

WOH UPDATE: CORPORATE TRANSPARENCY ACT NOW IN EFFECT

As follow-up to our Fall 2023 WOH Update, the reporting requirements under the Corporate Transparency Act (the “CTA”) went into effect on January 1, 2024. Below is a summary of key points impacting millions of businesses throughout the United States and beyond. Failure to comply with the CTA can result in significant civil and criminal penalties. Whiteman Osterman & Hanna LLP has a team of attorneys who can help with questions regarding the CTA and its applicability to your business, determination of the Beneficial Owners and Company Applicants, as well as filing obligations.

In addition to assisting with determining the applicability of the CTA to businesses, in many instances we are recommending the amendment of existing shareholders’ agreements and limited liability company agreements/ operating agreements to require owners to report certain information to help ensure CTA filings can remain accurate. In some instances, we are recommending CTA-related revisions to forms of employment agreements to require officers to provide certain information to assist Reporting Companies in collecting, tracking and filing more efficiently. The CTA also has impacts in the M&A and transactional context, particularly as it relates to diligence, representations and warranties, post-closing covenants, filing obligations and indemnification matters.

The summary below is not exhaustive, though it is intended to provide an overview that will help guide your understanding of the CTA and the potential impacts on you and/or your businesses.

What is the Corporate Transparency Act?

The CTA was enacted by Congress on January 1, 2021, as an effort to bolster anti-money laundering laws and make it more difficult for bad actors to conceal assets in shell companies. *In a nutshell, the CTA requires businesses to report certain information to the federal government about the business itself, its Beneficial Owners, and for entities formed on or after January 1, 2024, its Company Applicants*, all of which is discussed in more detail below. The information is collected by the United States Department of the Treasury’s Financial Crimes Enforcement Network (“FinCEN”), which stores the information in a secure, non-public database known as the “Beneficial Ownership Secure System.” The information will not be made publicly available, and due to the sensitivity of the information, FinCEN has implemented a number of security features and confidentiality requirements for those certain federal, state, local, and Tribal officials who are eligible to obtain the reported information for law enforcement, national security, and intelligence purposes.



Nicole Green
PARTNER



Michelle Marinello
PARTNER



Timothy Morrison
PARTNER



Scott Shimick
PARTNER

What Businesses are Required to Report Information?

An entity that fits within the CTA's definition of a "Reporting Company" is required to file a report with FinCEN. Reports can be filed here: <https://boiefiling.fincen.gov>. If the entity is not a Reporting Company, the CTA does not apply, and no filing is required.

What is a Reporting Company?

A Reporting Company is an entity that was created by filing a document with the secretary of state or similar office under the law of any U.S. State or Indian Tribe or was formed under the laws of another country that is registered to do business anywhere in the United States, unless it otherwise fits into one of 23 exemptions. The exemptions are intended to capture larger businesses that are already subject to similar reporting requirements.

- › **Common examples of reporting entities:** corporations, limited liability companies, limited partnerships, limited liability partnerships and statutory trusts. **Practical Point:** the definition of "Reporting Company" captures millions of businesses (FinCEN estimates approximately 30 million), many of which are small businesses. This is in line with the intention of the statute but is catching many small businesses off guard because they are mistakenly thinking an exemption must apply to them. By way of example, an entity formed to hold real property, a small restaurant business or other small operating business, professional practice or similar venture will, in most cases, be a Reporting Company that is required to file under the statute (unless it fits within one of the exemptions). Sole proprietorships, while not separately listed as exempt, are generally exempt because they are not formed by filing organizational documents with a secretary of state. FinCEN has confirmed that obtaining an employer identification number, filing for a fictitious business name, or securing a professional license does not render a sole proprietorship a Reporting Company because those filings do not form the entity itself.
- › **The Exceptions.** There are 23 types of entities that are exempt from the filing requirements under the CTA. The rationale behind exempting most of these entities is that they are already subject to extensive federal reporting requirements and oversight. A full list of the 23 exemptions can be found on the FinCEN website. Some of the more common examples include large operating companies, banks and credit unions, venture capital fund advisers, insurance companies, accounting firms, tax-exempt entities, and inactive entities.
- › **Large Operating Company Exemption.** This exemption applies if the entity: (1) employs more than 20 full-time employees (30+ hours per week or 130+ hours per month) in the United States; (2) has a physical office in the United States; and (3) filed a federal income tax return in the previous year showing over \$5 million in gross receipts from United States sources. **Practical Point:** A newly formed entity would not fit this exception because it would not have a federal tax return from the previous year. Further, while there exists a large operating company exception, there is no exemption for small or family-owned businesses.

