

Overview: Corporate Transparency Act

October 14, 2024



Introduction

- The Corporate Transparency Act (**CTA**), **effective January 1, 2024 (Effective Date)**, is intended to aid law enforcement in combatting illicit activity conducted through anonymous shell companies.
- It requires certain privately held entities to report beneficial ownership information (**BOI**) to the US Treasury Department's Financial Crimes Enforcement Network (**FinCEN**).
- The reporting requirements are intended to apply broadly and impact **small companies**, many of whom have never made federal filings other than those with the Internal Revenue Service.
- Many larger or otherwise highly regulated entities are exempt from the CTA.

Overview

This presentation discusses:

- The entities that are reporting companies under the CTA and must submit a BOI report to FinCEN.
- Exemptions from the CTA's reporting requirements.
- The information that a reporting company must report to FinCEN.
- When initial reports and changes to reports must be filed.
- The penalties for failing to comply with the reporting requirements.
- The individuals who are considered beneficial owners under the CTA.
- Steps to take to comply with the CTA.

Reporting Companies

Reporting Companies Under the CTA

- Both domestic and foreign entities can be reporting companies under the CTA.
- **Domestic reporting companies** are corporations, limited liability companies (**LLCs**), or other entities created by filing a document with a secretary of state (**SOS**) or any similar office under the law of either:
 - A state of the US, the District of Columbia, the Commonwealth of Puerto Rico, the Commonwealth of the Northern Mariana Islands, American Samoa, Guam, the US Virgin Islands, or any other commonwealth, territory, or possession of the US.
 - An Indian tribe.

Reporting Companies Under the CTA (cont'd)

- **Foreign reporting companies** are non-US entities that are:
 - Corporations, LLCs, or other entities.
 - Formed under the law of a foreign country.
 - Registered to do business in any state or tribal jurisdiction by the filing of a document with a SOS or any similar office under the law of a state or Indian tribe.

Exemptions from the CTA's Reporting Requirements

The CTA excludes from the reporting company definition **23 categories** of entities, including:

- Large operating companies.
- Public companies.
- Inactive entities.
- Federally registered investment companies or advisers.
- Venture capital fund advisers.
- Certain pooled investment vehicles.
- Insurance companies and producers.
- Public accounting firms.
- Tax-exempt entities and entities assisting tax-exempt entities.
- Governmental authorities.
- Subsidiaries of certain exempt entities.

Exemptions from the CTA's Reporting Requirements (cont'd)

The CTA also excludes certain other **highly regulated entities**, including:

- Banks, bank holding companies, and savings and loan holding companies.
- Credit unions.
- Money transmitting businesses and money services businesses.
- Securities brokers or dealers.
- Securities exchange or clearing agencies.
- Other entities not described in the bullets above that are registered with the SEC under the Exchange Act.
- Regulated public utilities.
- Financial market utilities.

Information a Reporting Company Must Report to FinCEN

A reporting company must disclose information about:

- Its **individual beneficial owners** and, for entities created or registered on or after the Effective Date, its **company applicants**. A company applicant is an **individual** who either:
 - Directly files the document that creates a domestic reporting company or first registers a foreign reporting company to do business in the US.
 - Is primarily responsible for directing or controlling the filing of the relevant document by another, if more than one individual is involved in the filing.
- **Itself.**

Information a Reporting Company Must Report to FinCEN (cont'd)

As to **each individual beneficial owner and company applicant**, a reporting company **must disclose**:

- Their full legal name.
- Their date of birth.
- Their complete current address.
- A unique identifying number.
- An image of the document with the unique identifying number.

Information a Reporting Company Must Report to FinCEN (cont'd)

The **unique identifying number** must come from one of the following **non-expired documents** issued to the individual:

- A US passport issued by the US government.
- A state, local government, or Indian tribal identification document issued to identify the individual.
- A state-issued driver's license.
- If an individual does not have one of the above, a passport issued to them by a foreign government.

Information a Reporting Company Must Report to FinCEN (cont'd)

- Instead of the specific information about each beneficial owner, a reporting company can report an individual's FinCEN identifier (**FinCEN ID**).
- As of the Effective Date, an individual may obtain a FinCEN ID by giving to FinCEN the same information a reporting company must provide regarding its beneficial owners.
- A reporting company may also obtain a FinCEN ID by checking a box on its BOI report when it submits the report.

