

# REPORTING REQUIREMENTS UNDER THE CORPORATE TRANSPARENCY ACT: HOW DOES IT AFFECT MY COMPANY?

February 7, 2023

Beginning January 1, 2024, most newly formed companies operating in the United States will be required to report personal information about their Beneficial Owners and Company Applicants (defined below) to the Department of Treasury's Financial Crimes Enforcement Network (FinCEN). Entities formed before January 1, 2024 have until January 1, 2025 to report. Entities created or formed after January 1, 2024 must file an initial report within 30 days of formation. These new reporting requirements are part of the Corporate Transparency Act (CTA), which was passed in an effort to combat money laundering, tax fraud, the financing of terrorism, and other illicit activities furthered by the use of anonymous shell companies. Failure to comply with the CTA may result in senior officer liability for civil penalties of up to \$500 per day, an additional fine of up to \$10,000, and up to two years in prison.[1]

Below is a summary of what companies are required to report ("Reporting Companies"), certain exemptions, who each Reporting Company must report information about, what information must be reported, and when the reporting requirements go into effect.

## What companies are required to report?

All corporations, limited liability companies (LLCs), and other entities either formed by filing a document with a secretary of state or similar office under the law of a U.S. state or Indian Tribe, or formed in a foreign country and registered to do business in the U.S. are required to report. This expansive definition of Reporting Company includes limited partnerships, limited liability partnerships, professional corporations, professional limited liability companies, and company trusts.

The CTA exempts 23 categories of entities from the definition of Reporting Company. The most commonly applicable exemptions include:

- **Publicly traded companies;**
- **Large operating companies** that have: (1) more than 20 full-time employees in the U.S.; (2) more than \$5 million in gross receipts or sales in the past year; and (3) an operating presence at a physical office within the U.S.;
- **Subsidiaries** that are controlled or wholly owned by an exempt entity (for example, if a parent corporation qualifies as a large operating company and owns

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## REPORTING REQUIREMENTS UNDER THE CORPORATE TRANSPARENCY ACT: HOW DOES IT AFFECT MY COMPANY?

100% of the membership interests of subsidiary LLC, neither parent corporation nor its subsidiary LLC would be required to report); and

- **Inactive entities** that meet certain requirements.

There are a number of additional exemptions that may apply depending on the nature of your company, and the CTA has authorized FinCEN to establish additional exemptions..[2] Hodgson Russ would be happy to perform an analysis to determine if your company qualifies for an exemption.

### Who must Reporting Companies report information about?

All Reporting Companies must report information on each of their Beneficial Owners. Companies formed on or after January 1, 2024 must also report information on each of their Company Applicants.

#### *Who is a Beneficial Owner?*

An individual qualifies as a Beneficial Owner in one of two ways: (1) by exercising **substantial control** over a Reporting Company; or (2) by owning or controlling at least **25 percent of the ownership interests** of a Reporting Company.

#### **Substantial control**

An individual exercises substantial control over a Reporting Company by:

- Having authority over the appointment or removal of any senior officer or a majority of the board of directors or similar body (this would typically include the director(s) and shareholder(s) of a corporation and the manager(s) and member(s) of an LLC);
- Serving as a senior officer of the company (by default, this includes the roles of president, CEO, CIO, general counsel, etc., but not secretary or treasurer); or
- Substantially influencing important company decisions such as entering into new lines of business, reorganizing, dissolving, or merging the company, selling principal assets, incurring substantial debt, developing compensation schemes for senior officers, and amending any substantial governance documents.

Reporting Companies will need to consider their basic governance documents (by-laws, operating agreement, etc.), any other documents that grant special voting rights such as shareholder and subscription agreements, and their informal decision making practices to determine who exercises substantial control.

#### **Ownership of 25% of the ownership interests of a Reporting Company**

“Ownership interests” means, for example, membership interests of a limited liability company or shares of stock of a corporation.

An individual can meet the 25% ownership threshold by owning or controlling an intermediary entity that owns ownership interests in a Reporting Company. For example, take subsidiary LLC that is 100% owned by parent LLC. If parent LLC is 100% owned by an individual, that individual would be considered a Beneficial Owner of both parent LLC and subsidiary

## REPORTING REQUIREMENTS UNDER THE CORPORATE TRANSPARENCY ACT: HOW DOES IT AFFECT MY COMPANY?

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Reporting Companies should pay special attention to FinCEN's guidance on ownership interests held in trust. Note that ownership interests held in trust will count towards a trustee's status as Beneficial Owner if the trustee has the authority to dispose of trust assets. Similarly, if a trust beneficiary is the sole recipient of trust income and principal and has the right to demand a distribution of substantially all the assets of the trust, any ownership interests held in that trust will count towards that beneficiary's status as a Beneficial Owner. Lastly, ownership interests held in trust will count towards a grantor or settlor's status as a Beneficial Owner if they have the right to revoke the trust or otherwise withdraw the assets of the trust.

