



## LB&I International Practice Service Process Unit – Overview

IPS Level	Number	Title	UIL Code	Number
Shelf	N/A	Cross-over Shelf		
Volume	17	Information Gathering and Penalties	Level 1 UIL	9560
Part	17.8	§6038A(e) - Failure to authorize an agent	Level 2 UIL	9560.6
Chapter	17.8.1	Authorization of Agent Considerations	Level 3 UIL	N/A
Sub-Chapter	N/A	N/A		

<b>Unit Name</b>	Using an Authorization of Agent when a US Corporation is 25% Foreign Owned
------------------	--

<b>Document Control Number (DCN)</b>	IGA/PUO/C_17.8.1_04(2014)
<b>Date of Last Update</b>	04/21/2015

*Note: This document is not an official pronouncement of law, and cannot be used, cited or relied upon as such. Further, this document may not contain a comprehensive discussion of all pertinent issues or law or the IRS's interpretation of current law.*

# Table of Contents

*(View this PowerPoint in “Presentation View” to click on the links below)*

[Introduction](#)

[Process Overview](#)

[Detailed Explanation of the Process](#)

[Process Applicability](#)

[Summary of Process Steps](#)

- [Step 1](#) Issue an IDR for the location of records
- [Step 2](#) Review the record maintenance requirements
- [Step 3](#) Prepare an Authorization of Agent request
- [Step 4](#) Issue the Authorization of Agent request

# Table of Contents (cont'd)

*(View this PowerPoint in "Presentation View" to click on the links below)*

- [Step 5](#) Review the executed Authorization of Agent
- [Step 6](#) Mail notice of failure to provide an Authorization of Agent
- [Step 7](#) Consider applying the noncompliance penalty

[Examples of the Process](#)

[Training and Additional Resources](#)

[Glossary of Terms and Acronyms](#)

[Index of Related Issues](#)

# Introduction

## Using an Authorization of Agent when a US Corporation is 25% Foreign Owned

It may be necessary for an examiner to examine books, records or other data in the custody or control of a foreign related person. Generally, a summons issued by the U.S. government to such foreign related person is not legally enforceable when that person resides in a foreign country. When such records regard a transaction of a domestic corporation that is 25-percent owned by a foreign shareholder, Internal Revenue Code (“IRC”) § 6038A(e) provides that such domestic corporation may be designated by such foreign shareholder (and/or other foreign related persons) as its agent with respect to any IRS request or summons for records. A domestic corporation with a 25% foreign shareholder is referred to in the regulations as a domestic reporting corporation (“DRC”).

When a 25-percent foreign shareholder (or a foreign related person) does not designate the DRC as agent pursuant to IRC §6038A(e), a noncompliance rule applies. Under this rule, the Service has sole discretion to determine the amount of DRC’s deductions related to, and the cost of property purchased from (or transferred to) that foreign related party. The adjustment may be based on the information the Service has available or from information the Service chooses to obtain through testimony or otherwise. The noncompliance rule also applies when a DRC that was designated as agent fails to substantially comply in a timely manner with an IRS summons to produce records of, or take testimony from, the designating foreign related party.

This Process Unit - Overview describes the steps for information gathering when requesting an authorization of agent (“A of A”) under IRC § 6038A(e), and also describes the steps when the foreign related party does not execute the authorization requested.

Example circumstances of when an examiner should consider using an A of A are listed at [Slide 43](#).

# Process Overview

## Using an Authorization of Agent when a US Corporation is 25% Foreign Owned

**Qualifications to request an A of A.** The Service may request an A of A when the taxpayer under exam is a domestic corporation, the domestic corporation is owned by a 25% foreign shareholder, and there was a transaction between the domestic corporation and a 25% foreign shareholder of the domestic corporation or any foreign person related to the domestic corporation or to a 25% foreign shareholder of the domestic corporation.

**Records and testimony sought.** The Service may seek copies of records related to a transaction between DRC and a foreign related party or ask for related testimony (such as for the location where those records are generally maintained).

**Small corporation exception.** A DRC with less than \$10 million of U.S. gross receipts in a tax year is not required to be authorized as an agent for that tax year. Gross receipts means all amounts received or accrued in determining the gross income of all related reporting corporations including the DRC under exam.

**Transactions of de minimis value exception.** A DRC with gross payments to and from foreign related parties of not more than \$5 million and less than 10% of its U.S. gross income for a tax year is not required to be authorized as an agent for that year.

**Noncompliance penalty.** When a foreign related party fails to execute an A of A, the Service has sole discretion to determine the amount of DRC's deductions related to, and the cost of property purchased from (or transferred to) that foreign related party. There is no reasonable cause exception to this determination. Once an A of A is executed, if DRC does not provide documents requested by an IDR consider issuing a summons under IRC § 6038A. For discussion of issuing summons under IRC § 6038A, see the IPS Unit (currently under development) titled "Issuing a summons under IRC § 6038A when a US corporation is 25% foreign owned."

# Detailed Explanation of the Process

## Using an Authorization of Agent when a US Corporation is 25% Foreign Owned

### Analysis

A DRC must maintain records that are sufficient to determine the correct U.S. tax treatment of DRC's transactions with foreign related parties. [Treas. Reg. § 1.6038A-3(a)]

The regulations describe the categories of the records that must be maintained for DRC to be treated as meeting the record maintenance requirements. [Treas. Reg. § 1.6038A-3(c)] Alternatively, DRC may negotiate and enter into a record maintenance agreement with the Service to establish which records must be maintained, by whom, how they must be maintained, and the period of record retention (see Treas. Reg. § 1.6038A-3(e) and Rev. Proc. 91-38). Under certain conditions, a DRC may maintain records outside the U.S. that are not ordinarily maintained in the U.S. [see Treas. Reg. § 1.6038A-3(f)]. However, the Service may require maintenance within the U.S. of any foreign-based records if there is a clear pattern of failure to maintain or timely produce such records.

Early in the exam, the examiner should issue an IDR to determine (a) if the DRC has met the record maintenance requirements and (b) where such records are located. Consider obtaining a complete listing of all foreign maintained records.

An examiner may request that a foreign related party authorize a DRC to act as the foreign related party's agent. The limited agency is solely for purposes of providing records or testimony to the Service, pursuant to IRC §§ 7602, 7603, and 7604, that may be relevant to the tax treatment of a DRC transaction. The Service may also issue a summons for such records or testimony.

# Detailed Explanation of the Process (cont'd)

## Using an Authorization of Agent when a US Corporation is 25% Foreign Owned

### Analysis

The Manager controlling the issue/case has discretion as to when an A of A is requested. It may be requested:

- at a preaudit conference,
- when IDRs are not satisfactorily answered,
- when complete cooperation is not provided, or
- never, if IDRs are satisfactorily answered.

# Detailed Explanation of the Process (cont'd)

## Using an Authorization of Agent when a US Corporation is 25% Foreign Owned

### Analysis

Once an A of A designation is made, it is effective for all tax years not barred by the statute of limitations [Treas. Reg. § 1.6038A-5(b)(1) and IRM 4.60.8.3.5.8].

When there is a failure to authorize the DRC as an agent (as described in Treas. Reg. § 1.6038A-5) or a failure to timely furnish information after granting the A of A (under Treas. Reg. § 1.6038A-6), the rules of Treas. Reg. § 1.6038A-7 for noncompliance apply to the DRC. In such case, the Service may determine:

- the amount of the deduction allowed for any amount paid or incurred by the reporting corporation to the related party in connection with such transaction, and
- 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.

The Service shall determine the amount of the deduction or cost based on the Service's knowledge or such information as the Service may choose to obtain through testimony or otherwise. The Service may disregard any information or materials submitted by DRC or a foreign related party if the Service deems such information or materials insufficiently probative of the relevant facts.