When Must Reporting Companies File with FinCEN?

Reporting Companies that were formed before January 1, 2024 have until December 31, 2024 to file an initial report with FinCEN. Reporting Companies formed in 2024 will have 90 days after formation to file. Reporting Companies formed on or after January 1, 2025 will have 30 days after formation to file. There is no fee imposed by FinCEN for filing a report. **Practical Point:** The report is not an annual report, but changes to the reported information must be reported to FinCEN within 30 days of the change. Examples of changes that would require updating the filing include: (1) a new fictitious name or new address for the Reporting Company; (2) any change in Beneficial Ownership, such as a new CEO, a transaction in which a new person owns more than 25% of the Reporting Company, or a Beneficial Owner passes away; and (3) any change in a Beneficial Owner's name, address, or unique identifying number. If no changes occur, no additional filings need to be made. As of right now, updates to the report itself will require the Reporting Company to completely fill out the same form it used for the initial filing. The report will include the updated information and all the previously reported, unchanged information. FinCEN's database does not currently permit a report with just updated information.

What Must be Reported?

Each Reporting Company must disclose information about the Reporting Company itself, each Beneficial Owner and, if the Reporting Company was formed on or after January 1, 2024, the Company Applicant(s). We have included more information further below as to the definitions and necessary disclosures regarding a “Beneficial Owner” and “Company Applicant.”

Reporting Company must disclose its:

- › full legal name and any trade name, fictitious name, assumed (“doing business as”) name
- › complete current business address
- › jurisdiction of formation or registration
- › taxpayer identification number (TIN)

For each Beneficial Owner and Company Applicant the Reporting Company must obtain from such individuals and disclose in the report to FinCEN the following information:

- › full legal name
- › date of birth
- › complete current residential/business address (a Company Applicant can use a business address if they are involved in the business of forming entities)
- › a unique identifying number, issuing jurisdiction and image of one of the following non-expired identification documents:
 - › U.S. Passport
 - › State issued driver’s license
 - › Identification document issued by a state, local government or Indian Tribe
 - › If none of the above exist, a foreign passport

Practical Point: In lieu of providing the foregoing information, Beneficial Owners and Company Applicants can obtain a FinCEN Identifier (a “FinCEN ID”) by providing the above information directly to FinCEN rather than to the Reporting Company. Once the Beneficial Owner or Company Applicant obtains a FinCEN ID, it can provide that to the Reporting Company to include in the filing. A FinCEN ID is immediately issued upon electronic submission of the personal information required and can be obtained at: <https://fincenid.fincen.gov/landing>. This is a streamlined option for a Beneficial Owner who has ownership in multiple Reporting Companies or for anyone who prefers not to directly share the personal information listed above with a Reporting Company. Any individual with a FinCEN ID must report any changes to their personal information (i.e., address or identification number) provided to FinCEN within 30 days of the change.

Who is a Beneficial Owner?

A “Beneficial Owner” is an individual who, directly or indirectly: (1) exercises “substantial control” over the Reporting Company; or (2) owns or controls at least 25% of the ownership interests of a Reporting Company. **Practical Point:** A Reporting Company can have multiple Beneficial Owners. It is possible that an individual is deemed a Beneficial Owner through both substantial control and ownership interests and the Reporting Company is not required to specify which rationale applies. FinCEN expects that every Reporting Company will have at least one Beneficial Owner.

