The Road to Compliance:

Understanding the Corporate Transparency Act and FinCEN Beneficial Ownership Reporting Requirements

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Legal Background

Corporate Transparency Act (2021) (“CTA”)

- The CTA is the culmination of a 10+ year federal effort to combat money laundering, fraud, and other financial crimes effected through shell and front entities.
- The CTA tasked the United States Department of the Treasury, Financial Crimes Enforcement Network ("FinCEN") with the implementation of the CTA.
- FinCEN developed the “Beneficial Ownership Information Reporting Rule”, effective January 1, 2024, to effectuate the CTA.

Stated Purpose of CTA:

- Collect basic identifying information on those individuals (the “Beneficial Owners”) who own and/or exert a certain degree of control over certain business entities in the United States (“Reporting Companies”).
- Facilitate the distribution of this accumulated information to governmental agencies to protect U.S. national security and the U.S. financial system, and to provide essential information to national security, intelligence, and law enforcement agencies; and state, local, and Tribal officials.

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Introduction

What is FinCEN and what does it do?

United States Department of the Treasury, **Fin**ancial **C**rimes **E**nforcement **N**etwork, known as FinCEN:

- Serves as the US Financial Intelligence Unit;
- Identifies, investigates, and analyzes suspicious financial activity (e.g., tax evasion, money laundering) reported by banks and/or government agencies;
- Coordinates information sharing among law enforcement agencies and offices (both domestically and abroad, if necessary); and
- Goal is to combat illicit finance and the abuse of shell and front companies by criminals and other bad actors from laundering or hiding money or other assets in the United States.

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Beneficial Ownership Information Reporting Rule

Rule: **As of January 1, 2024, Reporting Companies must file a Beneficial Ownership Information Report ("BOI Report") with FinCEN.**

This presentation is intended to answer the following questions:

- What entities are considered "Reporting Companies"?
- Who is a "Beneficial Owner"?
- What information is included in a "BOI Report"?
- When does an initial BOI Report need to be filed?
- When must a BOI Report be updated?
- Who are "Company Applicants"?
- What are the penalties if a Reporting Company does not file a BOI Report?

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What is a "Reporting Company"?

- Any **domestic entity** formed by filing a document with a Secretary of State (or similar office) in the US or any US commonwealth or territory.
  - "State" means any State of the United States, the District of Columbia, Puerto Rico, the Northern Mariana Islands, American Samoa, Guam, the U.S. Virgin Islands, and any other commonwealth or territory of the United States.
- Any **foreign entity** registered to do business within the US upon filing a document with a Secretary of State (or similar office) in the US.
- A Reporting Company includes Corporations, LLCs, PLLCs, LLPs, LPs, business trusts, and "other similar entities".
  - Reporting Companies <u>do not include</u> the following types of entities that do not file documentation with a Secretary of State or similar authority: general partnerships, sole proprietorships, and trusts.
- **The date of formation does not matter. All entities must comply with the CTA if not otherwise exempt.**
- There are **23 exemptions** for different types of entities that excuse them from filing BOI Reports.

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Exemptions to Classification as a Reporting Company

Exemption No.	Exemption Short Title
1	Securities reporting issuer
2	Governmental authority
3	Bank
4	Credit union
5	Depository institution holding company
6	Money services business
7	Broker or dealer in securities
8	Securities exchange or clearing agency
9	Other Exchange Act registered entity
10	Investment company or investment adviser
11	Venture capital fund adviser
12	Insurance company
13	State-licensed insurance producer
14	Commodity Exchange Act registered entity
15	Accounting firm
16	Public utility
17	Financial market utility
18	Pooled investment vehicle
19	Tax-exempt entity ★
20	Entity assisting a tax-exempt entity ★
21	Large operating company ★
22	Subsidiary of certain exempt entities ★
23	Inactive entity

← **23 Exemptions** to an entity's status as a Reporting Company.

- Many firm clients may qualify for an exemption.
- Clients that are **tax-exempt entities, large operating companies, and/or a subsidiary of other exempt entities** will not be required to file a BOI Report.
  - A "large operating company" is a company with:
    - at least 20 full-time employees in the US;
    - an operating presence with a physical office in the US; and
    - more than $5,000,000 in gross sales or receipts (excluding gross receipts or sales outside of the US) as reported on the company's applicable IRS Form for reporting its taxes.
      - Note that when determining exemption status, the entity's total gross receipts or sales **cannot** include funds received from foreign sources.

