

The Corporate Transparency Act: What Fractional Executives Need to Know

A new federal law requires businesses to disclose personal information and photographs of their owners and control persons, including retained fractional executives.

Why this matters for you. From Wall Street to Main Street to your street, the vast majority of private and many nonprofit entities, will be swept into Corporate Transparency Act (CTA) compliance. If you are a fractional executive to a business, you need to pay attention. Not only is initial reporting important, so is ongoing compliance.

What is this law about? If you have not heard of the CTA, you are not alone. Many business owners, executives 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 (PII) includes name, date of birth, physical home address and your photograph. The financial crimes enforcement arm of the U.S. Department of Treasury (FinCEN) is currently building out a beneficial ownership secure system (BOSS) to receive, store and manage this vast influx of information. FinCEN estimates that over 32 million now-existing businesses will be required to report in year one. This law aims to prevent money laundering, illicit financial activities, corrupt practices and terrorist financing, at the expense of many legitimate businesses (and their owners and control persons) being swept up in its bycatch.

Who must report? Beginning January 1, 2024, PII must be reported for persons owning, directly or indirectly, 25% or more of any class or category of profit ownership in a business, or who have or may assert, directly or indirectly, "substantial control" over a business.

Important for the fractional executive, the CTA provides that every senior officers of a business (which would include fractional executives) are, by definition, persons with "substantial control," and must therefore be disclosed in a reporting companies CTA report to FinCEN.

Although the CTA contains an "employee" exception to the beneficial owner reporting requirements, this except expressly does not apply to senior officers of the reporting company. According to FinCEN, senior officers "perform functions that inherently involve substantial control and go beyond mere employee status."

What ongoing reporting obligation exists? Once the initial report is filed, this information must be updated within 30 days of any subsequent event that makes the previously reported information inaccurate. Attribution of ownership and what constitutes substantial control will vary from business to business, and will require analysis and professional advice.

Further, by its very nature, fractional executive positions tend to be transitory by nature, and companies onboarding or offboarding fractional executives will necessitate contemporaneous updated reporting to FinCEN.

Exempt Entities. Some categories of business entities are exempted out of CTA compliance. These generally include regulated business entities, such as publicly traded companies, insurance businesses, banking businesses, 501(c) federally tax-exempt non-profit entities, and quasi-governmental organizations. In addition to the other exempt categories, a catch-all exemption is available for any business entity that meets all three of the following thresholds: (1) have a physical commercial street address in the U.S., (2) have 21 or more full-time employees, and (3) generate more than \$5 million in annual gross receipts as reported on the prior year's federal tax filing. Missing any of these thresholds will render a business ineligible for this exemption.

What will compliance look like? Businesses will need to compile, maintain and update their reported PII constantly to meet the CTA's compliance requirements. Any change to or correction of previously reported information must be done within 30 days of the event, not when the business becomes aware of the event. All newly formed business entities beginning January 1, 2024, will be required to file their initial CTA report within 30 calendar days of formation. Reporting company businesses in existence before January 1, 2024, will have one year to make their original CTA report filing, along with any subsequent amendment filings that would have been required had the report been filed on January 1, 2024.

What happens if you don't comply? There are steep fines (\$500 per day up to \$10,000) per incident and possible jail time (up to two years) for those failing to timely and properly comply with the CTA. Those who fail to file their initial report will also be subject to fines for failing to file what should have been subsequent filings – the fines can rack up. Further, the IRS recently announced increased enforcement, utilize new data analytics technology to identify audit targets. FinCEN's database has been identified by the IRS as a key component to such data analytics initiative.

Who may access FinCEN's Beneficial Ownership Secure System (BOSS)? Information in the BOSS will be accessible to law enforcement at the federal, state and local levels and includes the law enforcement arms of various federal agencies. Financial institutions may also have access upon their customer's consent. Importantly, this information is not available to the general public, and is not accessible through Freedom of Information Act (FOIA) requests.

Conclusion. The compliance requirements under the CTA go live January 1, 2024, and you have only the remaining waning months of this year to take any action to prepare for your future compliance position. Now is the time to discuss this with your legal team for guidance.