

US APA report for 2023 shows significant increase in executed APAs

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In brief

What happened?

The IRS Advance Pricing and Mutual Agreement Program (APMA) on March 26 issued its 25th Annual [Statutory Report Concerning Advance Pricing Agreements](#) (APAs). The report shows there was a significant increase in the number of APAs executed in 2023, with the number more than doubling from 77 in 2022 to 156 in 2023, making 2023 a record year in the history of the APA program in terms of the number of executed APAs. For APAs completed in 2023, there was a slight improvement in the time to finalize APAs, decreasing slightly in 2023 to three and a half years, and down from the all-time recent high of approximately 43 months in 2022. The increase in executed APAs, coupled with the slight decrease in processing times, suggests continued improvement in the efficiency of the APA process four years after the COVID-19 pandemic.

Notwithstanding the general uptick in executed APAs in 2023, there was also a slight decrease in the number of APA applications, which fell to 167 in 2023 from 183 in 2022. Lastly, there was a slight decrease in pending inventory to 558 cases, but this is still consistent with 2022's 564 cases, and significantly above levels from 2021 and earlier years.

Why is it relevant?

APMA's APA program continues to improve in efficiency with respect to finalizing APAs, suggesting that the organization is recovering from recent low numbers affected by impacts from the COVID-19 pandemic in 2020 and that APMA's commitment to increasing personnel along with a focus on resolving some of its older cases are paying off. Even with a slight decrease in applications and pending cases in 2023, the longer sustained trend of increased pending cases shows a continued interest in taxpayers participating in the APA program to manage risk around transfer pricing disputes. The interest in advanced tax certainty is likely to be heightened with the looming changes to existing international tax rules as a result of the implementation of the OECD's two-pillar solution.

Observation: In addition to a jump in productivity and efficiency, the increase in executed APAs and reduction in APA processing times may be in part due to the increase in personnel at APMA, which totalled 114 as of the end of 2023 compared with 97 employees for the prior year.

Action to consider:

Companies in the APA program should evaluate how the implementation of Pillar One, especially Amount B, and Pillar Two will impact APA-negotiated income allocations. The coexistence of parallel dispute resolution venues as a result of the new global tax regime will be a space to watch.

In detail

Significant increase in executed APAs and a slight decrease in processing time

The number of executed APAs more than doubled in 2023 to 156, up from 77 in 2022. Of the executed APAs, 130 were bilateral APAs. The number of executed APAs prior to 2022 was relatively consistent, with 124 in 2021 and 127 in 2020. Of the 156 APAs executed in 2023, approximately 53% were new APAs (i.e., not renewals of existing APAs), which is up from 45% in 2022. India accounted for the greatest increase in share of executed bilateral APAs, with 17% in 2023, up from 8% in 2022.

The median time to complete an APA decreased slightly in 2023 to 42.0 months, down from the all-time recent high of 43.4 months in 2022. The number of withdrawn APAs in 2023 increased to 13, compared with six APAs that were withdrawn in 2022.

Observation: The significant increase in executed APAs and the corresponding slight decrease in median processing time may be reflective of the ongoing recovery from the varied impacts of the COVID-19 pandemic, additional resources, and a focus on resolving older cases. Work processes are continuing to be streamlined, such as face-to-face meetings with certain treaty partners returning to pre-pandemic levels, so it will be interesting to see the results going forward. The potential effects of [APMA's recent interim guidance on APAs](#), in which APMA introduced an optional pre-submission review process aimed at reducing the time to complete APAs by filtering out cases that are unlikely to reach an agreement at an earlier stage, also should be considered.

APA filings decreased; pending inventory decreased slightly but still trending consistent

The number of APA applications decreased to 167 in 2023, down from 183 in 2022. In addition, as of the end of 2023, APMA received 22 user fee payments for APAs that were not yet accompanied by APA applications.

At the end of 2023, there were 558 pending APAs, compared to 564 at the end of 2022, 461 at the end of 2021, and 448 at the end of 2020. APAs with Japan (25%), India (23%), and Canada (13%) continued to account for over half of all pending bilateral APAs. Pending bilateral APAs with Mexico, Korea, Italy, Germany, the United Kingdom, and other countries accounted for the remaining pending case inventory.

Japan continues to dominate executed cases, followed by India and Italy

The 2023 report reflects that Japan accounted for approximately 32% of all executed bilateral APAs with the United States and 30% of all bilateral APA applications. The percentage of bilateral APAs executed with Japan has steadily declined over the years, from 39% in 2022 and 40% in 2021. Following Japan, India more than doubled their representation of completed bilateral APAs, to 17% of all executed bilateral APAs in 2023 from 8% of executed bilateral APAs in 2022.

Next in line was Italy, accounting for 11% of the executed bilateral APAs, up from 4% in 2022. Canada faced a significant drop in executed bilateral APAs, representing 8% of executed bilateral APAs, down from 14% in 2022. All other countries combined (including Korea, United Kingdom, Denmark, Switzerland, and others) accounted for the remaining 32% of the bilateral APAs executed in 2023.

