

## Action Required: Corporate Transparency Act Reporting Is Here

November 8, 2023

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***This advisory provides a general summary of the Corporate Transparency Act<sup>1</sup> and its requirements and is not intended to, and does not, provide legal, compliance or other advice to any individual or entity. Please reach out to your Katten Muchin Rosenman LLP contact for assistance regarding the application of the Corporate Transparency Act to your specific situation.***

Final rules implementing the beneficial ownership reporting requirements of the Corporate Transparency Act (CTA) become effective on **January 1, 2024**,<sup>2</sup> and require a Reporting Company to disclose specific information regarding itself, its Beneficial Owners, and its Company Applicants to the US Treasury Department's Financial Crimes Enforcement Network (FinCEN). The stated purpose of the CTA is to combat the use of shell companies for illicit activities such as money laundering, terrorism financing and other illegal activities.

### High-Level Overview

The CTA will require, beginning on January 1, 2024, entities formed or registered to do business in the United States (unless an exemption applies) to report to FinCEN, among other things, Beneficial Ownership Information for each of its Beneficial Owners and to promptly update the Beneficial Ownership Information for any changes. Compliance will require a fact-specific inquiry into applicable CTA requirements, company structures, control features and more. Substantial time and effort may be required to analyze, obtain and report the requisite information.

### Reporting Companies

The first step in CTA analysis is to determine whether an entity is a Reporting Company. A "Reporting Company" means any entity (whether a corporation, limited liability company or other entity type) that is (a) created by the filing of a document with the secretary of state or a similar office under the law of a State or Indian tribe or (b) is formed under the laws of a foreign country and registered to do business in the United States by the filing of a document with a secretary of state or a similar office under the laws of a State or Indian tribe. For purposes of the CTA, "State" is broadly defined to include any State of the United States, the District of Columbia, the Commonwealth of Puerto Rico, the Commonwealth of the Northern Mariana Islands, American Samoa, Guam, the United States Virgin Islands, and any other commonwealth, territory or possession of the United States.<sup>3</sup> Note that CTA analysis needs to be performed for each entity within a company structure.

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<sup>1</sup> 31 U.S.C. §5336 et seq.

<sup>2</sup> 31 CFR 1010.380.

<sup>3</sup> 31 U.S.C. §5336(a)(12).

The next step is to identify any applicable exemptions from Reporting Company status for each entity within a company structure. Currently, CTA rules provide 23 exemptions, most of which involve entities already subject to regulation by governmental authorities (e.g., certain Securities and Exchange Commission (SEC) registered issuers (public companies), banks, broker-dealers and investment advisers). One potentially significant exemption is the “large operating company” exemption, which applies to an entity that (a) directly (i.e., not on a consolidated or affiliated basis) employs more than 20 employees on a full-time basis in the United States; (b) filed in the previous year a federal income tax or information return in the United States demonstrating more than \$5,000,000 in gross receipts or sales in the aggregate (on a consolidated basis, if applicable); and (c) has an operating presence at a physical office within the United States. Entities, the ownership interests of which are controlled or wholly owned, directly or indirectly, by certain types of exempt entities (i.e., exempt entities other than money services business, pooled investment vehicles or entities assisting a tax-exempt entity), are also exempt from CTA reporting requirements (but the scope of this exemption is not clear). A description of all 23 exemptions is set forth in Appendix A of this advisory.

**Practical Points:** Note that there is no exemption for parent companies (for example, a holding company that owns only exempt entities). Accordingly, even though some entities in a company structure may qualify for one or more Reporting Company exemptions, other entities in the structure may nonetheless have reporting obligations.<sup>4</sup> Finally, entities that are only partially controlled or owned by exempt entities may not be themselves exempt entities.

## Beneficial Owners

After determining that an entity meets the definition of a Reporting Company and is not exempt from reporting obligations, the third step is to identify its Beneficial Owners. A “Beneficial Owner” of a Reporting Company is any **individual** (i.e., natural person) who, **directly or indirectly**, either (i) exercises substantial control over the Reporting Company (the “Substantial Control Test”) or (ii) owns or controls at least 25 percent of the ownership interests of the Reporting Company (the “Ownership Test”). There is no upper limit on the number of reportable Beneficial Owners of a Reporting Company under the CTA.

