

# The Corporate Transparency Act: Our Federal Government Is Casting a Dragnet for Trophy Fish, and Your Business Is Part of Its Bycatch

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## Executive Summary

**A** new federal law requires businesses and their owners to disclose personal information and photographs to a federal law enforcement agency, absent limited exceptions.

## Who's the BOSS?

If you have not heard of The Corporate Transparency Act,<sup>1</sup> you are not alone. Many business owners and their professional advisors are taken aback upon first learning of the CTA's existence and scope. At its core, the CTA requires reporting of personal direct and indirect beneficial ownership and control information pertaining to businesses operating in the U.S. The personal identifying information to be reported includes names, birthdates, addresses, and photographs.<sup>2</sup> The financial crimes enforcement arm of the U.S. Department of the Treasury, FinCEN, is currently building out a Beneficial Ownership Secure System to receive, store, and manage this vast influx of personal information.<sup>3</sup> BOSS will "go live" on Jan. 1, 2024.<sup>4</sup> FinCEN estimates 32 million businesses will be required to report in year one alone. The CTA aims to prevent money laundering, illicit financial activities, corrupt practices, and terrorist financing, but many innocent parties will be swept up in its bycatch. The information in BOSS will be accessible to federal, state, local, and tribal law enforcement, certain financial institutions (with customer consent), and other authorized requestors.<sup>5</sup> However, BOSS reports filed under the CTA are exempt from search and disclosure under the Freedom of Information Act, "open government" or similar laws.<sup>6</sup>

## Who must report?

The CTA requires certain businesses, including privately held and non-profit entities, to report direct and indirect human beneficial ownership, control, and service provider

information to FinCEN.<sup>7</sup> Beginning Jan. 1, 2024, PII must 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 or control structure. Once the initial report is filed, this information must be updated within 30 days of any subsequent event that causes such information to no longer be accurate. Attribution of ownership and what constitutes substantial control will vary from business to business and will require analysis and advice. Law enforcement authorities will use this information to streamline their investigations and enforcement activity, thus bypassing the "shell game" historically posed by multiple levels of business entity ownership and affiliation.<sup>8</sup>

The CTA impacts "reporting companies,"<sup>9</sup> their incorporators and organizers (i.e., "company applicants"), service providers (also "company applicants"), and owners and control persons (i.e., "beneficial owners"), as well as the financial institutions (i.e., banks, credit unions and money service businesses — think Venmo or PayPal) with whom they do business.<sup>10</sup> A "reporting company" is a corporation, limited liability company, or other "similar entity"<sup>11</sup> that is created by the filing of a document ("domestic reporting company") or registered to do business in the United States by the filing of a document ("foreign reporting company") with a secretary of state or a similar Indian tribal office<sup>12</sup> so long as it does not fall within specific, limited, excluded categories. It bears specific note that under the Kansas revised limited liability company act, a series of a Kansas limited liability company may only be established through a filing of a Kansas Limited Liability Company Certificate of Designation with the Kansas secretary of state's office, and, as such, series of a Kansas LLC are specifically and independently subject to the CTA's reporting obligations.



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Exclusion categories generally include already regulated business entities: SEC-regulated entities, utilities, financial institutions, insurance providers, commodity exchanges, pooled investment vehicles, Internal Revenue Code Section 501(c) registered nonprofits, and governmental and quasi-governmental entities.<sup>13</sup> In addition, there is an exclusion from “reporting company” status for “large operating companies” that meet all three of the following criteria:<sup>14</sup> (1) have a physical street address in the U.S.,<sup>15</sup> (2) have 21 or more full-time employees,<sup>16</sup> and (3) have more than \$5 million in annual gross receipts or sales as reported on the business’s prior year’s filed federal tax return.<sup>17</sup> As a matter of logical inference, it bears note, that except for an entity that is a wholly owned subsidiary of an exempt entity, all business entities newly formed after Jan. 1, 2024, will not qualify for an exclusion, and will be required to file a CTA report with FinCEN within 30 days of their formation.

The vast majority of U.S. small businesses will not meet any of the exceptions to reporting, including the “large operating company” exception, and thus will be CTA “reporting companies” requiring a BOSS filing. This fact likely will come as a shock to many small-business owners.

In addition, certain parent or subsidiary entities of exempt companies may themselves be CTA “reporting companies.” Each business entity is evaluated on its own merits. As such, even persons noting that their core business entity easily meets a CTA exemption may find that they are pulled into the CTA compliance regime through their affiliated entities and joint venture parties.

### When and how to report

The BOSS system is scheduled to “go live” on Jan. 1, 2024, and no CTA filings may be made prior to Jan. 1, 2024. Filings will be made via an electronic interface with BOSS. Businesses in existence on Jan. 1, 2024, will have a one-year grace period to file their initial report with FinCEN, but file such initial report they must, even if they subsequently dissolve or otherwise alter their structure in a manner to become

compliant with a CTA exemption. 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 “as of Jan. 1, 2024,” report filing required to be made on or before Dec. 31, 2024. Notably, there is no “grandfathering” of previously formed entities, and the CTA will sweep in all business entities in existence on Jan. 1, 2024.