25% Ownership Interest. The term “ownership interest” is defined broadly and includes shares of equity or stock in the Reporting Company, voting rights, and any other mechanism the Reporting Company may utilize to establish its owners. Instruments that are convertible into equity, stock, or voting rights can also be indicative of ownership even if the holder has not yet exercised any conversion rights and the right is the product of a debt. Puts, calls, and other options for the privilege of buying equity in the Reporting Company may also render a person a Beneficial Owner, except that it would not render a person a Beneficial Owner if the option were created without the knowledge or involvement of the Reporting Company. **Practical Point:** There are dozens of nuances associated with the determination of ownership interest and FinCEN has issued a series of rules related to the interpretation. For reporting companies with a simple structure (i.e., all the same class of common stock), the determination may be simple, but the analysis can quickly become murky with more complex business structures. As a failsafe, when an ownership interest cannot be calculated with “reasonable certainty,” FinCEN has provided that the Reporting Company should calculate the individual’s ownership percentage based on ownership of any class or type of ownership interest, and to the extent an individual owns or controls 25% or more of any such class or type of ownership interest, it is

deemed to own or control 25% or more of the ownership interests of the Reporting Company and thus is considered a Beneficial Owner for reporting purposes. Ownership interests in a Reporting Company owned by a trust may be attributed to the grantor or settlor of the trust, the trustee or the beneficiary of the trust, all based on additional nuanced rules issued by FinCEN, which has acknowledged that depending on the specifics of the trust arrangement, the ownership interests held in trust could be considered simultaneously as owned or controlled by multiple parties in a trust arrangement. We strongly advise the assistance of legal counsel in connection with the interpretation of Beneficial Ownership.

Substantial Control. For purposes of the CTA, a person exercises substantial control over the Reporting Company if one of the following is true: (1) the individual is a senior officer (president, CEO, CFO, COO, general counsel, or any other officer performing similar functions); (2) the individual has authority to appoint or remove officers or a majority of the directors (or equivalent) of the Reporting Company; (3) the individual directs, determines or has substantial influence over important decisions made by the Reporting Company; or (4) the individual has any other form of substantial control over the Reporting Company. **Practical Point:** Employees who have substantial control by virtue of their duties as employees, but who are not senior officers of the Reporting Company, are not Beneficial Owners. Separately, FinCEN has provided the following as examples of “important decisions” as it relates to being a Beneficial Owner by virtue of having influence over decisions of the Reporting Company: (a) the selection or termination of business lines or geographic focus; (b) the nature and scope of the Reporting Company, including the sale, lease, mortgage or other transfer of principal assets; (c) the entry into or termination of significant contracts; (d) major expenditures, investments, issuances of equity, incurrence of significant debt or approval of an operating budget; (e) compensation schemes and incentive plans for senior officers; (f) reorganization, dissolution, or merger of the Reporting Company; and (g) amendment of the Reporting Company’s governance and formation documents.

Exceptions to Beneficial Owner Rule. There are five (5) categories of individuals who are excluded from the definition of Beneficial Owner: (1) a minor child if information related to a parent or guardian is provided; (2) an individual acting on behalf of the actual Beneficial Owner by serving as a custodian or agent; (3) an individual who is an employee of the Reporting Company and that individual’s substantial control over the Reporting Company is the product of their status as an *employee*, and the individual is *not* a senior officer of the Reporting Company; (4) the individual’s only interest in the Reporting Company is a future interest through a right of inheritance; and (5) the individual is a creditor of the Reporting Company.