### The Substantial Control Test

An individual exercises substantial control over a Reporting Company if such individual:<sup>5</sup>

1. serves as a Senior Officer (i.e., any individual holding the position or exercising the authority of a President, Chief Financial Officer, General Counsel, Chief Executive Officer, Chief Operating Officer or any other officer, regardless of official title, who performs a similar function) of such Reporting Company;
2. has authority over the appointment or removal of any Senior Officer or a majority of the board of directors (or similar body) of such Reporting Company;
3. directs, determines, or has substantial influence over important decisions<sup>6</sup> made by such Reporting Company; or

<sup>4</sup> Generally, the interposition of one or more exempt entities in a chain of entity ownership will not shield ultimate Beneficial Owners from the Beneficial Ownership Information reporting obligations of Reporting Companies down the chain. However, under and subject to the limitations of 31 CFR 1010.380(b)(2)(i), if an individual is the Beneficial Owner of a Reporting Company **exclusively** due to ownership interests the Beneficial Owner holds in exempt entities (that is, exempt entities that, in turn, have an ownership interest in a Reporting Company), the related report may include the names of such exempt entities in lieu of personal information about such Beneficial Owner.

<sup>5</sup> 31 CFR 1010.380(d)(1)(i).

<sup>6</sup> Important decisions include “decisions regarding (1) the nature, scope, and attributes of the business of the reporting company, including the sale, lease, mortgage, or other transfer of any principal assets of the reporting company; (2) the reorganization, dissolution, or merger of the reporting company; (3) major expenditures or investments, issuances of any equity, incurrence of any significant debt, or approval of the operating budget of the reporting company; (4) the selection or termination of business lines or ventures, or geographic focus, of the reporting company; (5) compensation schemes and incentive programs for senior officers; (6) the entry into or termination, or the fulfillment or non-fulfillment, of significant contracts; or (7) 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.” 31 CFR 1010.380(d)(1)(i)(C).

4. has any other form of substantial control over such Reporting Company.

Note that substantial control may be exercised directly or indirectly, and the applicable Reporting Company is required to assess substantial control up its chain of ownership.<sup>7</sup>

### The Ownership Test

As noted above, an individual who owns or controls at least 25 percent of the “ownership interests” of a Reporting Company is a Beneficial Owner of such Reporting Company. As used in the CTA, ownership interest is broadly construed to include any equity, stock, or similar interest (whether such interest confers voting rights or not), any capital or profit interest, any instrument convertible into ownership interest, any option to purchase or sell ownership interests, or “any other instrument, contract, arrangement, understanding, relationship, or mechanism used to establish ownership.”<sup>8</sup> For purposes of determining whether the 25 percent threshold has been met with respect to an individual, all (a) options or similar interests are deemed exercised, and (b) ownership interests are aggregated.

For purposes of the Ownership Test, an individual may directly or indirectly control an ownership interest through a contract or other relationship, including joint ownership with one or more other persons of an undivided interest in such ownership interest, through another individual acting as a nominee, intermediary, custodian, or agent on behalf of such individual or through ownership or control of intermediary entities.<sup>9</sup> With respect to a trust that is deemed a Beneficial Owner under the Ownership Test, the following individuals are deemed a Beneficial Owner:

1. a trustee of the trust or other individual who has authority to dispose of trust assets;
2. a beneficiary of the trust, if (a) such beneficiary is the sole permissible recipient of income and principal from the trust or (b) if such beneficiary has the right to demand a distribution of or withdraw substantially all of the assets from the trust; and/or
3. a grantor or settlor of a trust, if such individual has the right to revoke the trust or otherwise withdraw the assets of the trust.<sup>10</sup>

### Exceptions

Notwithstanding the Ownership Test, the CTA explicitly excludes each of the following individuals from the definition of Beneficial Owner:<sup>11</sup>