Throughout the process described in this unit, the Service should consider whether a request pursuant to an income tax treaty, or a tax information exchange agreement ("TIEA"), with a country where the records are located could secure the information sought. If the authorization of agent is received, when records are obtainable within 180 days using a treaty or TIEA request, the Service generally will make use of such a request before issuing the IRC § 6038A summons. See Treas. Reg. § 1.6038A-6(b) Coordination with treaties.

# Process Applicability

## Using an Authorization of Agent when a US Corporation is 25% Foreign Owned

The following criteria must be met before requesting an authorization of agent.

Criteria	Resources	6103 Protected Resources
<p><b>Domestic Corporation.</b> The taxpayer must be a domestic corporation with a 25% foreign shareholder. Such corporation is referred to in the regulations as a domestic reporting corporation (“DRC”).</p>	<ul style="list-style-type: none"> <li>▪ IRC 6038A(a) Requirement.</li> <li>▪ Treas. Reg. 1.6038A-1(c) Reporting corporation.</li> </ul>	
<p><b>25% Shareholder.</b> A 25% foreign shareholder is one that directly or indirectly owns at least 25% of DRC’s stock by voting power or value at any time of the taxable year.</p> <p>If DRC and related parties own 25% or more of the interests in a partnership , DRC’s ratable share of the partnership’s transactions are treated as DRC’s transactions . Such attribution does not include transactions directly between the DRC and the partnership.</p>	<ul style="list-style-type: none"> <li>▪ Bittker &amp; Lokken Fed Tax’n Inc, Est and Gift Para 65.5.3</li> <li>▪ IRC 6038A(c)(1) 25-percent foreign-owned. Treas.</li> <li>▪ Reg. 1.6038A-1(c)(3) 25-percent foreign shareholder.</li> <li>▪ Treas. Reg. 1.6038A-1(e)(2) Attribution of transactions with related parties engaged in by a partnership.</li> </ul>	

# Process Applicability (cont'd)

## Using an Authorization of Agent when a US Corporation is 25% Foreign Owned

The following criteria must be met before requesting an authorization of agent.

Criteria	Resources	6103 Protected Resources
<p><b>Related Parties.</b> There must be a transaction between DRC and:</p> <ul style="list-style-type: none"> <li>• a direct or indirect 25% foreign shareholder of DRC,</li> <li>• any person related to the reporting corporation or to a 25% foreign shareholder of DRC within the meaning of IRC §§ 267(b) or 707(b)(1), or</li> <li>• a foreign person related within the meaning of IRC § 482.</li> </ul>	<ul style="list-style-type: none"> <li>▪ IRC 6038A(e)(1) Agreement to treat corporation as agent.</li> <li>▪ IRC 6038A(c)(2) Related party.</li> <li>▪ Treas. Reg. 1.6038A-1(e) Attribution rules.</li> </ul>	

# Process Applicability (cont'd)

## Using an Authorization of Agent when a US Corporation is 25% Foreign Owned

The following criteria must be met before requesting an authorization of agent.

Criteria	Resources	6103 Protected Resources
<p><b>Related Within the Meaning of IRC § 482.</b> Determining “within the meaning of IRC § 482 ” involves understanding when IRC § 482 applies, and the definition of a “controlled taxpayer.”</p> <p>IRC § 482 applies when two or more organizations, trades or businesses (whether or not incorporated, whether or not organized in the U.S., and whether or not affiliated) are owned or controlled directly or indirectly by the same interests.</p> <p>The regulations under IRC §482 refer to a ““controlled taxpayer,” rather than a “related party.” This difference is not significant in light of the legislative history which indicates that Congress intended IRC § 6038A to apply to transactions within the scope of IRC § 482.</p>	<ul style="list-style-type: none"> <li>▪ IRC 482 Allocation of income and deductions among taxpayers.</li> <li>▪ HR Rep No 101-247 at 1295 (1989)</li> <li>▪ FSA 200132003</li> </ul>	

# Process Applicability (cont'd)

## Using an Authorization of Agent when a US Corporation is 25% Foreign Owned

The following criteria must be met before requesting an authorization of agent.

Criteria	Resources	6103 Protected Resources
<p><b>Related Within the Meaning of IRC § 482 (cont'd).</b> A “controlled taxpayer” is “any one of two or more taxpayers owned or controlled directly or indirectly by the same interests, and includes the taxpayer that owns or controls the other taxpayers.”</p> <p>“Controlled” includes any type of control, whether legally enforceable or not, and however exercisable or exercised, including control resulting from the actions of two or more taxpayers acting in concert or with a common goal or purpose. It is the reality of the control that is decisive, not its form or the mode of its exercise. A presumption of control arises if income or deductions have been arbitrarily shifted.”</p> <p>A transaction not priced at arm's length suggests an arbitrary shifting of income and deductions, thus triggering the presumption of control.</p>	<ul style="list-style-type: none"> <li>▪ Treas. Reg. 1.482-1(i) Definitions.</li> <li>▪ B. Forman &amp; Co. v. Commissioner, 453 F.2d 1144 (2d Cir. 1972).</li> <li>▪ FSA 200132003</li> </ul>	

# Process Applicability (cont'd)

## Using an Authorization of Agent when a US Corporation is 25% Foreign Owned

The following criteria must be met before requesting an authorization of agent.

Criteria	Resources	6103 Protected Resources
<b>Consolidated Returns.</b> The term “related party” does not include any corporation filing a consolidated federal income tax return with DRC.	<ul style="list-style-type: none"><li>▪ Treas. Reg. 1.6038A-1(d) Related party.</li></ul>	

# Process Applicability (cont'd)

## Using an Authorization of Agent when a US Corporation is 25% Foreign Owned

The following criteria must be met before requesting an authorization of agent.

Criteria	Resources	6103 Protected Resources
<p><b>Authorization in Prior Year Continues.</b> Once an A of A designation is made, it is effective for all tax years not barred by the statute of limitations.</p>	<ul style="list-style-type: none"> <li>▪ Treas. Reg. 1.6038A-5(b)(1) Authorization by related party.</li> <li>▪ IRM 4.60.8.3.5.8 - Failure to Obtain Authorization of Agent</li> </ul>	

# Process Applicability (cont'd)

## Using an Authorization of Agent when a US Corporation is 25% Foreign Owned

The following criteria must be met before requesting an authorization of agent.

Criteria	Resources	6103 Protected Resources
<p><b>IDR Issued for Relevant Records.</b> The Service has discretion as to when to request an A of A. This may be when the Service has issued an IDR for copies of records related to a transaction between DRC and a foreign related party and, subsequently, DRC did not satisfactorily respond to the IDR.</p> <p>The requested records “may be relevant” or material to the tax treatment of an examined item. “May be relevant” is a broad standard according to U.S. v. Powell. Any information that might throw light on the U.S. taxpayer’s liability will generally be found to be relevant by the courts.</p> <p>Relevant records include those of DRC and/or any foreign related party that may be relevant to determine the correct U.S. tax treatment of transactions between DRC and foreign related parties.</p>	<ul style="list-style-type: none"> <li>▪ IRM 4.60.8.3.5.8 (2)(b) - Failure to Obtain Authorization of Agent.</li> <li>▪ U.S. v. Powell, 379 U.S. 48 (1964)</li> <li>▪ Matter of Intern. Marketing Ltd., 66 AFTR 2d 90-5466 (ND CA 1990).</li> <li>▪ U.S. v. Arthur Young &amp; Co., 465 U.S. 805 (1984)</li> <li>▪ Treas. Reg. 1.6038A-3(a) General maintenance requirements.</li> </ul>	

# Process Applicability (cont'd)

## Using an Authorization of Agent when a US Corporation is 25% Foreign Owned

The following criteria must be met before requesting an authorization of agent.