Japan also slightly led the list of pending bilateral APAs by country, followed by India and Canada. APAs involving Japan account for 25% of the pending requests, India accounts for 23%, and Canada comes in at 13% of the pending inventory. All other countries, including Korea, Italy, Mexico, Germany, United Kingdom, and Switzerland, comprise the remaining approximately 39%. This line-up also compares to the country-specific breakdown for bilateral APAs filed in 2023, with Japan, India, and Canada accounting for 65% of the total filed.

Role of bilateral APAs

Of the 167 APA submissions filed in 2023, 144 submissions (approximately 86%) requested bilateral APAs, 17 submissions (approximately 10%) requested unilateral APAs, and six submissions accounted for multilateral requests (approximately 4%). Of the 156 APAs that were executed in 2023, 130 involved bilateral APAs (approximately 83%).

Renewal bilateral APAs as a percentage of all executed APAs accounted for approximately 38% of executed APAs in 2023; this is a decrease from 42% in 2022, 48% in 2021, and slightly more than 50% in 2020. All renewal APAs (bilateral and unilateral) accounted for approximately 47% of all APAs executed in 2023. The overall number of renewals executed in 2023 (both unilateral and bilateral) totaled 74 (accounting for 47% of executed APAs in 2023), a significant increase from the 42 renewals (both bilateral and unilateral) that were completed in 2022 (accounting for 55% of executed APAs in 2022).

Types of transactions covered in APAs

As in prior years, more than half of the APAs executed in 2023 (56%) involved transactions between non-US parents and US subsidiaries.

Approximately 36% of the transactions covered by completed APAs in 2023 involved the transfer of tangible goods, including both inbound and outbound sales; this is a slight decrease from 37% in 2022. Approximately 44% of the APAs executed in 2023 involved inbound and outbound services transactions (a decrease from 39% in 2022) and 18% involved the use of intangible property (a decrease from 22% in 2022). Overall, the types of covered transactions remain stable.

Observation: The [Amount B final report](#) clarifies that if the competent authorities of the relevant jurisdictions reach a mutual agreement in an APA before Amount B is adopted, the terms and conditions of the APA will take priority for in-scope transactions. This is an important point to consider for in-scope companies with tangible goods transactions in the process of negotiating bilateral APAs.

Industries covered in APAs

Executed APAs in 2023 covered six general industry segments — manufacturing (31%); wholesale/retail trade (30%); services (17%); finance, insurance, and real estate (12%); management (6%); and all other industries (4%).

TPMs and PLIs: CPM and OM lead again

Consistent with the approximately 32-year history of the APA program, the comparable profits method (CPM) / transactional net margin method (TNMM), with varying profit level indicators (PLIs), was the primary transfer pricing

method (TPM) used in APAs executed in 2023. In 2023, 80% of APAs involving transfers of tangible and intangible property applied the CPM/TNMM (compared to 77% in 2022). Similarly, 86% of APAs involving services transactions relied on the CPM/TNMM (compared to 80% in 2022). The operating margin (OM), defined as the ratio of operating profit to sales, was the most common PLI used in applying the CPM/TNMM to tangible and intangible transactions, accounting for 60% of these cases. For APAs that applied the CPM/TNMM to services transactions, the OM and operating profit to operating expense were the most common PLIs and accounted for 48% of the PLIs employed.

Observation: The report does not specify the number of APAs that used the residual profit split method (RPSM). Although the report does not give visibility as to the TPM used for the remaining 20% of tangible or intangible property transactions (and 14% for services transactions), the CPM/TNMM continues to be the dominant method.

Ranges and adjustment mechanisms

Most transactions covered in APAs target a result that falls within the applicable interquartile range. In transactions involving the payment of royalties for the use of intangibles, both specific royalty rates and ranges were used. Where the covered transaction was the transfer of intangible property and the payment for such transfer would be a royalty based solely on external comparable uncontrolled transactions, a secondary method testing the post-royalty operating margin or cost-plus markup sometimes was used.

For APAs concluded in 2023, several mechanisms were used for adjusting the tested party's results when those results fell outside the agreed range or did not match the point required in the APA. The report provides several examples of the mechanisms used: an adjustment bringing the tested party's results to the closer edge of the range applied to the results of a single year; an adjustment to the closer edge of the range applied to the results over the APA term; an adjustment to the specified point or royalty rate; or an adjustment to the median of the range for a single year.

APA terms

Just under 45% of the executed APAs in 2023 had a five-year term, which is the standard length for an APA term. The longest APA term agreed to in 2023 was 14 years. Nineteen of the executed APAs had terms shorter than five years. The overall average number of years for an APA term was six years. Approximately 19% of the APAs executed in 2023 included rollback years, an increase from 16% in 2022.

Observation: As in the past, in 2023 APA terms were set, to the extent feasible, to allow for a reasonable amount of prospectivity at the time the APA was executed.

Let's talk

For a deeper discussion of how the 2023 APA report might affect your business, please contact:

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