1. a minor child (provided that the Reporting Company reports Beneficial Ownership Information of the parent or legal guardian of such minor child);
2. an individual acting as a nominee, intermediary, custodian, or agent on behalf of another individual (provided that the Reporting Company reports Beneficial Ownership Information for the individual on behalf of whom the nominee, intermediary, custodian or agent is acting);
3. an employee of a Reporting Company, acting solely as an employee, whose substantial control over or economic benefits from such entity is derived solely from the employment status of the employee (provided that such person is not a Senior Officer);

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<sup>7</sup> Substantial Control may be exercised over a Reporting Company “through: (A) board representation; (B) ownership or control of a majority of the voting power or voting rights of the reporting company; (C) rights associated with any financing arrangement or interest in a company; (D) control over one or more intermediary entities that separately or collectively exercise substantial control over a reporting company; (E) arrangements or financial or business relationships, whether formal or informal, with other individuals or entities acting as nominees; or (F) any other contract, arrangement, understanding, relationship, or otherwise.” 31 CFR 1010.380(d)(1)(ii).

<sup>8</sup> 31 CFR 1010.380(d)(2)(i).

<sup>9</sup> 31 CFR 1010.380(d)(2)(ii).

<sup>10</sup> 31 CFR 1010.380(d)(2)(ii)(C).

<sup>11</sup> 31 CFR 1010.380(d)(3).

4. an individual with only a future interest through a right of inheritance; and
5. a creditor of a Reporting Company whose interests are limited to the repayment of a pre-determined sum of money and whose only rights with respect to the Reporting Company are intended to secure the right to receive repayment or enhance the likelihood of repayment.

## Company Applicant

In addition to information about Beneficial Owners, the CTA requires certain information be filed regarding the “*Company Applicants*” of a Reporting Company. There are two types of Company Applicants. A “Category 1 – Direct Filer” is an individual who directly files the document that creates the entity (if a domestic Reporting Company) or registers the entity to do business in the US (if a foreign Reporting Company). A “Category 2 – Directs or Controls the Filing Action” is an individual who is primarily responsible for directing or controlling such filing. If advisors are engaged to form a Reporting Company on behalf of a client, a Company Applicant may be an attorney, paralegal or an employee at a business formation service.<sup>12</sup>

**Practical Points:** While there may be multiple individuals who can meet the definition of a Company Applicant, only two individuals will be reported by the Reporting Company to FinCEN. Reporting Companies formed or registered to do business in the United States prior to January 1, 2024, need not provide any information regarding Company Applicants. Reporting Companies formed or registered to do business in the United States on or after January 1, 2024, will have to provide information about Company Applicants but will not be required to update such information (unless the initial information provided was inaccurate).

## Reporting Company, Beneficial Ownership and Company Applicant Information to Be Reported

A Reporting Company will be required to report the following “*Beneficial Ownership Information*” to FinCEN:<sup>13</sup>

- A. The Reporting Company must report its:
  - i. full legal name;
  - ii. trade names or d/b/a names;
  - iii. principal place of business (or, in the case of a foreign Reporting Company, its primary location in the United States);
  - iv. State, tribal, or foreign jurisdiction of formation (and in the case of a foreign Reporting Company, the State or tribal jurisdiction where it first registers); and
  - v. unique taxpayer ID number (which for a domestic entity must be a TIN (including an Employer Identification Number (EIN)); and for a foreign entity may be a similar, foreign unique identifier if the entity has no US TIN).
- B. The Reporting Company must report the following information regarding its Beneficial Owners and, for entities formed or registered after January 1, 2024, its Company Applicants:
  - i. the full name of such individual;
  - ii. the date of birth of such individual;

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<sup>12</sup> See Beneficial Ownership Information Reporting Requirements, 87 Fed. Reg. 59536 (September 30, 2022) (“In many cases, company applicants may be employed by a business formation service or law firm. For example, there may be an attorney primarily responsible for overseeing the preparation and filing of incorporation documents and a paralegal who directly files them with a state office to create the reporting company. In this example, this reporting company would report two company applicants – the attorney and the paralegal – but additional individuals who may be indirectly involved in the filing would not need to be reported”).

