

## The Corporate Transparency Act and Proposed Rules - Most Small Companies Will Need to Report

by Elitsa Dimitrova

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### Background

On January 1, 2021, Congress enacted the Corporate Transparency Act (“CTA”). The CTA requires that certain “reporting companies” report their (i) beneficial ownership information (“BOI”) as well as (ii) “company applicant” to the Financial Crimes Enforcement Network (“FinCEN”), an agency of the Department of Treasury. Congress delegated the rulemaking for implementing the CTA to FinCEN.

On December 8, 2021, FinCEN published 55 pages of proposed rules relating to BOI reporting requirements under the CTA (“BOI Proposed Rules”). The BOI Proposed Rules invite comments from the public regarding their content and in response to specific questions. Written comments may be submitted on or before February 7, 2022. Upon review of the received comments, FinCEN will finalize and publish the final BOI rules and, upon such publication, they will be in force and the deadlines for reporting will commence as provided in the final BOI rules. While the final BOI rules will not come into effect for a few more months, the BOI Proposed Rules, as summarized below, will likely be close to the final ones and thus merit review.

A vast number of entities that are organized or registered in the U.S., whether domestic or foreign, will be subject to CTA’s reporting requirements. Reporting under the CTA “is intended to help prevent and combat money laundering, terrorist, financing, tax fraud, and other illicit activity.” The intent of the CTA is that its reporting rules be broadly applied and exemptions from reporting be limited. FinCEN reasons that, according to reports, more anonymous corporations are formed in the United States than in any other jurisdiction. In 2011, the World Bank assessed that 10 times more legal entities were formed in the United States than in all 41 tax haven jurisdictions combined.

Importantly, in addition to reporting obligations for millions of companies, Section 6403 of the CTA also amends the Bank Secrecy Act (“BSA”). The BSA’s existing customer due diligence requirements rule for financial institutions at 31 CFR 1010.230 (“CDD Rule”) will be revised and rescinded once FinCEN completes its rulemaking such that FinCEN may also disclose reported BOI to financial institutions for their compliance purposes, with the consent of the reporting company. While the general requirement under 31 CFR 1010.230(a) that financial institutions identify and verify the beneficial owners of legal entity customers will remain unchanged, the CTA does direct FinCEN to rescind the requirements for financial institutions under 31 CFR 1010.230(b)-(j). Thus, it is likely that financial institutions will in the future obtain their customer due diligence through FinCEN.

Thus, in addition to the BOI Proposed Rules, FinCEN will be issuing and seeking comments to two more sets of rulemakings under Section 6403: 1) to implement the statute’s protocols for access to and disclosure of BOI; and 2) to revise the existing CDD Rule consistent with the requirements of section 6403(d) of the CTA.

### CTA & FinCEN Proposed Rules Highlights

- CTA is equal to a seismic shift in U.S. corporate law.
- Under the CTA, most active small companies in unregulated industries in the U.S. will need to report to FinCEN information regarding certain substantial beneficial owners and company applicants.
- Large operating companies and companies in heavily regulated industries are exempt from reporting.
- Existing companies will have one year to comply while newly created entities will need to report within 14 calendar days of creation/registration.
- Government agencies and regulators will be able to access the information for national security, intelligence, or law enforcement activities.
- Banks and other financial institutions will be able to access the information, with consent of their customers, to aid in their customer due diligence.

### Takeaways

- Evaluate whether your company will be subject to reporting.
- If reporting is required, alert current beneficial owners that request for personal information will be forthcoming.
- Update corporate governance documents where applicable to ensure beneficial owners comply with reporting requirements.
- Prepare to be required to report some time in 2022 for newly created/registered entities and in 2023 for existing businesses.

## Reporting Companies

The Proposed BOI Rules define a reporting company as any entity that requires a filing with a state or similar entity for its creation/registration. The CTA reporting requirements target smaller, loosely regulated companies; the more heavily regulated larger companies are exempt from reporting. A general rule of thumb of the CTA is that, unless an entity falls within an exemption (a total of 23), it is a reporting company. "Reporting companies" include both domestic entities and foreign companies that are registered to do business in the U.S. The Proposed BOI Rules estimate that there will be over 25 million reporting companies.

### Exemptions

Although FinCEN was authorized to add new exemptions from reporting, it did not do so in the Proposed BOI Rules. Thus, generally, the exempted entities are: issuers of registered securities or publicly reporting companies, domestic governmental authorities, banks, domestic credit unions, depository institution holding companies, money transmitting businesses, brokers or dealers in securities, securities exchange or clearing agencies, other Securities Exchange Act of 1934 entities, registered investment companies and advisers, venture capital fund advisers, insurance companies, state licensed insurance producers, Commodity Exchange Act registered entities, accounting firms, public utilities, financial market utilities, pooled investment vehicles, tax exempt entities, entities assisting tax exempt entities, large operating companies (with more than 20 full-time employees, \$5,000,000 in gross consolidated U.S. sales reported to the IRS, and genuine operating presence in a physical office in the U.S.), subsidiaries of certain exempt entities, and dormant entities in existence on January 1, 2021 that hold no assets and have paid or received less than \$1,000 during any one-year review period.