Criteria	Resources	6103 Protected Resources
<p><b>Small Corporation Exception.</b> A DRC with less than \$10 million of U.S. gross receipts in a tax year is not required to be authorized as an agent for that tax year. Gross receipts means all amounts received or accrued in determining the gross income of all related reporting corporations including the DRC under exam.</p>	<ul style="list-style-type: none"> <li>▪ Treas. Reg. 1.6038A-1(h) Small corporation exception.</li> </ul>	

# Process Applicability (cont'd)

## Using an Authorization of Agent when a US Corporation is 25% Foreign Owned

The following criteria must be met before requesting an authorization of agent.

Criteria	Resources	6103 Protected Resources
<p><b>Related Reporting Corporations.</b> For purposes of determining U.S. gross receipts for the Small Corporation Exception (and both aggregate gross payments and U.S. gross income for the Transactions of De Minimis Value Exception), a related reporting corporation is:</p> <ul style="list-style-type: none"> <li>▪ a direct or indirect 25% foreign shareholder of DRC,</li> <li>▪ any person related to the reporting corporation or to a 25% foreign shareholder of DRC within the meaning of IRC §§ 267(b) or 707(b)(1), or</li> <li>▪ a foreign person related to DRC within the meaning of IRC § 482.</li> </ul> <p>The constructive ownership rules of IRC § 318 and the attribution rules of IRC § 267(c) apply.</p> <p>Related foreign reporting corporations (“FRCs”) are included in the determinations of U.S. gross receipts and/or U.S. gross income.</p>	<ul style="list-style-type: none"> <li>▪ Treas. Reg. 1.6038A-1(j) Related reporting corporations.</li> <li>▪ Treas. Reg. 1.6038A-1(d) Related party.</li> <li>▪ Treas. Reg. 1.6038A-1(e) Attribution rules.</li> </ul>	

# Process Applicability (cont'd)

## Using an Authorization of Agent when a US Corporation is 25% Foreign Owned

The following criteria must be met before requesting an authorization of agent.

Criteria	Resources	6103 Protected Resources
<p><b>Transactions of De Minimis Value Exception.</b> A DRC with gross payments to and from foreign related parties (in the aggregate, not netted) of not more than \$5 million and less than 10% of its U.S. gross income for a tax year is not required to be authorized as an agent for that year. Aggregate gross payments means those reportable on Form 5472 (Information Return of a 25% Foreign-Owned U.S. Corporation or a Foreign Corporation Engaged in a U.S. Trade or Business), Part IV (Monetary Transactions Between Reporting Corporations and Foreign Related Party). This test must be met for the U.S. gross income of both DRC and of all related reporting corporations including the DRC under exam.</p>	<ul style="list-style-type: none"> <li>▪ Treas. Reg. 1.6038A-1(i) Safe harbor for reporting corporations with related party transactions of de minimis value.</li> <li>▪ Bittker &amp; Lokken Fed Tax'n Inc, Est and Gift Para 65-99</li> <li>▪ Treas. Reg. 1.6038A-2(b)(3) Foreign related party transactions for which only monetary consideration is paid or received by the reporting corporation.</li> <li>▪ Treas. Reg. 1.6038A-3(b)(4) Foreign related party transactions involving nonmonetary consideration or less than full consideration.</li> </ul>	

# Summary of Process Steps

## Using an Authorization of Agent when a US Corporation is 25% Foreign Owned

### Process Steps

Before requesting an A of A, determine the identify of the person who has custody and control over the records sought. DRCs must keep permanent records sufficient to determine the correct U.S. tax treatment of transactions with related parties. Often, a DRC will not provide foreign-based evidence to the Service until an A of A is executed. Follow prudent procedures for issuing the A of A. An A of A must be timely-received and signed by persons with the authority to authorize and accept the agent designation. Notice of failure is required by the IRM. The noncompliance penalty amount can be overridden only by clear and convincing evidence that the Service abused its discretion.

#### [Step 1](#)

Issue an IDR for the location of records.

#### [Step 2](#)

Review the record maintenance requirements.

#### [Step 3](#)

Prepare an Authorization of Agent request.

#### [Step 4](#)

Issue the Authorization of Agent request.

# Summary of Process Steps (cont'd)

## Using an Authorization of Agent when a US Corporation is 25% Foreign Owned

### Process Steps

Before requesting an A of A, determine the identify of the person who has custody and control over the records sought. DRCs must keep permanent records sufficient to determine the correct U.S. tax treatment of transactions with related parties. Often, a DRC will not provide foreign-based evidence to the Service until an A of A is executed. Follow prudent procedures for issuing the A of A. An A of A must be timely-received and signed by persons with the authority to authorize and accept the agent designation. Notice of failure is required by the IRM. The noncompliance penalty amount can be overridden only by clear and convincing evidence that the Service abused its discretion.

#### [Step 5](#)

Review the executed Authorization of Agent.

#### [Step 6](#)

Mail notice of failure to provide an Authorization of Agent.

#### [Step 7](#)

Consider applying the noncompliance penalty.

# Step 1: Issue an IDR for the location of records

## Using an Authorization of Agent when a US Corporation is 25% Foreign Owned

### Step 1

Before requesting an A of A, determine the identify of the person who has custody and control over the records sought.

Considerations	Resources	6103 Protected Resources
<p>Generally, any person subject to a U.S. court's jurisdiction can be compelled to produce records and documents in its custody and control, whether or not such records and documents are located outside of the U.S.</p> <p>A person is deemed to have custody and control when it has the legal right and physical ability to provide the books and records to the government pursuant to an IRS summons or grand jury subpoena.</p>	<ul style="list-style-type: none"> <li>▪ In re Rivera, 79 F. Supp. 510 (S.D. N.Y. 1948)</li>   <li>▪ In re Folding Carton Antitrust Litigation, 76 FRD 420 (N.D. Ill. 1977)</li>   <li>▪ U.S. v. Brobeck, 363 F. Supp. 1035 (W.D. Pa. 1973)</li> </ul>	
<div style="display: flex; align-items: flex-start;">  <p><b>DECISION POINT:</b> Consider interviewing DRC's personnel most familiar with the transaction(s) for the location of the relevant records. Then, follow up with an IDR requesting the location of the records. See <a href="#">Slide 12</a> for more about issuing this IDR.</p> </div>		

# Step 1: Issue an IDR for the location of records (cont'd)

## Using an Authorization of Agent when a US Corporation is 25% Foreign Owned

### Step 1

Before requesting an A of A, determine the identify of the person who has custody and control over the records sought.

Considerations	Resources	6103 Protected Resources
<p>Although you may have issued at least one IDR requesting copies of records relevant to a transaction between DRC and a foreign related party, consider issuing an IDR that addresses the record maintenance requirements. This will help to identify where the relevant records are kept. For example, the IDR could state:</p> <p>Please identify the location of all books and records maintained under the:</p> <ul style="list-style-type: none"> <li>▪ general record maintenance requirements [Treas. Reg. § 1.6038A-3(a) &amp; (f)(1)],</li> <li>▪ safe harbor for record maintenance [Treas. Reg. § 1.6038A-3(a)(2), (c) &amp; (f)(1)], and/or</li> <li>▪ non-U.S. record maintenance requirements [Treas. Reg. § 1.6038A-3(f)(2)]</li> </ul>	<ul style="list-style-type: none"> <li>▪ IRM 4.60.8.3.5.4.3(1) -Record Maintenance Procedures and Guidelines</li> </ul>	

# Step 1: Issue an IDR for the location of records (cont'd)

## Using an Authorization of Agent when a US Corporation is 25% Foreign Owned

### Step 1

Before requesting an A of A, determine the identify of the person who has custody and control over the records sought.