<sup>13</sup> 31 CFR 1010.380(b).

- iii. the current address (residential: for Beneficial Owners; business: for Company Applicants who form or register entities in the course of their business) of such individual;
- iv. a unique identifying number for such individual from an unexpired US passport number, driver's license number or other specified documents; and
- v. an image of the document from which such unique ID number was obtained.

**Practical Point:** Individuals and business entities may obtain a FinCEN identifier, which is a unique identifying number assigned by FinCEN. A Beneficial Owner can supply the individual's FinCEN identifier to a Reporting Company in lieu of supplying the information set forth above<sup>14</sup> and the Reporting Company will report that FinCEN identifier in its filing.

## Reporting Requirements

Reporting Companies formed or registered to do business in the United States prior to January 1, 2024 will be required to submit Beneficial Ownership Information to FinCEN not later than January 1, 2025.<sup>15</sup> Reporting Companies formed or registered to do business in the United States on or after January 1, 2024 will be required to submit Beneficial Ownership Information to FinCEN within 30 days of formation or registration.<sup>16</sup> We note that FinCEN has proposed to extend the 30-day period to 90 days for entities formed or first registered to do business in the United States during calendar year 2024. As of this writing, such amendment has not yet been adopted.

To the extent a Reporting Company's Beneficial Ownership Information changes or it no longer qualifies for an exemption, it must file an updated report (or initial report, in the case of an entity that loses its exemption status) with FinCEN within 30 calendar days following such change. As a result, Reporting Companies are responsible for monitoring all manner of changes. For example, if a Beneficial Owner marries, there may be an initial 30-day update period triggered by a change of residence and another update period triggered by a surname change.

**Practical Point:** To the extent a Reporting Company submits a Beneficial Owner's FinCEN identifier, the Reporting Company will not be required to submit an updated report to reflect changes to such Beneficial Owner's reportable information; rather, the burden will rest solely with the Beneficial Owner to update such person's information with FinCEN within 30 days following any change.<sup>17</sup> However, even if FinCEN identifiers are used, the Reporting Company will still need to file updated reports to reflect any addition of new Beneficial Owners and/or removal of existing Beneficial Owners.

## Access

The information collected by FinCEN on the Beneficial Ownership Secure System (i.e., the database wherein CTA reports will be stored) (BOSS) will not be publicly accessible. As set forth in FinCEN's December 16, 2022, proposed access rules, the following will have access to Beneficial Ownership Information: (a) United States federal agencies engaged in national security, intelligence or law enforcement activity for information to be used in furtherance of such activity; (b) a State, local or tribal law enforcement agency for use in a criminal or civil investigation (if a court of competent jurisdiction has authorized such agency to seek such Beneficial Ownership Information); (c) upon a request from a federal agency on behalf of a law enforcement agency, prosecutor, or judge of another country, on behalf of a foreign central authority or foreign competent authority, if the request is made under an applicable international treaty, agreement or convention or, if the request is not made under an international treaty, agreement, or convention, the request is an official request by a law enforcement, judicial,

<sup>14</sup> 31 CFR 1010.380(b)(4).

<sup>15</sup> 31 CFR 1010.380(a)(1)(iii).

<sup>16</sup> 31 CFR 1010.380(a)(1)(i).

<sup>17</sup> 31 CFR 1010.380(b)(4)(iii).

or prosecutorial authority of a trusted foreign country; (d) a financial institution (provided that the applicable Reporting Company has consented to such access), which financial institution is subject to customer due diligence requirements under applicable law for information to be used in facilitating such compliance; and (e) US Department of Treasury officers and employees who require Beneficial Ownership Information in connection with their official duties (including tax administration). As of this writing, access protocols have not been finalized.

## Penalties<sup>18</sup>

It is unlawful for any person to willfully provide (or attempt to provide) false or fraudulent Beneficial Ownership Information or to willfully fail to report complete or updated Beneficial Ownership Information. The CTA provides for civil and criminal penalties for such violations, including a civil penalty of up to \$500 per day and, a fine of not more than \$10,000 and/or imprisonment for up to two years.