FinCEN's Small Entity Compliance Guide provides detailed guidance to determine whether an entity fits into a particular exemption.

****FAQ:** A non-profit or not-for-profit organization formed as of or after January 1, 2024 will have the obligation to file a BOI Report if it has not yet secured tax-exempt status. Such an entity can later file an updated BOI Report to claim "exempt" status once it secures tax-exempt status.

****Any entity that later meets an exemption after filing an initial BOI Report can file an updated BOI Report claiming exempted status.**

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Who is a "Beneficial Owner"?

A **Beneficial Owner** is any individual who, directly or indirectly:

- Owns or controls at least **twenty-five percent (25%)** of the ownership interests of the Reporting Company; or
- Exercises **substantial control** over the Reporting Company.
  - "**Substantial control**" can refer to an individual who exercises control over a Reporting Company through board representation, ownership, or control of a majority of voting rights, or through any other contract, arrangement, understanding, or relationship that allows such individual to exercise substantial influence over significant decisions of a Reporting Company.

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What is an Ownership Interest?

- Reporting Companies are required to identify all individuals who own or control at least **twenty-five percent (25%)** of the ownership interests of the Reporting Company. A Reporting Company may have multiple types of ownership interests.
- The following are types of ownership interests:
  - equity, stock, or voting rights;
  - a capital or profit interest;
  - convertible instruments;
  - options or other non-binding privileges to buy or sell any of the foregoing; and
  - any other instrument, contract, or other mechanism used to establish ownership.

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Examples of Ownership Interests

EQUITY, STOCK, OR VOTING RIGHTS

any interest classified as stock or anything similar, regardless whether it confers voting power or voting rights, and even if the interest is transferable

EXAMPLES include:

- equity, stock, or similar instrument
- preorganization certificate or subscription
- transferable share of, or voting trust certificate or certificate of deposit for, an equity security, interest in a joint venture, or certificate of interest in a business trust

CAPITAL OR PROFIT INTEREST

any interest in the assets or profits of a company organized as an LLC, which is similar to stock in a corporation and sometimes referred to as a 'unit'

CONVERTIBLE INSTRUMENTS

any instrument convertible into ***equity, stock, or voting rights*** or ***capital or profit interest***, whether or not anything needs to be paid to exercise the conversion. The **RELATED** items are also ownership interests:

- any future on any convertible instrument
- any warrant or right to purchase, sell, or subscribe to a share or interest in ***equity, stock, or voting rights*** or ***capital or profit interest***, even if such warrant or right is a debt

OPTION OR PRIVILEGE

any put, call, straddle, or other option or privilege of buying or selling ***equity, stock, or voting rights***, ***capital or profit interest***, or ***convertible instruments***, EXCEPT if the option or privilege is created and held by others without the knowledge or involvement of the reporting company

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any other instrument, contract, arrangement, understanding, relationship, or mechanism used to establish ownership

Beneficial Owners who Exercise Substantial Control

Any individual who meets any of the following four (4) criteria exercises substantial control over a Reporting Company if:

1. The individual is a **senior officer** (i.e. President, CEO, COO, CFO, General Counsel);
2. The individual has **authority to appoint or remove certain officers** or a majority of directors of the Reporting Company;
3. The individual is an **important decision-maker**; or
4. The individual exercises any other form of substantial control over the Reporting Company.

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Substantial Control Indicators

SENIOR OFFICER
any individual holding the position or exercising the authority of a:
1. President
2. Chief financial officer (CFO)
3. General counsel (GC)
4. Chief executive officer (CEO)
5. Chief operating officer (COO)

or any other officer, regardless of official title, who performs a similar function as these officers

APPOINTMENT OR REMOVAL AUTHORITY
any individual with the ability to appoint or remove any **SENIOR OFFICER** or a majority of the board of directors or similar body

IMPORTANT DECISION-MAKER
any individual who directs, determines, or has substantial influence over important decisions made by the reporting company, including decisions regarding the reporting company's:

