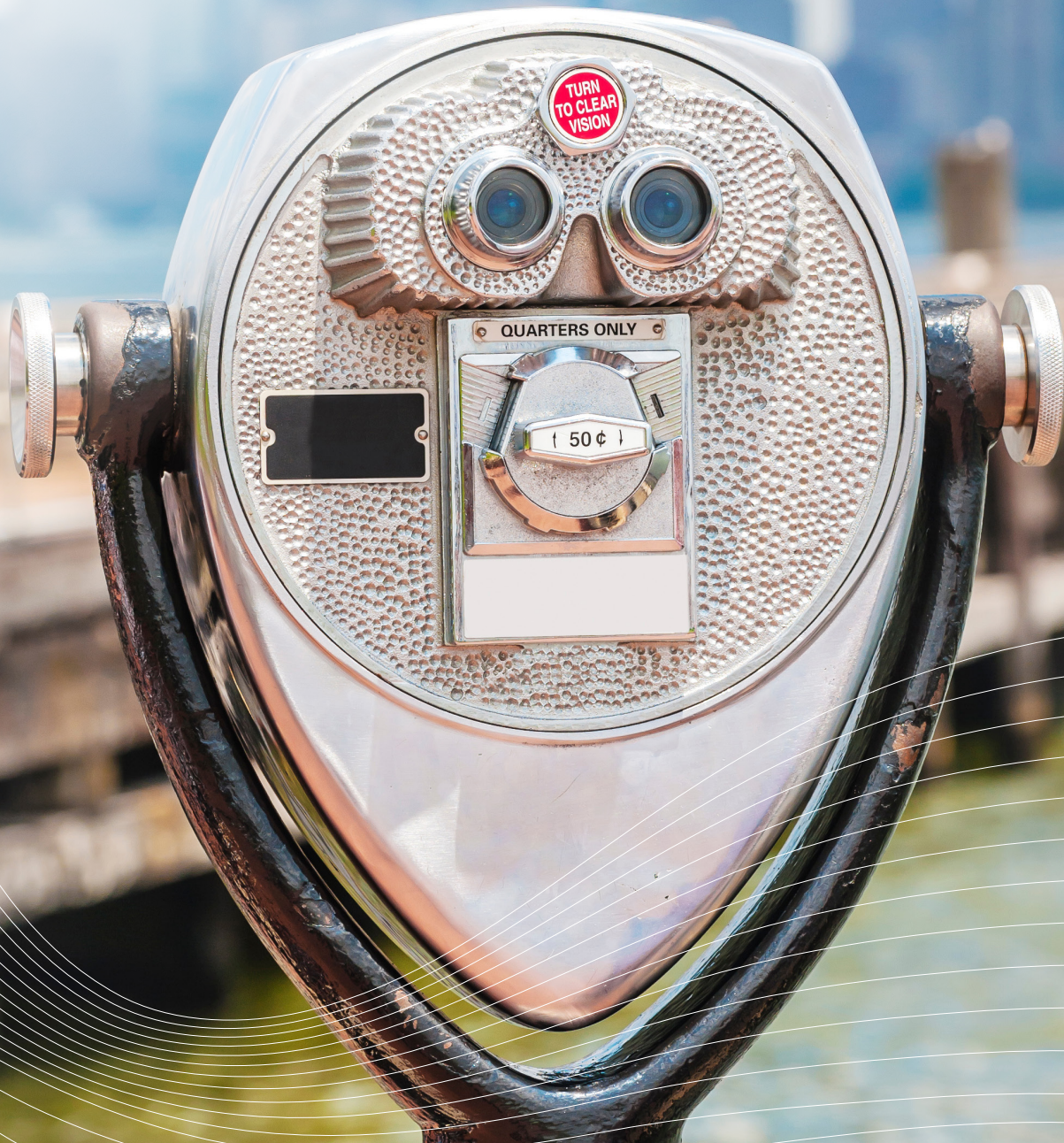


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A Guide to the Corporate Transparency Act

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The Corporate Transparency Act (the “Act”) will take effect January 1, 2024, and imposes requirements on most entities, with some exceptions, to report to the Financial Crimes Enforcement Network (“FinCEN”) information on natural persons who beneficially own and form these entities through the filing of a Beneficial Ownership Information Report (“BOI Report”).