### *Who is a Company Applicant?*

A Company Applicant is the individual who files the formation document for a Reporting Company (e.g. its certificate of incorporation, articles of organization, etc.) **and** any person who directs the filing of the formation document. For example, if a corporation's officer hires a law firm to form a new entity and a paralegal at the firm files the necessary formation documents with the secretary of state, the paralegal and the attorney supervising the matter would be considered Company Applicants subject to the reporting requirements. The number of Company Applicants is limited to two individuals per entity.

### **What information must be reported?**

Reporting Companies must submit the following information (i) for each of their Beneficial Owners ("Beneficial Ownership Information"), and (ii) for companies formed on or after January 1, 2024, each of their Company Applicants:

- Full legal name;
- Date of birth;
- Residential street address (or, in the case of a Company Applicant who files formation documents in the course of their company, their business address); and
- For U.S. citizens and individuals with dual citizenship in the U.S., an identifying number from and scanned image of a U.S. passport, driver's license, or other document issued by a state or local U.S. government, or
- For foreign persons, an identifying number from and a scanned image of a foreign passport.[3]

### **When do the reporting requirements go into effect?**

Companies that are formed or registered to do business in the U.S. on or after January 1, 2024 must file their initial report with FinCEN within 30 days of formation or registration. Companies that were formed or registered to do business in the U.S. prior to January 1, 2024 have a one year grace period to file their initial report, and must do so no later than January 1, 2025.

All reporting companies have an ongoing duty to notify FinCEN of any changes in reported Beneficial Ownership Information within 30 days of any change.

## REPORTING REQUIREMENTS UNDER THE CORPORATE TRANSPARENCY ACT: HOW DOES IT AFFECT MY COMPANY?

FinCEN is still building the database where reported information will be stored, which will be known as the Beneficial Ownership Secure System (BOSS). Currently available guidance on the BOSS indicates that Beneficial Ownership Information will not be accepted prior to January 1, 2024. FinCEN stated that it will publish additional guidance and resources, including a Small Entity Compliance Guide for the CTA, in the future. Hodgson Russ will issue another alert when this information becomes available.

### Who will have access to reported information?

Information reported to FinCEN under the CTA will be stored in the confidential, secured BOSS, which will not be accessible to the general public. FinCEN is authorized to disclose the information to certain tax and law enforcement agencies only in a limited number of circumstances.<sup>[4]</sup>

### Key Takeaways

Companies formed or registered to do business in the U.S. should review the list of reporting exemptions under the CTA to determine their reporting obligations and start gathering information on their Beneficial Owners to be prepared when the CTA takes effect in 2024. Importantly, reporting under the CTA to the BOSS is not a one-time requirement; Reporting Companies have an ongoing duty to keep reported information up to date and may face significant fines for noncompliance. In the M&A context, particular attention should be paid during the due diligence process to target company compliance with the CTA.

Hodgson Russ welcomes the opportunity to assist you in complying with these new requirements.

[1] Corporate Transparency Act, 31 U.S.C.A. § 5336(h)(3) (2021); Beneficial Ownership Reporting Requirements, 87 Fed. Reg. 59,498, 59,596 (Sept. 30, 2022) (to be codified at 31 C.F.R. § 1010.380(g)), available at <https://www.govinfo.gov/content/pkg/FR-2022-09-30/pdf/2022-21020.pdf>.

[2] See the full list of exemptions at Beneficial Ownership Information Reporting Requirements, 87 Fed. Reg. 59,593-94 (to be codified at 31 C.F.R. § (c)(2)(i)-(xxii).

[3] Beneficial Ownership Information Reporting Requirements, 87 Fed. Reg. at 59,592 (to be codified at 31 C.F.R. § 1010.380(b)(1)(ii)). Note that although the Internal Revenue Service, which is also housed under the Department of Treasury, accepts a foreign drivers' license as acceptable identification to apply for an Individual Taxpayer Identification Number (ITIN), FinCEN will only accept a foreign passport for individuals who cannot obtain a U.S. identification document and are required to submit personal information under the CTA. Internal Revenue Service, *Revised Application Standards for ITINs* (updated Aug. 26, 2022), <https://www.irs.gov/individuals/revised-application-standards-for-itins>.

[4] For more information, see "Reporting Requirements Under the Corporate Transparency Act: How Does it Affect My Company?"