## Parting Thoughts

Despite the fact that FinCEN has not yet finalized all CTA rules, the BOSS, or the CTA reporting application, barring any unexpected action, CTA beneficial ownership reporting rules will be live commencing on January 1, 2024. Business owners, asset managers, institutional investors and managers will be well served to promptly commence initial CTA reviews in order to identify their Reporting Companies and Beneficial Owners. Additionally, some states are considering implementing similar transparency rules, which, in at least one instance, includes a publicly accessible database.

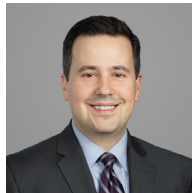
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## CONTACTS

For more information or assistance with your CTA analysis, please contact your Katten attorney.



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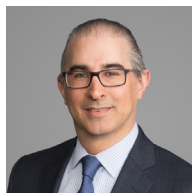
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<sup>18</sup> 31 U.S.C. §5336(h).

# Appendix A

## Exemptions to the Definition of a Reporting Company

Each of the following is exempted from the definition of a Reporting Company pursuant to 31 CFR 1010.380(c)(2).

1. **Securities Reporting Issuer.** (A) An issuer of a class of securities registered under Section 12 of the Securities Exchange Act of 1934; or (B) required to file supplementary and periodic information under Section 15(d) of the Securities Exchange Act of 1934.
2. **Governmental Authority.** Any entity that: (A) is established under the laws of the United States, an Indian tribe, a State, or a political subdivision of a State, or under an interstate compact between two or more States; and (B) exercises governmental authority on behalf of the United States or any such Indian tribe, State, or political subdivision.
3. **Bank.** Any bank, as defined in (A) Section 3 of the Federal Deposit Insurance Act; (B) Section 2(a) of the Investment Company Act of 1940; or (C) Section 202(a) of the Investment Advisers Act of 1940 (i.e., certain private trust companies).
4. **Credit Union.** Any federal credit union or State credit union, as those terms are defined in Section 101 of the Federal Credit Union Act.
5. **Depository Institution Holding Company.** Any bank holding company as defined in Section 2 of the Bank Holding Company Act of 1956, or any savings and loan holding company as defined in Section 10(a) of the Home Owners' Loan Act.
6. **Money Services Business.** Any money transmitting business registered with FinCEN under 31 U.S.C. 5330 and any money services business registered with FinCEN under 31 CFR 1022.380.
7. **Broker or Dealer in Securities.** Any broker or dealer, as those terms are defined in Section 3 of the Securities Exchange Act of 1934, that is registered under Section 15 of that Act.
8. **Securities Exchange or Clearing Agency.** Any exchange or clearing agency, as those terms are defined in Section 3 of the Securities Exchange Act of 1934, that is registered under Sections 6 or 17A of the Securities Exchange Act of 1934.
9. **Other Exchange Act Registered Entity.** Any other entity not described in items 1, 7, or 8 above that is registered with the Securities and Exchange Commission under the Securities Exchange Act of 1934.
10. **Investment Company or Investment Adviser.** Any entity that is: (A) an investment company as defined in Section 3 of the Investment Company Act of 1940, or is an investment adviser as defined in Section 202 of the Investment Advisers Act of 1940; and (B) registered with the Securities and Exchange Commission under the Investment Company Act of 1940 or the Investment Advisers Act of 1940.
11. **Venture Capital Fund Adviser.** Any investment adviser that: (A) is described in Section 203(l) of the Investment Advisers Act of 1940; and (B) has filed Item 10, Schedule A, and Schedule B of Part 1A of Form ADV, or any successor thereto, with the Securities and Exchange Commission.

