inexperienced staffers who are still learning the ropes.

At the same time, the IRS opted to keep many of its transfer pricing staff—possibly signaling that TP audits will remain a focus.

“There were a lot of furloughs. But what happened was, well the colleagues that I know of, they’ve been called back because transfer pricing was deemed to be a critical function,” Song said. “That signals an investment in understanding that transfer pricing is a big area in their eyes to pursue and evaluate so that we can start to recuperate tax revenue given the current environment.”

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