The Federal Corporate Transparency Act Requires Entities to Report Their Ownership Beginning January 1, 2024

New Federal law requires reporting of the ownership and organizers of many new entities (corporations, LLCs, etc.) formed on or after January 1, 2024, within 30 days (90 days for entities formed in 2024) after formation, and reporting of the ownership of many active existing entities formed prior to January 1, 2024. The law imposes significant penalties for failure to comply.

CORPORATE TRANSPARENCY ACT REPORTING COMING JANUARY 1, 2024

New reporting requirements under the federal Corporate Transparency Act ("CTA") for certain entities will go into effect starting **January 1, 2024**. The CTA was originally enacted as part of the National Defense Authorization Act for Fiscal Year 2021 and final regulations were released September 29, 2022. The core purpose of the CTA is to allow the Financial Crimes Enforcement Network ("FinCEN") to collect information about "Beneficial Owners" and "Company Applicants" (discussed below) of entities that fall under the CTA's regulations to assist with pursuing financial crimes including money laundering.

When the CTA goes into effect, it will materially impact the process and procedures for formation of new entities and the administration of existing entities, unless one of the exemptions from the requirements of the CTA applies. Not all details of the implementation of the law have been finalized, and persons who intend to form entities or administer existing entities should watch for updates. A summary of the CTA and its reporting obligations is set forth below. **Note** that this is **only a summary** and not intended to be comprehensive. Affected persons should consult with their attorneys prior to January 1, 2024, to develop a plan for compliance with the CTA, keeping in mind that nothing is required under the CTA until **January 1, 2024**.

SUMMARY OF THE CTA

WHEN: The reporting obligations begin **January 1, 2024**. "Reporting Companies" (discussed below) formed prior to January 1, 2024 will have one year to file their initial report with FinCEN. Reporting Companies formed after January 1, 2024 must file their initial report within 30 days (90 days for entities formed in 2024) after formation. If any information regarding beneficial owners in their filed report changes, the Reporting Company must file an update with FinCEN within 30 days.

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WHO MUST FILE: The CTA requires only "Reporting Companies" to file reports with FinCEN. Reporting Companies include: (1) domestic corporations, LLCs or other entities created by the filing of a document with any government authority of a state, Indian tribe or U.S. territory; and (2) foreign corporations, LLCs, or such other similar entities that are registered to do business in a state, tribe or U.S. territory. The CTA exempts 23 categories of larger and/or already-regulated entities from the reporting obligations under the CTA. The most common exempt categories are listed at the end of this summary.

WHAT MUST BE REPORTED: The required reports must include certain information about the Reporting Company, its "Beneficial Owners" and, if the Reporting Company is formed after January 1, 2024, its "Company Applicants." These CTA defined terms are discussed below. The report must include the following information:

- <u>Information about the Reporting Company –</u>
  - Full legal name;
  - Any trade names;
  - Current address;
  - State or other jurisdiction where formed or (for foreign entities) where first registered in the US; and
  - Taxpayer identification number.
- <u>Information about Beneficial Owners and Company Applicants –</u>
  - Legal name;
  - Date of birth;
  - Current address;
  - Unique identifying number from a government-issued document; and
  - An image of such government issued document.

"<u>Beneficial Owners</u>" include any individual (natural person) who, directly or indirectly, either (1) exercises "Substantial Control" (see discussion below) over the Reporting Company; or (2) owns or controls more than 25% of the ownership interests of the Reporting Company. Some individuals do <u>not</u> need to be reported as Beneficial Owners, including minors, nominees and agents, certain employees, heirs and certain creditors. Care needs to be taken in determining "ownership interests" in a Reporting Company, since "ownership interests" may include, in addition to equity interests, convertible instruments, options and debt instruments to the extent the holder has the right to exercise some of the same rights as the holders of equity interests.

- “Substantial Control” of a Reporting Company is exercised by an individual if such individual: (1) serves as a senior officer; (2) has authority over the removal or appointment of any senior officer or a majority of the Board (or similar body); (3) has control over important decisions; or (4) has any other form of substantial control over the Reporting Company. Careful analysis of who may have Substantial Control of a Reporting Company will be required. For instance, a trustee of a trust that holds assets in a legal entity that is a Reporting Company may be a Beneficial Owner of the Reporting Company because he or she has control over the trust’s property.

“Company Applicants” include any individual who either: (1) directly files the document creating or first registering the Reporting Company; or (2) is primarily responsible for directing or controlling such filing by another. While this definition could include numerous people, FinCEN intends to limit the number of Company Applicants that need to be reported to one or two individuals and a number of service providers are exempt from being considered Company Applicants.

HOW REPORTS ARE TO BE MADE: This is largely yet to be determined by FinCEN. FinCEN is working on a website where such reports can be filed.

WHO HAS ACCESS TO REPORTED INFORMATION: FinCEN will store the reported information on a secure, non-public data base. Disclosure of the information will be limited to various federal and state law enforcement agencies and financial institutions complying with government-imposed customer due diligence requirements.

PENALTIES: The CTA imposes civil and criminal penalties, including a fine up to $10,000 and/or imprisonment for up to 2 years, for any person who willfully fails to file required reports or provides false information in a report. Penalties may be imposed on the Reporting Company and certain individuals who cause the Reporting Company to violate the law. A 30-day cure period after discovery is provided to file corrective reports.

FinCEN IDENTIFIERS: If a person is regularly a Beneficial Owner or a Company Applicant, they may obtain a “FinCEN Identifier” (a unique number) from FinCEN, allowing that person to be identified in reports required by the CTA by such number, rather than having to provide all the information otherwise required. It is expected that FinCEN Identifiers will be widely used by attorneys and other professionals who regularly form entities.

EXEMPT COMPANIES: A full list of companies exempt from reporting under the CTA is beyond the scope of this article, and affected persons should consult their attorney. The most common exemptions are:

- Large operating companies – companies that:
  - Have more than 20 full time employees;
  - Have a physical office in the US; and
  - Reported more than $5 million in domestic gross receipts or sales in their last tax return.
- Public companies – issuers of securities registered with the SEC.

- Inactive companies – entities that:
    - Were in existence on or before January 1, 2020;
    - Are not engaged in any active business;
    - Are not wholly or partially owned by a non-US person;
    - Have not sent or received funds greater than $1,000 in the previous year; and
    - Do not otherwise hold any assets (including ownership interests in other entities).
- Certain other highly regulated companies – including banks, stock broker/dealers, investment advisers, regulated utilities, etc.
- Tax-exempt entities – including charities, PACs, charitable trusts and certain of their advisers and service providers.

The application of exemptions may be complicated and challenging. For instance, subsidiaries of an exempt company may be Reporting Companies if not 100% owned by exempt entities.

ADDITIONAL GUIDANCE FOR SMALL ENTITIES. FinCEN recently released a small business compliance guide for small businesses, to help them understand their obligations and how to report their beneficial ownership information under the CTA. See here for further details:

https://www.fincen.gov/sites/default/files/shared/BOI_Small_Compliance_Guide_FINAL_Sept_508C.pdf

DOES THIS LAW AFFECT ME? The breadth and reach of this law will reach many people who think they are not the target of law enforcement agencies in any respect, such as money laundering, foreign investment, or organized crime. Anyone who uses entities in their business or personal affairs should either (1) determine with their attorney that they are exempt from the CTA, or (2) develop a plan for compliance with the reporting requirements of the CTA. Fredrikson & Byron has formed a task force to assist non-exempt companies file reports required by the CTA. To obtain such assistance, you may contact your primary attorney at Fredrikson or Jessica Manivasager at 612.492.7020.