Considerations	Resources	6103 Protected Resources
for each of the following transactions between DRC and foreign related parties: <ul style="list-style-type: none"><li>▪ [describe transaction] and [name of foreign related party]</li><li>▪ [describe transaction], and [name of foreign related party]; and</li><li>▪ [describe transaction] and [name of foreign related party].</li></ul>		

# Step 1: Issue an IDR for the location of records (cont'd)

## Using an Authorization of Agent when a US Corporation is 25% Foreign Owned

### Step 1

Before requesting an A of A, determine the identify of the person who has custody and control over the records sought.

Considerations	Resources	6103 Protected Resources
An awareness of the regulatory authority under which DRC is required to maintain such records may be useful for your discussions with DRC and for the preparation of IDRs. See <a href="#">Step 2</a> for a review of the record maintenance requirements.	<ul style="list-style-type: none"><li>IRM 4.60.8.3.5.4.3(1) -Record Maintenance Procedures and Guidelines</li></ul>	

# Step 2: Review the record maintenance requirements

## Using an Authorization of Agent when a US Corporation is 25% Foreign Owned

### Step 2

DRCs must keep permanent records sufficient to determine the correct U.S. tax treatment of transactions with related parties.

Considerations	Resources	6103 Protected Resources
<p><b>Statutory authority for record maintenance</b> . The IRC authorizes regulations to identify the time and manner in which DRC must maintain records relating to:</p> <ul style="list-style-type: none"> <li>▪ the name,</li> <li>▪ principal place of business,</li> <li>▪ nature of business, and</li> <li>▪ country or countries of organization or residence of each foreign related party that had any transaction with DRC during its taxable year.</li> </ul> <p>Also, the IRC authorizes regulations to maintain records relating to:</p> <ul style="list-style-type: none"> <li>▪ how DRC is related to each foreign related party, and</li> <li>▪ the transactions between DRC and each foreign related party.</li> </ul>	<ul style="list-style-type: none"> <li>▪ IRC 6038A(a) Requirement.</li> <li>▪ IRC 6038A(b) Required information.</li> </ul>	

## Step 2: Review the record maintenance requirements (cont'd)

### Using an Authorization of Agent when a US Corporation is 25% Foreign Owned

#### Step 2

DRCs must keep permanent records sufficient to determine the correct U.S. tax treatment of transactions with related parties.

Considerations	Resources	6103 Protected Resources
<p><b>General maintenance requirements.</b> The regulations require DRC to maintain books and records that are sufficient to establish the correctness of its income tax return. Such records include information and documents to the extent they may be relevant to determine the correct U.S. tax treatment of transactions with related parties. [For example, DRC must maintain sufficient relevant cost data (from which a profit and loss statement may be created) for products or services transferred between DRC and its foreign related parties.] This includes DRC's and any foreign related party's records that may be relevant to determine the correct U.S. tax treatment of transactions between DRC and foreign related parties. The relevance of such records shall be determined based on all facts and circumstances</p>	<ul style="list-style-type: none"> <li>▪ IRC 6001 Notices or regulations requiring records, statements, and special returns.</li> <li>▪ Treas. Reg. 1.6038A-3(a) General maintenance requirements.</li> </ul>	

## Step 2: Review the record maintenance requirements (cont'd)

### Using an Authorization of Agent when a US Corporation is 25% Foreign Owned

#### Step 2

DRCs must keep permanent records sufficient to determine the correct U.S. tax treatment of transactions with related parties.

Considerations	Resources	6103 Protected Resources
<p><b>Safe harbor for record maintenance.</b> The regulations provide a safe harbor that sets forth the types of records to be maintained that are relevant to (a) DRC's business or industry and (b) the correct U.S. tax treatment of DRC's transactions with foreign related parties. A DRC that maintains, or causes another person to maintain, the following records will be deemed to have met the record keeping requirement:</p> <ul style="list-style-type: none"> <li>▪ Original entry books and transaction records. (For example, general ledgers sales journals, cancelled checks, bank statements, and purchase invoices.)</li> <li>▪ Records from which DRC can create (within a reasonable time) a material profit and loss statement that reflects the profit and loss of the related party group that is attributable to U.S.-connected products or services.</li> </ul>	<ul style="list-style-type: none"> <li>▪ Treas. Reg. 1.6038A-3(a)(2) Safe harbor.</li> <li>▪ Treas. Reg. 1.6038A-3(c) Specific records to be maintained for safe harbor.</li> </ul>	

## Step 2: Review the record maintenance requirements (cont'd)

### Using an Authorization of Agent when a US Corporation is 25% Foreign Owned

#### Step 2

DRCs must keep permanent records sufficient to determine the correct U.S. tax treatment of transactions with related parties.

Considerations	Resources	6103 Protected Resources
<p><b>Safe harbor for record maintenance (cont'd)</b></p> <ul style="list-style-type: none"> <li>▪ Documents relevant to determining the arm's length price of transfer pricing transactions. (For example, documents related to transactions involving the same or similar products or services entered into by DRC or a foreign related party with related and unrelated parties.)</li> <li>▪ Financial and other documents filed with, or prepared for, any foreign governmental entity, independent commission, or financial institution.</li> <li>▪ Records or charts showing the relationship between DRC and the foreign related parties; the location, ownership, and entity classification of all such entities; and the management structure of foreign affiliates.</li> </ul>	<ul style="list-style-type: none"> <li>▪ Treas. Reg. 1.6038A-3(c)(3) Material profit and loss statements.</li> <li>▪ Treas. Reg. 1.6038A-3(c)(7)(i) U.S.-connected products or services.</li> </ul>	

## Step 2: Review the record maintenance requirements (cont'd)

### Using an Authorization of Agent when a US Corporation is 25% Foreign Owned

#### Step 2

DRCs must keep permanent records sufficient to determine the correct U.S. tax treatment of transactions with related parties.

Considerations	Resources	6103 Protected Resources
<p><b>Safe harbor for record maintenance (cont'd)</b></p> <ul style="list-style-type: none"> <li>▪ Records of loans, services, and other non-sales transactions between DRC and foreign related parties. (For example, guarantees, hedging arrangements, security agreements, research and development expense allocations, service agreements, patent registrations, and documents regarding lawsuits in foreign countries.)</li> </ul> <p>“Material profit and loss statement” and “U.S.-connected services or products” are defined at Treas. Reg. § 1.6038A-3(c)(3) &amp; (c)(7)(i) respectively.</p>		

## Step 2: Review the record maintenance requirements (cont'd)

### Using an Authorization of Agent when a US Corporation is 25% Foreign Owned

#### Step 2

DRCs must keep permanent records sufficient to determine the correct U.S. tax treatment of transactions with related parties.

Considerations	Resources	6103 Protected Resources
<p><b>Non-U.S. record maintenance requirements.</b> Records required to be maintained under Treas. Reg. § 1.6038A-3, which are not ordinarily maintained in the U.S., must be maintained in the U.S. unless DRC:</p> <ul style="list-style-type: none"> <li>▪ delivers the original records (or copies) to the Service within 60 days of request and provides English translations of specific records within 30 days of request, or</li> </ul>	<ul style="list-style-type: none"> <li>▪ Treas. Reg. 1.6038A-3(f)(2) Non-U.S. maintenance requirements.</li> <li>▪ Treas. Reg. 1.6038A-3(b)(3) Translation of records.</li> <li>▪ Treas. Reg. 1.6038A-3(f)(2)(ii) Non-U.S. maintenance requirements.</li> </ul>	

## Step 2: Review the record maintenance requirements (cont'd)

### Using an Authorization of Agent when a US Corporation is 25% Foreign Owned

#### Step 2

DRCs must keep permanent records sufficient to determine the correct U.S. tax treatment of transactions with related parties.

