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CORPORATE TRANSPARENCY ACT NOW IN EFFECT— AN IMPORTANT
NEW COMPLIANCE OBLIGATION THAT AFFECTS MANY PRIVATE
COMPANIES

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INTRODUCTION

On January 1, 2024, the Corporate Transparency Act (CTA) became effective across the United States, thereby creating new reporting requirements for most companies and other entities created or registered after that date as well as for an estimated 32 million¹ preexisting companies and other entities. Enacted into US federal law back in January 2021 as part of the Anti-Money Laundering Act (AMLA), the CTA requires most privately held companies that are deemed “reporting companies” to file a beneficial ownership information report (BOIR) with the Financial Crimes Enforcement Network (FinCEN), in which they disclose information about the company, its “beneficial owners,” and the “company applicant(s).” BOIRs are filed online, and most companies will have no trouble doing their filings without need of professional assistance. Failure to comply with the CTA’s requirements can result in steep civil and/or criminal penalties. A link to the BOIR filing website is provided at the end of this article.

RATIONALE FOR THE CTA

The US has long lagged behind other developed countries when it comes to combating financial secrecy and preventing the flow of illegal money. The Tax Justice Network, an independent institution that releases an annual “Financial Secrecy Index”, ranking those jurisdictions which they consider most complicit in helping individuals hide their finances from the rule of law, has recently ranked the US as the country contributing the most to financial secrecy.² Congress passed the CTA to curb the use of shell companies to facilitate illegal activities, such as money laundering, financing terrorism, human and drug trafficking, and securities fraud.³

SCOPE - WHOM DOES IT APPLY TO?

The CTA will apply to all entities that meet the definition of a “reporting company” and do not qualify for an exemption. The wide array of companies that will be concerned are largely small and unregulated entities.

Reporting companies are divided into two categories: domestic reporting companies, and foreign reporting companies. The former encompasses corporations, limited liability companies (LLCs), or any company created by the filing of a document with the secretary of state or similar office. Foreign reporting companies are defined as companies created under the laws of a foreign country, which have registered to do business in any US state (or Tribal jurisdiction) by filing a document with the secretary of state or similar office.

Although this definition seemingly includes virtually all companies operating in the US, in fact many companies will qualify for an exemption. The CTA lists a total of twenty-three entity types which shall be exempt from its reporting requirements, despite meeting the definition of a reporting company. The eligibility rules for some of the exemptions are clear and simple, whereas for others, they are quite complex. Most of the exemptions are for companies that are already regulated, thus making the CTA’s reporting requirements redundant. Thus, for example, there are exemptions for certain pooled investment vehicles, public companies, banks, insurance companies, and wholly owned subsidiaries of certain exempt entities.

¹ FinCEN, *Beneficial Ownership Information Reporting Requirements*, 87 FR 59498 (Sept. 30, 2022), available at <https://www.federalregister.gov/documents/2022/09/30/2022-21020/beneficial-ownership-information-reportingrequirements>.

² <https://taxjustice.net/country-profiles/united-states/>

³ National Defense Authorization Act, § 6402 (3).

There also is an exemption for large operating companies.⁴ Although these are not necessarily regulated, large operating companies apparently are thought to be less susceptible to being used for money laundering or other illicit purposes.

WHEN DO COMPANIES HAVE TO MAKE THEIR INITIAL REPORT?

The date by which a reporting company must submit its original BOIR depends on the date on which it was created, or, in the case of a foreign reporting company, the date on which it first registered to do business in the US.⁵

- ❖ Reporting Companies created or registered to do business in the US in the year 2024 are required to file their initial BOIR within 90 days of formation or registration to do business.
- ❖ In the case of domestic reporting companies and foreign reporting companies that were either created or registered to do business in the US prior to January 1, 2024, the CTA provides for a temporary reprieve, as these entities have until December 31, 2024, to file their initial BOIR.
- ❖ Finally, any reporting company created or registered to do business on or after January 1, 2025, will have a shorter window to file, namely within 30 days of formation or registration.