1. **Business**, such as:
   - Nature, scope, and attributes of the business
   - The selection or termination of business lines or ventures, or geographic focus
   - The entry into or termination, or the fulfillment or non-fulfillment, of significant contracts
2. **Finances**, such as:
   - Sale, lease, mortgage, or other transfer of any principal assets
   - Major expenditures or investments, issuances of any equity, incurrence of any significant debt, or approval of the operating budget
   - Compensation schemes and incentive programs for senior officers
3. **Structure**, such as:
   - Reorganization, dissolution, or merger
   - Amendments of any substantial governance documents of the reporting company, including the articles of incorporation or similar formation documents, bylaws, and significant policies or procedures

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any other form of substantial control over the reporting company. Control exercised in new and unique ways can still be substantial. For example, flexible corporate structures may have different indicators of control than the indicators included here

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Trusts and Indirect Control Arrangements

- **Note for Trusts:** A Trustee of a trust or similar arrangement may exercise substantial control over a Reporting Company.
- The following individuals may hold ownership interests in a Reporting Company through a Trust or similar arrangement:
  - A trustee or other individual with the authority to dispose of trust assets;
  - A beneficiary who is the sole permissible recipient of trust income and principal, or who has the right to demand a distribution of or withdraw substantially all of the trust assets; and
  - A grantor or settlor who has the right to revoke or otherwise withdraw trust assets.
- **Indirect Control Arrangements**
  - Individuals can own or control ownership interests through contracts, arrangements, understandings, relationships, or otherwise.
  - Examples of indirect ways to own or control ownership interests in a Reporting Company are:
    - Owning or controlling one or more intermediary entities, or the ownership interests of any intermediary entities, that separately or collectively own or control ownership interests of a Reporting Company.
    - Through another individual acting as a nominee, intermediary, custodian or agent.

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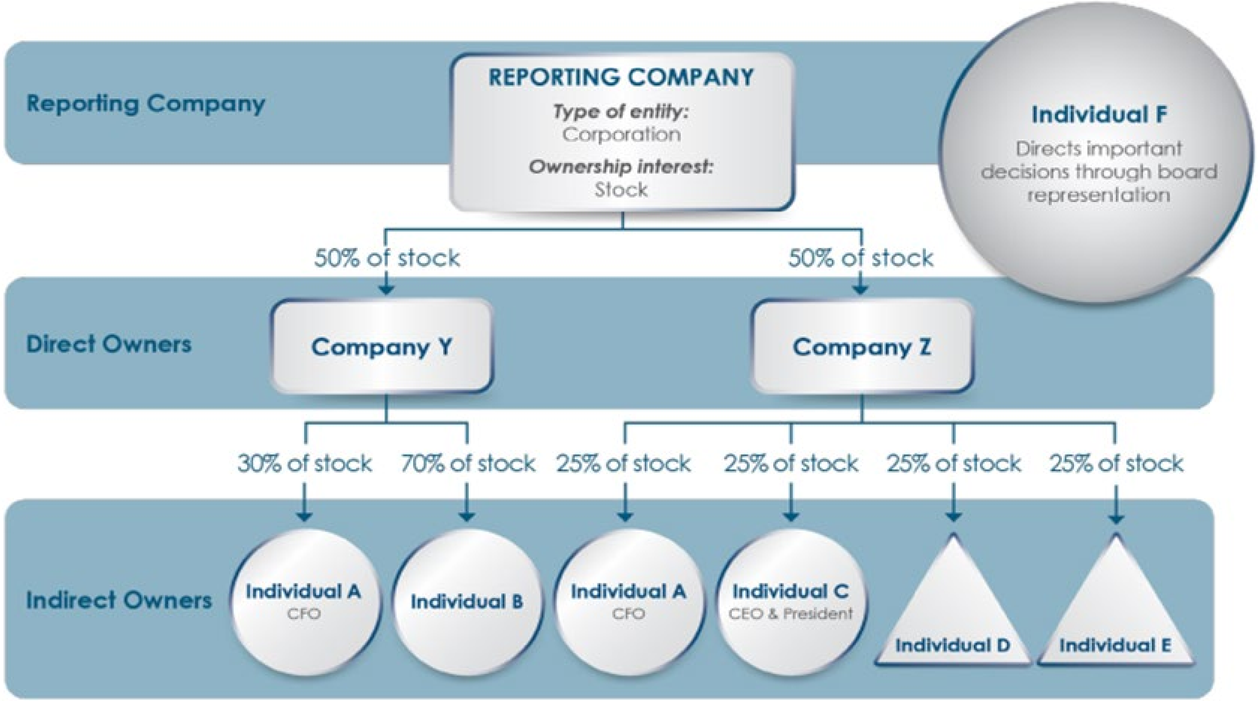
When a Reporting Company Has Multiple Indirect Owners Through Company Y and Company Z



