

# It's Time To Prep For Corporate Transparency Act Compliance

By **William Quick** (May 23, 2023)

The furthest and widest-reaching federal business entity law ever enacted, the Corporate Transparency Act[1] will affect an estimated 32 million now-existing businesses, with its implementation going into effect on Jan. 1, 2024. Each year after, an estimated additional 5 million newly formed businesses will also be swept under the CTA's purview.[2]

But many business owners, investors and advisers are still unaware of the CTA and its looming deadline, and are often taken aback by its scope. So, now is the time to review the act's requirements and get prepared before it goes into effect at the end of the year.



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## Who Must Comply?

The CTA requires certain businesses — including privately held and nonprofit entities — to report direct and indirect, human, beneficial ownership, control and service provider information to the Financial Crimes Enforcement Network.[3]

This information will be used by federal, state, local and tribal law enforcement authorities to streamline their investigations, bypassing the "shell game" historically posed by multiple levels of business entity ownership and affiliation.[4]

## Who Does the CTA Affect?

The CTA concerns reporting companies, which include corporations, limited liability companies, limited partnerships, business trusts and other similar entities[5] that are created or registered by the filing of a document with a secretary of state or a similar Native American tribal office,[6] provided that it does not fall within specific excluded categories.

These excluded entities generally include heavily regulated business entities such as U.S. Securities and Exchange Commission-regulated parties, utilities, financial institutions, insurance providers, commodity exchanges, pooled investment vehicles, Internal Revenue Code Section 501(c)-registered tax-exempt nonprofits and quasi-governmental entities. However, the vast majority of private and many nonprofit businesses will be swept up in required compliance.

One additional category of exclusion from "reporting company status" is for "large operating" companies that meet all three of the following criteria: They must have a physical street address in the U.S.,[7] 21 or more full-time employees,[8] and more than \$5 million in annual gross receipts or sales as reported on the prior year's filed federal tax return.[9]

By necessity, after Jan. 1, 2024, every newly formed business entity may not qualify for this exclusion because it will not have a prior-year tax return.

Further, the vast majority of U.S. small businesses will also not be able to meet all three of these criteria and thus will be deemed reporting companies under the CTA, requiring a Beneficial Ownership Secure System, or BOSS, filing. This fact will come as a shock to many

business owners, whose first reaction to learning of the CTA's existence is a variant of "Well, that has to be for large businesses, right?"

Further, certain subsidiaries or parent entities of exempt companies may themselves be reporting companies under the CTA. As such, even persons noting that their core business entity easily meets a CTA exemption may find that they are still pulled into the CTA compliance regime through affiliated entities and joint venture parties.

Additionally, beyond the reporting company itself, the act affects incorporators and organizers (i.e., company applicants), service providers (also company applicants), and owners and control persons (i.e., beneficial owners) of such reporting companies, as well as the financial institutions (i.e., banks, credit unions and money service businesses) with whom they do business.[10] The CTA also implicates the enforcement activity of federal, state, local, tribal and foreign law enforcement agencies.[11]

### **What To Report**

Personal identifying information must be reported to FinCEN, including: (1) full legal name, (2) date of birth, (3) residential — or sometimes business — physical street address, and (4) an acceptable government-issued ID number. In addition, a scanned image of the underlying government ID, with the person's photograph, must also be included in the submission into BOSS.

This information will need to be reported for persons owning, directly or indirectly, 25% or more of the business, or who have "substantial control" over the business. Every business will have at least one person to report, regardless of its ownership structure. Informed business decisions will need to be made as to who constitutes reportable beneficial owners in many instances.

The same personal identifying information must also be reported for company applicants — i.e., incorporators and organizers — including those who directed the formation filing, commencing after Jan. 1, 2024.

### **When and How To Report**

FinCEN is in the process of standing up BOSS to go live on Jan. 1, 2024. At present, and not anticipated in the future, there is no available opportunity to make any CTA filings prior to Jan. 1, 2024.

Filings will be made through an electronic interface with BOSS. Businesses in existence on Jan. 1, 2024, will have one year to file their initial report, even if they subsequently dissolve or otherwise alter their structure in a manner to become compliant with a CTA exemption.

Businesses formed on or after Jan. 1, 2024, will have 30 days from formation to file their initial report with FinCEN. They will need to compile, maintain and update their reportable personal identifying information for their beneficial owners on an ongoing basis.

After Jan. 1, 2024, all businesses will have 30 days to file any correction or change to the information previously reported.[12] This includes instances where a reporting company subsequently becomes eligible for an exemption from the reporting requirement — a change in status that's deemed to require an updated report.[13] Any exempt company that no longer meets the criteria for an exemption is required to file an initial report within 30 days after the date that it no longer meets the exemption criteria.[14]

Any change to the status quo of a business in existence on Jan. 1, 2024, will need to be reported as a separate amendment filing, delivered with the initial report filing required to be made on or before Dec. 31, 2024. It bears emphasizing that there is no grandfathering of previously formed entities, and the CTA will sweep in all business entities in existence on Jan. 1, 2024, unless otherwise expressly exempted.

### **Penalties for CTA Noncompliance**

There are steep, escalating fines — \$500 per day, up to \$10,000 per violation — and possible jail time, up to two years, for those failing to timely comply with the CTA's requirements.[15]

It bears note that a failure to timely file a required initial report could result in up to a \$10,000 fine, but subsequent events that would necessitate an amendment to a required but missing filing, had the initial report been made, also accrue — meaning a failure to file an initial report may result in aggregate fines accruing well in excess of \$10,000 prior to an initial notification of a violation from FinCEN to the reporting company.

