

## You Can Run But You Can't Hide: The Corporate Transparency Act

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In December 2020, as part of the larger National Defense Authorization Act, the Corporate Transparency Act (the "Act") was enacted. The Act requires that anonymous shell companies, most notably limited liability companies and partnerships, disclose their ultimate beneficial ownership and control in an effort to combat corruption, money laundering and financing of terrorism, among other things, in the United States.<sup>[1]</sup>

The Act requires that corporations, partnerships and limited liability companies formed in the United States, or non-U.S. entities registered to do business in the United States, disclose the beneficial ownership of such companies at the time of entity formation to the Financial Crimes Enforcement Network ("FinCEN"), a bureau of the Department of the Treasury that collects and analyzes information about financial transactions in order to combat financial crimes. The Act requires the following information: the beneficial owner's name, address, date of birth, and an identification number, such as a driver's license or passport number. Additionally, if the company is sold or its ownership changes, it is required to update that information with the Department of the Treasury.

Pursuant to the Act, a "beneficial owner" is defined as an individual who, directly or indirectly, either "exercises substantial control over the entity" or "owns or controls not less than 25% of the ownership interests of the entity." However, the phrase "substantial control" is not defined in the Act. The statute specifically excludes the following from the definition of "beneficial owner": (i) minor children if the information of their parent or guardian is reported, (ii) an individual acting as a nominee, intermediary, custodian, or agent, (iii) an employee whose control or economic benefits is derived solely from the employment status of that person, (iv) an individual whose right in interest to such entity is through a right of inheritance, or (v) a creditor of such entity, unless that person exercises substantial control or owns more than 25% of the ownership interests in the reporting company.<sup>[2]</sup>

The Act applies to limited liability companies, corporations, and other similar entities. The Act provides a list of entities that are exempt from the reports that are required, including banks, insurance companies, investment funds, charities, public companies, broker dealers, public accounting firms, public utilities and pooled investment vehicles that are advised or operated by banks or registered investment advisors. Moreover, if an entity (i) "employs more than twenty employees on a full-time basis," (ii) "filed in the previous year federal income tax returns in the United States demonstrating more than \$5,000,000 in gross receipts or sales" (this threshold aggregates subsidiary income and income of parent entities), and (iii) "has an operating presence at a physical office within the United States," then such entity is exempt from the reporting requirement under the Act.<sup>[3]</sup> In addition, "any corporation, limited liability company, or other similar entity of which the ownership interests are owned or controlled by one or more entities" which are otherwise exempt are also exempt from reporting.<sup>[4]</sup>

The Act is retroactive, applying to both new companies formed after the effective date of the Act was enacted, as well as to existing companies. The Act is not immediately effective since the Treasury Department has one year to issue the regulations detailing how the Act will be implemented. Generally, each company must submit to FinCEN a report that contains the information detailed above. Within one year after the enactment of the Act, the Treasury Department will set up a registry to collect the required information. New companies that are formed after the effective date of the regulations must "at the time of formation or registration, submit to FinCEN a report that contains the information" detailed above. However, existing companies that have been "formed or registered before the effective date of the regulations" must submit a report with the required information "in a timely manner, and not later than two years after the effective date of the regulations." If there is a change with respect to any information that is required to be reported under the Act, such entity must, no later than one year after the date on which there is a change to such information, submit a report with the updated information relating to the change.<sup>[5]</sup>

Generally, these disclosures will be maintained as confidential and not be made public by FinCEN, with a few limitations to such confidentiality. Such limitations include: (i) upon a request through appropriate protocols from a

government agency, (ii) a request made by a “financial institution subject to customer due diligence requirements, with the consent of the reporting company, to facilitate the compliance of the financial institution with customer due diligence requirements under applicable law,” and (iii) a request made by a “federal functional regulator or other appropriate regulatory agency.”<sup>[6]</sup>

A violation of the Act provides for civil penalties of up to \$500 for each day that a violation has not been remedied and criminal penalties of up to \$10,000 and two years’ imprisonment for individuals who intentionally submit incorrect or fraudulent beneficial ownership information or who knowingly do not provide comprehensive or updated beneficial ownership information.

As indicated, in addition to the formation of new entities, all existing entities will need to comply with these new regulations. The Act will, in essence, affect thousands of entities. Going forward, financial institutions should consider the need to ensure that the reporting of this information (or exemption therefrom) is added as a checklist item for their transactions, as well as a condition precedent to any permitted transfers.

<sup>[1]</sup> Corporate Transparency Act, H.R. 6395, 116th Cong. §§ 6402-6404 (2020).

<sup>[2]</sup> Corporate Transparency Act, H.R. 6395, 116th Cong. §§ 6403 (a)(3)(A)(i)-(ii), p. 1219.

<sup>[3]</sup> Corporate Transparency Act, H.R. 6395, 116th Cong. §§ 6403 (a)(11)(B)(xix)(I)-(III), pp. 1222-1223.

<sup>[4]</sup> Corporate Transparency Act, H.R. 6395, 116th Cong. §§ 6403 (a)(11)(B)(xxii), p. 1223.

<sup>[5]</sup> Corporate Transparency Act, H.R. 6395, 116th Cong. §§ 6403 (a)(14)(1)(A)-(D), pp. 1223-1224.

<sup>[6]</sup> Corporate Transparency Act, H.R. 6395, 116th Cong. §§ 6403 (c)(2)(B)(i)-(iv), pp. 1227-1228.