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The Corporate Transparency Act What You Need to Know

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Holland & Knight

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Topics Covered

- *Background*
- *What Is a Reporting Company?*
- *What Entities Are Out of Scope?*
- *What Entities Are Exempt from Reporting?*
- *Who Is a Beneficial Owner?*
- *How Do Common-Law Trusts Interact with the CTA?*
- *Who Is a Company Applicant?*
- *What Information Must Be Disclosed in a Report?*
- *What Is a FinCEN Identifier & How Does the New FinCEN Identity Entity Rule Work?*
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- *What Are the Penalties for Non-Compliance?*
- *What Steps Should One Take to Comply?*
- *CTA Exemption Planning?*
- *Impacts and Questions under the CTA?*
- *FinCEN: Challenges, Developments & Resources?*
- *What's Next?*

Background

“The World’s New Tax Haven is the United States”

Bloomberg 2016



CTA

Why Was It Enacted?

THE PROBLEM

- The lack of US beneficial ownership information (“BOI”) reporting requirements made the United States the jurisdiction of choice to establish shell companies to hide ultimate beneficial owners
 - BOI is Identifying information about the individuals who directly or indirectly own or control a company
- This weakened US efforts to combat the flow of illicit money into the US

THE GOAL

To combat the proliferation of anonymous shell companies that facilitated the flow and sheltering of illicit money into the US

THE REMEDY

BOI reporting to counter money laundering, terrorist financing, corruption, tax fraud and other illicit activity so as to protect national security, intelligence and law enforcement interests

CTA

In a “Nutshell”

- **Federal legislation:**
 - **First ever national BOI legislation**
 - Applicable to states | territories | possessions
 - Note, US defined as broader than continental US
 - **Who Reports:** Entities that are “reporting companies”
 - **What is Reported:** Information about Reporting Company, Beneficial Owners & Company Applicants
 - **To Whom:** Financial Crimes Enforcement Network (“FinCen”)
 - FinCEN will maintain centralized, secure data base
 - **Disclosure:** Non-public
 - Only to selected government agencies (domestic and foreign) & financial institutions (“FI”) for customer due diligence (“CDD”) and FI regulators
 - **Penalties:** Civil & criminal
 - **Reporting Companies:**
 - Pre-2024 companies
 - Newly-formed in 2024 and forward
 - Domestic
 - Foreign (that register w/ state to do business)
 - **Exclusions and Exemptions:**
 - Out-of-scope arrangements/entities
 - 23 Entity Exemptions
 - 5 Beneficial Owner Exclusions
 - **Effective Date: January 1, 2024**
- Reporting Guidance described herein promulgated by FinCEN in Final Regulations published in September 2022, supplemented by subsequent FINCEN administrative guidance***

Rule Effective January 1, 2024



Beneficial Ownership Information Reporting

CTA

What Will It Do?

The Corporate Transparency Act will require certain entities, such as corporations, limited liability companies and other similar entities, to report identifying information about the individuals who directly or indirectly own or control a company, unless the entity is out of scope or an exemption to reporting were to apply

CTA Overview of Reporting Initial Report Information



**Reporting Company created
or registered before January
1, 2024**

Provide information about:

- Itself
- Beneficial owners
- **But not Company Applicants**



**Reporting Company created
or registered on or after
January 1, 2024**

Provide information about:

- Itself
- Beneficial Owners
- Company Applicants

CTA Is a Big Deal

**Commencing in 2024,
FinCEN estimates**

**About 32.6 million pre-
existing entities (pre-2024)
will be required to report**

**About 5 million new companies
will be created in 2024 and each
year thereafter over a decade
and required to report**

Concerns of Business

The Wall Street Journal, in an Opinion written by The Editorial Board entitled “The Coming Deluge for Small Business” (Nov. 20, 2023), wrote about the CTA:

The feds and business aren't ready for new reporting rules on Jan. 1.

Most of these small operators are unaware of the reporting requirements that are coming their way in a couple of months.

The small business owners have asked that the statute be delayed for a year so they and their regulator can get their acts together. As it currently stands, the government isn't ready to handle what they are requesting, and small businessowners don't know what they are supposed to provide. Short of cancelling the whole thing, a time-out is the least the feds can do to avoid a national bureaucratic meltdown.

What Is a Reporting Company?

Reporting Companies Domestic & Foreign

Reporting Company. A corporation, LLC or other similar entity

Can be Domestic or Foreign

- **Domestic.** A corporation, LLC and any other entity created by the filing of a document with a secretary of state or a similar office under the law of a state or Indian Tribe
- **Foreign.** An entity (including a corporation and LLC) formed under the law of a foreign country that has 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
- **Broad Definition of State.** Any state of the US | the District of Columbia | the Commonwealth of Puerto Rico | the Commonwealth of the Northern Mariana Islands | American Samoa | Guam | the U.S. Virgin Island | any other commonwealth | territory | or possession of the US

Targets bad actors seeking to use shell companies or other opaque structures for illicit purposes in the United States

Comments

Reporting Company

- Used to hold assets or conduct a business
- Formed prior to, or after, 2024

Domestic Reporting Company

- Created by the filing of a document with a secretary of state or Indian Tribe
- Wide range of activities, such as
 - HOAs (Homeowner Associations) – certain types included
 - Statutory trusts used to own a US aircraft
 - Certain family offices
 - Art or real estate holding companies

Foreign Reporting Company

- Entity created outside of US
- Registered to do business in a state or with an Indian Tribe
 - Amount and types of activity that trigger business registration in states vary
 - What about holding residential real estate | income producing real estate | acting as a “blocker”?

What Entities Are Out of Scope?

Entities Out of Scope



Sole proprietorship (not an entity)



General partnership



Unincorporated association



Wealth planning trust (but not a statutory trust, such as a DE statutory trust)

Why? Because no document filed with a secretary of state/Indian Tribe



Foreign entity **not registered to do business** in a state or with an Indian Tribe

What Entities Are Exempt from Reporting?

23 Exemptions

- Securities reporting issuer
- Governmental Authority
- Bank
- Credit union
- Depository institution holding company
- Money service business
- Broker or dealer in securities
- Securities exchange or clearing agency
- Other Exchange Act registered entity
- Investment company or investment advisor
- Venture capital fund advisor
- Insurance company
- State-licensed insurance producer
- Commodity Exchange Act registered entity
- Accounting firm registered with Sarbanes-Oxley Act
- Public utility
- Financial market utility
- Pooled investment vehicle*
- Tax-exempt entity
- Entity assisting tax-exempt entity
- Large operating companies in US | > 20 full-time employees | > \$5M gross receipts reported to IRS in prior year | physical US office
- Subsidiary of certain exempt entities
- Inactive entity

** If an entity is a pooled investment vehicle and is formed under the laws of a foreign country (a "foreign pooled investment vehicle"), the entity is subject to a separate reporting requirement*

Each exemption has detailed requirements, so read carefully
FinCEN has authority to add (but has not added) additional entities

Who Is a Beneficial Owner?