## Beneficial Owners and Company Applicants

Under the Proposed BOI Rules, the reporting companies are required to report: 1) the beneficial owners of the entity; and 2) the individuals who have filed to create or register the entity.

A "beneficial owner" is any individual who meets at least one of two criteria:

- A. Exercising substantial control (whether direct or indirect) over the reporting company. Some examples include persons serving as senior officers, with an ability to appoint senior officers or elect directors or with an ability to influence important matters at the reporting company.
- B. Owning or controlling an aggregate of at least 25% of the ownership interest of the reporting company. This prong is also extremely broad, tracks the "securities" definition used by the SEC and includes debt instruments that can be converted to equity, such as notes and warrants and any other equity kickers. Joint ownership or control of interests, parents or legal guardians, beneficiaries' interests, trustees, and trust grantors and settlors that retain the ability to dispose of the assets or to revoke the trust all fall within the reportable interests.

Reporting companies should report all individuals that meet the criteria (as opposed to one person in substantial control per the CDD Rule). Nominees, agents, employees, inheritors, other intermediaries, minors and "pure" creditors need not be reported. The CTA's intent is that actual, rather than, apparent BOI is reported.

"Company applicant" is the individual who files the document that forms or registers the entity, and includes anyone who directs or controls the filing of the document by another.

## Information to Report

1. Identify the reporting company (name and any d/b/a names);
2. Business street address – please note that business street address does not mean an address of an agent or a third-party nominee;
3. Jurisdiction of formation or registration;
4. Company unique identification number (TIN (including an EIN)), a Dun & Bradstreet Data Universal Numbering System (DUNS) number, a Legal Entity Identifier (LEI), or FinCEN Identifier (see **FinCEN Identifier** section on how to apply for one);
5. Each beneficial owner's full legal name, date of birth, current residential street address, unique identifying number from an acceptable identification document or a FinCEN Identifier;
6. Each company applicant's full legal name, date of birth, current business address (for corporate or formation agents) and residential street address that the individual uses for tax residency purposes (for all other company applicants), unique identifying number from an acceptable identification document or, if this information has already been provided to FinCEN, a FinCEN Identifier; and
7. Scanned copy of the identification document from which the unique identifying number of the beneficial owner or company applicant is obtained, in connection with reporting that unique number.

The person filing the report will need to certify that it is accurate and complete.

Instead of personal information of an individual or an entity, the FinCEN Identifier may be reported to FinCEN. For corporate and formation agents and repeat investors, it will probably make sense that they obtain the FinCEN Identifier rather than repeatedly providing such information.

## Report Due Dates

1. within 14 calendar days of the company being created or registered;
2. one year after the final rules come into effect for existing entities;
3. 30 calendar days after any change of information already reported or at the time a company is no longer exempt from reporting; and
4. within 14 calendar days of discovery of errors or of when an error should have been known.

FinCEN is yet to provide information on the means by which reporting will be done.

## FinCEN Identifier

An individual may obtain a FinCEN Identifier by providing FinCEN with the information that the individual would otherwise have to provide to a reporting company if the individual were a beneficial owner or company applicant; an entity can obtain a FinCEN Identifier from FinCEN when it submits a filing as a reporting company or at any time thereafter.

## Special Rules

1. Exempt entities that are beneficial owners simply report the name of the exempt entity.
2. Reporting companies that become exempt will need to report that change.
3. Parent or legal guardians need to report that they report in such capacity.
4. Foreign pooled investment vehicles must report the BOI of the individuals exercising substantial control.
5. If a company applicant died before they had to report, the reporting company can report that fact along with information relating to the deceased person.
6. In case of a beneficial owner's death, changes should be reported at the time the estate of a deceased beneficial owner is settled.

## Storing and Accessing BOI Information

FinCEN is required to maintain the information that it collects under the CTA in a "confidential, secure, and nonpublic database." Unlike similar databases in other countries, such as the U.K., the information will not be available to the public. FinCEN is authorized to share this BOI with certain government agencies, financial institutions, and regulators, subject to appropriate protocols in furtherance of national security, intelligence, or law enforcement activity. State, local, and tribal law enforcement agencies require "a court of competent jurisdiction" to authorize them to seek BOI as part of a criminal or civil investigation. Foreign government access is limited to foreign law enforcement agencies, prosecutors, and judges in specified circumstances.

## Reporting Violations

Willful violators of the CTA may be liable for a civil penalty of up to \$500 for each day a violation continues or has not been remedied, and may be fined up to \$10,000 and imprisoned for up to two years, or both, for a criminal violation.

**If you have any questions about the CTA or your company's reporting requirements, please reach out to Elitsa Dimitrova at (312) 360-6839 or [edimitrova@freeborn.com](mailto:edimitrova@freeborn.com) or another member of [Freeborn's Corporate Practice Group](#).**

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Elitsa's practice is focused on private equity and venture capital, mergers and acquisitions, private placements and securities, and employee benefits and executive compensation. Elitsa frequently advises lead investors in seed, convertible note and alternative investments in the fintech, biotech, software, transportation and cannabis spaces. As part of the M&A Team for First-Time Sellers®, Elitsa regularly counsels privately held, middle-market companies in exit transactions. She also regularly represents clients in their buy-side M&A transactions and also consults clients as it relates to general corporate governance matters.

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