Information a Reporting Company Must Report to FinCEN (cont'd)

A reporting company **must report** the following **about itself**:

- Full legal name, any trade names, and any doing business as (d/b/a) or trading as (t/a) names under which it conducts business, whether formally registered or not.
- Complete current address.
- Its state, tribal, or foreign jurisdiction of formation and, for a foreign reporting company, the state or tribal jurisdiction where it first registered in the US.
- Its IRS taxpayer identification number, including an employer identification number.

When a Reporting Company Must File Its Initial Report

A reporting company that is created or becomes a foreign reporting company:

- **Before the Effective Date** has until **January 1, 2025**, to file its initial BOI report.
- **On or after the Effective Date** must file its initial BOI report within **90 days**, if created or registered in **2024**, and within **30 days**, if created or registered **on or after January 1, 2025**, of the earlier of the date on which:
 - It receives actual notice that its creation or registration is effective.
 - A SOS or similar office first provides public notice that the company has been created or registered to do business.

When a Reporting Company Must File Changes to Reports

A reporting company has **30 days** to:

- **Report any changes** to information in its BOI report regarding itself or its beneficial owners. For example:
 - The reporting company changes its name or address or becomes exempt.
 - A beneficial owner transfers their interest or there is a change to their address or unique identifying number.
- **Correct any inaccuracies** in its BOI report if it becomes aware or has reason to know of the inaccuracy.

Penalties If a Reporting Company Fails to Comply

- There are both **civil** and **criminal** penalties for violating the CTA, including a **fine up to \$10,000**, **imprisonment for up to two years**, or **both**, for any person willfully:
 - Providing or attempting to provide false or fraudulent BOI.
 - Failing to report complete or updated BOI to FinCEN.
- Penalties may also apply to reporting companies and individuals who:
 - Cause a reporting company not to report.
 - Are **senior officers** of a reporting company at the time of its failure to accurately report or update BOI.

Penalties If a Reporting Company Fails to Comply (cont'd)

A **safe harbor** exists if a reporting company with reason to believe its BOI report contains inaccurate information files a corrected report **within 30 days** of becoming aware or having reason to know of the inaccuracy, and the inaccuracy:

- Is corrected **within 90 days** of filing the inaccurate BOI report.
- Was not made to evade reporting requirements.
- Was not known to the person filing the report at the time it was submitted.

Beneficial Owners

Beneficial Owners

A **beneficial owner** is any **individual** who, directly or indirectly, **either**:

- Exercises **substantial control** over the reporting company.
- **Owns or controls 25% or more** of the **ownership interests** of the reporting company.

Substantial Control

An individual **exercises substantial control** over a reporting company if the individual does any of the following:

- Serves as a **senior officer** of the reporting company.
- Has **authority to appoint or remove** either:
 - Any senior officer.
 - A majority of the reporting company's board of directors or similar body.
- Directs, determines, or has **substantial influence over important decisions** made by the reporting company.
- Has **any other form of substantial control** over the reporting company.

Senior Officers

Senior officers are:

- The president.
- The chief financial officer.
- The general counsel.
- The chief executive officer.
- The chief operating officer.
- Any other officer, **regardless of title, performing a similar function.**

Substantial Influence over Important Decisions

Important decisions a reporting company makes include:

- Those concerning the nature and scope of the reporting company's business.
- Selling or leasing principal assets.
- Making major expenditures or investments.
- Issuing any equity.
- Incurring significant debt.
- Selecting or terminating business lines or ventures, or geographic focus, of the reporting company.

Substantial Influence over Important Decisions (cont'd)

Important decisions a reporting company makes also include:

- Approving its operating budget.
- Compensation schemes and incentive programs for senior officers.
- Entering into or terminating significant contracts.
- Amending any of the reporting company's substantial governance documents or significant policies or procedures.

Examples of Substantial Control

Exercising substantial control may include:

- Board representation (but being a director by itself is **not** determinative).
- Owning or controlling a majority of the voting power or voting rights of the reporting company.
- Rights associated with any financing arrangement or interest in the reporting company.

Examples of Substantial Control (cont'd)

Exercising substantial control may also include:

- Control over one or more intermediary entities that separately or collectively exercise substantial control over the reporting company.
- Arrangements or financial or business relationships, formal or informal, with other individuals or entities acting as nominees.
- **Any other contract, arrangement, understanding, relationship, or other exercise of control.**

Ownership Interests

The Final Reporting Rule defines ownership interests **broadly** to include the following regardless of whether the interest is transferable, classified as stock or similar, or confers voting power or rights:

- Any equity, stock, or similar instrument.
- Any preorganization certificate or subscription.
- Any transferable share of, or voting trust certificate or certificate of deposit for, an equity security.
- An interest in a joint venture.
- A certificate of interest in a business trust.