Two Tests

Any individual who, directly or indirectly, through any contract, arrangement, understanding, relationship, or otherwise:

Exercises Substantial Control over a Reporting Company

or

Owns or Controls at least 25 percent of the *Ownership* Interests of a Reporting Company

Substantial Control (1/3)

Four Indicators

- **Legal Authority.** Senior officer (nominal or *de jure* authority)
 - Senior officer includes a president, CEO, COO, CFO, GC or any other officer, regardless of official title, who performs a similar function
- **Appointment/Removal Authority.** Authority over appointment/removal of a senior officer or majority of board of directors (or similar body) (*de facto* authority)
- **Important Decision Maker.** Directs/determines or substantial influence over important decisions made by the Reporting Company (business/finance/structure) (*de facto* authority)
- **Any Other Form of Control.** Any other form of substantial control over Reporting Company (*i.e.*, “catch all” provision)
 - Example. Individual who may not have “power” to direct or determine important decisions, but plays a significant role in decision-making process

Substantial Control (2/3)

Direct/Indirect – Broad & Encompassing

Direct or Indirect

Illustrations

- Board representation
- Ownership/control of a majority of voting power/voting rights of a Reporting Company
- Rights associated with any financing arrangement or interest in a Reporting Company
- Rights/control of one or more intermediary entities that separately/collectively exercise substantial control over a Reporting Company
- Arrangements/financial/business relationships with other individuals/entities acting as nominees
- Any other contract arrangement, understanding, relationship or otherwise

Substantial Control (3/3)

Takeaways

- **Substantial Control**
 - Does not require ownership in an entity
 - Relates solely to authority to direct, determine or have substantial influence over important decisions
 - Includes an individual that exercises substantial control over Reporting Company through an unaffiliated company
- **FinCEN**
 - **Expects:** A Reporting Company to identify at least one Beneficial Owner under Substantial Control test
 - **Requires:** *All* persons in Substantial Control must be reported
- **FinCEN's Expansive Approach**
 - Supports basic goal of CTA. To require Reporting Company to identify individuals who stand behind the Reporting Company and direct its actions
 - Purpose. To foreclose corporate structuring to obscure owners or decision-makers, essential to unmasking shell companies
- **Directors**
 - FinCEN has provided that Director is not always a Beneficial Owner; rather, it is a facts and circumstances determination
 - Includes an individual who directly or indirectly exercises substantial control over a Reporting Company or who owns or controls at least 25% of the ownership interests of a Reporting Company

The identification of all persons in Substantial Control in a multi-tier company/trust structure will be difficult

25% Ownership Interest (1/4)

Three Prong Test

- **Ownership Interest.** Broadly defined to include:
 - Equity | stock | similar instrument (irrespective of whether interest is transferable | classified as stock or anything similar | or confers voting powers or rights)
 - Preorganization certificates or subscription
 - Capital interest in an entity
 - Convertible instruments into equity, stock, voting rights or capital or profits interest
 - Options (except those created by third party w/o knowledge of Reporting Company)
 - “Catch all”: any other instrument, contract, arrangement, understanding, relationship or mechanism used to establish ownership
- **Ownership or Control of Ownership Interest.** Individual may directly or indirectly own or control an ownership interest in a Reporting Company through any contract, arrangement, understanding, relationship, or otherwise, including:
 - Debt instruments included if they enable holder to exercise the same rights as one of the specified types of equity interests, including conversion right to an equity interest
 - Joint ownership
 - Through another acting as nominee | intermediary | custodian | agent of an individual
 - Through a trust or similar arrangement that holds such ownership interest

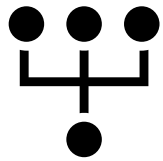
Ownership interest does not include
ownership through constructive ownership or attribution

Ownership Interest (2/4)

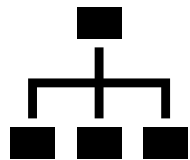
Three Part Test

- **Calculation to determine whether individual owns | controls 25% of Ownership Interests in Reporting Company.**
 - ***Individual's total ownership interests*** determined at present time, treating options and similar interests as exercised, and calculated as a % of total outstanding ownership interests in the Reporting Company.
 - ***Reporting Companies that issue capital and profits interests*** (including entities taxed as a partnership) and calculated as a % of the total outstanding capital and profits interests in the entity
 - ***Corporations that issue shares of stock***, individual's % is equal to vote/value to total outstanding vote/value of all classes entitled to vote, or of ownership interests, as the case may be
 - ***"Catch-all rule."*** If above calculations cannot be performed with certainty, an individual is deemed to hold 25% or more of total ownership interests provided individual owns or controls 25% or more of any class of ownership interests

Other 25% Ownership Interest (3/4) Reporting Rules



Joint Interests. If several individuals own a 25% interest in a Reporting Company, the 25% interest is attributed to each joint owner as if that person owned that interest



Intermediate Entities. Ownership or control of a Reporting Company's interest through one or more intermediate entities attributed to the owners of the intermediate entity(s), irrespective of whether the intermediaries own the interests separately or collectively

Ownership Interests (4/4)

Comments

Purpose of Rule: To identify Beneficial Owners of Reporting Companies in complex ownership/investment structures

Determination based on:

- Facts and circumstances
- Direct and indirect ownership interests considered

Persons Excepted from Beneficial Owner Status?

- **Minor children** (provided Reporting Company reports required information of a parent/guardian)
- **Nominees, intermediaries, custodians, or agents** (in these relationships, reporting of principal required)
- **Employee** of a Reporting Company, acting solely as an employee, provided individual is not a Senior Officer and substantial control/economic benefits from Reporting Company derived solely from employment status
- **Inheritor** Individual whose only interest in a Reporting Company is a future interest through a right of inheritance
- **Creditor** of Reporting Company who only has a right to be paid a predetermined sum of money who meets the definition of a beneficial owner solely through a loan covenant (or similar right) intended to secure their right to receive repayment

How Do Common Law Trusts Interact with the CTA?