The Act will have a disproportionate impact on small businesses; in particular, it imposes a federal reporting requirement on businesses that are otherwise subject to little or no regulatory oversight.

BACKGROUND

The Act was passed as part of the Anti-Money Laundering Act of 2020, as an amendment to the Bank Secrecy Act of 1970. Congress notes that a lack of state law requiring companies to identify beneficial owners has enabled bad actors to conceal illicit activities through the use of shell companies to own businesses (it should be noted most entities in the U.S., such as corporations, limited liability companies, etc., are created pursuant to state law through a filing with each state’s secretary of state). Congress notes that, for example, all twenty-eight (28) European Union countries require corporate registries that include beneficial ownership information.

The Act directs FinCEN to propose rules specifying information to be collected from “Reporting Companies” to identify “Beneficial Owners” (the individuals who own and control a Reporting Company) and “Company Applicants” (the individuals who form a Reporting Company). The Act also tasks FinCEN with establishing and maintaining a national registry of Reporting Companies, their Beneficial Owners and Company Applicants, and authorizes FinCEN to share this information with U.S. and foreign government authorities and certain financial institutions for enforcement purposes.

Pursuant to the Act, FinCEN proposed initial rules in December 2021, and issued a final rule on Beneficial Information Reporting Requirements on September 29, 2022, which takes effect January 1, 2024 (such final rule, including subsequent amendments, the “Reporting Rule”). FinCEN has also proposed rules on Beneficial Ownership Information Access and Safeguards, which aims to provide access to information collected under the Reporting Rule to authorized recipients while maintaining the highest levels of data protection and oversight over such information. A third rule will also be proposed by FinCEN in the future which will govern the

collection of information by financial institutions. References to the Act throughout will include references to rules promulgated under the Act, particularly the Reporting Rule.

The Act comes into effect January 1, 2024, and provides for separate reporting requirements for entities created or registered prior to that date (“Existing Reporting Companies”), and on or after that date (“New Reporting Companies”). The current FinCEN rule provides that Existing Reporting Companies do not need to report until January 1, 2025, and additionally do not need to report information on its Company Applicants. New Reporting Companies created or registered before January 1, 2025 (i.e. entities created or registered during 2024) will be required to report within ninety (90) days of creation or registration, while New Reporting Companies created or registered on or after January 1, 2025 will be required to report within thirty (30) days of creation or registration.

REPORTING COMPANIES

Who Must Report?

The Act requires that each Reporting Company provide information on its Beneficial Owners and Company Applicants in its BOI Report. “Reporting Companies” include any corporation, limited liability company, *or other similar entity created by filing a document with the secretary of state* or similar office in any state or territory, or with a federally recognized Indian Tribe, *or formed under the laws of a foreign country and registered to do business in the U.S* (it should be noted that U.S. states require any entity created in a foreign jurisdiction, whether that be another state or a foreign country, to register to do business in-state).

The definition above explicitly includes corporations and limited liability companies, but the “or other similar entity...” language also captures limited partnerships and statutory/business trusts, which require a filing with the state, but do not include sole proprietorships, general partnerships, and certain types of trusts since these are not created through a filing with a secretary of state.

Note that there is no minimum threshold (such as based on size of operations, revenue, or number of owners) for reporting; this means that, for example, even a subsidiary created for a merger, which is not otherwise exempt, would have to report.

Who is Exempt?

Congress notes that the focus of the Act is on shell companies and other entities with limited or no operations; the Act therefore provides twenty-three (23) categories of exemptions

for companies that have business operations and companies that are already subject to oversight.

One of the most significant exemptions is for Large Operating Companies, defined as entities that satisfy each of the following requirements:

1. employ more than twenty (20) employees;
2. filed a tax return in the previous year demonstrating more than five million (\$5,000,000) in gross receipts or sales; *and*
3. has an operating presence at a physical location in the U.S.

Other exemptions include certain publicly traded companies, companies in regulated industries, investment vehicles operated by investment advisors, tax-exempt entities, and governmental entities, each of which is already subject to reporting obligations. Entities that are subsidiaries of exempt companies are also exempt from reporting under the Act. A full list of exemptions can be found [here](#).

