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Congress Passes Corporate Transparency Act Creating Expansive Beneficial Ownership Registry with Significant Implications for U.S. and Foreign Business

Venable LLP

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Congress and the White House have agreed to include broad anti-money laundering reforms in one of the last major pieces of legislation expected to become law in this legislative session—the annual National Defense Authorization Act.¹ Passed in both the House and the Senate, one such reform is the Corporate Transparency Act (CTA), which would create a beneficial ownership registry within the U.S. Department of the Treasury's Financial Crimes Enforcement Network (FinCEN), requiring millions of "reporting companies" to report information on their "beneficial owners" to FinCEN. The purpose of the registry is to "crack down on anonymous shell companies, which have long been the vehicle of choice for money launderers, terrorists, and criminals."² To date, the burden of beneficial ownership has fallen on financial institutions, which are required to identify and verify beneficial owners through the Bank Secrecy Act's customer due diligence and "know your customer" requirements. The CTA would shift the collection burden to the reporting companies and create a first-of-its-kind comprehensive U.S. data base that will improve the ability of law enforcement to combat money laundering, the financing of terrorism, and other illicit activity.

Which Companies Need to Report

The CTA broadly defines "reporting company" to include any "corporation, limited liability company, or other similar entity" that is "(i) created by the filing of a document with a U.S. state or Indian Tribe or (ii) formed under the law of a foreign country and registered to do business in the United States...." As the CTA targets "shell companies" and other entities with limited or no operations, it excludes numerous broad classes of publicly traded, regulated, nonprofit, and government entities, as well as companies owned or controlled by those entities. The definition of a "reporting company" is further narrowed to exclude companies that (i) employ more than 20 full-time employees in the United States; (ii) annually report more than \$5 million in gross receipts or sales to the Internal Revenue Service (IRS); and (iii) have an operating presence at a physical office within the United States.

What Information Needs to Be Reported

Under the CTA reporting companies will be required to submit to FinCEN specified information on any beneficial owners, including (i) full legal name, (ii) date of birth, (iii) residential or business street address, and (iv) unique identifying number from an acceptable identification document, including a state driver's license, U.S. passport, or other U.S. state-issued identification document. If the beneficial owner does not hold any U.S.-issued identification documents, a non-U.S. passport number is required.

A "beneficial owner" of an entity is defined by the CTA as any individual who (i) owns a 25% equity stake or (ii) exercises "substantial control" over the reporting company. The CTA does not define "substantial control," and reporting companies should monitor future implementing regulations and guidance issued by FinCEN on the subject. Certain individuals are expressly excluded from the definition of "beneficial owner," including (i) individuals acting as agents, intermediaries, or custodians on behalf of another; (ii) an employee of a reporting company whose control or economic benefit with respect to the entity is derived solely from their employment; and (iii) creditors of the reporting company (unless the creditor meets either the "substantial control" prong or owns or controls 25% or more of the reporting company).

Timing of Reporting

After the effective date of FinCEN's implementing regulations, new reporting companies will be required to report beneficial ownership information at formation. Existing reporting companies will need to report such information within two years after the effective date of the regulations. Reporting companies will need to update beneficial ownership information with FinCEN within one year of any change in the reported information.

Access to the Registry

The beneficial ownership registry will not be publicly available, and the CTA imposes penalties for the unlawful disclosure of collected information. However, the CTA does permit FinCEN to disclose beneficial ownership information, upon request, to (i) U.S. federal law enforcement agencies, (ii) U.S. federal law enforcement agencies requesting information on behalf of a non-U.S. law enforcement agency, or (iii) with the consent of the reporting company, a financial institution in order to meet customer due diligence requirements. FinCEN is also permitted to disclose beneficial ownership information to state, local, and tribal law enforcement agencies pursuant to a court order authorizing the agencies to seek the requested information.

Implications for Reporting Companies

U.S. companies, and foreign companies operating in the U.S., should, first and foremost, review the CTA to determine whether they will be considered a reporting company. Smaller companies with revenue over \$5 million annually, 20 or more employees, and a physical operation in the U.S. may need to report information on their beneficial owners if they are not subject to an additional exemption. Regulated, publicly traded, and large private entities operating in the U.S. (as well as the entities they control) are most likely exempt from the proposed reporting requirements; however, they too may need to consider their due diligence practices required by law, such as those companies typically implement in order to ensure compliance with the Foreign Corrupt Practices Act and other anti-corruption laws, when engaging in third-party transactions with companies subject to the CTA reporting requirement.

Companies required to report should be cognizant of the penalties imposed for certain reporting violations. Willful failure to report, or the submission of a report containing false or fraudulent beneficial ownership information, is subject to a \$500 per day penalty and/or a maximum \$10,000 penalty and up to 2 years imprisonment. The CTA contains a safe harbor from civil or criminal liability

for the submission of inaccurate information if the person "voluntarily and promptly" (and no later than 90 days after the submission of the original inaccurate report) submits a report containing corrected information.

Implications for Financial Institutions

The BSA requires certain financial institutions, including banks, to develop and maintain an effective AML program, including customer due diligence. The requirement to identify and verify the identity of beneficial owners of legal entity customers was imposed by FinCEN in 2016. The CTA will provide financial institutions with a means to verify the information on reporting companies, thereby increasing the effectiveness the AML program.

Implications for Law Enforcement

The focus of the CTA is on money laundering risks, and federal law enforcement agencies will have greater access to the ownership information of third parties than ever before. Those agencies will also have the ability to share that information with foreign law enforcement in an increasingly cooperative international enforcement landscape through the international network of Financial Intelligence Units (FIUs).

Venable LLP - Laura R. Biddle, W. Warren Hamel, D. E. (Ed) Wilson, Jr., Evan T. Shea and Nicholas A. Mongelluzzo

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