Also, the reporting company and its agent's intent behind noncompliance would be a factor in FinCEN's assessment of possible criminal penalties.

### **What Is a FinCEN Identifier?**

The CTA says an individual may provide his or her personal identifying information to FinCEN and thereby obtain a FinCEN identifier, which may then be provided to the agency in the future in lieu of other required information about that individual.[16]

Reporting companies can also obtain a FinCEN identifier in a similar manner, but a reporting company may report an intermediate entity's FinCEN identifier, rather than specific beneficial owners' information, only when the intermediate entity and the reporting company have the same beneficial owners.[17]

### **What Is BOSS and Who May Access It?**

Reporting company information and associated personal identifying information of a business entity's beneficial owners and company applicants may be accessed for national security, intelligence or law enforcement activity, for use in furtherance of such activity, by officers or employees of any U.S. agency; officers or employees of any state, local or tribal agency; or officers or employees of any permitted financial institution, each an authorized recipient.[18]

Except as authorized by the CTA and the protocols promulgated thereunder by FinCEN, company information and personal identifying information reported under the act is confidential and may not be disclosed by an authorized recipient.[19] These officials are subject to stiff sanctions for any violation of the CTA's access parameters.[20]

### **Professional Associations**

The CTA also applies to professional associations. There is not a specific CTA exemption for them, other than an express exemption for "[a]ny public accounting firm registered in accordance with section 102 of the Sarbanes-Oxley Act of 2002." [21]

The only likely category of potential CTA exemption for a professional association would be through the large operating company exemption noted above.

Some professional associations may be particularly susceptible to reporting company compliance obligations owing to their ownership structure, whereby the professional owners of the entity may be excluded from the employee count, owing to their nonemployee status.

## **Takeaways**

For some businesses, CTA compliance will require only simple, straightforward online reporting. For many sophisticated businesses, however, CTA compliance will be a minefield for potential failures.

The CTA reporting obligations touch on the sensitive issue of personal anonymity historically enjoyed by U.S. beneficial owners. No one will relish the idea of providing their personal identifying information into a governmental law enforcement database — and all that implicates for personal privacy, attribution of associations with business partners and types of investment, and data security, among other considerations.

Business owners and their control persons have only the waning months of 2023 to take any actions to avail themselves of a CTA exemption, or otherwise influence their ownership or control position within their business entities, to limit or eliminate their required disclosure into BOSS.

Business owners and their control persons will also have the same time period to stand up necessary authorized personnel, policies, procedures, protocols and systems to timely comply with the act's 30-day compliance window commencing and continuing from Jan. 1, 2024.

Now is the time to prepare for this new business world order.

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[1] §§ 6401 – 6403 under Title LXIV of the National Defense Authorization Act for Fiscal Year 2021.

[2] See 31 CFR § 1010.380 (2022).

[3] § 6403 under Title LXIV of the National Defense Authorization Act for Fiscal Year 2021.

[4] See 31 CFR § 1010.380.

[5] E.G., limited liability partnerships, limited liability limited partnerships, decentralized autonomous organizations (DAOs) and other entities created through filings with a secretary of state or tribal authority.

[6] 31 U.S.C. § 5336 (a)(11)(A) (2021).

[7] See 31 CFR 1010.380(f)(6), ("The term "has an operating presence at a physical office within the United States" means that an entity regularly conducts its business at a physical location in the United States that the entity owns or leases and that is physically distinct from the place of business of any other unaffiliated entity.").

[8] 31 U.S.C. § 5336(a)(11)(B)(xxi)(A). 31 CFR § 1010.380(f)(1). A full-time employee must average 30 hours per week or 130 hours per month. (see 26 CFR 54.4980H-1(a) (21) (2014)) This may not include part-time employees, independent contractors or leased employees, nor full-time-equivalents.

[9] 31 U.S.C. § 5336(a)(11)(B)(xxi)(I). A "large operating company" must have filed "a Federal income 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."

[10] § 6403 under Title LXIV of the National Defense Authorization Act for Fiscal Year 2021.

[11] CTA § 6403(c)(2)(B)(i). See 31 CFR § 1010.380 (printed page 59547).

[12] 31 CFR 1010.380(a)(2).

[13] 31 CFR 1010.380(a)(2)(i).

[14] 31 CFR § 1010.380(a)(1)(iv). However, 501(c) exempt companies, "for the 180-day period beginning on the date of the loss of such tax-exempt status" "shall be considered to be continued to be [exempt under that CTA exemption]. 31 CFR § 1010.380(c)(2)(xix).

will have 180 days to comply with the CTA's reporting requirements.

[15] 31 U.S.C. §§ 5336(h)(1), 5336(h)(3)(A).

[16] 31 CFR § 1010.380 (b)(5).

[17] See Proposed 31 CFR 1010.380(b)(4)(ii)(B).

[18] CTA § 6403(c)(2)(B)(i).

[19] CTA § 6403(c)(2)(B)(ii).

[20] 31 U.S.C. §§ 5336(h)(2), 5336 (h)(3)(B).

[21] See Proposed 31 CFR § 1010.380 (c)(2)(xv); (NPRM 87 FR 77404). See FinCEN FAQs (Question 8, Answer XV: <https://www.fincen.gov/boi-faqs>).