

Can You See Me Now? The Corporate Transparency Act

Description

Title professionals are no strangers to the difficulties in getting to the bottom of ownership issues for those operating a business through opaque entities. Peeling back the layers is often required to get to the ultimate owner. The anonymity provided is important to some companies as a means of legally doing business. However, these same entities make it easy for criminals to hide their illegal gains and thwart investigations into illegal activities.

In 2021, Congress passed the Corporate Transparency Act (CTA) to shed light on these entities; it became effective January 1, 2024. To protect the national interest and to counter criminal behavior, the CTA provides for the collection of ownership information in a confidential manner. Financial Crimes Enforcement Network (FinCEN) has issued rulings to provide guidance on the CTA. Next is an overview of the details of reporting along with the penalties for noncompliance and who will benefit from the transparency. This article wraps up with a report on the U.S. District Court case that has held the CTA to be unconstitutional.

Who must report?

Nonexempt entities incorporated, organized, or registered to do business with a state or commonwealth (State) must disclose beneficial ownership information (BOI). The CTA requires small legal entities, both domestic and foreign to file information about the owners, individuals that control the entity, and, if formed after January 1, 2024, the individuals who formed them. The CTA names 23 entity types that are exempt, largely those companies already subject to reporting. The exemptions include insurance companies, some tax-exempt entities, subsidiaries of exempt entities, and inactive entities. A large company is also exempt, if the entity employs more than 20 employees in the U. S., files income taxes showing more than 5 million dollars in gross receipts and operates from a physical office in the U.S. Sole proprietorships, general partnerships, and some trusts are not subject to the CTA because they do not register with the State.

Looking closer at the insurance company exemption, an entity qualifies for the exemption if 1) its primary business is writing insurance or reinsuring risks underwritten by insurance companies and is subject to supervision of the State, or any liquidating agent of such company (15 U.S.C. 80a-2); or 2) a) an insurance producer that is authorized by and subject to supervision of the State, and b) has a physical office within the U.S.

Who is a beneficial owner?

A beneficial owner is an individual who directly or indirectly either exercises substantial control or owns or controls at least 25 percent ownership interest. Individuals have substantial control if they satisfy one of the following: are a senior officer; have authority over senior officers or most of the board; have substantial influence over the company's important decisions; or have other substantial control. Individuals that cannot be considered beneficial owners are minor children (parents or legal guardians must claim their interest); a nominee, intermediary, escrow officer or agent; an employee solely acting as an employee (not a senior officer); those with a future interest; and a creditor of the reporting company unless they exercise substantial control or have 25 percent interest.

What must be reported and when must it be reported?

The information that must be reported for the entity includes the full legal name and any trade names, the address of the entity and jurisdiction of formation, and the entity's federal taxpayer ID number. The information that must be reported for each beneficial owner is full legal name, date of birth, home address, unique identifying number and issuing jurisdiction from a U.S. passport and an image of the U.S. passport. Alternatively, one of the following: state driver's license or identification issued by state, local government, or tribe, and if none, then a foreign passport.

Entities created or registered prior to January 1, 2024, will have one year to report. Entities created after January 1, 2024, will have 90 days from their creation to report. Entities created after January 1, 2025, will have 30 days to report. Entities must file amendments within 30 days of a material change of the reported information such as ownership or address.

What are the penalties for noncompliance?

Willful reporting violations can carry civil penalties of up to \$500 a day that each violation continues and criminal penalties of up to \$10,000 per occurrence and 2 years' imprisonment. Unauthorized use violations can incur civil penalties of up to \$500 for each day the violation continues and criminal penalties of up to \$250,000 or 5 years' imprisonment.

Transparent to whom?

FinCEN may disclose BOI only upon request from a federal agency engaged in national security, intelligence or law enforcement, a state, local, or tribal law enforcement agency, if court authorized, or foreign law enforcement agencies, judges, prosecutors, and competent authorities. In addition, FinCEN may disclose BOI at the request of a financial institution subject to consumer due diligence requirements, with the consent of the reporting company. FinCEN in its recent access rule states that the rule does not create a new regulatory requirement of non-bank financial institutions to access this information nor an expectation that they do so. Thus, title professionals' access to the records are unlikely. Factor in the recent proposal of FinCEN that reporting not be geographically limited and have no dollar threshold and title professionals are only facing a greater burden. The issuance of a third rule to implement the CTA later this year will provide more detail.

On March 1, 2024, the U.S. District Court for the Northern District of Alabama in *National Small Business United d/b/a the National Small Business Association, et al. v. Yellen, et.al.* declared that the CTA exceeded the powers granted to Congress and held it to be unconstitutional. The government was enjoined from the enforcement of the CTA but only against the plaintiffs in the case. March 4, 2024, FinCEN stated that it will continue to enforce the CTA against all others. The case is expected to be appealed and other cases are already filed. This issue is far from being settled. For now, everyone, not a plaintiff in the case, should plan to comply before the end of the applicable reporting period and stay tuned.



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