The Company Applicant(s). In addition to information about the Beneficial Owners, information regarding the “Company Applicant” must also be disclosed by the Reporting Company as part of the FinCEN filing if the Reporting Company was formed on or after January 1, 2024 (companies formed prior to that date need not report Company Applicants). A “Company Applicant” is: (1) the person who directly files the document that creates or registers the Reporting Company; and (2) if more than one person is involved with the filing of the documents creating the Reporting Company, the person who is primarily responsible for directing or controlling the filing. FinCEN allows for a maximum of two Company Applicants. A Company Applicant must be a person, it cannot be an entity. **Practical Point:** For purposes of determining who is a Company Applicant, the person who signs the formation document (i.e., as incorporator) is not relevant. FinCEN wants to know who is primarily responsible for directing or controlling the actual filing of the document – who is making the decisions about the filing such as how the filing is managed, what content the document includes and when the filing occurs. For example, if an attorney prepares the formation document using information provided by the client and then instructs a paralegal to file the document, both the attorney and the paralegal are the Company Applicants. If the attorney instead directs a corporate service provider to file the document, the attorney and the individual at the corporate service provider are the Company Applicants. If the client asks a corporate service provider to file, then the client and the individual at the corporate service provider are the Company Applicants. As mentioned above, Company Applicants may provide a FinCEN ID to the Reporting Company to include in the filing if the Company Applicant prefers not to directly disclose the personal information to the Reporting Company.

What are the Penalties for Non-Compliance?

An individual who willfully violates the reporting requirements may be subject to civil penalties of up to \$591 per day for each day the violation continues, as well as criminal penalties of up to two years imprisonment and a fine of up to \$10,000. Imprisonment can jump to up to ten years and fines can be up to \$500,000 when such failure is combined with other illegal activities or as part of a pattern of illegal activity involving more than \$100,000 in a twelve-month period.

What is New York's Counterpart to the CTA Known as the "LLC Transparency Act"?

The LLC Transparency Act (the "LLC Act") was signed into law in December 2023. Further amendments are anticipated that will impact the effective date of the law and, in turn, when New York limited liability companies must file. The New York Department of State ("DOS") will collect Beneficial Owner information for limited liability companies formed or authorized to do business in New York State. Unlike the CTA, the LLC Act is specific to limited liability companies. The LLC Act follows the same definitions for "Reporting Company," "Beneficial Owner," and "Exempt Company" as contained in the CTA and outlined above. Entities that are exempt from filing are still required to provide a signed statement to DOS outlining how the entity is exempt. This differs from the CTA as exempt companies do not have to file anything with FinCEN if they are exempt. It is anticipated that an amendment to the LLC Act will require that the database be secure and not available to the public, though in its current form, the LLC Act calls for a publicly-available database. Whiteman Osterman & Hanna is monitoring the developments related to the LLC Act.

What are the Next Steps?

The attorneys at Whiteman Osterman & Hanna welcome any questions you may have about the CTA or the LLC Act. We have team of attorneys who are versed on the subject matter and can help with questions regarding applicability to your business, determination of the Beneficial Owners and Company Applicants, as well as filing obligations. We recognize this may be a challenging undertaking for some businesses, and as such we suggest evaluating your obligations now, as opposed to mere days before a filing may be due.

As noted above, in many instances we are recommending the amendment of existing shareholders' agreements and limited liability company agreements/operating agreements to require owners to report certain information to ensure FinCEN filings remain accurate. Additionally, in some instances we are recommending CTA-related revisions to forms of employment agreements to require officers to provide Beneficial Ownership information to assist Reporting Companies in collecting, tracking and filing more efficiently. It is also important to be mindful of the impact of the CTA in the M&A context, particularly as it relates to diligence, representations and warranties, post-closing covenants and filing obligations and indemnification matters.

Whiteman Osterman & Hanna continues to monitor the FinCEN related guidance applicable to compliance with the CTA. We welcome your questions.



Nicole Green
PARTNER

✉ ngreen@woh.com
☎ 518-487-7775



Michelle Marinello
PARTNER

✉ mmarinello@woh.com
☎ 518-487-7609



Timothy Morrison
PARTNER

✉ tmorrison@woh.com
☎ 518-487-7639



Scott Shimick
PARTNER

✉ sshimick@woh.com
☎ 518-487-7678