

CORPORATE TRANSPARENCY ACT REQUIREMENTS BEGIN IN 2024

The Corporate Transparency Act (“CTA”) became federal law in 2021. The CTA is part of the Anti-Money Laundering Act of 2020, which is contained in the National Defense Authorization Act for Fiscal Year 2021 (“NDAA”). The NDAA was vetoed by President Trump but then became effective through an override by Congress.

The CTA is expected to impose new disclosure duties on most companies and certain other persons beginning on January 1, 2024. This information is to be reported to the U.S. Department of Treasury’s Financial Crimes Enforcement Network (“FinCEN”). FinCEN estimates that approximately 32 million companies will become subject to the reporting requirements of the CTA.

Here are some key questions and answers about the CTA.

What companies are subject to the CTA?

Corporations, limited liability companies and similar entities formed or registered in the U.S. are considered “reporting companies” under the law unless they meet one of the specified exemptions. There are 23 separate exemptions, but many of the exemptions are intended to cover companies that are otherwise regulated businesses, such as public companies, banks, credit unions, securities brokers and licensed insurance companies.

One exemption that may receive a closer review by some is the exemption for “large reporting companies”. A large reporting company is a company with a physical presence in the U.S. and both more than 20 full-time employees and more than \$5 million in gross receipts or sales in the prior fiscal year as reported on its tax return filed with the Internal Revenue Service. Many small and mid-size businesses do not meet these requirements so the burden of CTA compliance will fall on them.

What does a reporting company have to report?

The reporting company has to report information to FinCEN about itself and its beneficial owners.

Additionally, reporting companies formed or registered on or after January 1, 2024 must report information to FinCEN about certain individuals who are involved in the formation or registration of the entity (known as “applicants”). An applicant is an individual who directly files the document with a secretary of state’s office to form the entity or registers it to do business and an individual who is primarily responsible for directing the filing. A newly formed entity must have at least one applicant and may have as many as two applicants.

With respect to the reporting company, the reporting company must report (1) its full legal name, (2) all trade names and “doing business as” names, (3) its principal place of business (if domestic) or primary location in the U.S. (if foreign), (4) state of jurisdiction where it was formed (if domestic) or where it was first registered to do business in the U.S. (if foreign), and (5) its IRS taxpayer identification number.

With respect to each beneficial owner, the reporting company must report (1) the individual’s full legal name, (2) date of birth, (3) residential street address, (4) the unique ID number from the individual’s

identification document (for most people this will be a driver's license number or passport number), (5) the jurisdiction which issued the identification document, and (6) an image of the identification document (for most people this will be a photo or photocopy of the driver's license or passport). See more detail below about who would be considered a beneficial owner of a reporting company.

With respect to each applicant, the reporting company formed on or after January 1, 2024 must report (1) the individual's full legal name, (2) date of birth, (3) residential street address (or business street address if the individual forms entities as part of his or her business), (4) the unique ID number from the individual's identification document (for most people this will be a driver's license number or passport number), (5) the jurisdiction which issued the identification document, and (6) an image of the identification document (for most people this will be a photo or photocopy of the driver's license or passport).

When does the reporting company have to begin submitting this information to FinCEN?

For reporting companies formed or registered during 2024, the required information must be reported within 90 days after the notice of formation or registration of the entity.

Beginning January 1, 2025, the deadline for newly formed or registered reporting companies will be lowered to 30 days after the notice of formation or registration of the entity.

For reporting companies that were in existence prior to January 1, 2024, the required information must be reported by January 1, 2025.

Note the Protect Small Business and Prevent Illicit Financial Activity Act (H.R. 5119) (the "Protect Small Business Act") is being considered in Congress as of the date of this briefing. If enacted as currently proposed, the 90-day filing requirement for reporting companies formed or registered on or after January 1, 2024 would become permanent and the deadline for reporting companies in existence prior to January 1, 2024 would be extended to January 1, 2026.

What if the reported information changes after submission to FinCEN?

In most cases, the reporting company is obligated to make a report to FinCEN of the change within 30 days after the change in the reported information. However, the applicant information does not need to be updated if it was correct when submitted.

The Protect Small Business Act would extend the deadline to 90 days after the change if it is enacted as currently proposed.

Where does the reporting company report this information?

FinCEN is in the process of developing an online portal for reporting the information. This portal is not live as of the date of this briefing, and FinCEN has not formally indicated when it will be available for reporting.

Who is a beneficial owner?

Depending on the circumstances, this could be a complicated question. A “beneficial owner” is any individual who, directly or indirectly, either exercises substantial control over the reporting company or owns or controls at least 25% of the ownership interests of such reporting company.

An individual possesses substantial control by serving as a “senior officer”, having authority to remove or appoint a senior officer or a majority of the board of directors (or similar body), or having “substantial influence” over important matters at the reporting company (regardless of the title or role at the reporting company).

A “senior officer” is any individual holding the position or exercising the authority of a president, chief executive officer, chief financial officer, general counsel, chief operating officer, or any officer, regardless of title, who performs a similar function.

The “substantial influence” test is intended to capture individuals who exercise actual control over the reporting company even though they lack a specified title or role. If substantial influence exists, the individual will be considered a beneficial owner even if the individual holds no title or position with the reporting company and isn’t an owner of any equity securities of the reporting company.

The application of the 25% ownership test also involves some complexities. For instance, the ownership interests can take the form of interests that typically do not provide all rights associated with ownership status, such as profits interests, convertible instruments, options, warrants, non-voting equity and possibly other contracts or understandings used to establish ownership.

There are also certain groups who may be exempted from the definition of beneficial owner if they do not exert substantial control, such as minor children (but in this case the parent or guardian must report), individuals whose only interest is through a future right of inheritance, creditors of a reporting company whose only interest is for the payment of a predetermined sum, and others.

What if a reporting company doesn’t comply with the CTA?

There are potentially significant penalties for failing to comply with the CTA. The CTA provides that willfully reporting or attempting to report false information, or willfully failing to report complete or updated beneficial ownership information will be punishable with a civil penalty of up to \$500 a day while the violation continues, and possible criminal fines of up to \$10,000 and up to two years in prison.

Will the information submitted by reporting companies be publicly available?

The information should not be publicly available. However, FinCEN may share the information upon request from federal, state and local agencies in certain circumstances and a financial institution if the reporting company has consented to the disclosure of the information for compliance with the know-your-customer regulatory obligations of the financial institution.



HILL WARD
HENDERSON

Does a beneficial owner or applicant have to provide personal information for each reporting company?

An individual will have to provide the personal information for each reporting company in which he or she qualifies as a beneficial owner or applicant, although FinCEN intends to establish a program in which the individual has the option to apply directly to FinCEN for a FinCEN identifier (“FinCEN ID”). Once the individual receives the FinCEN ID, that ID number could be given to the reporting company so that it can meet its reporting obligations. This option will allow the individual to submit the personal information directly to FinCEN to avoid having to provide it to each reporting company.

If you have any questions or would like more information on the matters discussed above, please reach out to your contact at our firm.

The information in this briefing is for general education and knowledge and is neither intended to be, nor should it serve as, legal advice or as a comprehensive analysis of the new legal requirements. The information is not intended to create, and receipt of it does not constitute, an attorney-client relationship. If you have any questions regarding your specific situation, you should reach out to your contact at Hill Ward Henderson.