WHAT INFORMATION IS THE COMPANY REQUIRED TO REPORT?

To satisfy the requirements of the CTA, the reporting company must file a BOIR, which includes:

- (i) the name, trade name (if any), current US address,⁶ state or foreign jurisdiction of formation, state or Tribal jurisdiction of first registration (for foreign companies only), and employer identification number (EIN),⁷ and
- (ii) for each “beneficial owner” and each “company applicant,”⁸ his or her full legal name, date of birth, current address (does not need to be in the US), an image of a non-expired

⁴ Generally defined by the CTA as an entity (i) with an operating presence at a physical location in the US, that the entity owns or leases and that is physically distinct from the place of business of any other unaffiliated entity, (ii) with more than 20 full-time employees employed in the United States, and (iii) that has reported more than \$5,000,000 in gross receipts or net sales from sources within the United States..

⁵ Most foreign businesses operating in the US do so through a separate US entity, so foreign reporting companies will be relatively small in number.

⁶ A company that has its principal place of business in the US should report that address. If its principal place of business is not in the US, the company should report the primary address from which it conducts its business in the US. When a company does not have any address from which it conducts business in the US (as is the case for a pure holding company), it may report the address of its registered agent in the US.

⁷ Foreign reporting companies that are not subject to US corporate income tax may report a foreign tax identification number and the name of the jurisdiction in which it was obtained in lieu of an EIN.

⁸ Only those domestic reporting companies that are created on or after January 1, 2024, and those foreign reporting companies that were registered to do business in the US after January 1, 2024, will be required to report “company applicant” information.

identification document,⁹ and the unique identifying number and issuing jurisdiction of such document.

The terms “beneficial owner” and “company applicant” are explained below.

WHO QUALIFIES AS A “BENEFICIAL OWNER”?

The CTA defines a “beneficial owner” as each individual who either (i) exercises substantial control over the reporting company (and thus need not be a beneficial owner in the normal sense of the phrase) OR (ii) owns or controls, directly or indirectly, at least 25 percent of the ownership interests of the reporting company. Importantly, the CTA puts no upper limit on the number of beneficial owners each reporting company may be required to report. There is no limit to the number of people “exercising substantial control” over the reporting company. In addition, the ownership of options to purchase more than 25% of the reporting company qualifies as “owning or controlling” 25% of the ownership interests of the reporting company, and thus there may be more than four people owning or controlling more than 25% of the reporting company under the CTA.

FinCEN has explained that an individual exercises substantial control when that individual (i) is a senior officer of the reporting company, (ii) has authority to appoint or remove any senior officer or a majority of the board of directors, (iii) directs, determines, or substantially influences important decisions regarding the reporting company, or (iv) has “any other form of substantial control over the reporting company.”

As to what exactly constitutes an “important decision,” FinCEN has provided a (non-exhaustive) list of decisions that constitute important decisions,¹⁰ which includes (among other examples) decisions relating to the selection or termination of business lines or ventures, the entry into, or termination (or fulfillment or non-fulfillment) of, significant contracts, and compensation schemes and incentive programs for senior officers. In the context of a typical corporation, this would include decisions taken by the president/CEO and the CFO, and it could encompass others as well.

In many cases, directors may also be considered as exercising substantial control over the reporting company. This is clear when a company has only one director, as that director, among other things, has the authority to appoint/remove senior officers and to make important decisions regarding the reporting company. However, when there are several directors, whether a particular director exercises substantial control must be analyzed on a director-by-director basis. In such cases, especially when boards only have a few members, the safest option may be to report all directors as beneficial owners.

Although FinCEN has, as described above, provided some level of guidance into when someone may qualify as a beneficial owner through substantial control, the catch-all category (i.e., any other form of substantial control over the reporting company) leaves a lot of room for interpretation. Depending on the circumstances, an individualized analysis might be required to determine whether someone is a beneficial owner by virtue of the catch-all category.

