

How Corporate Transparency Act will affect your small business



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Background

- Anti-Money Laundering Act of 2020 (AMLA) was introduced to update the anti-money laundering laws in the US.
- The Corporate Transparency Act (CTA) is the most notable addition.
- Purpose is to stop bad actors from concealing their ownership of US entities, which are used to facilitate money laundering, terrorism, tax fraud, and other illegal acts.
- Through the CTA, Congress directs the US Treasury Department's Financial Crimes Enforcement Network (FinCEN) to establish and maintain a national registry of beneficial owners of entities that are deemed "Reporting Companies."
- Severe penalties will be assessed for violating the CTA.

General Overview

1. **Who** must file?
2. **When** must an entity file?
3. **What** information is required?
4. **What** are the penalties?



Who must file?

“Reporting Companies”

All “*Reporting Companies*”, unless an exemption applies.

Domestic Reporting Company: any corporation, LLC, or other similar entity created by filing a document with the secretary of state or similar office in any state or territory or with a federally recognized Indian Tribe.

Foreign Reporting Company: any corporation, LLC or other similar entity formed under the laws of a foreign country and registered to do business in the United States.

Exempt Entities

SEC-reporting companies (public companies, registered broker-dealers, registered investment companies or investment advisor, Venture capital fund advisers)	Commodity Exchange Act registered entities
Insurance companies	Banks and Credit Unions
Tax-exempt entities e.g., 501c3	Government Entities or Public Utilities
Accounting Firms	Large operating companies
Financial market utilities	Pooled investment vehicles
Entities assisting a tax-exempt entity	Inactive entities

**wholly-owned or controlled subsidiaries of certain exempt entities.*

Exempt Entities: Large Operating Company

1. Entity that employs >20 employees on a full-time basis in the US
2. Has filed a federal US income tax return for the year prior showing more than \$5 million in gross receipts or sales (not including receipts and sales from sources outside of the US),
and
3. Operates from physical office premises in the US.

** Including any other entity owned by the entity.*

*** Entity that initially qualifies as a “large operating company” but later fails to qualify will need to file a beneficial owner report (BOI Report). Conversely, an entity that initially is a “Reporting Company” but then becomes exempt, must file an update noting such change.*

Exempt Entities: Inactive Entities

1. In existence prior to Jan. 1, 2020
2. Is not engaged in active business
3. Is not owned by a foreign person (directly or indirectly)
4. Does not hold any assets
5. In the last 12 months, has not seen a change in ownership
6. In the last 12 months, has not received or sent funds more than \$1,000

When must an entity file?

When to File?

- The reporting regime goes into effect on January 1, 2024.
- The due date for the initial report depends **on when the entity was created**.

Post January 1, 2024

Initial report is due within 30 calendar days of the date the entity is created.

Before January 1, 2024

Initial report is due no later than January 1, 2025.

What must an entity file?

Information to Report

Reports include information about:

1. The Reporting Company;
2. The Reporting Company's beneficial owners (BO); and
3. "Company applicants" (CA) who made the filings to create the entity.

Information on the Reporting Company

1. Full legal name
2. Any trade name or “doing business as” (d/b/a) name
3. Current address
4. Jurisdiction of formation
5. Federal taxpayer ID number

Information on (each) BO & CA

1. Full legal name
2. Date of birth
3. Current address (*residential for BO / Company for CA*)
4. Unique identifying number and issuing jurisdiction (e.g., U.S. passport or driver license)
5. Image of document with identifying number

** FinCEN Identifier: individuals & entities may apply for and obtain a FinCEN identifier, which can be included on filings in lieu of this information.*

Who is a “Beneficial Owner”?

Beneficial Owner

“Beneficial owner” of a Reporting Company is any individual who, **directly or indirectly**:

- Exercises “**substantial control**” over the Reporting Company

OR

- **Owns or controls 25%+ of ownership** in the Reporting Company.

How is “Substantial Control” defined?

“Substantial Control”

An individual exercises “substantial control” over a Reporting Company if the individual:

1. Serves as a senior officer of the Reporting Company
2. Has authority to appoint or remove any senior officer or a majority of the board;
3. Directs, determines, or has substantial influence over important decisions made by the Reporting Company (nature & scope of business, transfer of assets, reorganization, dissolution, major expenditures & investments, compensation of senior officers, and significant contracts); **OR**
4. Has any other form of substantial control over the Reporting Company (catch-all provision)

“Substantial Control”

- Individuals with control over the Reporting Company are “Beneficial Owners”, even if they have no ownership interests.
- Exercise of “substantial control” can be **direct or indirect** including as a trustee of a trust or similar arrangement, board representation, management contracts, rights associated with financing arrangements, or control over intermediary entities that exercise substantial control.