What is the Timing of Initial Reports for Reporting Companies

Each **New Reporting Company created or registered before January 1, 2025** (i.e. entities created or registered during 2024) is required to file its BOI Report within ninety (90) days after receiving notice of an effective formation or registration (for foreign entities). Each **New Reporting Company created or registered on or after January 1, 2025** is required to file its BOI Report within thirty (30) days after receiving notice of an effective formation or registration (for foreign entities).

Each **Existing Reporting Company** has until January 1, 2025 to file its BOI Report.

The BOI Report for all **New Reporting Companies** must include disclosure of the required information for: 1) the Reporting Company; 2) the Beneficial Owners; and 3) the Company Applicants. The BOI Report for Existing Reporting Companies must only include disclosure of the required information for: 1) the Reporting Company; and 2) the Beneficial Owners (Existing Reporting Companies do not need to disclose Company Applicants).

All Reporting Companies are required to update information on its Beneficial Owners within thirty (30) days of any change in Reporting Company information or Beneficial Owner information (e.g., pursuant to a merger, investment, or other change in control resulting in a change in ownership) or if it learns any previous filing was inaccurate. Company Applicant information is not required to be updated once the initial filing has been submitted.

REPORTING COMPANY INFORMATION

What Must Be Reported?

A Reporting Company must provide the following information:

1. Name of the entity, including any alternative or doing-business-as (d/b/a) names.
2. Current U.S. street address.
3. Jurisdiction of formation (for foreign entities, include the state or Tribal jurisdiction where first registered to do business in the U.S.).
4. Unique identification number (e.g., TIN, EIN, LEI).
5. Certain information for each Beneficial Owner and, if it is a new Reporting Company, up to two Company Applicants (each as described below).

BENEFICIAL OWNERS

What is a Beneficial Owner?

A Beneficial Owner of a Reporting Company is any individual who:

1. exercises “substantial control” over the Reporting Company; *or*
2. “owns or controls” not less than twenty-five percent (25% equity in the entity.

“Substantial Control” is defined broadly, and includes:

1. A senior officer, including the President, CEO, CFO, COO, and General Counsel;
2. Anyone having the authority to appoint or remove a senior officer or the majority of the board of directors of the Reporting Company;
3. Anyone who can direct, determine, or has substantial influence over important matters of the Reporting Company; *or*
4. Anyone who has any other form of substantial control over the Reporting Company (this latest category is meant as a catch-all for anyone that can make important decisions on behalf of a Reporting Company with atypical governance structures).

“Ownership Interest” is also defined broadly, and, in addition to straightforward equity ownership, also includes profits interest, convertible instruments (whether categorized as equity or debt), warrants, and puts, calls and options (except to the extent created and held by a third party without the knowledge of the Reporting Company). FinCEN will look at ownership “directly and indirectly”, meaning they will look through intermediary holding companies to the ultimate, individual owners.

Who is Exempt?

The following are exempt from the definition of Beneficial Owner:

1. Minor children.
2. Individuals acting as a mere intermediary or agent.
3. Individuals whose control over a Reporting Company derives *solely* from employment (note that this exemption *does not* apply to senior officers).
4. Individuals whose only interest in a Reporting Company is through a right of inheritance.
5. Creditors of Reporting Companies.

What Must Be Reported?

A Reporting Company must provide the following information for each Beneficial Owner:

1. Full legal name.
2. Date of birth.
3. Current address.
4. Unique identifying number from an acceptable identification document (such as a state drivers' license or passport), along with an image of such document.

COMPANY APPLICANTS

What is a Company Applicant?

A Company Applicant of a Reporting Company is any individual who:

1. directly files the document that creates or first registers the Reporting Company; *or*
2. is primarily responsible for directing or controlling such filing if more than one individual is involved in the filing of the document creating the domestic Reporting Company.

What Must Be Reported?

Up to two (2) Company Applicants must be identified for each New Reporting Company (Existing Reporting Companies are not required to report their Company Applicants). While a number of individuals in the "chain of command" could be considered a Company Applicant, from a partner directing the creation of an entity, to an associate drafting the formation documents, to an employee actually filing the documents, FinCEN has indicated that it would look to both ends of the chain: the person directing the filing and the person making the filing.

FINCEN IDENTIFIERS

In lieu of providing the same set of Beneficial Owner and Reporting Company information, the Act provides for individuals and entities to obtain FinCEN Identifiers, a unique number similar to a username.