⁹ The identification document can only be (i) a US passport, (ii) a state driver’s license, (iii) an identification document issued by a state, local government, or tribe, or (iv) only if the individual does not have any of the previous documents, a foreign passport.

¹⁰ See BOI Small Entity Compliance Guide, Section 2.1

WHO QUALIFIES AS A “COMPANY APPLICANT”?

Each reporting company that is required to provide company applicant information (i.e., those created or registered to do business in the US post January 1, 2024) will have at least one company applicant and at most two. Despite the terminology, only individuals (human beings) can be considered company applicants. The CTA distinguishes between two types of company applicants – the “direct filer” and the individual “directing or controlling the filing.”

The direct filer is the individual who actually physically or electronically filed the document which either created the domestic reporting company, or first registered the foreign reporting company to do business in the US. Each reporting company that is required to report company applicant information will have a direct filer.

In some cases, there may have been more than one individual involved in the filing of the document. In these cases, in addition to the direct filer, the reporting company will also have to report the individual who is primarily responsible for “directing or controlling the filing,” although this individual did not directly file the creation or registration document.

If only one individual is involved in the creation or registration, the reporting company will only have to report that individual as the company applicant. However, if two or more individuals are involved in the filing of the document, the reporting company will have to identify both the direct filer and the individual primarily responsible for directing or controlling the filing. For example, if the creation or registration document is prepared by a lawyer, who then directs a corporate services provider (e.g., CSC, Cogency) to file the document, both the lawyer (as the individual primarily responsible for controlling or directing the filing), and the specific employee of the corporate services provider who filed the document (as the direct filer) will have to be reported as company applicants.

WHAT IS A FINCEN IDENTIFIER (FINCEN ID) AND WHEN MIGHT IT BE USEFUL?

Instead of reporting all of the required information for every beneficial owner and company applicant, the reporting company may simply report the respective individuals’ FinCEN ID (identification number) if these individuals have one. A FinCEN ID can be obtained through an online application in which the applicant provides the same information that would be required for a beneficial owner or company applicant under the normal process. Although FinCEN IDs are optional, having one should greatly simplify the reporting process for those individuals who expect to report their BOI for several different companies.

Individuals may apply for a FinCEN ID through the following link: <https://fincenid.fincen.gov/landing>.

CHANGES OR INACCURACIES IN REPORTED INFORMATION

When there is any change to the previously reported information regarding the beneficial owner or the reporting company itself,¹¹ the reporting company must file an updated BOIR within 30 days of the occurrence of such changes. For example, an updated BOIR will have to be filed if the reporting company changes its US address, registers an assumed name, changes its senior officers, or if a beneficial owner undergoes a change in address. On a similar note, a reporting Company must file a corrected BOIR within 30 days of it becoming aware of any inaccuracy (or having reason to know of the inaccuracy) in the

¹¹ There is no need to file an updated BOIR when the information relating to the company applicant changes.

information reported to FinCEN. A reporting company will not face a penalty for the inaccurate report as long as the report is corrected within 90 days of it being filed.

Individuals who have a FinCEN ID will be subject to the same 30-day timeline if any of the information changes, or if they become aware of an inaccuracy. In these cases, having a FinCEN ID can save a lot of time and effort, as an individual who changes his address, for example, will only have to update the information associated with his or her FinCEN ID. Had this individual not had a FinCEN ID, each reporting company that had listed this individual as a Beneficial Owner would have been obligated to file an update BOIR separately, with the individual having to provide that information to all of the reporting companies – all of this within the 30-day timeline.

WHO WILL HAVE ACCESS TO THE INFORMATION PROVIDED IN THE BOIR?