How is “Ownership Interest” defined & calculated?

Ownership Interests

- Equity, stock, or similar instrument
- Capital or profit interest in an entity
- Convertible instruments
- Put, call, straddle, or other options
- Any other instrument, contract, arrangement, understanding, relationship, or other mechanism used to establish ownership (catch-all provision)

Ownership Interests

Ownership or “Control” of ownership interests may be **direct or indirect**:

1. Actual ownership
2. Through other individuals acting as a nominee, intermediary, custodian, or agent on behalf of such individual
3. As party to a trust
4. Through ownership or control of intermediary entities, which then owned or control ownership interests in a Reporting Company
5. Through any contract, arrangement, understanding, relationship, or otherwise (catch-all provision)

Calculations of Ownership Interests

- Ownership interests of the individual is calculated **at the present time**, and **any options or similar interests are treated as exercised**.
- **Profits/Capital Interests**: Individual's capital and profit interests in Reporting Company is calculated as a percentage of the total outstanding capital and profit interests of the Reporting Company.
- **Corporations**: Percentage is calculated as the greater of:
 - Individual's total combined **voting power** as a percentage of outstanding voting power of all classes; **or**
 - Individual's total combined **value of ownership interests** as a percentage of total outstanding value of all classes of ownership interests.

Are there any exemptions to the definition of
“Beneficial Owners”?

Beneficial Owner Exemptions

- Minor children.
- 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).
- 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).
- An individual whose only interest in a Reporting Company is a future interest through a right of inheritance.
- A creditor of the Reporting Company.

Who is a “company applicant?”

Company Applicant

“Company Applicant” is one of two people:

1. The individual who **directly** files the document that creates the Reporting Company; **OR**
2. The individual who is **primarily responsible** for directing or controlling the filing of the Reporting Company. Typically, the company applicant may also be a beneficial owner of the company.

**Attorneys & paralegals may be considered “company applicants” if they file corporate formation documents on behalf of clients.*

*** Entities created prior to January 1, 2024, do not need to include information on company applicants.*

Once an initial report is filed, does it need to be updated?

Updated Reporting

Yes! An updated report must be filed within 30 calendar days after the change occurs.

Examples of changes that would require an updated report include:

1. Changes in who is a beneficial owner, e.g., due to transfers of ownership or death
2. Reporting Company becomes exempt from the reporting requirements
3. Transfers of ownership when a minor child reaches the age of majority
4. Changes to an identifying document previously submitted, e.g., changes in address

What are the penalties for non-compliance?

Penalties

- Failing to comply; **OR**
- Willfully providing false or fraudulent reports

Civil fines of \$500 a day for as long as the reports remain inaccurate.

Failure to comply may also subject the violators to the criminal penalties of a \$10,000 fine or 2 years in jail.

** Individual liability for any person who causes failure or is a senior officer at the time of failure*

*** Safe harbor from such civil and criminal liability for the submission of inaccurate information if the person who submitted the report voluntarily and promptly corrects the report within 90 days.*

Who can access the information once the report is filed?

Access to Reported Information

Reports filed with FinCEN will not be accessible to the public and are not subject to requests under the Freedom of Information Act.

The following government agencies will have access to the information upon requests:

1. Federal law enforcement agencies (national security, intelligence, & civil and criminal enforcement)
2. Treasury Department
3. State, local or tribal law enforcement agencies (if authorized by a court order)
4. Financial institutions for customer due diligence purposes, if authorized by the Reporting Company

What steps must you take now?

Next Steps

- Reports will be submitted via electronic reporting system that is currently under development. Launches on Jan. 1, 2024.
- In the meantime, existing Reporting Companies (i.e., created prior to Jan. 1, 2024) need to identify individuals who qualify as “beneficial owners” and “company applicants” in order to meet the reporting deadlines.
- **Keep in mind**: Any future changes to BO / CA will also need to be reported to FinCEN.

Disclaimer: There remain many grey areas, particularly with respect to what constitutes “substantial control” and responsibilities of the “company applicant”.

THANK YOU!



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