



Understanding How the Corporate Transparency Act Will Apply to the Delaware Statutory Trust Structure

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UNDERSTANDING HOW THE CORPORATE TRANSPARENCY ACT WILL APPLY TO THE DELAWARE STATUTORY TRUST STRUCTURE

What is the Corporate Transparency Act?

In general terms, the Corporate Transparency Act (the “CTA”) requires reporting to the U.S. Department of Treasury’s Financial Crimes Enforcement Network (“FinCEN”) of personal direct and indirect beneficial ownership and control information pertaining to business entities formed or registered in the U.S. Under these new reporting rules, a business entity must report certain personal identifying information (“PII”) to FinCEN for each natural persons that owns, directly or indirectly, 25% or more of any class or category of economic ownership in the business entity, or who have or may assert, directly or indirectly, “substantial control” over the business entity. 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.

Who Has to Comply with the Reporting Requirements?

The CTA sets forth 23 exemptions from its reporting rules. Among the exemptions are (i) public reporting companies, (ii) banks and credit unions, (iii) registered broker /dealers, (iv) public accounting firms registered under Sarbanes-Oxley (v) governmental and quasi-governmental bodies, and (vi) certain non-profit entities.

There is also a “large operating companies” exemption for any business entity that meets all three of the following thresholds: (1) operate from a physical commercial street address in the U.S., (2) have 21 or more full-time U.S. employees, and (3) generate more than \$5 million in annual U.S. gross receipts as reported on the business entity’s prior year’s federal tax filing. Missing any of these criteria will render a business ineligible for this exemption. One key to this exemption is that only full-time, W-2 employees of the entity itself qualify. If an entity falls within the large operating companies exemption, each of its subsidiaries, whose ownership interests are controlled or wholly owned, directly or indirectly by that exempt entity, may also be exempt.

Absent an express exemption, a business entity (including statutory trusts) will be a reporting company subject to the reporting obligation under the CTA.

Understanding What Information Must Be Disclosed to FinCEN under the CTA.

For each natural person owning, directly or indirectly, 25% or more of any class or category of economic ownership in a business entity, or who have or may assert, directly or indirectly, “substantial control” over a business entity, the CTA requires the submission of the person’s PII: name, date of birth, physical home address, and an image of the person’s unexpired driver’s license or unexpired passport showing both the person’s photograph and the government issued identification number. In addition, each business entity must provide the legal name of the business, a current physical address, the jurisdiction of its formation, and its taxpayer identification number (FEIN).

Any non-exempt business entity formed prior to January 1, 2024, will have until January 1, 2025, to make its initial CTA report filing (reporting its January 1, 2024, factual information), along with any subsequent amendment filings that would have been required had the report been filed on January 1, 2024. Any non-exempt business entity formed on or after January 1, 2024, but prior to January 1, 2025, will have 90 calendar days from its formation to make its initial CTA report filing, along with any subsequent amendment filings that would have been required had the report been filed on the date of its formation. In addition, for entities formed on or after January 1, 2024, individuals who directly file formation documents for a business entity, or who direct such filing (collectively “company applicants”), are also obligated to have their PII included in the business entity’s CTA filing.

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Beginning January 1, 2025, all newly formed business entities will be required to file their initial CTA report within 30 calendar days of formation. As noted above, 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.

Significant Monetary Penalties May Be Imposed for a Failure to Comply with the CTA

Under the CTA, fines of \$500 per day up to \$10,000 per incident may be imposed. In addition, the CTA provides for criminal penalties of up to two years in jail for willful misconduct. Because these monetary fines are imposed for each required filing, a business that fails to file its initial report and fails to file what should have been subsequent filings for changes in control or ownership can be subject to significant penalty.

Applying the CTA to the Delaware Statutory Trust Structure

Under a Delaware statutory trust structure intended to comply with Revenue Ruling 2004-86, in addition to the Delaware statutory trust, the sponsor will typically form the depositor, the signatory trustee and the master tenant as Delaware limited liability companies wholly owned by the sponsor entity. In many cases, a newly formed Delaware limited liability company will also be formed to act as the sponsor for that particular offering.

Initially, no reporting under the CTA should arise if the ultimate sole owner of each of these entities (1) operates from a physical commercial street address in the U.S., (2) has 21 or more full-time U.S. employees, and (3) generates more than \$5 million in annual U.S. gross receipts as reported on the business entity's prior year's federal tax filing. Similarly, no initial obligation should be required under the CTA if the ultimate sole owner of each of these entities otherwise falls within certain of the other express exemptions from the CTA's reporting rules (e.g., a public reporting company).

However, if the sponsor does not qualify for an exemption, or is not the sole direct or indirect owner of each of these entities, then it and the other entities in the portfolio may each have independent reporting obligations under the CTA: for the Delaware statutory trust, the signatory trustee, the depositor and the master tenant. In addition, even if a sponsor falls within one of the exemptions, the Delaware statutory trust might cease to qualify as an exempt subsidiary once investors acquire beneficial interests in the statutory trust. Similarly, the use of bridge equity may also trigger the reporting obligations under the CTA. The determination of CTA exemptions and compliance obligations in a statutory trust structure will require a business judgment determination following a facts and circumstances analysis.

Conclusion

Reporting under the CTA commenced on January 1, 2024. The reporting requirements under the CTA are mandatory. Accordingly, both traditional sponsors of DST programs, and REITs and real estate companies adopting the DST structure to expand their sources of capital to include Section 1031 like-kind exchange investors, need to examine how the CTA will require a change in the information the sponsor will need to obtain from and report for investors, substantial control individuals and bridge equity providers, both for existing Delaware statutory trust structures and for newly created structures adopted after January 1, 2024.



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