Information provided by reporting companies to FinCEN will be stored in what FinCEN describes as a secure, non-public database. FinCEN has made clear that the information security methods used to store the information will be of the highest level typically used in the Federal government to protect non-classified yet sensitive information. The goal of the CTA is not to make beneficial ownership information available to the general public, as may be the case in other countries, but rather to provide access to the information for the relevant governmental authorities (and certain financial institutions with the permission of the reporting company), as explained below.

FinCEN's published "Access Rule" lists the categories of recipients that will be allowed to have "Beneficial Owner Information" (BOI) disclosed to them. The authorized recipients are (1) US federal agencies engaged in national security, intelligence, or law enforcement activity, (2) US state, local, and Tribal law enforcement agencies, (3) foreign law enforcement agencies, judges, prosecutors, central authorities, and competent authorities, (4) financial institutions subject to customer due diligence (CDD) rules, but only with the consent of the reporting company, (5) "federal functional regulator"¹² and other appropriate regulatory agencies for purposes of supervising financial institutions' compliance with CDD requirements, and (6) the US Department of Treasury. Each category of recipient will only be provided with access to the BOI database upon request, and only under specific circumstances, which are outlined in detail in the Access Rule.¹³ These authorized recipients will generally not be permitted to re-disclose the BOI, minus a few exceptions (e.g., intermediary federal agency to authorized foreign requesters), and will face steep civil and criminal penalties if they do.¹⁴

¹² Defined by the CTA as: (i) the Board of Governors of the Federal Reserve System, (ii) the Office of the Comptroller of the Currency, (iii) the Board of Directors of the Federal Deposit Insurance Corporation, (iv) the Office of Thrift Supervision, (v) the National Credit Union Administration; (vi) the Securities and Exchange Commission, and (vii) the Commodity Futures Trading Commission.

¹³ <https://www.govinfo.gov/content/pkg/FR-2023-12-22/pdf/2023-27973.pdf>

¹⁴ Civil penalties of up to \$500/day for each day the violation continues or has not been remedied, and criminal penalties of up to \$250,000 and 5-year imprisonment. These criminal penalty amounts are doubled if the violation is committed while violating another law of the US or as part of a pattern of any illegal activity involving more than \$100,000 in a 12-month period.

PENALTIES FOR FAILURE TO FILE BOIR AND OTHER CTA VIOLATIONS

Both corporate entities and individuals can be held liable for willful violations of the CTA. Any person that willfully fails to comply with the CTA may be subject to civil penalties of up to \$500 for each day that the violation continues. This includes the reporting company itself, but also any person who is a senior officer at the reporting company at the time of willful failure, or beneficial owners and company applicants who willfully cause the reporting company's failure to submit a correct or updated BOIR. A person responsible for a willful violation may also be subject to criminal penalties which include up to two years in prison and/or a \$10,000 maximum fine.

As reporting companies are responsible for ensuring that they submit complete and accurate BOI to FinCEN, they may be held liable in those cases where a beneficial owner has refused to provide them with the required information or has provided them with inaccurate information. For example, in a situation where one of the beneficial owners is being uncooperative with the reporting company, and is refusing to provide the required information, the company, its senior officers, and the beneficial owner may all be held liable.¹⁵

To prevent these situations, FinCEN encourages reporting companies to make sure they have mechanisms in their corporate documents that will allow them to obtain all required information from beneficial owners, and that the latter inform them immediately of any changes to such information.

SPECIFIC ISSUES FOR FOREIGN-OWNED COMPANIES

While it is evident that CTA compliance will be something of an administrative burden for US companies, the situation has already proven to be particularly troublesome for foreign-owned US companies and foreign companies registered to do business in the US.

As they may be part of a larger international group, foreign-owned US companies will have to pay particular attention to changes within the group that would require the US entity to file an updated BOIR within 30 days. For example, it is common practice for some foreign-owned companies to rotate certain individuals through director, officer, or managerial positions within the US subsidiary. As explained in this article, any such changes which either add or remove a beneficial owner, will require the filing of an updated BOIR. Similarly, changes in management, or in the identity of those who own a stake in a foreign parent of a US subsidiary may trigger an obligation to file an updated BOIR for the US subsidiary.