- **In this example, Individuals A, B, C, and F are Beneficial Owners.**
- Individual A also indirectly owns 27.5 percent of the Reporting Company's stock through direct ownership of Company Y and Company Z.

- Individual A owns 15 percent of the Reporting Company's stock through Company Y (50% × 30% = 15%) and 12.5 percent of the Reporting Company's stock through Company Z (50% × 25% = 12.5%). Adding these two percentages together equals 27.5 percent of the Reporting Company's stock.)
- Individual B does not exercise substantial control. Individual B is a Beneficial Owner by owning or controlling 25 percent or more of the Reporting Company's ownership interests (70% x 50% = 35%).

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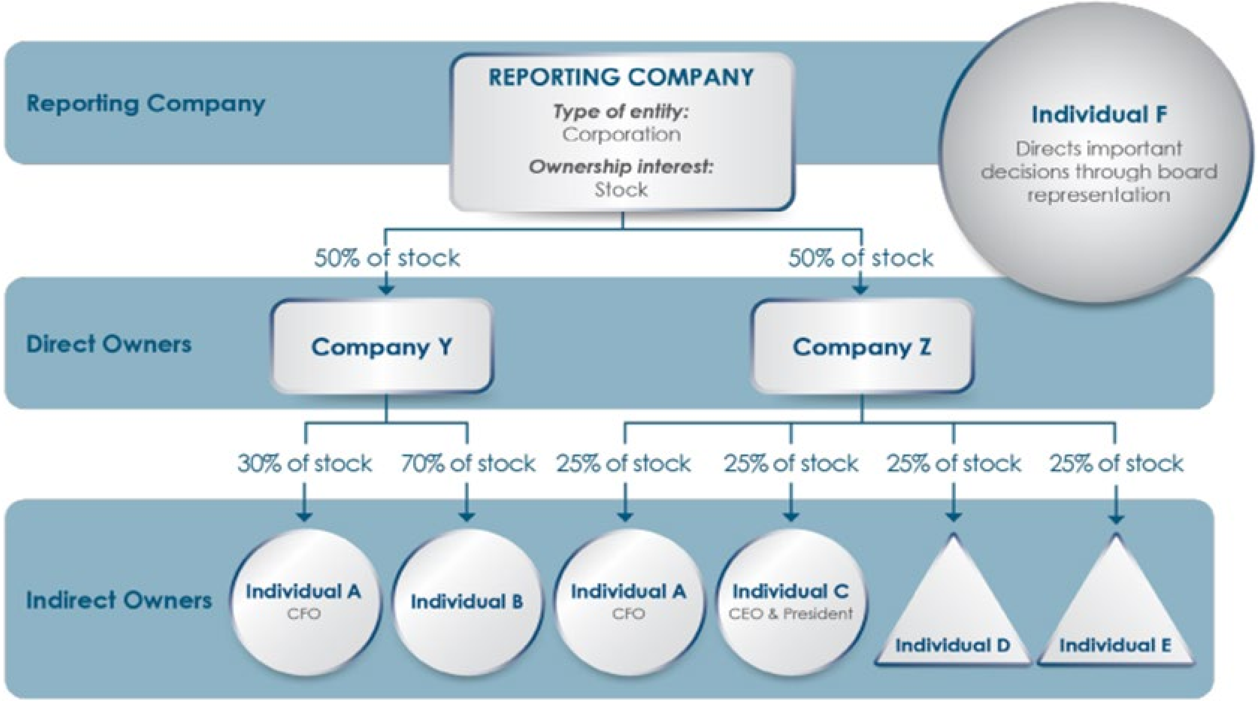
When a Reporting Company Has Multiple Indirect Owners Through Company Y and Company Z



- **In this example, Individuals A, B, C, and F are Beneficial Owners.**
- Individual C's ownership interests in the Reporting Company do not make Individual C a Beneficial Owner, but Individual C is nevertheless Beneficial Owner because Individual C exercises substantial control over the Reporting Company.