Businesses formed on or after Jan. 1, 2024, will have a shorter, 30-day grace period after formation to file their initial report. Businesses will need to compile, maintain, and update their reportable PII 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 their previously reported information.<sup>18</sup> This includes instances where a reporting company subsequently becomes eligible for an exemption from the reporting requirement.<sup>19</sup> Any exempt company that no longer meets the criteria for an exemption must file an initial report within 30 days after the date that it no longer meets the exemption criteria.<sup>20</sup>

### What is a company applicant?

The same PII as disclosed for beneficial owners must also be reported for company applicants (i.e., the entity’s incorporators or organizers), including those who directed the business’ formation filing.<sup>21</sup> However, this applies only for businesses newly formed after Jan. 1, 2024. Once reported, company applicant information is not required to be updated in the future.

### What is a FinCEN identifier?

The CTA contemplates that an individual may provide their PII to FinCEN, and may thereby obtain a “FinCEN Identifier,” an identification number that may then be provided to reporting companies and to FinCEN in the future in lieu of other required PII about that person.<sup>22</sup> Reporting companies may obtain a FinCEN Identifier in a similar manner, but a reporting company may report an intermediate entity’s FinCEN identifier, rather than a specific beneficial owner’s information, only when the intermediate entity and the reporting company have the same beneficial owners.<sup>23</sup>

### Who may access the BOSS?

The reporting company information and associated PII of such 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; by officers or employees of any state, local or tribal agency; or by officers or employees of any permitted financial institution.<sup>24</sup> Except as authorized by the CTA and the associated FinCEN promulgated protocols, however, company information and PII reported under the CTA is confidential and may not be disclosed by a U.S. officer or employee, an officer or employee

◀ of any state, local or tribal agency, or an officer or employee of any financial institution or regulatory agency receiving information that was collected under the CTA.<sup>25</sup> Such officials are subject to stiff sanctions for any instance of violation of the CTA's access parameters.<sup>26</sup>

### What are the consequences of noncompliance?

There are steep, escalating fines — \$500 per day, up to \$10,000 per violation — and possible jail time of up to two years for those failing to timely and appropriately comply with the CTA's requirements.<sup>27</sup> Although failure to timely file a required initial report could result in up to a \$10,000 fine, fines also may accrue for subsequent events that necessitate an amendment to such required, but delinquent, filing, so that a failure to file an initial report may result in aggregate fines well in excess of \$10,000 accruing before FinCEN initially issues a reporting company a notification of violation. One may assume that the intent behind noncompliance of a reporting company and its agent(s) will serve as a factor in FinCEN's assessing of possible criminal penalties.

### What is the CTA's application to professional associations, including law practices?

The CTA applies to professional associations such as law practices and many accounting practices. There is no specific CTA exemption for professional associations other than an express exemption for “[a]ny public accounting firm registered in accordance with Section 102 of the Sarbanes-Oxley Act of 2002.”<sup>28</sup> 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, including law firms, may be particularly susceptible to reporting company compliance obligations based on their ownership structure, whereby the entity's professional owners may be excluded from the “full time employee” count based on their non-employee status, which may impede meeting a “large operating company” exception.<sup>29</sup>

### Conclusion

The CTA amounts to a new extension of federal oversight to the regulation of business entities and their operations. This oversight has traditionally resided with U.S. states. Attorneys and their clients will now need to swiftly adjust to this new legal landscape. For some businesses, CTA compliance will require nothing more than filing a simple, straightforward online report into the BOSS. For many sophisticated businesses, however, CTA compliance will be a minefield for potential failures. The CTA's 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 considerations such as personal



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privacy, attribution of associations with business partners and association with types of investment,<sup>30</sup> and data security.

Business owners and their control persons have only the waning months of 2023 to take actions to best 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 the BOSS. Business owners and their control persons will also have the same time period to establish necessary authorized personnel, policies, procedures, protocols and systems to ensure timely compliance with the CTA's 30-day compliance window commencing and continuing from Jan. 1, 2024. Now is the time to engage expert, professional advisors to prepare for this new federal reporting system for U.S. operating businesses. ◆



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### References

1. §§ 6401 – 6403 under Title LXIV of the National Defense Authorization Act for Fiscal Year 2021, Jan. 1, 2021.
2. 31 C.F.R. § 1010.380(b) (2022).
3. Note: The U.S. Department of Treasury also houses the Internal Revenue Service. The IRS recently announced plans to hire nearly 20,000 new employees and invest \$80B over the coming years to improve tax enforcement and customer service, with more than one-third of the new hires being enforcement staff. The agency also plans to hire more data scientists to complement traditional tax attorneys and revenue agents in using new data analytics technology to identify audit targets. FinCEN's BOSS database, created under the CTA, could be a key component to such data analytics technology, and will provide an inexpensive, efficient, investigative tool and corroborating (or “red flag”) source of taxpayer information available to the IRS. The IRS initiative aims to close the “tax gap” between taxes owed and those paid, and to rebuild