Common Law Trusts

- **Common law trust**

- Not a Reporting Company, because not created by filing a document with a secretary of state
- While trusts appear to be exempt for now, that could change in the future
- Why? The CTA calls for future study of trusts, partnerships, and other legal entities
- Registering a common law trust with a court does not cause the trust to be a Reporting Company (the process of registration allows the state to preside over disputes involving the Trust)

- **Statutory trust**

- Considered to be a juridical category, separate from the parties to a common law trust
- Considered to be a business organization
- Thus, an investment fund structured as a trust to do business in a state may constitute a Reporting Company

Reporting by a Trust | Beneficiary | Grantor

Operating Rules

- A trustee exercises Substantial Control over a Reporting Company
- A trust owning or controlling 25% or more of a Reporting Company implicates reporting by:
 - Each trustee
 - If the trustee is a corporate trustee, query whether reporting stops at the corporate trustee level or is one required to identify the trust officer(s) who work on the trust for the corporate trustee?
 - Any individual with authority to control or dispose of trust assets, to include:
 - Each beneficiary who is the sole permissible recipient of income and principal from the trust
 - Each beneficiary who has a right to demand a distribution of, or withdraw substantially all assets from, the trust
 - Each grantor or settlor who has a right to revoke the trust or otherwise withdraw trust assets

Ownership interests held in trust could be considered simultaneously as owned or controlled by multiple parties in a trust arrangement

Who
Is a
Company Applicant?

Company Applicant Operating Rules

- **Definition (can only be two Company Applicants)**
 - For a **Domestic Reporting Company**.
 - Company Applicant No. 1. The individual who directly files the creation document with the secretary of state
 - Company Applicant No. 2. The individual primarily responsible for directing or controlling the filing of the creation document
 - For a **Foreign Reporting Company**.
 - Company Applicant No. 1. The individual who directly files the document that first registers the Reporting Company with the Secretary of State
 - Company Applicant No. 2. the individual primarily responsible for directing or controlling the filing of the registration document
- **Examples**
 - Two Company Applicants. Attorney primarily responsible for overseeing preparation and filing of incorporation documents and paralegal, at attorney's request, directly files docs with a state office to create the Reporting Company
 - One Company Applicant. An individual creates a Reporting Company and files its formation documents (w/o assistance of a business formation service, law firm, or similar service)
 - Where a business formation service provides software, online tools or applicable written guidance, an employee of the service company is not Company Applicant.
 - Contrast that situation where a service company employee personally files the document to form a company -- here, employee is a Company Applicant

Takeaways



Revised definition in Final Regulations designed to identify the individual responsible for the creation of a Reporting Company through the filing of formation documents, **and** the individual that directly submits the formation documents, if that function is performed by a different person



Revision reduces potential burdens of keeping track of Company Applicant *by limiting the definition of Company Applicant to only one or no more than two* individuals

Compare that to definition in Proposed Regulations, requiring multiple persons “in the chain” to be identified as Company Applicants



Lawyers who provide legal services are not considered beneficial owners because ordinary, arm’s length advisory or other third-party professional services to a Reporting Company are not considered to be “substantial control”

In addition, a lawyer who is designated as an agent of the Reporting Company may qualify for the “nominee, intermediary, custodian, or agent” exception from the beneficial owner definition.

What Information Must Be Disclosed in a Report?

Information Required to be Disclosed in Report

Reporting Company

- Complete Legal Name
- Tradename, “doing business as” (dba), or trading as (t/a) names
- Business address:
 - For Reporting Company with a principal place of business in US
 - For a foreign Reporting Company with a principal place of business outside US -- provide street address of primary location in US where company conducts business
- Domestic Company. State/Tribal jurisdiction of formation
- Foreign Company. Jurisdiction of Registration
 - State/Tribal jurisdiction where company is first registered
- IRS TIN (including EIN)
 - Where foreign reporting company does not have a TIN, use the tax ID issued by a foreign jurisdiction and provide name of foreign jurisdiction

Personal Identifiable Information (“PII”)

- Full legal name
- Date of Birth
- Current Residential Address*
- Unique ID number and issuing jurisdiction from **only** acceptable ID document (non-expired (i) passport, (ii) state or local ID document, (iii) driver’s license)
 - If individual has none of the foregoing, a non-expired foreign passport
- Image of document from which the unique ID number was obtained

* If Company Applicant is in business of corporate formation (e.g., an attorney), then use business address rather than residential address

What
Is a
FinCEN Identifier
&
How Does the New FinCEN Identifier Entity
Rule Work?

What is a FinCEN Identifier & Who Should Get One?

- **What Is It?**

- A unique ID number assigned by FinCEN to an individual (Beneficial Owner or Company Applicant) to be submitted to a Reporting Company to be used in the Report in lieu of individual's PII
- Reporting Company can also obtain a FinCEN Identifier for use on a Report

- **Why Would An Individual Get One?**

- For data security purposes -- so individual's PII is protected -- individual submits PII to FinCEN and FinCEN Identifier to Reporting Company, so individual's PII not submitted to Reporting Company
- For administrative efficiency -- if individual, either Beneficial Owner or Company Applicant required to file numerous Reports

- **How to Obtain FincCEN Identifier?**

- Individual. Submits electronic web form application containing PII to FinCEN and certifies information is true, correct & complete
- Reporting Company. Can request a FinCEN Identifier at or after the time that Reporting Company submits an Initial Report (by checking a box) or, if after submitting its Initial Report, by submitting an Updated BOIR, requesting a FinCEN Identifier, even if company does not need to update information

FinCEN Identifier Updated or Corrected Information

- **Change in Information**

- Individual. Within 30 days of change of PII, individual must file an application with FinCEN with updated PII
 - Note, currently there is no way of deactivating a FinCEN Identifier to eliminate filing changes. FinCEN is assessing options to fix that issue
- Reporting Company. File an Updated Report within 30 days of change

