

## Understanding The Corporate Transparency Act

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The Corporate Transparency Act (CTA), which goes into effect January 1, 2024, will implement uniform federal information disclosure requirements for domestic and foreign reporting companies registered to do business in the United States, unless otherwise exempt. The CTA will require such reporting companies to disclose to the Financial Crimes Enforcement Network (FinCEN) certain information about the company and its beneficial owner. For entities that are created or first registered beginning in 2024, the report must also include information about individuals who primarily control or directly file the formation documents for a domestic entity or the registration documents for a foreign entity.

The CTA is aimed at enhancing corporate transparency and combating financial crimes, particularly money laundering and terrorist financing. Noncompliance with the CTA may result in significant fines and prison terms.

### Which Companies Must Report Under the CTA and Which are Exempt?

A "Reporting Company" is broadly defined to include corporations, limited liability companies, and similar entities - such as a limited partnership, created or registered by a filing with a state, Indian Tribe, or similar agency. Sole proprietorships, general partnerships, and certain trusts generally fall outside the scope of the CTA if no state filing is required for their formation. FinCEN has estimated approximately 32.6 million companies will be subject to the CTA reporting rules in the first year of implementation.

There are 23 categories of entity exemptions under the CTA, including certain entities that are already subject to robust federal reporting requirements, such as (i) public companies that are issuers of securities registered under section 12 of the SEC Act of 1934 or are required to file supplementary and periodic information under section 15(d) of the SEC Act of 1934; (ii) "large operating companies" with more than 20 full time employees, an operating presence in a physical office within the United States, and a filed U.S. federal income tax return for the previous year demonstrating more than \$5 million in gross receipts or sales from U.S. sources; (iii) banks; (iv) credit

unions; (v) depository institution holding companies; (vi) money services or transmitter businesses registered with FinCEN; (vii) brokers or dealers of securities; (viii) securities exchange or clearing agencies; (ix) other Exchange Act registered entities; (x) investment companies and advisers; (xi) venture capital fund advisers; (xii) insurance companies; (xiii) state-licensed insurance producers; (xiv) Commodity Exchange Act registered entities; (xv) public accounting firms registered in accordance with section 102 of the Sarbanes-Oxley Act of 2002; (xvi) regulated public utility companies; (xvii) financial market utilities; (xviii) pooled investment vehicles operated or advised by certain exempt entities; (xix) tax-exempt entities including 501(c) nonprofits, 527 political organizations, a trust described in paragraph (1) or (2) of section 4947(a) of the Internal Revenue Code; (xx) an entity assisting a tax-exempt entity if it is operated exclusively to provide financial assistance to, or hold governance rights over, any tax-exempt entity, is a United States person, beneficially owned or controlled exclusively by one or more United States persons that are United States citizens or lawfully admitted for permanent residence, and derives at least a majority of its funding or revenue from one or more United States persons that are United States citizens or lawfully admitted for permanent residence; (xxi) a subsidiary of certain exempt entities where the ownership interests are controlled or wholly owned by the exempt entity; (xxii); government authorities; and (xxiii) inactive entities as defined by the CTA (i.e., in existence prior to 1/1/2020, no active business, no foreign ownership, no ownership change and has not sent or received more than \$1,000 in the past 12 months, and holds no assets of any kind).

## **What Information Must Reporting Companies Disclose?**

The initial Beneficial Ownership Information (BOI) report under the CTA must include the following information:

- (i) Full legal name;
- (ii) Any trade name or “doing business as” name;
- (iii) Complete current street address of principal place of business;
- (iv) State, Tribal, or foreign jurisdiction of formation;
- (v) If foreign, the U.S. jurisdiction where the company first registers;
- (vi) IRS Taxpayer Identification Number (i.e., an Employer Identification Number [EIN]); and
- (vii) Beneficial Owners.

A Reporting Company is also required to report its Company Applicants if it is either a domestic entity created on or after January 1, 2024, or a foreign entity first registered to do business in the U.S. on or after January 1, 2024.

## **Who is Considered a Beneficial Owner and What Must be Reported?**

Beneficial Owners are defined broadly as individuals who, directly or indirectly, exercise substantial control over the Reporting Company or own at least 25% of its ownership interests. Ownership for purposes of the 25% test is determined by: the outstanding ownership interests of the Reporting

Company, the total combined voting power of all classes of stock for corporations, or the total combined value of the ownership capital or profits interests.