Considerations	Resources	6103 Protected Resources
<ul style="list-style-type: none"> <li>▪ moves the original records (or copies) to the U.S. within 60 days of request and:               <ul style="list-style-type: none"> <li>i. provides an index to the records,</li> <li>ii. provides the name and address of the U.S. custodian,</li> <li>iii. provides the address where the records are located, and</li> <li>iv. maintains the records in the U.S. as long as they may be relevant or material to determining the correct tax treatment of any transaction between DRC and a related party. In no event, may that period end before the expiration of the statute of limitations period on assessment of tax of the tax year in which the transaction affects DRC's tax liability.</li> </ul> </li> </ul>		

## Step 2: Review the record maintenance requirements (cont'd)

### Using an Authorization of Agent when a US Corporation is 25% Foreign Owned

#### Step 2

DRCs must keep permanent records sufficient to determine the correct U.S. tax treatment of transactions with related parties.

Considerations	Resources	6103 Protected Resources
<p><b>Non-U.S. record maintenance requirements. (cont'd)</b></p> <p>The period for providing material profit and loss statements which are required to be created may be extended to 120 days of the Service's request. The labels and text in these statements must be in English.</p>		
<p><b>Record retention period.</b> The records are required to be maintained as long as they may be relevant or material to determine DRC's U.S. tax liabilities.</p>	<ul style="list-style-type: none"> <li>Treas. Reg. 1.6038A-3(g) Period of retention.</li> </ul>	
<p><b>Clear pattern of failure to maintain or timely produce records.</b> A LB&amp;I Director of Field Operations, with the concurrence of the Deputy Commissioner (International), may require maintenance within the U. S. of foreign-based records if there exists a clear pattern of failure to maintain or timely produce the records.</p>	<ul style="list-style-type: none"> <li>IRM 4.60.8.3.5.4.2(3) - Failure to Maintain Records or Comply with Non-U.S. Maintenance Requirements</li> </ul>	

## Step 2: Review the record maintenance requirements (cont'd)

### Using an Authorization of Agent when a US Corporation is 25% Foreign Owned

#### Step 2

DRCs must keep permanent records sufficient to determine the correct U.S. tax treatment of transactions with related parties.

Considerations	Resources	6103 Protected Resources
<p><b>Monetary penalties.</b> A \$10,000 initial penalty applies to each tax year that DRC fails:</p> <ul style="list-style-type: none"> <li>▪ to maintain or cause another to maintain records required by Treas. Reg. § 1.6038A-3 or</li> <li>▪ to produce required records which are maintained outside the U.S. within the time required by Treas. Reg. § 1.6038A-3(f).</li> </ul> <p>If the deficiency is not corrected within 90 days of notification from the Service, a \$10,000 continuation penalty applies for each 30-day period (or fraction thereof) until the deficiency is corrected.</p> <p>The initial and continuation penalties apply per foreign related party with which DRC has a transaction. There is no maximum amount of continuation penalties for successive 30-day periods. However, the Service may assess only one initial</p>	<ul style="list-style-type: none"> <li>▪ Treas. Reg. 1.6038A-4 Monetary penalty.</li> <li>▪ Treas. Reg. 1.6038A-4(d) Increase in penalty where failure continues after notification.</li> </ul>	

## Step 2: Review the record maintenance requirements (cont'd)

### Using an Authorization of Agent when a US Corporation is 25% Foreign Owned

#### Step 2

DRCs must keep permanent records sufficient to determine the correct U.S. tax treatment of transactions with related parties.

Considerations	Resources	6103 Protected Resources
<p><b>Monetary penalties (cont'd)</b> penalty per foreign related party per year when DRC fails:</p> <ul style="list-style-type: none"> <li>▪ to maintain or cause another to maintain the required records,</li> <li>▪ to produce the required records located outside the U.S., and/or</li> <li>▪ to timely file a complete and accurate Form 5472.</li> </ul> <p>When you receive an incomplete response to an IDR for the location of records required to be maintained, consider sending a pattern letter to DRC regarding the monetary penalty. Blank copies of pattern letters are located at IRM Exhibit 4.60.8:</p> <ul style="list-style-type: none"> <li>▪ -3 for Failure to Maintain Records, and</li> <li>▪ -4 for Failure to Produce Foreign Maintained Records</li> </ul>	<ul style="list-style-type: none"> <li>▪ Treas. Reg. 1.6038A-4(a)(3) Calculation of monetary penalty.</li> <li>▪ IRM 4.60.8.4 - IRM 4.60.8 Exhibits</li> <li>▪ Treas. Reg. 1.6038A-4(c) Failure to maintain records or to cause another to maintain records.</li> </ul>	

## Step 2: Review the record maintenance requirements (cont'd)

### Using an Authorization of Agent when a US Corporation is 25% Foreign Owned

#### Step 2

DRCs must keep permanent records sufficient to determine the correct U.S. tax treatment of transactions with related parties.

Considerations	Resources	6103 Protected Resources
<p><b>Reasonable cause exception.</b> The monetary penalties for failure:</p> <ul style="list-style-type: none"> <li>▪ to maintain the required records,</li> <li>▪ to produce the required records located outside the U.S., and</li> <li>▪ to timely file a complete and accurate Form 5472</li> </ul> <p>may be excused for reasonable cause. Discussions of when and how to consider the reasonable cause exception is outside the scope of this Unit.</p>	<ul style="list-style-type: none"> <li>▪ Treas. Reg. 1.6038A-4(b) Reasonable cause.</li> <li>▪ IRM 4.60.8.3.5.5 - Reasonable Cause</li> </ul>	

## Step 2: Review the record maintenance requirements (cont'd)

### Using an Authorization of Agent when a US Corporation is 25% Foreign Owned

#### Step 2

DRCs must keep permanent records sufficient to determine the correct U.S. tax treatment of transactions with related parties.

Considerations	Resources	6103 Protected Resources
<p><b>Small corporation exception.</b> A DRC with less than \$10 million in U.S. gross receipts for a tax year is not subject to the record maintenance requirements of Treas. Reg. § 1.6038A-3 for that tax year. However, the DRC remains subject to the general record maintenance requirements of IRC § 6001. Gross receipts means all amounts received or accrued in determining the gross income of all related reporting corporations including the DRC under exam.</p>	<ul style="list-style-type: none"> <li>▪ Treas. Reg. 1.6038A-1(h) Small corporation exception.</li> </ul>	

## Step 2: Review the record maintenance requirements (cont'd)

### Using an Authorization of Agent when a US Corporation is 25% Foreign Owned

#### Step 2

DRCs must keep permanent records sufficient to determine the correct U.S. tax treatment of transactions with related parties.

Considerations	Resources	6103 Protected Resources
<p><b>Transactions of De Minimis Value Exception.</b> A DRC with gross payments to and from foreign related parties (in the aggregate, not netted) of not more than \$5 million and less than 10% of its U.S. gross income for a tax year is not subject to the record maintenance requirements of Treas. Reg. § 1.6038A-3 for that year. Aggregate gross payments means those reportable on Form 5472, Part IV. This test must be met for the U.S. gross income of both DRC and of all related reporting corporations including the DRC under exam.</p>	<ul style="list-style-type: none"> <li>▪ Treas. Reg. 1.6038A-1(i) Safe harbor for reporting corporations with related party transactions of de minimis value.</li> <li>▪ Bittker &amp; Lokken Fed. Tax'n Inc, Est and Gift Para 65.99</li> </ul>	

# Step 3: Prepare an Authorization of Agent request

## Using an Authorization of Agent when a US Corporation is 25% Foreign Owned

### Step 3

Often, a DRC will not provide foreign-based evidence to the Service until an A of A is executed.

