

group is not legally effective for purposes of sections 7602, 7603, and 7604, the noncompliance penalty adjustment under section 6038A(e) and §1.6038A-7 shall apply.

(d) *Legal effect of authorization of agent.* The legal consequences of a foreign related party authorizing a reporting corporation to act as its agent for purposes of sections 7602, 7603, and 7604 of the Code are as follows.

(1) *Agent for purposes of commencing judicial proceedings.* A reporting corporation that is authorized by a foreign related party to act as its agent for purposes of sections 7602, 7603, and 7604 (including service of process) is also the agent of the foreign related party for purposes of—

(i) The filing of a petition to quash under section 6038A(e)(4)(A) or a petition to review an Internal Revenue Service determination of noncompliance under section 6038A(e)(4)(B), and

(ii) The commencement of a judicial proceeding to enforce a summons under section 7604, whether commenced in conjunction with a petition to quash under section 6038A(e)(4)(A) or commenced as a separate proceeding in the federal district court for the district in which the person to whom the summons is issued resides or is found.

(2) *Foreign related party found where reporting corporation found.* For any purposes relating to sections 7602, 7603, or 7604 (including service of process), a foreign related party that authorizes a reporting corporation to act on its behalf under section 6038A(e)(1) and this section may be found anywhere where the reporting corporation has residence or is found.

(e) *Successors in interest.* A successor in interest to a related party must execute the authorization of agent as described in paragraph (b) of this section.

(f) *Deemed compliance—(1) In general.* In exceptional circumstances, the District Director may treat a reporting corporation as authorized to act as agent for a related party for purposes of sections 7602, 7603, and 7604 in the absence of an actual agency appointment by the foreign related party, in circumstances where the actual absence of an appointment is reasonable. Factors to be considered include—

(i) If neither the reporting corporation nor the other party to the transaction knew or had reason to know that the two parties were related at the time of the transaction, and

(ii) The extent to which the taxpayer establishes to the satisfaction of the District Director that all transactions between the reporting corporation and the related party were on arm's length terms and did not involve the participation of any known related party.

(2) *Reason to know.* Whether the reporting corporation or other party had reason to know that the two parties were related at the time of the transaction will be determined by all the facts and circumstances.

(3) *Effect of deemed compliance.* If a reporting corporation is deemed under this paragraph (f) to have been authorized to act as an agent for a foreign related party for purposes of sections 7602, 7603, and 7604, such deemed compliance is applicable only for that particular transaction and other reportable transactions entered into prior to the time when the reporting corporation knew or had reason to know that the related party, in fact, was related. The noncompliance rule of §1.6038A-7 shall apply to any transaction subsequent to that time with the same related party, unless the related party actually authorizes the reporting corporation to act as its agent under paragraph (a) of this section. In addition, the record maintenance requirements of §1.6038A-3 will apply to all subsequent transactions and, with respect to prior transactions, will apply to relevant records in existence at the time the relationship was discovered.

(g) *Effective dates.* For effective dates for this section, see §1.6038A-1(n).

[T.D. 8353, 56 FR 28073, June 19, 1991; T.D. 8353, 56 FR 41792, Aug. 23, 1991]

**§ 1.6038A-6 Failure to furnish information.**

(a) *In general.* The rules of §1.6038A-7 may be applied with respect to a transaction between a foreign related party and the reporting corporation (including any transaction engaged in by a partnership that is attributed to the reporting corporation under §1.6038A-1(e)(2)) if a summons is issued to the reporting corporation to produce any

records or testimony, either directly or as agent for such related party, to determine the correct treatment under title 1 of the Code of such a transaction between the reporting corporation and the related party; and if—

(1)(i) The summons is not quashed in a proceeding, if any, begun under section 6038A(e)(4) and is not determined to be invalid in a proceeding, if any, begun under section 7604 to enforce such summons; and

(ii) The reporting corporation does not substantially and timely comply with the summons, and the District Director has sent by certified or registered mail a notice under section 6038A(e)(2)(C) to the reporting corporation that it has not so complied; or

(2) The reporting corporation fails to maintain or to cause another to maintain records as required by § 1.6038A-3, and by reason of that failure, the summons is quashed in a proceeding under section 6038A(e)(4) or in a proceeding begun under section 7604 to enforce the summons, or the reporting corporation is not able to provide the records requested in the summons.

(b) *Coordination with treaties.* Where records of a related party are obtainable on a timely and efficient basis under information exchange procedures provided under a tax treaty or tax information exchange agreement (TIEA), the Service generally will make use of such procedures before issuing a summons. The absence or pendency of a treaty or TIEA request may not be asserted as grounds for refusing to comply with a summons or as a defense against the assertion of the noncompliance penalty adjustment under § 1.6038A-7. For purposes of this paragraph, information is available on a timely and efficient basis if it can be obtained within 180 days of the request.

(c) *Enforcement proceeding not required.* The District Director is not required to begin an enforcement proceeding to enforce the summons in order to apply the rules of § 1.6038A-7.

(d) *De minimis failure.* Where a reporting corporation's failure to comply with the requirement to furnish information under this section is *de minimis*, the District Director, in the exercise of discretion, may choose not to apply the noncompliance penalty. Thus, for ex-

ample, in cases where a particular document or group of documents is not furnished upon request or summons, the District Director (in the District Director's sole discretion), may choose not to apply the noncompliance penalty if the District Director deems the document or documents not to have significant or sufficient value in the determination of the correctness of the tax treatment of the related party transaction.

(e) *Suspension of statute of limitations.* If the reporting corporation brings an action under section 6038A(e)(4)(A) (proceeding to quash) or (e)(4)(B) (review of secretarial determination of noncompliance), the running of any period of limitation under section 6501 (relating to assessment and collection of tax) or under section 6531 (relating to criminal prosecutions) for the taxable year or years to which the summons that is the subject of such proceeding relates shall be suspended for the period during which such proceeding, and appeals therein, are pending. In no event shall any such period expire before the 90th day after the day on which there is a final determination in such proceeding.

(f) *Effective dates.* For effective dates for this section, see § 1.6038A-1(n).

[T.D. 8353, 56 FR 28075, June 19, 1991]

#### § 1.6038A-7 Noncompliance.

(a) *In general.* In the case of any failure described in § 1.6038A-5 or § 1.6038A-6, the rules of this § 1.6038A-7 apply to the reporting corporation. In such a case—

(1) The amount of the deduction allowed under subtitle A for any amount paid or incurred by the reporting corporation to the related party in connection with such transaction, and

(2) The cost to the reporting corporation of any property acquired in such transaction from the related party or transferred by such corporation in such transaction to the related party, may be determined by the District Director.

(b) *Determination of the amount.* The amount of the deduction or the cost to the reporting corporation shall be the amount determined by the District Director (in the District Director's sole discretion) from the District Director's