#### **A. Who Has Substantial Control of a Company?**

The CTA provides four categories for determining if someone has substantial control over a Reporting Company: (1) the individual is a senior officer (i.e., President, CFO, GC, CEO, COO, or any other person, regardless of title, exercising authority of a similar function and not ministerial functions alone); (2) the individual has authority to appoint or remove certain officers or a majority of directors of the Reporting Company; (3) the individual is an important decision-maker; or (4) the individual has any other form of substantial control over the Reporting Company. It is important to note that whether a particular member of the board of directors meets any of these criteria is a question that the Reporting Company must consider on a director-by-director basis. Any individual who directs, determines, or has substantial influence over important decisions made by the Reporting Company, includes decisions regarding the Reporting Company's:

1. Business, such as:
  1. Nature, scope, and attributes of the business;
  2. The selection or termination of business lines or ventures, or geographic focus; and
  3. The entry into or termination, or the fulfillment or non-fulfillment, of significant contracts.
2. Finance, such as:
  1. Sales, lease, mortgage, or other transfer of any principal assets;
  2. Major expenditures or investments, issuances of any equity, incurrence of any significant debt, or approval of the operating budget; and
  3. Compensation schemes and incentive programs for senior officers.
3. Structure, such as:
  1. Reorganization, dissolution, or merger; and
  2. Amendments of any substantial governance documents of the Reporting Company, including the articles of incorporation or similar formation documents, bylaws, and significant policies or procedures.

#### **B. What are Relevant Examples of Ownership Interests?**

Ownership interests include an individual's interests in:

1. Equity, stock, or voting rights such as a (i) preorganization certificate or subscription, (ii) transferable share of, or voting trust certificate or certificate of deposit for, an equity security, interest in a joint venture, or certificate of interest in a business trust.
2. Capital or Profit Interest from assets or profits of a company organized as an LLC.
3. Convertible Instruments including any instrument convertible into equity, stock, or voting rights or capital or profit interests whether or not anything needs to be paid to exercise the conversion. This also includes any future interest in any convertible instrument, a warrant or right to purchase, sell, or subscribe to a share or interest in those instruments, even if such warrant or right is a debt.
4. Option or Privilege including any put, call, straddle, or other option or privilege of buying or selling of those instruments, except if the option or privilege is created and held by others without the knowledge or involvement of the Reporting Company.
5. Catch All, which includes any other instrument, contract, arrangement, understanding, relationship or mechanism used to establish ownership.

#### **C. What Information Must Be Reported About the Beneficial Owner?**

All Beneficial Owners must report their: (i) full name; (ii) date of birth; (iii) current residential address; (iv) an identifying ID number along with; (v) a photo of the ID. The ID can be either: a valid U.S. driver's license, a valid U.S. passport, a non-expired identification document issued by a U.S. state or local government, or Indian Tribe. If an individual does not have any of these documents, a foreign passport must be provided.

#### **D. What Owners Are Exempt from Being a Beneficial Owner?**

The narrow exemptions from the definition of a Beneficial Owner are: (i) minor children (provided the Reporting Company reports the information of a parent or legal guardian); (ii) a nominee, intermediary, custodian, or agent; (iii) an employee (acting solely as an employee whose substantial control over, or economic benefits from, the Reporting Company are derived solely from his or her employment status) and who is not a senior officer; (iv) future interest through a right of inheritance; and (v) a creditor with no other incidents of control. Special rules for limited reporting also apply in certain cases, such as Beneficial Owners whose interests are held through entities exempt from the CTA and foreign-pooled investment vehicles.

### **Who Is Considered A Company Applicant and What Must Be Reported?**

A Reporting Company will have only up to two individuals who qualify as Company Applicants: (i) the individual who directly files the document that creates or registers the company; and (ii) if more than

one person is involved in the filing, the individual who is primarily responsible for directing or controlling the filing. A company is only required to report its Company Applicants if it is a domestic company formed on or after January 1, 2024, or a foreign company registered in the U.S. on or after such date.

The reportable Company Applicant information is the same as that of a Beneficial Owner generally. The FinCEN guidance clarifies that the report should include the individual's residential street address, except for Company Applicants who form or register a company in the course of their business - such as legal advisors, in which case the business address should be included.

### **When Must a Company Report Information Under the CTA?**

Companies formed or first registered in the U.S. on or after January 1, 2024, must complete their report with FinCEN within 90 days. Existing companies formed or registered before January 1, 2024, will need to report to FinCEN by January 1, 2025. The Reporting Company must certify that all information it reports is correct. Additionally, where a once-exempt entity is no longer exempt, it must file its initial report within 30 calendar days of the date it loses that status pursuant to the CTA, which is 180 days after revocation. An entity that reports and then obtains an exemption must correct the report within 30 days of obtaining the exemption. Material changes to a Reporting Company, Beneficial Owner, or Company Applicant's information must be reported to FinCEN no later than 30 days after the change.