Another issue that must be considered by foreign-owned companies is making sure that they are able to access BOI at every level of the corporate group, at any time it is required. As changes to the foreign parent may trigger an update requirement for the US subsidiary, the US subsidiary should try to ensure that it will be able to obtain this information from the shareholders of the foreign parent.

Finally, while companies owned in part by US investment funds will be able to report the identity of the funds (instead of having to "look through" to the ultimate owners of the funds), no such exception will apply to companies owned in part by foreign investment funds. In effect, companies which are owned in whole or in part by foreign investments funds will have to ensure they provide the identity of any ultimate owners who indirectly own at least 25% of the company via the foreign investment fund.

¹⁵ This provision seems unfair, and there has been much commentary about this. Presumably in such a case, the person who is only reflectively liable cannot be considered to be willful. Potentially affected persons might want to give thoughts to requesting or requiring indemnification from the beneficial owners.

For example:

US operating company (Opco) is owned 10% by Jean, a French citizen living in France who is also president of Opco. Bill, a US citizen living in the US and running the day-to-day operations of Opco, is Opco's executive VP but owns no stock in Opco. French PE fund (Fund 1) owns 64% of Opco. Its largest individual shareholder, Martin, owns 40% of the PE fund. Its next largest shareholder, David, owns 26% of Fund 1. Another French PE fund (Fund 2) owns 25.5% of Opco. Pierre-Yves owns 99% of Fund 2.

In the above scenario, the following reporting obligations would apply:

- ❖ Jean would have to be reported as a beneficial owner as he is a senior officer (President) of Opco;
- ❖ Bill would have to be reported as a beneficial owner as he is a senior officer (executive VP) of Opco;
- ❖ Martin would have to be reported as a beneficial owner as he indirectly owns 25.6% of Opco (64%*40%);
- ❖ David would not have to be reported as a beneficial owner as he indirectly owns just 16.6% (64%*26%) and does not exercise substantial control over Opco;
- ❖ Pierre-Yves would have to be reported as a beneficial owner as he indirectly owns 25.2% of Opco (99%*25.5%).

HOW DOES A REPORTING COMPANY FILE ITS BOIR?

Reporting companies can file their BOIR online through FinCEN's website at the following link: <https://boiefiling.fincen.gov/fileboir>.

PENDING LEGAL CHALLENGES

In the previous year, there have been numerous legal challenges brought against the CTA, with various plaintiffs seeking to have courts declare the CTA unconstitutional. Many are still pending today. Most notably, on March 1, 2024, a federal district court in Alabama declared the CTA unconstitutional and permanently enjoined the Department of Treasury and FinCEN from enforcing the CTA against the plaintiffs in that case.¹⁶ However, FinCEN has taken the position that, pending resolution of the case, it would continue enforcing the CTA against all entities and persons other than the named plaintiffs in the Alabama case.¹⁷ The case is currently on appeal. It seems unlikely that an ultimate decision regarding the constitutionality of the CTA will be rendered before January 1, 2025. As a result, all entities affected by the CTA are advised to comply on schedule.

¹⁶ *National Small Business United d/b/a National Small Business Association, et al. v. Yellen*, Case No. 5:22-cv-01448 (N.D. Ala.)

¹⁷ <https://www.fincen.gov/news/news-releases/updated-notice-regarding-national-small-business-united-v-yellen-no-522-cv-01448>

USEFUL LINKS

<https://www.fincen.gov/boi/small-entity-compliance-guide>

https://www.fincen.gov/boi-faqs#K_2

For more information, please contact Robert MacDonald, Della Hill, or other Dunning Rievman & MacDonald attorneys.

CONTACTS

Robert MacDonald

Partner

rcm@drmlaw.com

Tel.: +1 646-513-3287

Della Hill

Partner

dhill@drmlaw.com

Tel.: +1 646-513-3256

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