Knox McLaughlin Gornall & Sennett, P.C.
Erie • Pittsburgh • Jamestown, NY
814-459-2800 • www.kmgslaw.com

Corporate Transparency Act: New Reporting Requirements

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December 5, 2024 UPDATE: Please see our update regarding a nationwide preliminary injunction, which prohibits the government's enforcement of the CTA. More details can be found in our article: Texas District Court Temporarily Blocks Enforcement of CTA and Reporting Requirements

Summary

Unless subject to an exemption, every limited liability company, limited partnership, limited liability partnership, corporation, or other business entity (including non-profit organizations that have not obtained a 501(c)(3) determination letter) will have a ?ling obligation with FinCEN under the CTA – whether it is a new entity or an existing entity.

Read on for more details:

New Reporting Requirements for Entities and Beneficial Owners in 2024

This article provides a general summary of the Corporate Transparency Act and its requirements and is not intended to, and does not, provide legal, compliance or other advice to any specific individual or entity. Please reach out to your contact at Knox McLaughlin Gornall & Sennett, P.C. for assistance regarding the application of the Corporate Transparency Act to your specific situation.

Final rules implementing the beneficial ownership reporting requirements of the federal Corporate Transparency Act (CTA) became effective on January 1, 2024.

In a nutshell, the CTA requires a “reporting company” to disclose specific designated information regarding the company, its “beneficial owners”, and certain of its so-called “company applicants” in an on-line registry and database with and established by the U.S. Treasury Department’s Financial Crimes Enforcement Network (FinCEN). Enacted by the federal government on January 21, 2021, a 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. Thus, at its heart, the CTA is primarily an anti-money laundering law to ?ght against bad actors that seek to use various shell companies to facilitate such illicit and illegal activities.

As further detailed in this article, in an effort to stagger and alleviate the burdens of compliance with the CTA for existing entities versus new entities, the final rules established the following compliance deadlines entities reporting their beneficial ownership information to FinCEN under the CTA:

- **Reporting companies formed prior to January 1, 2024 must file an initial report with FinCEN by January 1, 2025.**
- **Reporting companies formed from January 1, 2024 to December 31, 2024 will have ninety (90) days from notice of their formation to file their initial report with FinCEN.**
- **Reporting companies formed after December 31, 2024 will have thirty (30) days from notice of their formation to file their initial report with FinCEN.**

We prepared this article to provide you with some key points and details concerning the CTA, its implementing rules, and issues to consider when evaluating whether the CTA applies to your particular situation and/or entity.

What is a reporting company, and what entities are required to comply with CTA's reporting obligations?

Subject to various exemptions (as further discussed below), entities that qualify as a “reporting company” are required to register and submit relevant information with FinCEN. Under the CTA, a “reporting company” is broken down into “domestic” reporting companies and “foreign” reporting companies, whereby it is any entity (whether a corporation, limited liability company or other entity type) that is:

- 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
- is formed under the laws of a foreign (i.e., non-US) 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.

It should be noted that, under the CTA, the term “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.

As a result and for example, in Pennsylvania, reporting companies include corporations (for-profit, nonprofit, and professional), limited liability companies, limited partnerships, and limited liability partnerships. However, since they are not “creatures” created by the filing of a document with the secretary of state, sole proprietorships and general partnerships are **not** considered to be reporting companies under the CTA.

Exemptions to Registration

After determining if your entity is a “reporting company” under the CTA, it is possible that such entity is “exempt” from the filing and registration requirements. However, the analysis must look at and evaluate each entity within an entire company structure. Currently, the CTA rules provide 23 exemptions, most of which involve companies or entities already subject to regulation by governmental authorities (i.e., Securities and Exchange Commission (SEC) registered issuers (public companies), banks, broker-dealers and investment advisers, and Code Section 501(c)(3) tax-exempt nonprofit entities). In addition to the foregoing, the following

are two significant exemptions that are worth reviewing to determine if registration is required:

1. *"Large Operating Company" Exemption*: The so-called "large operating company" exemption applies to an entity that (i) directly (i.e., not on a consolidated or affiliated basis) employs more than 20 employees on a full-time basis in the United States; (ii) 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, BUT excluding gross receipts or sales from sources outside of the United States); and (iii) has an operating presence at a physical office within the United States.
2. *"Subsidiary" Exemption*: The subsidiary exemption exempts certain subsidiaries of entities otherwise exempt from the reporting requirements if structured correctly. In this exemption, 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. For example, if a parent company ("A") owns one hundred percent (100%) of a subsidiary ("B") and A is an exempt large operating company, then B will also be exempt from CTA's reporting requirements.

So No Exemption Exists - Whose Information and/or What Information Must Be Reported?