### **Using a FinCEN Identifier to Streamline Reporting**

An entity or individual may obtain a FinCEN identifier by providing the required information applicable to such entity or individual to FinCEN. A FinCEN identifier will be issued upon request and may be used for future reporting in lieu of repeatedly providing all of the required information. In limited circumstances, a Reporting Company may use a related entity's FinCEN identifier.

A Reporting Company may report another entity's FinCEN identifier and full legal name in lieu of the information required with respect to the Beneficial Owners of the Reporting Company only if: (i) the other entity has obtained a FinCEN identifier and provided that FinCEN identifier to the Reporting Company; (ii) an individual is or may be a Beneficial Owner of the Reporting Company by virtue of an interest in the Reporting Company that the individual holds through an ownership interest in the other entity; and (iii) the Beneficial Owners of the other entity and of the Reporting Company are the same individuals.

If a Reporting Company, Company Applicant, or Beneficial Owner need to participate in more than one filing, obtaining a FinCEN identifier will make the reporting process easier. Note that using a FinCEN identifier places the burden of updating the required information on the applicable individual or Reporting Company, as each FinCEN identifier is specific to the individual or Reporting Company.

## **What are the Penalties for Providing Inaccurate Information or Failing to Report?**

If a Reporting Company files its BOI report and later realizes information about either the company, its Beneficial Owners, or its Company Applicants was inaccurate, the Reporting Company must correct the information no later than 30 days after the date the Reporting Company becomes aware of or has reason to know of the inaccuracy. This same timeline for correction applies to information provided to obtain a FinCEN identifier. There are no penalties for filing an inaccurate BOI report provided it is corrected within 90 calendar days of when it was filed. However, the 90-day safe harbor will not apply where the person acts for the purpose of evading the reporting requirements and has actual knowledge that any information contained in the report is inaccurate.

The CTA imposes penalties for non-compliance or providing false information. Willful failure to report accurate and complete beneficial ownership information can result in fines and imprisonment. Senior officers of an entity that fails to file a required BOI report may be held accountable for that failure. The civil penalties start at \$500 per day, up to \$10,000, for every day the violation continues. The criminal penalties can be a fine of up to \$10,000 or 2 years in prison, and in some cases both. Disclosing or using beneficial ownership information without authorization is also subject to a civil penalty of \$500 per day and a potential criminal penalty of up to \$250,000 or up to 5 years imprisonment. If failure to comply occurs while violating another law of the United States as part of a pattern of any illegal activity involving more than \$100,000 in a 12-month period, the fine would increase up to \$500,000, a prison term of not more than 10 years, or both.

## **Who Can Access the Report?**

The report may only be accessed by approved parties which include: (i) U.S. federal agencies engaged in national security, intelligence and law enforcement; (ii) state, local and Tribal law enforcement with court authorization; (iii) US Department Of The Treasury; (iv) financial institutions using beneficial ownership information to conduct legally required customer due diligence; (v) federal and state regulators assessing financial institutions for compliance; and (vi) foreign law enforcement agencies and certain other foreign authorities who submit qualifying requests.

## **Where Does A Company File Its Report?**

The BOI report must be filed electronically through the FinCEN portal known as the Beneficial Ownership Secure System (BOSS).

## **How to Prepare**

As January 1, 2024 approaches, companies must determine whether they are subject to reporting under the CTA regime. If so, the company must prepare to comply by determining its Beneficial Owners, gathering the required information and documents, making a plan for record-keeping and

information storage given applicable privacy laws, and establishing a process to track changes and filing updated reports as required. The Reporting Company must certify the information in the BOI report is correct. As such, it may wish to implement a plan to verify the information. Consideration of a company's corporate structure may also be important to both remain compliant with the CTA and satisfy the legitimate privacy concerns of its stakeholders.

**This article is a brief summary of the Corporate Transparency Act (CTA) and is intended for informational purposes only. It does not constitute legal, compliance or other advice for any individual or entity. Please consult your legal advisor for further information regarding the application of the CTA to any specific situation.**

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## CONTACTS



**Jonathan  
Storper**  
Partner  
San Francisco, CA



**Morgan Gray**  
Associate  
Los Angeles, CA

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