Considerations	Resources	6103 Protected Resources
<p>When you receive an unsatisfactory IDR response for copies of records and DRC stated (or you believe) that such records are maintained outside of the U.S., consider preparing an A of A request.</p> <p>An A of A appoints DRC to act as a limited agent for purposes of IRC §§ 7602, 7603, and 7604 with respect to any request by the Service to examine records or produce testimony that may be relevant to the tax treatment of any transaction between DRC and a foreign related party.</p>	<ul style="list-style-type: none"> <li>▪ Treas. Reg. 1.6038A-5(a) Failure to authorize.</li> </ul>	

# Step 3: Prepare an Authorization of Agent request

## Using an Authorization of Agent when a US Corporation is 25% Foreign Owned

### Step 3

Often, a DRC will not provide foreign-based evidence to the Service until an A of A is executed.

Considerations	Resources	6103 Protected Resources
<p><b>Review the process applicability.</b> Before preparing an A of A request, review these requirements discussed in the Determination of Process Applicability slides:</p> <ul style="list-style-type: none"> <li>▪ the taxpayer under exam is a domestic corporation,</li> <li>▪ the domestic corporation is owned by a 25% foreign shareholder,</li> <li>▪ there was a transaction between DRC and:               <ol style="list-style-type: none"> <li>a. a direct or indirect 25% foreign shareholder of DRC,</li> <li>b. any person related to the reporting corporation or to a 25% foreign shareholder of DRC within the meaning of IRC §§ 267(b) or 707(b)(1), or</li> <li>c. a foreign person related within the meaning of IRC § 482,</li> </ol> </li> </ul>		

# Step 3: Prepare an Authorization of Agent request (cont'd)

## Using an Authorization of Agent when a US Corporation is 25% Foreign Owned

### Step 3

Often, a DRC will not provide foreign-based evidence to the Service until an A of A is executed.

Considerations	Resources	6103 Protected Resources
<p><b>Review the Process Applicability (cont'd)</b></p> <ul style="list-style-type: none"> <li>d. the Service seeks copies of records related to a transaction between DRC and a foreign related party or asks for related testimony, such as for the location where those records are generally maintained, and</li> <li>e. neither the small corporation exception, nor the transaction of de minimis value exception, apply.</li> </ul> <p>Each of these requirements must be met before the Service issues an A of A request.</p>		

# Step 3: Prepare an Authorization of Agent request (cont'd)

## Using an Authorization of Agent when a US Corporation is 25% Foreign Owned

### Step 3

Often, a DRC will not provide foreign-based evidence to the Service until an A of A is executed.

Considerations	Resources	6103 Protected Resources
<p>The IE should determine which foreign related parties to include in the request based on the transactions under exam and the possible locations of the records. The A of A can be executed by DRC's foreign parent to act as its agent, or to act as its and its foreign affiliates' agent. Also, A of As can be executed by DRC's foreign related parties separately.</p>	<ul style="list-style-type: none"> <li>▪ Treas. Reg. 1.6038A-5(b) Authorization by related party.</li> <li>▪ Treas. Reg. 1.6038A-5(c) Foreign affiliated groups.</li> <li>▪ IRC 6038A(e)(1) Agreement to treat corporation as agent.</li> </ul>	

# Step 3: Prepare an Authorization of Agent request (cont'd)

## Using an Authorization of Agent when a US Corporation is 25% Foreign Owned

### Step 3

Often, a DRC will not provide foreign-based evidence to the Service until an A of A is executed.

Considerations	Resources	6103 Protected Resources
<p>Blank copies of A of A forms are located in the regulations, the IRM, and the resource section of the Information Gathering IPN sharepoint site. IRM Exhibit 4.60.8:</p> <ul style="list-style-type: none"> <li>▪ -5, -8, &amp; -11 for Agency Designation letters (i.e., cover letters)</li> <li>▪ -6 for A of A form for a foreign related parent</li> <li>▪ -9 for A of A form for parent and other foreign related parties</li> <li>▪ -10, -12, -13, &amp; -14 for attachment listings</li> </ul>		
<p>When a successor-in-interest to a related party succeeded to the records and information sought by the Service, the successor-in-interest must execute the A of A.</p>	<ul style="list-style-type: none"> <li>▪ Treas. Reg. 1.6038A-5(e). Successors in interest.</li> <li>▪ ASAT, Inc. v. Commissioner, 108 TC 147 (1997)</li> </ul>	
<p>Prepare one of the Agency Designation letters, which is a cover letter that requests that the A of A be executed and returned to the Service.</p>		

# Step 3: Prepare an Authorization of Agent request (cont'd)

## Using an Authorization of Agent when a US Corporation is 25% Foreign Owned

### Step 3

Often, a DRC will not provide foreign-based evidence to the Service until an A of A is executed.

Considerations	Resources	6103 Protected Resources
<p>Prepare an A of A form. When the Service desires the foreign parent and other foreign related parties to execute the A of A, insert the name of the foreign parent and of DRC in the applicable places of the authorization form for “parent and other foreign related parties.” Also, list the names of the other foreign related parties (which had transactions with DRC) and describe their relation to DRC on the “attachment listing.”</p> <p>The Service, not DRC, identifies the names of each foreign related party that is requested to authorize DRC as its agent.</p>	<ul style="list-style-type: none"> <li>▪ Treas. Reg. 1.6038A-5(b) Authorization by related party.</li> </ul>	

# Step 3: Prepare an Authorization of Agent request (cont'd)

## Using an Authorization of Agent when a US Corporation is 25% Foreign Owned

### Step 3

Often, a DRC will not provide foreign-based evidence to the Service until an A of A is executed.

Considerations	Resources	6103 Protected Resources
<p>When a consolidated return was filed, either the common parent or the principal operating company of the affiliated group may be authorized to act as agent for the group.</p>	<ul style="list-style-type: none"> <li>▪ Treas. Reg. 1.6038A-1(k)(2) Maintenance of records and authorization of agent.</li> </ul>	
<p>Often, DRC is concerned that the foreign parent may not have legal authority to bind other foreign related parties to an authorization of DRC as their agent. Consider discussing this with DRC before issuing the request. Then, consider preparing one authorization form for the “parent and other foreign related parties” with a completed “attachment listing.” That form can be issued to DRC with a separate blank authorization form for “a foreign related party.” Then, DRC can choose to prepare a separate authorization form for each foreign related party as listed on the “attachment listing.”</p>		

# Step 3: Prepare an Authorization of Agent request (cont'd)

## Using an Authorization of Agent when a US Corporation is 25% Foreign Owned

### Step 3

Often, a DRC will not provide foreign-based evidence to the Service until an A of A is executed.

Considerations	Resources	6103 Protected Resources
 <b>CONSULTATION:</b> Ideally, A of A forms are reviewed by an Information Gathering Technical Specialist or by counsel before issuance. Consider contacting the Information Gathering IPN for help in preparing authorization forms and to facilitate review.		

# Step 3: Prepare an Authorization of Agent request (cont'd)

## Using an Authorization of Agent when a US Corporation is 25% Foreign Owned

### Step 3

Often, a DRC will not provide foreign-based evidence to the Service until an A of A is executed.

Considerations	Resources	6103 Protected Resources
Once the Agency Designation letter and the A of A request(s) are reviewed, the IE is authorized to sign the request.	<ul style="list-style-type: none"><li>IRM 4.60.8.3.5.1 -Delegation of Authority</li><li>LB&amp;I DO 193-2</li></ul>	

# Step 4: Issue the Authorization of Agent request

## Using an Authorization of Agent when a US Corporation is 25% Foreign Owned

### Step 4

Follow prudent procedures for issuing the A of A.

Considerations	Resources	6103 Protected Resources
<p>The A of A request may be mailed or hand delivered to DRC or its representative.</p> <p>The Service is not required to send the A of A request by registered or certified mail. Consider mailing it either of these two ways, with “return receipt requested,” to provide evidence of the dates the A of A request was mailed to and received by DRC.</p>		

# Step 4: Issue the Authorization of Agent request

## Using an Authorization of Agent when a US Corporation is 25% Foreign Owned

### Step 4

Follow prudent procedures for issuing the A of A.