Now that you have determined your entity is a reporting company and no exemption exists, the question is whose and what information must be reported to FinCEN under the CTA. For reporting companies formed on January 1, 2024 and thereafter, there are 3 groups that need to be addressed and reported:

1. Each reporting company must disclose and file information with FinCEN about itself, as well as the "Beneficial Ownership Information" ("BOI") containing certain personal information of each "bene?cial owner" and each "company applicant."
2. As further noted below, a "bene?cial owner" is any individual who exercises "substantial control" over the reporting company or who owns or controls a 25% or more "ownership interest" in the reporting company.
3. Again, as further noted below, a "company applicant" is any individual who directly ?les the document that creates the domestic reporting company or registers the foreign reporting company, and the individual who is primarily responsible for directing or controlling such ?ling if more than one individual is involved in the ?ling. In many cases, this may be the attorney who files to create the entity, or any similar person or company that handles filings with the various departments of states across the United States.

It should be noted that, for entities/reporting companies that were formed prior to January 1, 2024, the "company applicant" information is **not** required to be reported to FinCEN.

Also, there is no filing fee for submitting the BOI details to and registering with FinCEN and many reporting entities may be able to do so on their own and without assistance. Also, this registration is not an annual reporting requirement – once the initial BOI report is submitted to FinCEN, no further reports are required to be made UNLESS there are changes in the reporting company and/or in the beneficial owners (or if a correction is required to the original filing), all as further discussed below.

In terms of what information is required to be reported to FinCEN, the rules and regulations require the following for each key group:

(a) Reporting companies must provide an initial report to FINCEN which includes the following information:

- Full legal name of entity and any trade or d/b/a names;
- Principal place of business (or, in the case of a foreign reporting company, its primary location in the United States);

- State, foreign or tribal jurisdiction of formation (and in the case of a foreign reporting company, the State or tribal jurisdiction where it first registers to do business); and
- Unique taxpayer identification 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) In addition to the above, a reporting company must report the following BOI regarding its "beneficial owners" and, for entities formed or registered after January 1, 2024, its "company applicants," in its initial report to FinCEN:

- Full legal name of individual;
- Date of birth;
- Current address of the individual (residential address for "beneficial owners" and business address for "company applicants" who form or register entities in the course of their business operations);
- Unique identification number of such person from an unexpired, valid driver's license, state-issued ID, or U.S. passport; and
- An image or copy of the document from which such unique ID number was obtained.

"Beneficial owners" and individuals required to report to FinCEN as "company applicants" may apply for and obtain a unique FinCEN identifier, which may be reported in lieu of reporting the beneficial owner or filer's identifying information noted above. The FinCEN identifier is a unique number that can be used instead of the above information, but the "beneficial owner" and/or "company applicant" must make sure to keep the information updated for that specific FinCEN identifier (such as the address associated with the identifier).

So, Who Qualifies as a "Beneficial Owner" for Purposes of BOI Reporting?

Individuals required to report identifying information as "beneficial owners" include any individual who, directly or indirectly, either (i) exercises "substantial control" over the reporting company; or (ii) owns or controls at least a 25% of the "ownership interests" of the reporting company. It should be noted that there is no limit on the number of reportable beneficial owners of a reporting company under the CTA, and some individuals may fall within both of the foregoing tests – namely, the "substantial control" test and the "ownership" test.

For the so-called "substantial control" test under the CTA, a person is deemed to exercise substantial control over a reporting company if they:

- serve 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 the reporting company;
- have authority over the appointment or removal of any senior officer or a majority of the board of directors (or similar body) of the reporting company;
- direct, determine, or have substantial influence over important decisions made by the reporting company; or
- have any other form of substantial control over the reporting company (which, for example, may include the manager of a limited liability company).

Needless to say, this test will capture a number of individuals who may not consider themselves to be "beneficial owners" in the strict sense of the word. However, the CTA looks at substantial control as being exercised directly or indirectly, and thus requires an evaluation of the reporting company's entire chain of ownership.

Specifically, the CTA regulations provide, in part, that 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." See 31 C.F.R. 1010.380(d)(1)(ii).

For the so-called "ownership" test under the CTA, an individual who owns or controls at least 25% of the "ownership interests" of a reporting company is deemed to be a beneficial owner of that reporting company. Unfortunately, the CTA looks at "ownership interest" in a very broad context and is 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 an ownership interest, any option to purchase or sell ownership interests, or any other instrument, contract, arrangement, understanding, relationship, or mechanism used to establish ownership. As a result, when evaluating whether the 25% threshold has been met with respect to an individual, we must consider all (a) options or similar interests are deemed exercised, and (b) ownership interests are aggregated.

Since our law firm deals with a significant amount of estate planning and trust formation and administration, especially by and with entities that are reporting companies, it is worth noting that 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. This may include ownership by and through trust instruments.