- **Correct Inaccurate Information**

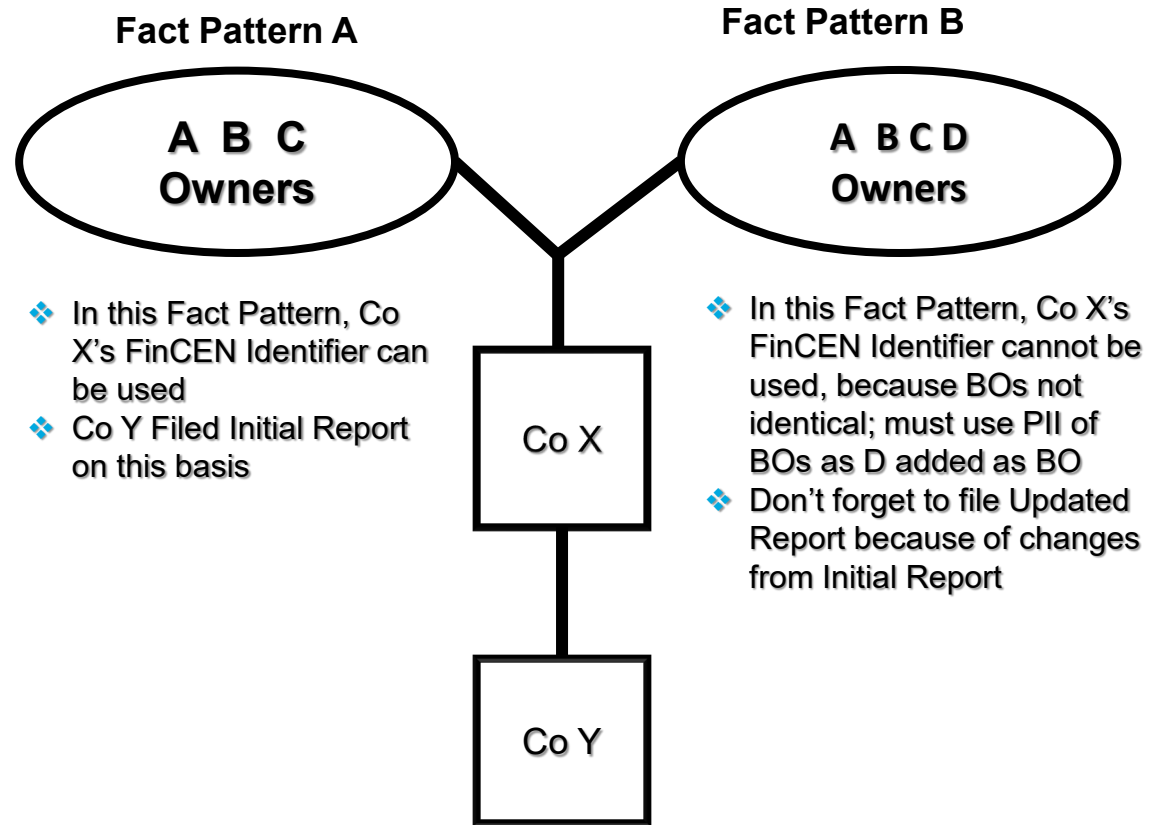
- Individual. Must file a corrected application within 30 days after date on which individual became aware or has reason to know of inaccuracy
 - A corrected application filed within 30-day period will be deemed to satisfy safe harbor if filed within 90 calendar days after the date on which the inaccurate application was submitted
- Reporting Company
 - Same rule, but files an Updated or Corrected Report

New FinCEN Identifier Rule for Entities

- **Rule.** A Reporting Company may report another entity's FinCEN Identifier and full legal name in lieu of the PII required with respect to a Beneficial Owner (Slide 37) only if:
 - The other entity has obtained a FinCEN Identifier and provided that FinCEN Identifier to the Reporting Company
 - An individual is, or may be, a Beneficial Owner of the Reporting Company *by virtue of an interest in the Reporting Company that the individual holds through an ownership interest in the other entity*; and
 - The Beneficial Owners of the other entity and of the Reporting Company are the same individuals

Illustration of Rule

- The FinCEN Identifier Entity Rule applies if the Beneficial Owners (BOs) of Co X and of Company Y are the **same** individuals
- BOs determined by Substantial Control and 25% Ownership test
- If Co X has obtained a FinCEN Identifier, and BOs (Senior Officers), 25 % Owners and all Directors in both Co X and Co Y are identical, then Co X's FinCEN Identifier, rather than PII of BOs of Co X, can be used by Co Y for reporting CO X's BOs
- But if BOs not identical, then PII of BOs of Co X must be reported, rather than using Co X FinCEN Identifier



What is the Current Status of the Beneficial Owner Information Report?

Form of Report & Certification

- **FinCEN to prescribe form & manner of Beneficial Owner Information Report (BOIR)**
 - FinCEN developing Report
 - Form will be posted on FinCEN webpage
 - FinCEN will not accept reports before January 1, 2024
 - Parent company cannot file a single Report on behalf of group of companies
 - Company does not have to file a Report if it has always been exempt
- **FinCEN anticipates most filings of Report will be filed electronically**
 - Paper filing required if foreign person that doesn't have an ITIN by time of filing and had applied for an EIN
 - Foreign companies that are not subject to US corporate income tax may report a foreign ID and the name of the relevant jurisdiction instead of an EIN
- **Certification: Reported information is “true, correct, and complete”**
 - FinCEN emphasized that it *“believes that it is reasonable to require reporting companies to certify the accuracy and completeness of their own reports, and it is appropriate to expect that reporting companies will take care to verify the information they receive from their beneficial owners”*
- While an individual may file a Report on behalf of a Reporting Company, Reporting Company is ultimately responsible for filing and the Certification
- Reporting Companies may use third-party services provider to submit BOIR Forms

The Final Regulations do not contain any mechanism to verify accuracy of information reported

THIS IS A MAJOR DEFICIENCY IN SYSTEM

Beneficial Owner Information Reports Conceptual Basis (1/2)

- **Overview**

- The reporting form is known as the Beneficial Ownership Information Report (BOIR)
- A BOIR will collect information about: (i) the Reporting Company, (ii) Beneficial Owners, and (iii) Company Applicants
- A BOIR will be filed by completing the BOIR form and submitting it through an online portal or submitting the information through an Application Programming Interface (“API”)
- The collected information will be maintained by FinCEN and made accessible to authorized users of the Beneficial Ownership Information Technology System

- **Comments on Initial Form**

- FinCEN’s initial proposed BOIR had “unknown checkboxes,” *i.e.*, checkboxes that would allow a Reporting Company to indicate if certain information about a Beneficial Owner or Company Applicant was “unknown” or if the Reporting Company was unable to identify information about a Beneficial Owner or Company Applicant.
- Commentators had expressed concern that these checkboxes would incorrectly suggest to filers that it was optional to report required information and that a Reporting Company was not required to conduct a diligent inquiry to comply with their reporting obligations and that these unknown checkboxes should be removed

Beneficial Owner Information Reports Conceptual Basis (2/2)

- **New Proposal on Form**

- FinCEN is pursuing a revised approach; the BOIR Form no longer will contain unknown checkboxes
- *First implementation commencing January 1, 2024:*
 - Every field must be completed
 - BOIR Form only can be submitted once each required field has been filled out
 - Any field left blank, will prevent the filer from submitting the BOIR Form
- *Alternative implementation that may be adopted at a later date following feedback from stakeholders:*
 - Same response fields as in first implementation
 - However, in addition, a new mechanism for filers to temporarily indicate if they are unable to provide certain information for certain reasons, through drop-down options in the Beneficial Owner section (but not other sections) to ascribe reasons why they were unable to provide a piece of information about a Beneficial Owner
 - Reasons would include: (i) “Cannot Contact BO,” (ii) “BO Unresponsive,” (iii) “BO Refused to Provide,” (iv) “Third Party Refused to Provide.”
 - Forms whose filers select a drop-down option will be accepted into the filings system but will still be considered incomplete and non-compliant filings
 - Forms will only be considered complete and compliant once the missing information is subsequently added, the drop-down option is removed from each field, and the form is updated
 - Drop-down option would allow Reporting Companies to submit all available information, but not excuse requirement to submit complete and truthful responses

Questions on BOIR Form In Summary

- Type of filing (Initial/Corrected/Updated/New Exempt Entity)
 - Reporting Company Information
 - Company Applicant Information
 - Beneficial Owner Information
-
- The Request for Comments also contains date fields for the Potential Second Implementation for Beneficial Owners, by inclusion of drop-down boxes where filer is unable to obtain information

When Are Reports Due?