Rules for individual FinCEN Identifiers were released as part of the Reporting Rule, and FinCEN released rules for entity FinCEN Identifiers on November 8, 2023.

While FinCEN Identifiers are not required, they are useful for entities and individuals that will complete multiple filings as they can both ease the administrative burden and also, with respect to individuals, help to safeguard personal information from having to be transmitted to FinCEN repeatedly.

However, once issued, FinCEN ID Numbers are lifelong. At present, there is no expiration or method of withdrawal, though FinCEN is considering proposing rules with respect to withdrawal. If any change occurs to information previously submitted by an individual in the application for a FinCEN Identifier, the individual must file an update with FinCEN reflecting the change within thirty (30) calendar days.

FILING AND PENALTIES

How to File

The Act requires that FinCEN create and maintain non-public, cloud-based database for filings by Reporting Companies, which must include extensive protocols and safeguards for authorized users. FinCEN is authorized to share information with the following organizations:

- Federal agencies engaged in national security, intelligence, and civil and criminal law enforcement;
- The Department of the Treasury in connection with its official duties, including tax administration; and
- State and local law enforcement agencies in connection with criminal or civil investigations.

Reported information will not be subject to any FOIA requests nor otherwise accessible by the public; the purpose of the Act is to target criminality and not to serve as a public repository of information. Safeguards are especially important especially considering that the Act requires reporting of sensitive personal information of individuals.

PENALTIES

Individuals who *willfully provide, or attempt to provide, false information or fail to report complete information* can face daily civil fines of \$500, up to a maximum of \$10,000, and imprisonment for up to two (2) years. Note that an individual must act willfully, or intentionally, to be subject to penalties under the Act; individuals acting with a less culpable state of mind, even gross negligence, would not be liable.

LOOKING AHEAD

Considerations for Entity Formation

Given that Existing Reporting Companies (those that are created prior to January 1, 2024), do not have to make a report until January 1, 2025 and, additionally, do not have to report its Company Applicants, it can be expected (and advisable) to create any entities which are expected to be used prior to January 1, 2025 before the effective date of the Act on January 1, 2024.

Furthermore, since Delaware is the preeminent jurisdiction for entity formation, it can be expected that the end of 2023 will see a record number of filings with the Delaware Secretary of State, so it would be advisable to file early to avoid any delays.

Business Formation and Filing Service Agencies

One of the primary concerns for Company Applicants is personal liability for penalties under the Act. Company Applicants, like Beneficial Owners, are defined as individual persons. Therefore, entities and law firms may not be listed as a Company Applicant; rather, the specific individual who directly performs the filing with a state office to create the Reporting Company must be disclosed. While the threshold for non-compliance is high (requiring an intentional act, as described above), the risk for individuals whose affiliation with a Reporting Company is derived solely from their employment status providing services at another's direction can be mitigated by the use of third-party vendors.

Such vendors, who already provide business formation and filing services, will offer the option to list their own employees and representatives performing a filing or registration as Company Applicants.

More information should be available after FinCEN releases their paper form for Beneficial Owner and Company Applicant reporting.

State Laws

The passage of the Act has also prompted a number of states to pass similar laws. In June of 2023, the New York legislature passed the "LLC Transparency Act" (the "NY Act"). The NY Act will require limited liability companies to disclose the names of their beneficial owners in order to qualify to do business in New York. Similar to the Act, the NY Act was also passed in response to concerns that shell companies are being used to shield illicit activity; currently in New York, limited liability companies are not even required to disclose their members or managers.

California is also considering similar legislation; the California state senate is currently considering both the California Transparency in Corporate Structures Act and the California Corporate Transparency Act.

Time will tell whether this will be a continuing trend in state legislation (in particular, Delaware), and how these various state laws will interact with the Act.

Challenges to the Act

National Small Business United, a small business advocacy group affiliated with the National Small Business Association, has already filed suit against the Department of Treasury and FinCEN challenging the constitutionality of the Act itself, as well as its implementation by FinCEN.¹ While the case is still in the early stages, it may portend future challenges as more and more business owners begin to realize that the Act applies to them and their companies.

¹Nat'l Small Bus. United v. Yellen, No. 5:22-cv-01448-LCB (N.D. Ala. 2022).