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Insights

UPDATED - Corporate Transparency Act: New Obligations to Disclose Beneficial Ownership of Private Companies

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UPDATED - On January 1, 2021, Congress enacted the Corporate Transparency Act (the "CTA" or the "Act") as part of the greater National Defense Authorization Act for Fiscal Year 2021. Since then, some actions have been taken towards implementation of the CTA, though not as rapidly as two senators would like.

On December 8, 2021, the U.S. Department of Treasury's Financial Crimes Enforcement Network ("FinCEN") issued a Notice of Proposed Rulemaking ("NPRM") to implement the Act's beneficial ownership information reporting provisions. This alert updates **our initial alert on the CTA** first published on January 12, 2021, to reflect these matters and to add guidance on the Act's previously undefined terms "other similar entities" and "substantial control."

The CTA requires certain domestic and foreign companies to disclose beneficial ownership information to FinCEN and establishes information sharing obligations on private businesses (and others) designed to help fight the misuse of corporate structures that facilitate various criminal enterprises, such as money laundering, terrorism, tax fraud, human and drug trafficking and other financial-related criminal acts that are harmful to the national security interests. The CTA will become effective after the Secretary of the Treasury issues regulations implementing the CTA's requirements; however, a timetable for accomplishing these steps has not been published.

On May 10, 2022, Senators Marco Rubio (R-FL) and Elizabeth Warren (D-MA) sent a letter to U.S. Treasury Secretary Janet Yellen and Acting Director of FinCEN Himamauli Das criticizing the delayed implementation of the CTA. The Senators wrote: "The Treasury Department has yet to finalize the implementation of the CTA—or even set a timetable for its completion." While final action will likely not occur until 2023, the regulations when finally in effect will impact millions of entities doing business in the United States that had not previously been subject to information sharing obligations contemplated by the CTA.

Who Must Comply

The obligations under the CTA apply to "reporting companies." Even though this phrase has a meaning tied to public companies with reporting obligations under the securities laws, its meaning under the CTA differs and includes corporations, limited liability companies and other similar entities that are created by filing a document with a secretary of state or similar office under state or Tribal law or that are formed under the laws of a foreign country and registered to do business in the United States. The Act does not define "similar entities." However,

the NPRM interprets “other similar entities” in the Act to mean any entity that is created (in the case of a domestic reporting company) or registered to do business in the United Stated (in the case of a foreign reporting company) through a filing with a secretary of state in a U.S. jurisdiction.

The CTA excludes the following categories of companies from the definition of “reporting company,” thus making these companies exempt from the reporting requirements of the CTA:

(a) publicly traded companies;
(b) companies closely regulated by the federal government (e.g. banks, credit unions, bank holding companies, registered money transmitting businesses, insurance companies, and others);
(c) U.S.-based companies with more than 20 full-time, U.S.-based employees which reported at least $5 million in gross receipts or sales to the IRS in the previous year and which have an operating presence at a physical office in the United States;
(d) companies owned or controlled by exempt companies; and (e) dormant companies that meet certain conditions under the Act.

Reporting companies are required to submit information on “beneficial owners.” The definition of “beneficial owner” provided by the Act excludes certain individuals, such as individuals acting solely as employees, and those who receive interest in the reporting company through a right of inheritance. Beneficial owners include individuals who:

(a) own or control not less than 25% of the ownership interests of the reporting company, or
(b) exercise “substantial control” over the reporting company.

As defined by the NPRM, “substantial control” includes:

(1) service as a senior officer of the reporting company;
(2) authority over the appointment or removal of any senior officer or a majority or dominant minority of the board of directors (or similar body);
(3) direction, determination or decision of, or substantial influence over, important matters affecting the reporting company; or
(4) any other form of substantial control over the reporting company.

Additionally, individuals are also required to submit information pursuant to the CTA who:

(a) file an application to form a reporting company under the laws of a state or an Indian Tribe, or
(b) register or file an application to register a foreign reporting company to do business in the United States.

Information to be Reported and Who Will Have Access

The CTA requires reporting companies to provide as to each beneficial owner and company applicant the full legal name; the date of birth; the current address; and a unique identifying number (e.g., driver’s license number or passport number) or a unique identifier supplied by FinCEN. “Company applicant” refers to the person who filed the entity’s formation documents.

While beneficial ownership information will be confidential and may not be disclosed to the public, the information will be accessible for inspection or disclosure to the Department of Treasury. Further, beneficial ownership information reported to FinCEN may also be disclosed upon request to:

(a) federal agencies and law enforcement for national security intelligence purposes or other purposes consistent with the CTA;

(b) state, local and tribal law enforcement with a court order for purposes in connection with a criminal or civil investigation;
(c) financial institutions, with the consent of the reporting company, pursuant to customer due diligence requirements; and
(d) federal agencies on behalf of foreign law enforcement pursuant to an international treaty, agreement or convention.

Timeline for Compliance

Once the CTA becomes effective, reporting companies formed or registered after the effective date must submit the beneficial ownership information within 14 days of the date of formation or registration. Reporting companies formed prior to the effective date of the CTA will have one year after the effective date of the implementing regulations to provide beneficial ownership information to FinCEN. Additionally, reporting companies will be subject to ongoing reporting obligations to update any change in beneficial ownership information within 30 days after the date the change occurred. In the event of inaccurate information, reporting companies have 14 days to correct a report after they discover or have reason to know the information was incorrect.

Penalties for Non-Compliance

The CTA establishes criminal and civil penalties for willful failure to report complete or updated beneficial ownership information, for willfully providing false or fraudulent information to FinCEN or for knowingly disclosing or using information obtained through the report submitted to FinCEN or disclosed by FinCEN. Any person (and not just the reporting company) violating reporting requirements under the Act may be subject to civil penalties of up to $500 per day for each violation. Criminal violations may result in a fine of up to $10,000 and imprisonment for up to two years, or both. Safe harbors from these penalties are provided to allow for correction of inaccurate information.

Observations

While little argument can be made against the intended benefit of the CTA relating to combating criminal behavior, the CTA presents an expansion of the scope of private information that will be filed with a government agency. Based on the list of excluded companies, the reporting obligations and risks will impact small, privately-held businesses most directly and expose those having responsibility and involvement in the reporting process to criminal risk for failure to report or update accurately the required information about beneficial ownership of the reporting companies. Guidance will no doubt come from the regulations to be issued by the Department of the Treasury, but companies will almost certainly need to consider processes for gathering and updating accurate information from its owners. This could include changes to governing documents, shareholder agreements, operating agreements and similar documentation among the owners. We will continue to monitor the developments with the CTA and provide further updates as appropriate.

If you have any questions regarding the CTA or obligations to comply with the reporting requirements, please contact **Robert A. Greising**, **Virginia A. Talley**, **Maria M. Vladimirova,** or any member of our **Business, Acquisitions, & Securities Practice**.

The authors acknowledge and appreciate the contributions of Caleb Perez to this Update.

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