Initial Report Due Dates

- **Pre-2024 Reporting Companies** (Formed | Registered prior to January 1, 2024):
NLT January 1, 2025

Reporting Company Formed or Registered in 2024 must file Report within **90** days of the *earlier* of :

- Date on which Reporting Company received actual notice that its creation/ registration became effective *or*
- Date on which a secretary of state or similar office first provides public notice, such as through a publicly accessible registry, that Reporting Company has been created (domestic) or registered (foreign)

Reporting Company Formed or Registered in 2025 or Thereafter must file Report within **30** days of the *earlier* of :

- Date on which Reporting Company received actual notice that its creation/ registration became effective *or*
- Date on which a secretary of state or similar office first provides public notice, such as through a publicly accessible registry, that Reporting Company has been created (domestic) or registered (foreign)

FinCEN has specified Initial Report only should include Beneficial Owners as of the at time of the filing,
and not historical Beneficial Owners

Updated | Corrected Due Date

Updated Report:

- Within **30** days of a change in the required information previously submitted to FinCEN relating to Reporting Company or its Beneficial Owners
- Company Applicant changes do not require Updated Report, assuming information reported was correct, but a Corrected Report required if information was not correct
- **But** a FinCEN Identifier requires that individual file Updated FinCEN Application

Corrected Report:

- Errors in Reports filed remedied by filing a corrected report within **30** days of becoming aware or having a reason to know of inaccuracies in an earlier Report
 - Unclear whose knowledge triggers 30 day start period
 - *Safe Harbor for Liability from Penalties.*
See Slide 56

What Changes Require an Updated Report?

General Rule



Updated Report required only where Reporting Company information or individual's PII previously submitted on Report changes



PII changes include name, address or unique ID number previously provided to FinCEN

Updated Report not required upon change in personal characteristics on ID document

Examples

Reporting Company that was exempt but no longer meets exemption criteria

- Updated Report within 30 calendar days after date that exemption criteria is not met

Reporting Company meets exemption criteria subsequent to filing of an Initial Report

- Updated Report within 30 days of change of status + indicate on BOIR that company no longer is a Reporting Company

Minor child attains age of majority

- Updated Report within 30 days after child reaches majority

Deceased Beneficial Owner

- Updated Report must identify new beneficial owners within 30 days of the settlement of the estate (see next slide) of the deceased beneficial owner
- Updated filing arises because the deceased individual was a beneficial owner by virtue of property interests or other right subject to transfer upon death

Decedent Rule

- Complicated
- A future interest of an individual in a Reporting Company through a right of inheritance is **not** an ownership interest and is not reportable
- Upon the inheritance by an individual of an ownership interest, the individual has the same relationship to an entity as any other individual who acquires an ownership interest through any means
- This means, for purposes of the CTA, that such person's interest becomes reportable within the requisite 30-day period, only if his or her interest is a reportable interest
- Unclear as to when the 30-day period commences in respect of the “settlement” of the decedent's estate, which could be through intestacy or a testamentary disposition
 - One commentator has suggested that appointment of a personal representative or executor may be the triggering event, since appointment is the event that grants the power to transfer the interests in the Reporting Company

What Are the Penalties for Non- Compliance?

Penalties

- **Overview of Reporting Violations**

- Failure to Report
- Failure to Update BOI
- Failure to Correct Inaccurate BOI

- **Rule.** *It shall be unlawful for any **person** to **willfully** provide, or attempt to provide, false or fraudulent **beneficial ownership information**, including a false or fraudulent identifying photograph or document, to FinCEN, in accordance with this section, or to **willfully** fail to report complete or updated **beneficial ownership information** to FinCEN in accordance with this section*

- **Penalties.**

- *Civil Penalty.* \$500 per day in civil monetary penalties
- *Criminal Penalty.* \$10,000 fine, imprisonment of no more than 2 years, or both
 - Safe Harbor (for liability from penalties).
 - **No penalties for filing an inaccurate report provided report corrected within 90 calendar days of when it was filed.**

Reporting Violation Regulatory Expansion

- *The term "person" includes any individual, reporting company, or other entity*
- *The term "beneficial ownership information" includes any information provided to FinCEN under this section*
- *A person provides or attempts to provide beneficial ownership information to FinCEN if such person does so directly or indirectly, including by providing such information to another person for purposes of a report*
- *A person fails to report complete or updated beneficial ownership information to FinCEN if, with respect to an entity: (i) such entity is required, pursuant to Title 31, United States Code, section 5336, or its implementing regulations, to report information to FinCEN; (ii) the reporting company fails to report such information to FinCEN; and (iii) such person either causes the failure, or is a senior officer of the entity at the time of the failure*

Meaning of Willfully

- The CTA statute defines “willfully” as the “voluntary, intentional violation of a known legal duty” 31 U.S.C. § 5336(g)(6)
- Civil and criminal penalties arise if non-reporting, failure to update reporting or incorrect reporting based on willfulness
- An act is done "willfully" if done voluntarily and intentionally and with the specific intent to do something the law forbids. There is no requirement that the government show evil intent on the part of a defendant in order to prove that the act was done "willfully"

Takeaways

- Assessment of potential violations will depend on all the facts and circumstances

As stated in the Preamble to the Final Regulations: “As a general matter, FinCEN does not expect that an inadvertent mistake by a reporting company acting in good faith after diligent inquiry would constitute a willfully false or fraudulent violation”

- Although it is the Reporting Company that is obligated to file the report with FinCEN, penalties may apply to:
 - The Reporting Company
 - An entity or an individual who causes a Reporting Company not to report
 - Individuals who are Senior Officers of a Reporting Company at the time a Reporting Company fails to accurately and completely report or update/correct its report
- Reporting violations were extended to include individuals because individuals are the persons who primarily will provide information about themselves to Reporting Companies in order for the Reporting Company to comply with its CTA reporting obligations
- Further, absent individual liability, illicit actors who form entities and fail to report may not be deterred if liability were applicable only to entities

What Steps Should One Take To Comply?