Considerations	Resources	6103 Protected Resources
<p>According to the IDR Enforcement Process, once DRC does not satisfactorily respond to an IDR by its due date, it is delinquent. Within ten days of the IDR due date, the Team Coordinator (“TC”) is required to meet with DRC to understand the reasons for, and to explain the consequences of, the unsatisfactory response. The TC’s explanation includes discussion of a pre-summons letter and a domestic summons.</p> <p>Consider attending the TC’s meeting with DRC to hand deliver the A of A and to discuss how to execute it. Also, explain the noncompliance penalty under IRC § 6038A(e) when a foreign related party does not execute an A of A. (For discussion of applying the noncompliance penalty, see <a href="#">Step 7</a>)</p>		

# Step 5: Review the executed Authorization of Agent

## Using an Authorization of Agent when a US Corporation is 25% Foreign Owned

### Step 5

An A of A must be timely-received and signed by persons with the authority to authorize and accept the agent designation.

Considerations	Resources	6103 Protected Resources
<p>Compare the postmark date on the envelope that contained the executed A of A (or the date the A of A was received by hand delivery) to the date the Service requested the A of A. The regulations require that both the A of A and DRC's acceptance be provided to the Service within 30 days of the Service's request. If not so provided, mail the required notice of failure (<a href="#">Step 6</a>) and consider applying the noncompliance penalty (<a href="#">Step 7</a>).</p>	<ul style="list-style-type: none"> <li>▪ Treas. Reg. 1.6038A-5(b)(1) Authorization by related party.</li> </ul>	
<p>Determine that the A of A was signed by the foreign related party or by an officer of the foreign related party who possesses the authority to authorize an agent. A foreign party signing on behalf of a group of foreign related parties must have the effective legal authority to do so. If not so signed, mail the required notice of failure (<a href="#">Step 6</a>) and consider applying the noncompliance penalty (<a href="#">Step 7</a>).</p>	<ul style="list-style-type: none"> <li>▪ Treas. Reg. 1.6038A-5(b)(1) Authorization by related party.</li> <li>▪ Treas. Reg. 1.6038A-5(c) Foreign affiliated groups.</li> </ul>	

# Step 5: Review the executed Authorization of Agent (cont'd)

## Using an Authorization of Agent when a US Corporation is 25% Foreign Owned

### Step 5

An A of A must be timely-received and signed by persons with the authority to authorize and accept the agent designation.

Considerations	Resources	6103 Protected Resources
<p>Determine that DRC accepted the appointment as agent by providing a statement to that effect signed by an officer of DRC. The bottom of the authorization forms include a section for an agent of DRC:</p> <ul style="list-style-type: none"> <li>▪ to sign indicating that DRC accepts the appointment, and</li> <li>▪ to certify that it has the authority to accept the appointment for DRC.</li> </ul> <p>If not so signed, mail the required notice of failure (<a href="#">Step 6</a>) and consider applying the noncompliance penalty (<a href="#">Step 7</a>).</p>	<ul style="list-style-type: none"> <li>▪ Treas. Reg. 1.6038A-5(b)(1) Authorization by related party.</li> </ul>	

# Step 5: Review the executed Authorization of Agent (cont'd)

## Using an Authorization of Agent when a US Corporation is 25% Foreign Owned

### Step 5

An A of A must be timely-received and signed by persons with the authority to authorize and accept the agent designation.

Considerations	Resources	6103 Protected Resources
 <p><b>CONSULTATION:</b> Generally, the A of A should not be modified by DRC or a foreign related party. Some minor modifications may be acceptable, but the designation must contain the heading and statement set out in Treas. Reg. § 1.6038A-5(b)(1). When modified, consult with the Information Gathering IPN and counsel to determine the legal effect of such authorization.</p>	<ul style="list-style-type: none"> <li>▪ IRM 4.60.8.3.5.8(1) -Failure to Obtain Authorization of Agent</li> <li>▪ Treas. Reg. 1.6038A-5(b)(1) Authorization by related party.</li> </ul>	
<p>If the A of A is executed properly, discuss the previously received incomplete IDR responses with DRC and establish a response due date. Consider issuing new IDRs asking that the requested records be translated into English within thirty days.</p>	<ul style="list-style-type: none"> <li>▪ Treas. Reg. 1.6038A-3(b)(3) Translation of records.</li> </ul>	

# Step 6: Mail notice of failure to provide an Authorization of Agent

## Using an Authorization of Agent when a US Corporation is 25% Foreign Owned

### Step 6

Notice of failure is required by the IRM.

Considerations	Resources	6103 Protected Resources
 <p><b>CONSULTATION:</b> When DRC does not properly execute an A of A, consider sending an informal notice of the failure to DRC. Consider contacting the Information Gathering IPN for assistance regarding the content of an informal notice.</p>		
<p>A formal notice of the failure must be sent to DRC before imposing the noncompliance penalty.</p> <p>The Formal Notice of Failure to Authorize as Agent notifies DRC that the noncompliance penalty will be imposed and included in the notice of deficiency.</p>	<ul style="list-style-type: none"> <li>▪ IRM 4.60.8.3.5.12 - IRC Section 6038A(e) Procedures and Guidelines</li> <li>▪ IRM Exhibit 4.60.8-15 - Formal Notice of Failure to Authorize as Agent</li> </ul>	
 <p><b>CONSULTATION:</b> The Formal Notice of Failure to Authorize as Agent must be approved by ACC(I).</p>	<ul style="list-style-type: none"> <li>▪ IRM 4.60.8.3.5.13(1)b - Application of the Non-Compliance Penalty</li> </ul>	
<p>The formal notice must be sent by certified or registered mail.</p>	<ul style="list-style-type: none"> <li>▪ IRM 4.60.8.3.5.12(1)b - IRC Section 6038A(e) Procedures and Guidelines</li> </ul>	

# Step 7: Consider applying the noncompliance penalty

## Using an Authorization of Agent when a US Corporation is 25% Foreign Owned

### Step 7

The noncompliance penalty amount can be overridden only by clear and convincing evidence that the Service abused its discretion.

Considerations	Resources	6103 Protected Resources
<p><b>Congressional Intent.</b> Congress enacted IRC § 6038A to help the Service enforce IRC § 482 in light of the difficulties the Service had in obtaining information from foreign parents of U.S. corporations. The noncompliance penalty is among the principal enforcement mechanisms of the statute.</p>	<ul style="list-style-type: none"> <li>▪ HR Rep 101-247 (1989)</li> <li>▪ ASAT, Inc. v. Commissioner, 108 T.C. 147 (1997).</li> <li>▪ FSA 200132003</li> </ul>	

# Step 7: Consider applying the noncompliance penalty (cont'd)

## Using an Authorization of Agent when a US Corporation is 25% Foreign Owned

### Step 7

The noncompliance penalty amount can be overridden only by clear and convincing evidence that the Service abused its discretion.

Considerations	Resources	6103 Protected Resources
<p><b>Noncompliance penalty amount.</b> When a foreign related party fails to execute an A of A, the Service has sole discretion to determine the amount of DRC's deductions related to, and the cost of property purchased from (or transferred to) that foreign related party. The adjustment may be based on the information the Service has available or from information the Service chooses to obtain through testimony or otherwise.</p> <p>In exercising its discretion, the Service shall consider the information provided by DRC and related parties unless, in the Service's discretion, such information is insufficient to prove relevant facts.</p> <p>Such discretion is subject only to limited judicial review. There is no reasonable cause exception to the noncompliance penalty.</p>	<ul style="list-style-type: none"> <li>▪ HR Rep 101-386 at 594 (1989).</li> <li>▪ IRC 6038A(e)(3) Applicable rules in case of noncompliance.</li> <li>▪ Treas. Reg. 1.6038A-7(a) Noncompliance.</li> <li>▪ IRM 4.60.8.3.5.7 - IRC Section 6038A(e) Noncompliance Penalty</li> <li>▪ IRM 4.60.8.3.5.13 - Application of the Non-Compliance Penalty</li> </ul>	

# Step 7: Consider applying the noncompliance penalty (cont'd)

## Using an Authorization of Agent when a US Corporation is 25% Foreign Owned

### Step 7

The noncompliance penalty amount can be overridden only by clear and convincing evidence that the Service abused its discretion.