- Similar to Individual C, Individuals D and E own 25 percent of Company Z's stock, and each therefore indirectly owns 12.5 percent of the Reporting Company's stock. In contrast to Individual C, Individuals D and E do not exercise substantial control over the Reporting Company.
  - Individuals D and E are not Beneficial Owners.
- Individual F is on the Reporting Company's board of directors and makes important decisions on the Reporting Company's behalf, thereby exercising substantial control over it. Individual F does not own or control any stock in the Reporting Company.
  - Individual F is therefore a Beneficial Owner by exercising substantial control over the Reporting Company, but not through holding ownership interests in it.

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Status of Beneficial Owners

- A Reporting Company can have multiple Beneficial Owners.
  - For example, a Reporting Company could have several Beneficial Owners who exercise substantial control, and a few other Beneficial Owners who own or control at least **twenty-five percent (25%)** of the ownership interests of the Reporting Company.
- There is **no maximum** number of Beneficial Owners who must be reported, but each Reporting Company will have **at least one** Beneficial Owner.
- Reporting Companies are not required to report the reason that an individual is a Beneficial Owner (i.e., substantial control or ownership interests).

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Exemptions

When an individual who would otherwise be considered a Beneficial Owner qualifies for an exemption (see below), the Reporting Company **does not** have to report that individual as a Beneficial Owner in its BOI Report.

Five exemptions for individuals:

1. A Beneficial Owner is a minor child;
   - A Reporting Company should instead submit the information for the child's parent/guardian. The exemption expires when the child turns 18.
2. The individual acts on behalf of an actual Beneficial Owner as a nominee, intermediary, custodian, or agent;
3. The individual is (a) an employee, (b) whose substantial control or economic benefit is derived solely from employment status, and (c) whose employment with the Reporting Company is not that of senior officer;
   - For example, a salaried Property Manager might exercise substantial control over a Reporting Company, but because their control is derived solely from their status as an employee, they are exempt.
4. A Beneficial Owner's interest in the Reporting Company is a future interest (e.g., through inheritance); or
5. The individual is a creditor of the Reporting Company and does not meet any of the other criteria of a Beneficial Owner.
   - For example, an individual qualifies for this creditor exemption if the individual is entitled to payment from the Reporting Company to satisfy a loan or debt, so long as this entitlement is the only interest the individual has in the Reporting Company.

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What is a "BOI Report"?

The **BOI Report** is a list of basic identifying information about the Reporting Company **and** the Beneficial Owners who own at least 25% of the interests in, or exert substantial control over, the Reporting Company.

For the Reporting Company, the following information is required:

1. **Full Legal Name;**
2. **Any trade name or "doing business as" (DBA) name;**
3. **Complete current U.S. business address, and State, Tribal, or foreign jurisdiction of formation. For a foreign Reporting Company only: State or Tribal jurisdiction of first registration; and**
4. **IRS Tax Identification Number.**

For Beneficial Owners, the following information is required :

1. **Beneficial Owner's Name;**
2. **Date of Birth;**
3. **Residential address; and**
4. **ID number from either a passport, drivers license, or state-issued ID (and an image of such).**

BOI Reports will be submitted through an online portal, which is currently in development and will not be available until January 1, 2024.

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BOI Report Confidentiality

- All BOI Reports are confidential, stored in a non-public database, and will only be accessible to law enforcement agencies who submit a request through a U.S. Federal government agency to obtain BOI Reports for authorized activities related to national security, intelligence, and law enforcement agencies.
- With the Reporting Company's consent, financial institutions will also have access to BOI Reports, but only upon proper submission of a request to FinCEN.
- **Reporting Companies should maintain copies of any information submitted to the portal because once such information is submitted, it can no longer be accessed by the Reporting Company.**