First Step

The CTA's
Effective Date
Is Imminent
So Prepare Now

CTA Compliance Plan

- Explain CTA reporting regime to Company management and owners
- Appoint a Responsible Officer for CTA reporting purposes – Responsibilities: information gathering, updating/correction & confirmation of facts | storage & security of information | reporting | CTA developments | dealing with FinCEN
- Determine whether Entity is a Reporting Company
 - Is it out of scope?
 - Do any of the 23 Exemptions apply?
- If not, Entity is a Reporting Company
- Determine Beneficial Owners, based on the Substantial Control and 25% Ownership Tests
- Are any of the Beneficial Owners excluded from having to be reported?
- Address privacy issues and concerns for Reporting Company, Beneficial Owners and Company Applicants
- Determine when Initial Report is due
 - Confirm all requisite information to report for the Reporting Company, Beneficial Owners and Company Applicants (if applicable) is available and correct
- File Report
- Consider CTA implications in content of existing and new organizational and transactional documentation (representations | warranties | covenants | indemnifications)
- **Adopt processes and procedures to inform and thereafter alert Beneficial Owners about timely and correctly reporting changes – this is absolutely key**

Develop CTA Model Provisions for Documentation

General

- CTA will impact a broad range of transactional activities, including:
 - Corporate
 - Finance
 - Banking
 - Real Estate
 - Private Equity
 - Private Wealth
 - Tax
 - Aviation
 - Data Privacy

Illustrations

- LLC Operating Agreements
- Shareholder Agreements
- JV Agreements
- Purchase Agreements
- Loan Agreements
- M&A Due Diligence Checklists
- Private Wealth Documentation
- Reps/Warranties/Covenants
 - Transactional
 - BMS/AML
- Indemnification/Liability Provisions
- Risk Factors in Offering Documentation

How to Enforce Compliance

- What do you do if PII is not provided?
- How does one enforce compliance by Beneficial Owners/Company
Applicants re: cooperation to provide: accurate | timely | & updated Information?
 - Indemnification?
 - Suspension of distributions?
 - Expulsion?
 - Other?

Privacy Planning & Protection

- The CTA will require the collection, maintaining, securing, processing, updating and sharing of data, particularly PII
- A Reporting Company will need to consider its potential exposure, both in the US and abroad, in connection with the data and its CTA obligations
- Privacy policy agreements are required by law, both within and without the US
- A Reporting Company should consider modifying its privacy policies to deal with data and the CTA
- These laws generally contain an exception to sharing data with governmental authorities to the extent required by law, which is the case with the CTA
- Data submitted to FinCEN is not subject to public access
- A Reporting Company should also enter into an agreement with its respective owners and those who may be in control, whereby each Beneficial Owner agrees to provide and update their PII and **explicitly** consents to the Reporting Company furnishing the Beneficial Owner's PII (initial and updated PII) to FinCEN. The agreement also should deal with other issues, such as maintaining and securing PII, non-disclosure of the Beneficial Owner's PII to other than FinCEN, and indemnification for costs and penalties if a Beneficial Owner does not furnish his/her PII to the Reporting Company
- If Beneficial Owners are from abroad, particular attention must be paid to the collection of data from non-US persons as non-US laws may apply to Reporting Companies in the US or abroad – important to check laws of applicable jurisdictions and modify agreement

Bottom Line:

Important to obtain advice from a privacy professional relating to privacy aspects

European Union & UK*

Privacy Issues

- EU and UK data protection requirements are similar
- Gathering and providing information on Beneficial Owners to US authorities involves processing of personal data
- Key considerations:
 - **Applicability** of EU and UK GDPR (including to non-EU/UK Reporting Companies);
 - Ensuring **fair and lawful processing** (includes any collection, storage, disclosure or use);
 - Complying with the **requirements on international transfers**
- EU and UK GDPR apply to organisations established in the EU/UK and to organisations established outside the EU/UK that offer goods and services to individuals in the EU/UK (targeting them) or monitor their online behaviour (Article 3 of the EU/UK GDPR)
- Fair processing requires provision of a compliant privacy notice, unless limited exemptions apply
- Lawful processing requires a lawful ground to be in place. Necessity for legitimate interests likely to be the best option (requires assessment) or necessity for task in the public interest is another, but would need more careful consideration based on the circumstances (and related registration regime)

* Information provided by Lawrence Brown and Eric Le Quellenec, Partners in the London and Paris offices, respectively, of Simmons & Simmons

United Kingdom Privacy Issues

- In relation to international transfers, the general rule is that transfers to the US are only permitted if adequate safeguards are in place (for example, Standard Contractual Clauses). EU-US Privacy Framework (and UK Data Bridge) do not apply to transfers to FinCEN.
- Limited exceptions for one-off or occasional transfers apply but these are limited to:
 - Necessity in the public interest (same challenges as above); or
 - Transfers from a register available either to general public or to those demonstrating a legitimate interest, where provided for under EU/UK law

Bottom Line:

Information is key and the Reporting Company must make the Beneficial Owner aware of the processing under the CTA, even if no cross-border flow is identified in the meaning of the GDPR

Additionally, the Reporting Company must ensure there is a documented lawful basis for the disclosure to FinCEN and, where applicable, comply with the international transfer requirements

Switzerland*

Transfer of Swiss UBO personal data to the U.S.

- Under the Swiss Federal Data Protection Act (“DPA”) – the required Ultimate Beneficial owner (UBO) information qualifies as personal data
- According to the DPA, personal data may be disclosed abroad if the Federal Council has decided that the legislation of the State concerned or the international body guarantees an adequate level of protection (Art. 16 para. 1 DPA)
- The US does not have an adequate level of data protection (Annex 1 of the Ordinance on Data Protection)
- *Exception:* According to the DPA, personal data may be disclosed abroad if the data subject has explicitly consented to disclosure (Art. 17 para. 1 let. a DPA)
- In case of violation, fines of up to 250,000 Swiss francs may apply
- **Conclusion:** US / Foreign reporting companies should obtain explicit consent in advance from the shareholders / UBOs that the personal data of the Shareholders / UBOs may be disclosed to FinCEN

* Information provided by Dr. Daniel Lucien BÜHR, Partner, LALIVE, Zurich Switzerland

CLE Information

CTA Exemption Planning?

