

Preparing for the Corporate Transparency Act

By Michael J. O'Brien, John G. Coleman, and Matthew G. Vassil

On January 1, 2024, the Corporate Transparency Act ("CTA") will come into effect and significantly revise current disclosure requirements for nearly every entity engaging in commerce in the United States. Business leaders should be proactive in assessing their responsibilities under the CTA in order to ensure timely compliance and avoid legal exposure.

BACKGROUND ON THE CTA

Prior to passing of the CTA, there was no uniform standard for collecting beneficial owner information from businesses in the United States outside of certain regulated industries. This vacuum created an opportunity for bad actors to form shell companies in the United States to facilitate money laundering, fraud, terrorist financing, and other illicit activities.

Accordingly, Congress enacted the CTA in January of 2021, as part of the National Defense Authorization Act, seeking to enhance corporate transparency and to deter the use of U.S. shell companies to commit illicit activities.

WHO DOES THE CORPORATE TRANSPARENCY ACT APPLY TO?

Under the CTA, all "reporting companies" are required to disclose beneficial ownership information ("BOI") to the U.S. Treasury's Financial Crimes and Enforcement Network ("FinCEN"). A "reporting company" includes all entities that are formed or registered to do business in the United States by filing of a document with a secretary of state or similar offices, such as corporations, LLCs, LLPs, etc., subject to various exemptions. If an entity is not created with this type of state filing, like most trusts, the entity is exempt from the CTA. The CTA also exempts "large operating companies." CTA defines a large operating company as any business that employs more than 20 full-time employees, earns more than \$5 million in revenue, and has an operating presence at a physical office in the United States. The CTA creates 23 total exemptions from its reporting requirements.

EXEMPTIONS

Some of the most notable exceptions include:

- Nonprofit entities, political organizations, and specific tax-exempt trusts.
- "Large operating companies," which are entities that (i) have more than 20 full-time U.S. employees (not counting employees of affiliated entities), (ii) reported more than \$5 million of revenue from U.S. sources on a consolidated basis to the IRS for the previous year, and (iii) have an operating presence at a physical location in the U.S.; and
- Publicly traded companies, insurance companies, banks, credit unions, public accounting firms, registered investment companies, registered investment advisers, as well as other entities that are already subject to federal regulatory oversight.

If an entity falls under one of the enumerated exemptions, they are not required to take any further action under the CTA.

MAINTAINING COMPLIANCE WITH THE CTA

The CTA requires reporting companies to disclose “beneficial owners” and “company applicants.” Reporting companies that existed prior to January 1, 2024, will be required to submit their initial report within **one year** (i.e., by January 1, 2025). All reporting companies created or registered on or after January 1, 2024, are required to submit their initial report within **30 days**, but could be extended to 90 days for entities formed in 2024 if FinCEN’s proposal is adopted as law.

BENEFICIAL OWNERS EXPLAINED

A beneficial owner is an individual who, **directly or indirectly**, (i) exercises “substantial control” over a reporting company or (ii) owns or controls at least 25% of the ownership interest of the reporting company. The CTA defines “substantial control” as an individual who satisfies **any** of the following factors:

1. Serves as a senior officer of the company.
2. Possesses authority over the senior officers or a majority of the board of a company.
3. Possesses substantial influence over the company’s important decisions; or
4. Possesses any other type of substantial control over the company.

It is important to note that these factors also apply to individuals that are **indirectly** related to the company if they satisfy any of the requirements of substantial control. Therefore, an individual may indirectly exercise substantial control over a reporting company by controlling intermediary entities that also exercise substantial control over such reporting company.

There are certain types of individuals which **cannot** be considered beneficial owners, including:

1. minor children.
2. an individual acting as a nominee, intermediary, custodian, or agent on behalf of another individual (in which case that individual would be the beneficial owner).
3. an employee of the reporting company, acting solely as an employee, whose substantial control over or economic benefits from the entity are derived solely from the employment status (provided that the person is not a senior officer of the entity).
4. an individual whose only interest in a reporting company is a future interest through a right of inheritance; and
5. a creditor of the reporting company (unless they exercise substantial control or have a 25% or more ownership interest in the reporting company).

COMPANY APPLICANTS EXPLAINED

A company applicant is either: 1) the individual who is responsible for the filing of the documents that create the entity or, in the case of a foreign entity qualified to do business in the United States, the individual who directly files the document that first registers the foreign reporting company to conduct business in a state of the United States; or 2) the individual who is primarily responsible for directing or controlling the filing of the relevant formation or registration document by another. This can include legal counsel or a service company used for corporate filings.

Reporting companies are **not required** to identify or report company applicants if they existed prior to January 1, 2024.

PENALTIES FOR FAILURE TO COMPLY WITH THE CTA

Failure to comply with the CTA can result in civil and criminal penalties. Potential civil penalties include fines of up to \$500 for each day the violation continues. In addition, possible criminal penalties include fines up to \$10,000 and/or imprisonment for up to two years. Criminal penalties will be imposed if there is evidence that the company willfully provided false information, failed to provide complete information, or failed to update information. Individuals can be held liable under the CTA if there is evidence that they caused a reporting failure or were a senior officer at the time of the failure.

WHAT CAN YOU DO NOW?

Businesses and industry leaders should take proactive steps to determine their specific status as either a “reporting company” or an exempt entity under the CTA. Companies should take necessary steps now to ensure compliance in 2024. Further, companies should work with legal counsel now to establish policies and procedures designed to ensure continued compliance with the CTA, including maintaining a current list of all beneficial owners (which includes indirect beneficial owners) and appointing an employee or department within their organization tasked with monitoring compliance with the CTA and changes of beneficial owners.

Additional information on the CTA is available here: [Beneficial Ownership Information Reporting | FinCEN.gov](#).

HOW WE CAN HELP

Eckert Seamans attorneys represent publicly traded companies, privately held corporations, and small businesses in regulatory and corporate governance matters and assist clients in meeting state and federal reporting requirements. Eckert attorneys can assist clients with CTA guidance, compliance, and completing and submitting required reports.