- the IRS's audit capabilities and computer technology. The IRS's stated goal is to expand enforcement for taxpayers with complex tax filings and high-dollar noncompliance, including high-income and high-wealth individuals, complex partnerships, and large corporations. *See* Internal Revenue Service Inflation Reduction Act Strategic Operating Plan FY2023 – 2031 (transmitted April 5, 2023), <https://www.irs.gov/pub/irs-pdf/p3744.pdf>, (last visited May 5, 2023).
4. 3. *See* FinCEN Frequently Asked Questions 3 and 5, <https://www.fincen.gov/boi-faqs>, (last visited May 5, 2023) (“No one needs to report beneficial ownership information to FinCEN until Jan. 1, 2024. FinCEN is currently not accepting any beneficial ownership information reports.” “Beneficial ownership information reports will not be accepted before then.”).
  5. 31 C.F.R. § 1010.380 (b)(5).
  6. *See* 31 U.S.C. 5319, Jan. 7, 2011; 31 C.F.R. 1010.960 (2022).
  7. § 6403 under Title LXIV of the National Defense Authorization Act for Fiscal Year 2021.
  8. CTA § 6403(c)(2)(B)(i). *See* 31 C.F.R. § 1010.380 (printed page 59547).
  9. It is important to note that these are “reporting companies” as defined in the CTA only, and NOT “reporting companies” obligated to file reports under Sections 13 or 15(d) of the Securities Exchange Act (which entities are expressly excluded from the CTA’s “reporting” company classification).
  10. § 6403 under Title LXIV of the National Defense Authorization Act for Fiscal Year 2021.
  11. *See, e.g.*, limited partnerships, limited liability partnerships, limited liability limited partnerships, business trusts, decentralized autonomous organizations (DAOs), cooperative associations, series of a series LLC and other entities created through filings with a secretary of state or tribal authority.
  12. 31 U.S.C. § 5336 (a)(11)(A) (2021).
  13. 31 U.S.C. § 5336 (a)(11)(B).
  14. Failure to meet any one or more of these three criteria will result in the exemption not applying to the business entity in question, and such business entity being classified as a “reporting” company under the CTA.
  15. *See* 31 C.F.R. 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 [which] the entity owns or leases, and [which] is physically distinct from the place of business of any other unaffiliated entity.” Neither shared space (e.g., WeWorks or Regis facilities), nor a registered agent’s office nor the law office of a client’s attorney may serve as such an address.).
  16. 31 U.S.C. § 5336(a)(11)(B)(xxi)(A) (2014). 31 C.F.R. § 1010.380(f)(1). A full-time employee must average 30 hours per week or 130 hours per month. *See* 26 C.F.R. 54.4980H-1(a) (21) (2014). This may not include part-time employees, independent contractors or leased employees, nor full-time-equivalents. *But note* that FinCEN, in its FAQs (Question 8, Answer XXI, <https://www.fincen.gov/boi-faqs>, (last visited May 5, 2023)), describes this threshold as “Large operating companies with at least 20 full-time employees...” (emphasis added) (internal citation omitted); note: this position is contrary to the express provision in the CTA. *See* 31 U.S.C. § 5336 (a)(11)(B)(xxi)(I).
  17. 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.” 31 C.F.R. 1010.380(c)(2) (xxi)(C). It bears note that aggregation on consolidated returns only applies to federal tax purposes “corporations” and not federal tax purposes “partnerships,” the tax category most limited liability companies and limited partnerships fall within.
  18. 31 C.F.R. 1010.380(a)(2).
  19. 31 C.F.R. 1010.380(a)(2)(i).
  20. 31 C.F.R. § 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).
  21. 31 C.F.R. § 1010.380 (b)(1)(ii); 31 CFR § 1010.380(e).
  22. 31 C.F.R. § 1010.380 (b)(5).
  23. *See* Proposed 31 C.F.R. 1010.380(b)(4)(ii)(B).
  24. CTA § 6403(c)(2)(B)(i).
  25. CTA § 6403(c)(2)(B)(ii).
  26. 31 U.S.C. §§ 5336(h)(2), 5336 (h)(3)(B).
  27. 31 U.S.C. §§ 5336(h)(1), 5336(h)(3)(A).
  28. *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>, (last visited May 5, 2023)).
  29. 31 C.F.R. § 1010.380 (c)(2)(xxi), *referencing* 26 CFR 54.4980H-1(a); *see* 26 C.F.R. 54.4980H-1(a)(15): “Employee. The term employee means an individual who is an employee under the common-law standard. *See* § 31.3401(c)-1(b). For purposes of this paragraph (a)(15), a leased employee (as defined in section 414(n)(2)), a sole proprietor, a partner in a partnership, a 2-percent S corporation shareholder, or a worker described in section 3508 is not an employee.” (Emphasis added).
  30. Consider co-investments with notorious individuals. Or in businesses receiving poor press and investigative attention, such a pay day lending. Or investments in businesses with challenging legal status (such as businesses in the cannabis industry, which, while legal under many States’ laws, remains illegal in other States (including Kansas), and under federal law for any purpose — *see* the Controlled Substances Act of 1970, 21 U.S.C. 801 et. seq.).