Ownership Interests (cont'd)

Ownership interests also include:

- Any **capital** or **profits interest** in an entity.
- Any **instrument that is convertible**, with or without consideration, into any share or instrument described in the bullets above or any future on such an instrument, whether characterized as debt or not.
- Any **warrant** or **right to purchase, sell, or subscribe** to a share or other interest described in the bullets above.
- Any **put, call, straddle, or other option or privilege** of buying or selling any of the above interests without being bound to do so, except to the extent that the option or privilege is held by a third party and not known to the reporting company.
- **Any other instrument, contract, arrangement, understanding, relationship, or mechanism used to establish ownership.**

Ownership Interests (cont'd)

An individual may **directly or indirectly** own or control an ownership interest through:

- Any contract, arrangement, understanding, relationship, or otherwise, including joint ownership with one or more other persons.
- A nominee, intermediary, custodian, or agent.
- Ownership or control of one or more intermediary entities.

Ownership Interests (cont'd)

If an ownership interest in a reporting company is held **through a trust**, the following **individuals** are deemed to have an **ownership interest** in the reporting company:

- A **trustee** of the trust or any other individual having authority to dispose of trust assets.
- A **beneficiary** who either:
 - Is the sole permissible recipient of the trust's income and principal.
 - Has the right to demand a distribution of or withdraw substantially all of the trust's assets.
- A **grantor or settlor** having the right to revoke the trust or otherwise withdraw trust assets.

Calculating Total Ownership Interests

There are **standards to calculate if an individual meets the 25% ownership or control threshold** for a reporting company:

- An individual's total ownership interests that they own or control, directly or indirectly, are to be calculated:
 - As a percentage of the total outstanding ownership interests of the reporting company.
 - At the present time, with any options or similar interests being treated as exercised.
- If capital or profits interests are issued (including in entities taxed as partnerships), the individual's ownership interests are their capital and profits interests as a percentage of the total outstanding capital and profits interests.

Calculating Total Ownership Interests (cont'd)

- For **corporations, entities treated as corporations for tax purposes, and other reporting companies that issue shares of stock**, the applicable percentage is **the greater of the total combined**:
 - Voting power of all classes of ownership interests of the individual as a percentage of the total outstanding voting power of all classes of ownership interests entitled to vote.
 - Value of the individual's ownership interests as a percentage of the total outstanding value of all classes of ownership interests.
- If the calculations **cannot** be made with **reasonable certainty**, an individual owning or controlling 25% or more of any class or type of ownership interest of a reporting company is **deemed to have exceeded the 25% ownership or control threshold**.

Individuals Exempt as Beneficial Owners

Five categories of individuals are exempt from the beneficial owner definition:

- Minor children.
- Individuals acting as a nominee, intermediary, custodian, or agent on another's behalf.
- Certain employees who are not senior officers.
- Heirs.
- Certain creditors of a reporting company.

Complying with the CTA

Complying with the CTA

To comply with the CTA, a reporting company must be able to:

- **Determine** the individuals who are its **beneficial owners**.
- **Timely obtain** the **required personal information** of its beneficial owners so the company can meet the CTA reporting deadlines.
- Be **promptly notified** of any **change** in its beneficial owners' required personal information so the company can timely report the change to FinCEN.

Determining Beneficial Owners

- An individual may **indirectly** own or control an ownership interest in a reporting company through ownership or control of one or more intermediary entities.
- A reporting company with **one or more entities** as owners or in management (like a limited partnership (**LP**) with an LLC acting as its general partner) may need those entities to provide the required personal information of all the individuals who are their direct and indirect owners.

Obtaining Beneficial Ownership Information and Being Notified of Changes

- To meet the CTA's filing deadlines, a reporting company needs to be able to **promptly**:
 - Obtain its beneficial owners' required personal information.
 - Receive notification of any changes to that personal information.
- A reporting company must decide how and when it will acquire this information from the appropriate individuals and implement appropriate policies and procedures if necessary.

Obtaining Beneficial Ownership Information and Being Notified of Changes (cont'd)

- Owners, management, and other persons that may need to give a reporting company personal information should be required to provide the information and updates to the information with enough time for the company to timely review and report the information.
- These **obligations** may be contained in **agreements** such as:
 - The reporting company's governing documents (an LLC or LP agreement or a stockholders' agreement, for example).
 - A company policy.
 - An investment, warrant, employment, equity incentive, or other agreement.

Questions

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