The Corporate Transparency Act is Coming! Are You Ready?

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Beginning January 1, 2024, the Corporate Transparency Act (CTA) will require certain entities to begin reporting beneficial ownership information (BOI) to the Financial Crimes Enforcement Network (FinCEN). As part of the National Defense Authorization Act, the CTA represents years of congressional efforts to enforce beneficial ownership reporting for business entities. The reporting requirement applies to all corporations, limited liability companies, limited partnerships, and similar entities unless an exemption applies. The CTA shifts the burden of collecting BOI from financial institutions to the entities themselves and imposes stringent penalties for non-compliance and unauthorized disclosures. It is imperative for companies to carefully review the CTA to determine if they are a "reporting company" and assess their potential obligations under the forthcoming regulations.

What is a Reporting Company?

Broadly speaking, a "reporting company" refers to any domestic or foreign corporation, limited liability company, limited partnership, or similar entity formed or registered to do business within any U.S. state or tribal jurisdiction by filing a document with the secretary of state or a similar office. Simply put, if the entity is formed by filing a document, it could be considered a reporting company and requires further evaluation. In contrast, legal entities not considered reporting companies include common law general partnerships and some trusts (e.g., Rabbi Trust).

What Entities are Exempt?

While the definition of a "reporting company" is broad, the CTA has created 23 separate exemption types, some of which include:

- Regulated commodity brokers
- Publicly traded companies
- Banks
- Federal and state credit unions
- Governmental entities
- Insurance companies operating in the U.S.
- Securities brokers
- Public utility companies
- Financial market utilities
- Certain investment advisers
- Venture capital fund advisers
- Accounting firms
- Pooled investment vehicles
- Inactive entities not owned by a foreign person
- Tax-exempt entities (such as nonprofits, political organizations, and certain trusts)
- Subsidiaries of exempt entities
- Large operating companies

An entity will qualify for a large operating company exemption if it meets the following requirements:

- The entity employs more than 20 employees on a full-time basis in the U.S.,
- The entity filed federal income tax returns in the U.S. showing more than $5,000,000 in gross receipts or sales in the previous year, and
- The entity has an operating presence at a physical office within the U.S.

However, a large operating company that ceases to satisfy all three requirements will lose its exemption status and be required to file BOI reports within 30 days of losing its status.

Who is a Beneficial Owner?
Each reporting company must file a report that discloses certain information about each of its beneficial owners. A beneficial owner is an individual who, directly or indirectly, through contract, understanding, or relationship:

- Exercises substantial control over a reporting company or
- Owns or controls at least 25% of the ownership interests of the reporting company.

According to FinCEN, an individual directly or indirectly exercises substantial control over a reporting company if he or she:

- Is a senior officer of the reporting company,
- Has authority over the appointment or removal of any senior officer,
- Directs or has substantial influence over essential matters affecting the reporting company, or
- Has any other significant control over the reporting company.

Because the penalties for omitting individuals can be severe, most reporting companies will include BOI for the following:

- All directors and managers,
- Senior executive officers, and
- Any person with “veto” or “consent right” over critical decisions.

What Information Must be Reported?
Reporting companies must disclose the following for each of their beneficial owners:

- Their name
- Date of birth
- Residential or company address, and
- A unique identifier number from a recognized issuing jurisdiction and a photo of that document.

If an individual decides to file their information with FinCEN directly, they will be given a “FinCEN identifier,” which the reporting company can provide on its BOI report instead of the required information.

Reporting companies should also be mindful of penalties associated with noncompliance with the CTA or providing misleading information to FinCEN. Any individual who commits a reporting violation may be held liable for civil fines of up to $500 per day or criminal penalties of up to two years in prison for violating the CTA.

When are Reports Due?

- Entities formed prior to January 1, 2024 must file their initial report on or before January 1, 2025.
- Entities formed on or after January 1, 2024 must file their initial report within 30 days of their formation date.
- Changes in the information reported must be reported within 30 days.

On September 27, 2023, FinCEN issued a Notice of Proposed Rulemaking that would extend the deadline for reporting companies formed in 2024 to file their initial BOI reports from 30 to 90 days.

How Should Your Company Prepare?

Attorneys and the companies they represent will first need to familiarize themselves with the reporting requirements, then:

- Evaluate if the company is exempt or must file a BOI report,
- Update governing documents and create a comprehensive compliance plan to compel beneficial owners, managers/directors, and senior officers to report requisite information and any changes to that information in an organized manner,
- Implement procedures that monitor changes in BOI,
- Ensure owners, managers/directors, and senior officers are educated on the CTA's purpose, requirements, and penalties, and
- If exempt, consider adopting CTA compliance policies and gathering the necessary information in case legislation broadens the CTA.

Key Takeaways

While the CTA is intended to provide better company oversight and help circumvent criminal activity, it will impose a significant administrative burden on the vast majority of companies in the U.S. It is important for attorneys to familiarize themselves with the CTA and their companies' reporting obligations before the CTA becomes effective on January 1.