Considerations	Resources	6103 Protected Resources
<p><b>Challenges to the noncompliance penalty.</b></p> <p>That DRC could not obtain an A of A from a foreign related party is not a defense to the noncompliance penalty.</p> <p>The noncompliance penalty amount cannot be overturned in court because the amount (a) simply differs from the actual costs incurred or (b) does not clearly reflect income. It is not a sufficient reason to redetermine the penalty amount just because the information to prove that the penalty amount is clearly erroneous is not within the Service's knowledge or possession.</p>	<ul style="list-style-type: none"> <li>▪ ASAT, Inc. v. Commissioner, 108 T.C. 147 (1997).</li> <li>▪ HR Rep 101-386 at 594 (1989).</li> </ul>	

# Step 7: Consider applying the noncompliance penalty (cont'd)

## Using an Authorization of Agent when a US Corporation is 25% Foreign Owned

### Step 7

The noncompliance penalty amount can be overridden only by clear and convincing evidence that the Service abused its discretion.

Considerations	Resources	6103 Protected Resources
<p>The noncompliance penalty amount can be overridden only by clear and convincing evidence that the Service abused its discretion. That is, that the amount was determined with an improper motive or was clearly erroneous in light of all reasonably credible interpretations or assumptions of facts. However, when DRC asserts an abuse of discretion, all allegations and inferences that support the penalty amount are accepted as true even though the Service could have obtained more reliable evidence.</p> <p>The same standard of proof (i.e., clear and convincing evidence that the Service abused its discretion, while accepting as true all allegations and inferences that may support the Secretary's position) applies to the Service's sole discretion to determine the weight to give a document or an item of information when determining the noncompliance penalty.</p>		

# Step 7: Consider applying the noncompliance penalty (cont'd)

## Using an Authorization of Agent when a US Corporation is 25% Foreign Owned

### Step 7

The noncompliance penalty amount can be overridden only by clear and convincing evidence that the Service abused its discretion.

Considerations	Resources	6103 Protected Resources
<p><b>Challenges to the noncompliance penalty (cont'd)</b></p> <p>In ASAT, Inc. v. Commissioner, the Service applied the noncompliance penalty to determine transfer pricing amounts. The amounts were based on information from (a) the audit of a similar taxpayer,(b) a trade association survey of companies providing similar services in a different industry, and (c) the report of a Service economist who was not called to testify. “The court upheld the Service determination in the face of the taxpayer’s failure to obtain the agency authorization.”</p>	<ul style="list-style-type: none"> <li>ASAT, Inc. v. Commissioner, 108 T.C. 147 (1997).</li> </ul>	

# Examples of the Process

## Using an Authorization of Agent when a US Corporation is 25% Foreign Owned

### Description

**Example 1:** A foreign shareholder owns at least 25% of a U.S. corporation, and such corporation claims it cannot provide documents under the custody and control of a foreign related party regarding any transaction between such U.S. corporation and a foreign related party. Also, when any such transaction engaged in by a partnership is attributed to such U.S. corporation under Treas. Reg. §1.6038A-1(e)(2), attribution of transactions with related parties engaged in by a partnership.

**Example 2:** A U.S. subsidiary of a foreign parent claims the U.S. subsidiary cannot provide documents (e.g., key information relating to a function and risk analysis, and potential comparables) under the custody and control of a foreign affiliate regarding a transfer pricing transaction.

**Example 3:** A revenue agent is investigating the deductibility of payments, from a U.S. subsidiary to its foreign parent, and seeks foreign-based finance documents to properly characterize a prior investment or guarantee from the foreign parent to the U.S. subsidiary that was made as part of the subsidiary's purchase of a business.

# Training and Additional Resources

Using an Authorization of Agent when a US Corporation is 25% Foreign Owned		
Type of Resource	Description(s) and/or Instructions for Accessing	References
Online treatise	<ul style="list-style-type: none"> <li>▪ IRC § 6038A discussions of authorizations of agent and record keeping requirements for 25% foreign-owned corporations in Bittker &amp; Lokken: <u>Federal Taxation of Income, Estates and Gifts</u>. Part 9 Foreign Income and Foreign Taxpayers:               <ul style="list-style-type: none"> <li>- Chapter 65 Introduction and Classification of Individuals and Entities:                   <ul style="list-style-type: none"> <li>▪ Para. 65.5.3 Foreign-Owned Domestic Corporations and Businesses</li> </ul> </li> </ul> </li> </ul>	<ul style="list-style-type: none"> <li>▪ Bittker &amp; Lokken Fed. Tax'n Inc, Est and Gift Para 65.5.3</li> </ul>
Online treatise	<ul style="list-style-type: none"> <li>▪ Discussions of authorization of agent in BNA's Tax Management Foreign Income Portfolio No. 891-2<sup>nd</sup>, § IV - Sections 6038A and 6038C.</li> </ul>	<ul style="list-style-type: none"> <li>▪ BNA Tax Management Foreign Income Portfolio 891-2<sup>nd</sup> Sec. 2-IV</li> </ul>
Online treatise	<ul style="list-style-type: none"> <li>▪ Discussions of special aspects of foreign records including authorization of agent and formal document requests in BNA's Tax Management U.S. Income Portfolio No. 633-1<sup>st</sup>, § VI – Special Aspects of Foreign Records.</li> </ul>	<ul style="list-style-type: none"> <li>▪ BNA Tax Management U.S. Income Portfolio No. 633-1<sup>st</sup> Sec. VI</li> </ul>

# Glossary of Terms and Acronyms

Term/Acronym	Definition
A of A	Authorization of Agent
ACC(I)	Associate Chief Counsel (International)
DRC	Domestic reporting corporation
FRC	Foreign reporting corporation
FSA	Field Service Advice
IDR	Information document request
IPN	International Practice Network
IRC	Internal Revenue Code
IRM	Internal Revenue Manual
LB&I	Large Business & International
TC	Team Coordinator
TIEA	Tax Information Exchange Agreement

# Index of Related Issues

Issue	Associated UIL(s)	References
Issuing a Formal Document Request When a US Taxpayer is Unresponsive to an IDR	<ul style="list-style-type: none"> <li>▪ 9460.02</li> </ul>	<ul style="list-style-type: none"> <li>▪ IGA/9460.02_02 (2013)</li> </ul>
Issuing a summons under IRC 6038A when a US corporation is 25% foreign owned	<ul style="list-style-type: none"> <li>▪ 9560.06</li> </ul>	<ul style="list-style-type: none"> <li>▪ In process as of March 2015</li> </ul>
Using Alternative Means to Obtain Foreign Based Evidence	<ul style="list-style-type: none"> <li>▪ 9460.02</li> </ul>	<ul style="list-style-type: none"> <li>▪ IGI/9460.02_01(2013)</li> </ul>
Monetary penalties for failure to timely file a substantially complete Form 5471 -- Cat 4 & 5 filers	<ul style="list-style-type: none"> <li>▪ 9560.01</li> </ul>	<ul style="list-style-type: none"> <li>▪ IGA/9560.01_03(2014)</li> </ul>
Considering penalties when a Form 5472 did not report transactions between a US corporation and related parties	<ul style="list-style-type: none"> <li>▪ 9560.05</li> </ul>	<ul style="list-style-type: none"> <li>▪ In process as of March 2015</li> </ul>