As a result, when dealing with a trust that is determined or deemed to be a beneficial owner under the aforesaid "ownership" test, the following individuals are deemed to be separate beneficial owners who must be reported to FinCEN:

- A trustee of the trust or other individual who has authority to dispose of trust assets;
- A beneficiary of the trust, if (i) such beneficiary is the sole permissible recipient of income and principal from the trust or (ii) if such beneficiary has the right to demand a distribution of or withdraw substantially all of the assets from the trust; and/or
- 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.

And Who Qualifies as a "Company Applicant" for Purposes of BOI Reporting?

As noted above, for reporting companies formed on or after January 1, 2024, the CTA requires BOI details be filed regarding certain "company applicants" of a reporting company. These company applicants fall into two categories – namely, a person who is "direct filer" and a person who "directs or controls the filing" for the formation of the reporting company.

Specifically, a person who qualifies as a "direct filer" is an individual who directly files the document that creates the entity or registers the entity to do business in the United States. Separately, a person you qualifies as one who "directs or controls the filing" is an individual who is primarily responsible for directing or controlling such filing to create or register the entity. As you can imagine, this is more relevant to law firms and companies that handle corporate filings on behalf of reporting companies as the CTA rules identify that a "company applicant" may be an attorney, paralegal or an employee at a business formation service. To that end, multiple attorneys and paralegals at Knox Law have obtained unique FinCEN identifiers in order to assist clients with FinCEN reporting requirements when forming new entities after January 1, 2024.

As noted earlier, 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. Moreover, reporting companies formed or registered to do business in the United States on or after January 1, 2024, will have to provide information about the company applicants but will not be required to update such information, unlike other changes to BOI reporting that may be required (as noted below).

After Filing the Initial Report, What Information Must Beneficial Owners Report on an Ongoing Basis?

In addition to filing an initial report, beneficial owners must also update the information provided to FinCEN on an ongoing basis. Thus, if a reporting company's BOI changes or it no longer qualifies for an exemption under the CTA (i.e., no longer qualifies as a large operating company, etc.), then 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.

Ultimately, each reporting company is responsible for monitoring all manner of changes to its information or those of its beneficial owners.

For example, if a beneficial owner changes its residence address or gets married, there may be an initial 30-day update period triggered by a change of residence and another update period triggered by a surname change depending on the timing of each.

Are There Penalties for Failure to File or Failure to Update BOI Changes?

Violation of CTA's reporting requirements may result in both civil and/or criminal penalties. Under the CTA, it is unlawful for any person to willfully provide (or attempt to provide) false or fraudulent BOI details or to willfully fail to report complete or updated BOI. The CTA provides for a civil penalty of up to $500 per day (which is now $519 per day with annual inflation adjustments) and criminal penalties of a fine of not more than $10,000 and/or imprisonment for up to two years.

How Does This Impact Me, and Where Can I Learn More About Compliance with the CTA?

In summary, unless subject to an exemption, every limited liability company, limited partnership, limited liability partnership, corporation, or other business entity (including non-profit organizations that have not obtained a 501(c)(3) determination letter) will have a ?ling obligation with FinCEN under the CTA – whether it is a new entity or an existing entity.

By its nature, the CTA will require the vast majority of small and medium businesses in the United States to register with FinCEN, and thereby add pressure on all beneficial owners and reporting companies to track their various business organizations and interest, as well as to ensure that BOI reports are ?led and updated with FinCEN in a timely manner. Thus, as these small and medium companies grow, expand their business lines and/or conduct succession planning, they will need to update FinCEN with any such changes, including new owners, new senior officers, new investors, and any new business lines operating under a di?erent trade name. It is key to note that FinCEN designates the ultimate responsibility for the accuracy of the information remains and rests with the reporting company itself.

If you have any questions or would like more information on the issues discussed in this article, please reach out to your contact at Knox Law, who can coordinate and assist with the provision of appropriate advice on CTA compliance. Please also visit the FINCEN website, FAQ's and Small Entity Compliance Guide which all provide additional information on the requirements for CTA compliance, as well as guidance on how to register and file your BOI with FinCEN.

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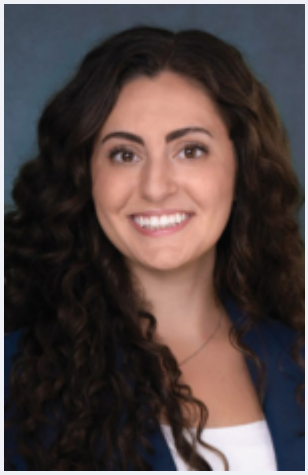

Colleen D. Campbell

Colleen focuses her practice in business, commercial and tax law; banking and commercial lending; nonprofit and tax-exempt entities; and community development projects.

ccampbell@kmgslaw.com

814-923-4891



Mark A. Denlinger

Mark A. Denlinger concentrates his practice in the areas of business, commercial and tax law; banking and commercial lending; nonprofit and tax-exempt entities; real estate; health law and the healthcare industry; and intellectual property & technology.

mdenlinger@kmgslaw.com

814-923-4840

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