Introduction

- In this section, we discuss some of the more important of the 23 exemptions
- It will be important to consider these exemptions in the context of your operations and to determine whether any of the exemptions apply, or whether you can restructure your operations so that an exemption becomes applicable
- In terms of exemptions, FinCEN advises:
 - It is appropriate to interpret ambiguities in exemptions “reasonably narrowly”
 - The definition of a Reporting Company is broad, the exemptions are “carefully circumscribed”

Large Operating Company

- **Rule.** An entity that:
 - Employs more than 20 full-time employees in the continental United States
 - Has an operating presence (owned/leased) at a physical office within the United States, and
 - Has filed a federal income tax or information return in the United States for the previous year demonstrating more than \$5 million in gross receipts or sales from US sources
- **Favored Structure:** Parent Co is an operating company | with its own offices | employees | and income and owns 100% equity of lower tier subsidiaries so as to claim Subsidiary Exemption (discussed infra)
- **Issues:**
 - Must have filed a return for a prior year (so exemption does not apply to start-up in first year)
 - Foreign source sales/receipts excluded (contrary to how US income tax return works)
 - Is office and employees in company claiming exemption? If not, exemption not available
 - But gross receipts from a transparent entity or from a consolidated group counted
 - If requirements not met, can one restructure?

Bank



A bank defined in:

Section 3 of the Federal Deposit Insurance Act

Section 2(a) of the Investment Company Act of 1940

Section 202(a) of the Investment Advisers act of 1940



Comment. Consider whether a Private Trust Company (“PTC”), which functions as a trustee for family trusts and is supervised and examined by a state banking authority, would be considered a “bank” under the ’40 Act and excluded from the definition of a Reporting Company?

Investment Company, Investment Advisors & Certain Pooled Entities



Investment company registered with the SEC



Investment advisor registered with the SEC



Venture capital fund advisor filing with the SEC



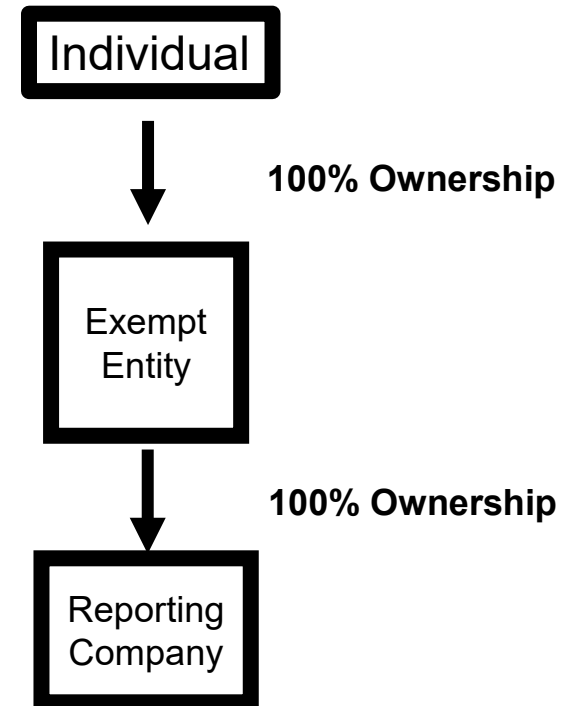
Certain pooled investment vehicles advised by other exempt entities (*i.e.*, bank, credit union (federal or state), broker or dealer in securities, federally registered investment advisor, or venture capital fund advisor)

Subsidiary Exemption

- An entity whose ownership interests are **controlled** or **wholly owned**, directly or indirectly, by one or more exempt entities (other than those listed below) is not a Reporting Company
 - Subsidiary Exemption Rule does not apply if subsidiary is owned by:
 - a money transmitting or money services business,
 - a pooled investment vehicle,
 - an entity assisting a tax-exempt entity, *or*
 - an inactive entity
- Note, this exemption requires an entity to be **owned** entirely by one or more specified exempt entities in order to qualify the entity for the exemption
- FinCEN does not need to add “**wholly**” before “**controlled**” because FinCEN assesses that the latter covers the intended concept of control set out in the CTA

Special Rule: Individual Owning Reporting Company through Exempt Entity

- **Special Rule.** If one or more exempt entities has or will have a direct or indirect ownership interest in a Reporting Company, and an individual is a beneficial owner of the Reporting Company exclusively by virtue of the individual's ownership interest in such exempt entities, the Report **may include** the names of the exempt entities in lieu of the PII with respect to the individual beneficial owner
 - **Note, Reporting Company has option to ID BO, rather than identify exempt entity**
- Note, this special rule applies only if there is ownership by the individual, but not if individual is in substantial control of the Reporting Company through the exempt entity



Private Wealth: Family Offices, PTCs, Subsidiary Exemption

Family Office

- A family office organized as an LLC, LP, or a corporation by definition is a domestic reporting company
- Possible exemptions:
 - Large operating company
 - A registered investment advisor under the Investment Advisors Act of 1940 (multi-family office)
 - Venture capital fund advisor under Investment Company Act of 1940
 - Commodity pool operator |commodity trading advisor | or other entity registered with the CFTC

Private Trust Company (PTC)

- A registered PTC may be exempt as a “bank” under the Investment Company Act of 1940 if it provides fiduciary services for family trusts and is state supervised and examined

Subsidiary Exemption

- Entities owned by an exempt family office or PTC may be exempt from the CTA reporting requirements under this exemption

Inactive Entity

- This exemption applies to an entity that meets the following conditions:
 - **Was in existence on or before January 1, 2020** (date of CTA enactment)
 - Is not engaged in active business
 - Is not owned by a non-US person, whether directly or indirectly, wholly or partially
 - Has not experienced any change in ownership in the preceding twelve-month period
 - Has not sent or received any funds in an amount greater than \$1,000, either directly or through any financial account in which the entity or any affiliate of the entity maintains an interest, in the preceding 12-month period, and
 - Does not otherwise hold any kind or type of assets, whether in the United States or abroad, including any ownership interest in any corporation, LLC, or other similar entity

Tax Exempt Entity

- This includes:
 - Generally, nonprofit organizations that are exempt from tax (IRC § 501(c) & (a))
 - Private foundations (IRC § 501(c)(3))
 - Certain political organizations qualify (IRC § 527(e)(1) & (a))
 - Certain trusts described in IRC § 4947(a) (1) or (2) qualify
- The peculiar case of Homeowner Associations (HOAs)
 - More than 370,000 HOAs in the US
 - Although most HOAs are formed as not-for-profit corporations under state law, and many are exempt under IRC § 528, they would not be an exempt entity under the CTA since the CTA exemption does not encompass IRC § 528
 - To be exempt, these HOAs would have to apply for an exemption under IRC § 501(c)(4) or 501(c)(7), which likely would not be worth doing
 - HOAs also would have a challenge in reporting since they do not have shareholders

Impacts & Questions Under the CTA?