12. **Insurance Company.** Any insurance company as defined in Section 2 of the Investment Company Act of 1940.
13. **State-Licensed Insurance Producer.** Any entity that: (A) is an insurance producer that is authorized by a State and subject to supervision by the insurance commissioner or a similar official or agency of a State; and (B) has an operating presence at a physical office within the United States.
14. **Commodity Exchange Act Registered Entity.** Any entity that: is a registered entity as defined in Section 1a of the Commodity Exchange Act or is: (A) a futures commission merchant, introducing broker, swap dealer, major swap participant, commodity pool operator, or commodity trading advisor, each as defined in Section 1a of the Commodity Exchange Act, or a retail foreign exchange dealer as described in Section 2(c)(2)(B) of the Commodity Exchange Act; and (B) registered with the Commodity Futures Trading Commission under the Commodity Exchange Act.
15. **Accounting Firm.** Any public accounting firm registered in accordance with Section 102 of the Sarbanes-Oxley Act of 2002.
16. **Public Utility.** Any entity that is a regulated public utility as defined in 26 U.S.C. 7701(a)(33)(A) that provides telecommunications services, electrical power, natural gas, or water and sewer services within the United States.
17. **Financial Market Utility.** Any financial market utility designated by the Financial Stability Oversight Council under Section 804 of the Payment, Clearing, and Settlement Supervision Act of 2010.
18. **Pooled Investment Vehicle.**<sup>1</sup> Any pooled investment vehicle that is operated or advised by a person described in items 3, 4, 7, 10, or 11 above.
19. **Tax-Exempt Entity.** Any entity that is: (A) an organization that is described in Section 501(c) of the Internal Revenue Code of 1986 (the “Code”) (determined without regard to Section 508(a) of the Code) and exempt from tax under Section 501(a) of the Code, except that in the case of any such organization that ceases to be described in Section 501(c) and exempt from tax under Section 501(a), such organization shall be considered to continue to be described in this item for the 180-day period beginning on the date of the loss of such tax-exempt status; (B) a political organization, as defined in section 527(e)(1) of the Code, that is exempt from tax under Section 527(a) of the Code; or (C) a trust described in Paragraph (1) or (2) of Section 4947(a) of the Code.
20. **Entity Assisting a Tax-Exempt Entity.** Any entity that: (A) operates exclusively to provide financial assistance to, or hold governance rights over, any entity described in Item 19; (B) is a United States person; (C) is beneficially owned or controlled exclusively by one or more United States persons that are United States citizens or lawfully admitted for permanent residence; and (D) 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.
21. **Large Operating Company.** Any entity that: (A) employs more than 20 full-time employees in the United States, with “full-time employee in the United States” having the meaning provided in 26 CFR 54.4980H-1(a) and 54.4980H-3, except that the term “United States” as used in 26 CFR 54.4980H-1(a) and 54.4980H-3 has the meaning provided in § 1010.100 (hhh); (B) has an operating presence at a physical office within the United States; and (C) filed a federal income

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<sup>1</sup> Pooled Investment Vehicle has the meaning set forth in 31 CFR 1010.380(f)(7).



tax or information return in the United States for the previous year demonstrating more than \$5,000,000 in gross receipts or sales, as reported as gross receipts or sales (net of returns and allowances) on the entity's IRS Form 1120, consolidated IRS Form 1120, IRS Form 1120-S, IRS Form 1065, or other applicable IRS form, excluding gross receipts or sales from sources outside the United States, as determined under federal income tax principles. For an entity that is part of an affiliated group of corporations within the meaning of 26 U.S.C. 1504 that filed a consolidated return, the applicable amount shall be the amount reported on the consolidated return for such group.

22. **Subsidiary of Certain Exempt Entities.** Any entity whose ownership interests are controlled or wholly owned, directly or indirectly, by one or more entities described in items 1, 2, 3, 4, 5, 7, 8, 9, 10, 11, 12, 13, 14, 15, 16, 17, 19, or 21.
23. **Inactive Entity.** Any entity that: (A) was in existence on or before January 1, 2020; (B) is not engaged in active business; (C) is not owned by a foreign person, whether directly or indirectly, wholly or partially; (D) has not experienced any change in ownership in the preceding 12-month period; (E) has not sent or received any funds in an amount greater than \$1,000, either directly or through any financial account in which the entity or any affiliate of the entity had an interest, in the preceding 12-month period; and (F) does not otherwise hold any kind or type of assets, whether in the United States or abroad, including any ownership interest in any corporation, limited liability company or other similar entity.

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