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FinCEN Identifier

- A "FinCEN Identifier" is a unique identifying number that FinCEN can issue to a Beneficial Owner, Reporting Company, or Company Applicant upon request after such Beneficial Owner, Reporting Company, or Company Applicant provides certain information to FinCEN.
  - A Beneficial Owner, Reporting Company, or Company Applicant is **not required** to obtain a FinCEN identifier.
    - To obtain a FinCEN Identifier, a Beneficial Owner or Company Applicant must provide their name, date of birth, address, unique identifying number and issuing jurisdiction from an acceptable identification document, and an image of the identification document – **the same four pieces of personal information and image required for BOI Reports.**
    - A Reporting Company must submit an initial BOI Report before it may request a FinCEN Identifier. The request is made by checking a box on the BOI reporting form. The FinCEN Identifier can later be supplied where a BOI Report would otherwise be required.
- **<u>What is the Purpose of a FinCEN Identifier?:</u> If an individual or entity is a Beneficial Owner or Company Applicant of multiple Reporting Companies, the FinCEN Identifier can be submitted in place of a full BOI Report for such Beneficial Owner or Company Applicant.**

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BOI Report Filing

<u>When does an initial BOI Report need to be filed?</u>

- Entities formed **on/after January 1, 2024** must submit a BOI Report within **90** days of notification of the entity's official formation.
- Entities **formed prior to January 1, 2024** must submit a BOI Report **<u>by</u> January 1, 2025.**
- Entities formed on or after **January 1, 2025** must submit a BOI Report within **30** days of notification of the entity's official formation.

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BOI Report Updates

When does a BOI Report need to be updated?

- Entities must update a BOI Report within 30 days if an entity's Beneficial Ownership changes, or an error in a previously-submitted BOI Report is realized.
- Examples of when a Reporting Company must file an updated BOI Report:
  - A Reporting Company changes its name, DBA or trade name, or address;
  - A Reporting Company appoints a new CEO, upon the death of a Beneficial Owner, or someone acquires 25% of the Reporting Company's ownership interests; or
  - Any change to a Beneficial Owner's name, address, or reported ID number (passport, driver's license, state-issued ID). An updated image of such document is also required.

  Note that there is no requirement to report a Reporting Company's dissolution.

- There is no statutory requirement that Beneficial Owners must inform the Reporting Company of any changes to their BOI.
- Reporting Companies should consider revising their Operating Agreements, Shareholders Agreements, or Buy-Sell Agreements to include a requirement that Beneficial Owners must disclose any changes of their Beneficial Ownership Information to the Reporting Company (e.g., President, General Counsel, Secretary) to ensure compliance.

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Who is a "Company Applicant"?

A "Company Applicant" is any person **who actually files** the documentation that forms an entity, or **any person who otherwise directs the formation of an entity**.

- Each Company Applicant of a Reporting Company formed **on or after January 1, 2024** will have to submit a BOI Report, on an individual basis, comprised of the same information required of Beneficial Owners, **except that Company Applicants shall report their business address in lieu of their residential address.**
- Each Reporting Company that is required to report its Company Applicants will have to identify and report to FinCEN at least one Company Applicant, and at most two. All Company Applicants will be individuals. Companies or legal entities will not be Company Applicants.
- **Company Applicants may request FinCEN Identifiers in the event they form multiple entities.**

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Penalties for Failing to Submit a BOI Report

- **What happens if a Reporting Company does not timely file its BOI Report?**
  - Civil penalty: Fines of up to $500 **per day** that the violation continues.
  - Criminal penalty: Imprisonment for up to 2 years, **and/or** a fine of up to $10,000.
  - Note that in September 2023, FinCEN stated (on its website and within the Small Entity Compliance Guide) that "if you correct a mistake or omission within 90 days of the deadline for the original report, you may avoid being penalized."
  - Senior officers of the Reporting Company that fails to file a BOI Report may be held accountable.

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Obligation to Report

- **The Obligation to file a BOI Report (and update, when necessary) is solely that of the Reporting Company.**
- GW's FinCEN Committee can help with any legal questions and navigating the requirements:
  - **Contact FincenCommittee@garfunkelwild.com to be connected directly to a GW FinCEN Committee Attorney.**

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Additional Resources

BOI Reporting Rule Fact Sheet

https://www.fincen.gov/beneficial-ownership-information-reporting-rule-fact-sheet

Small Entity Compliance Guide:

https://www.fincen.gov/sites/default/files/shared/BOI_Small_Compliance_Guide_FINAL_Sept_508C.pdf

Frequently Asked Questions

https://www.fincen.gov/boi-faqs

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THANK YOU

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