Impacts & Questions

SOME IMPACTS

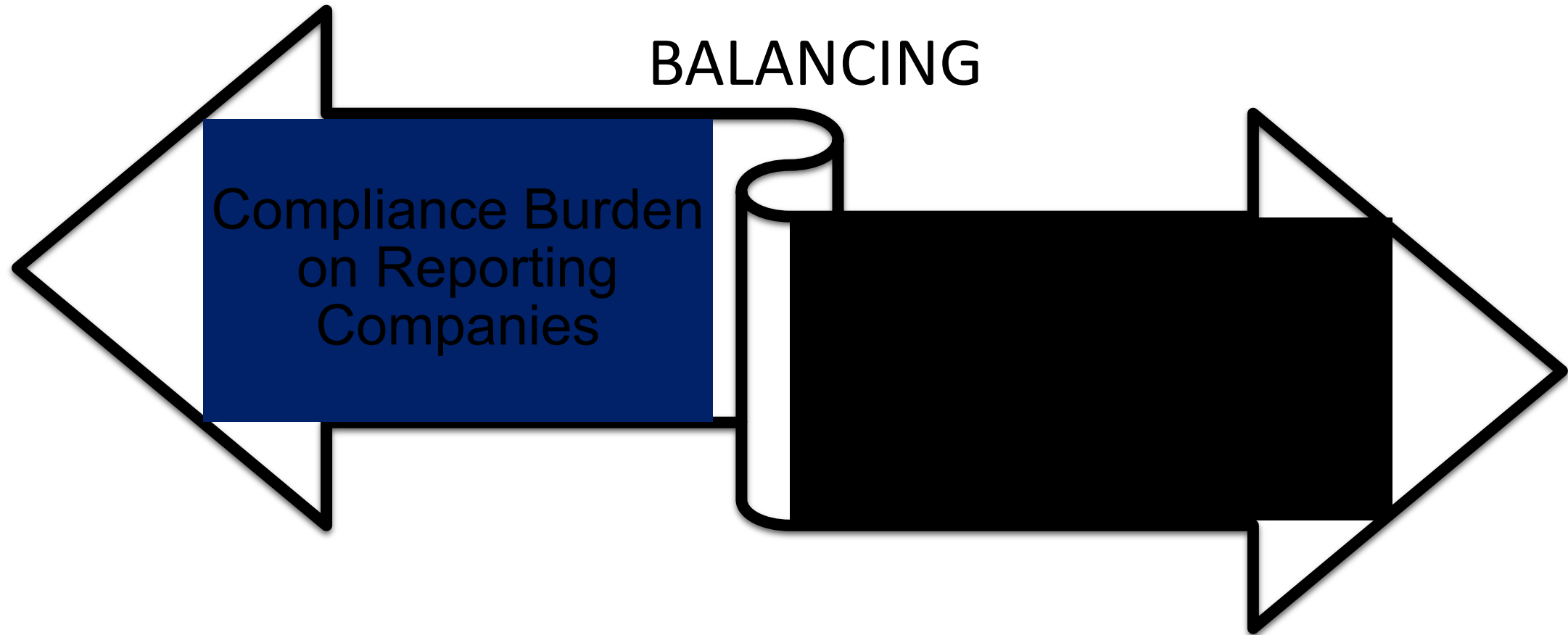
- Imposes administrative burden on small, privately owned, non-regulated businesses, as public and heavily regulated companies excepted
- Will impact not only Reporting Company but also its Beneficial Owners

SOME QUESTIONS

- How will foreign companies and their BOs be apprised of the CTA?
- How will Reporting Companies keep track of BOs and changes to their information?
 - Internal procedures and/or software?
- Do law firms | professional services firms | other firms -- have an obligation to inform current clients? | Prior clients?
- How will law firms and others deal with entity formation | Company Applicant | FinCEN Identifiers?
- How does one deal with recalcitrant BOs?
- How will PII be verified? If no verification, how useful is information?
- New transparency initiative – in states | federal legislation | overseas
- Will CTA alter behavior of foreign persons use of US LLCs for privacy protection purposes?

FinCEN Challenges, Developments & Resources

FinCEN's Balancing Challenge



What FinCEN Still Needs to Do Prior to Year-End Re Reporting Rule



Finalize Beneficial Ownership Secure System (BOSS)

Publish the technical specifications of the Application Program Interface (API) to link filers to FinCEN's BOSS

Finalize Beneficial Owner Information Reporting Form

Publish application procedure for an individual to obtain a FinCEN Identifier

Roll out Contact Center – where stakeholders can ask questions

Further outreach to stakeholders and Secretaries of State

Further Explanation of Guidance through FAQs

Recent FinCEN Information and Assistance

- **FinCEN's BOI Webpage**
- **Small Entity Compliance Guide**. To assist potential filers in complying with the beneficial ownership information (BOI) reporting rule
- **Revised & New FAQs**. To provide amplified guidance about BOI Reporting Requirements
 - (Currently, there are FAQs in 14 topics)
- **FinCEN Contact Center**. FinCEN will launch a hotline and chatbot to help answer questions about the beneficial owner information requirements (go to FinCEN web page)

What's New?

Lawsuit Challenging CTA

- **Plaintiffs Assert:** CTA unconstitutional because it infringes on protected rights of state sovereignty, privacy and due process
 - Called CTA: “A law enforcement dragnet of sweeping proportions imposed by Congress on law-abiding U.S. citizens and permanent residents who own or control small businesses”
- **Case:** *National Small Business United et al. v. Yellen et al.*, case number 5:22-cv-01448, in the U.S. District Court for the Northern District of Alabama

State Law Developments

- New York (NY), Massachusetts (MA) and California (CA) are considering state analogs to the CTA, with the major difference that under the proposed legislation of the states, the information would be accessible to the public, unlike the CTA
 - The New York LLC Transparency Act is awaiting action by the Governor.
 - The MA “An Act to Ensure LLC Transparency” is modeled after NY’s bill
 - The CA legislation would go beyond NY and MA by imposing beneficial ownership reporting requirements on corporations and real estate investment trust that are organized as unincorporated associations under CA law
- NY and CA would publish the legal names and current business addresses of true owners on searchable, online databases maintained by the secretaries of state
- MA treats the information as a public record subject to public records requests
- Why are the states doing this?
 - NY and MA are concerned about how LLCs facilitate anonymous real estate purchases, which, in turn, has prevented tenants from discovering the true identities of negligent landlords
 - CA is concerned about how anonymous entities facilitate employers to avoid accountability for labor violations
- Proposed legislation has raised confidentiality and privacy concerns
- For a good article on the subject, see Amy Hamilton, *More States Considering Public Databases of LLC Beneficial Owners*, Tax Notes (Nov. 28, 2023)

QUESTIONS???

Panelists

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Thank You!