

TRANSPARENCY

# The New Law That Nobody Is Talking About

BY TED SUTTON, ESQ.

**A new disclosure law took effect on January 1, 2024, and yet very few lawyers know about it. This lack of knowledge has caused confusion and anxiety among legal professionals, especially since those who established entities for their clients can face very steep penalties for failing to follow this new law.**

The new law is called the Corporate Transparency Act (CTA), and it was passed on January 1, 2021. What exactly is the CTA? And how does it affect lawyers? We will discuss these things below. Let's first discuss the CTA's history.

## History of the CTA

The CTA was passed on January 1, 2021. Congress' aims for passing this bill included stopping illegal activity, helping law enforcement, protecting national security, and matching other countries' corporate compliance standards.

To justify its passage, Congress cited evidence of foreign nationals who formed shell companies in the U.S. to engage in illegal activities. And because there is no such national database for law enforcement to access, they have a difficult time tracking down these bad actors.

The enactment of the CTA changes this completely. The CTA requires a national database to be maintained with the Financial Crimes and Enforcement Network (FinCEN), a branch of the U.S. Department of the Treasury. This database is called the Beneficial Ownership Secure System (BOSS), and it is only available for access by federal, state, and foreign law enforcement agencies, as well as financial institutions.

While the aims are well-intentioned, they place an additional burden on small businesses, and the lawyers who assist them. To comply with the CTA, these small businesses must report three types of beneficial ownership information (BOI) to FinCEN. Each type is described below.

### **Company Applicant Information**

The first type of BOI is the company applicant information. Under the rules, a company applicant is defined as:

- The individual who directly files the document to create or register the reporting company; and
- The individual who is primarily responsible for directing or controlling such filing, if more than one individual is involved in the filing.

Under this definition, a company applicant may only be one person. However, if a lawyer and a paralegal help file these documents to form the entity, both count as being “company applicants.”

The text of the rules specifically addressed this issue. This is because the lawyer is primarily responsible for overseeing the preparation and filing of incorporating documents, and the paralegal is the person who directly files them with the state office. And in this situation, two company applicants would be required to report their information.

Fortunately, FinCEN only requires company applicant information for entities formed after January 1, 2024. So, if you have a client who formed an entity before January 1, you will not have to report any company applicant information.

So, what must a company applicant report? FinCEN requires the following pieces of company applicant information:

1. The company applicant’s name;
2. The company applicant’s birthdate;
3. A business or residential street address; and

4. A driver’s license or passport (with a document number and an image).

### **Reporting Company Information**

The second type of information is the reporting company information. And there are two types of reporting companies.

The first type is a “domestic reporting company.” This is defined as an entity that is created by the filing of a document with a secretary of state, or any similar office under the law of a state or Indian tribe. These can include corporations, LLCs, limited partnerships, or any other entity that is created by the filing of a document. However, the definition does not include sole proprietorships or general partnerships, because those entities are not created by the filing of a document with the secretary of state.

The second type is a “foreign reporting company.” This is defined as an entity that is formed under the law of a foreign country and that is registered to do business in the U.S. by the filing of a document with a secretary of state or equivalent office under the law of a state or Indian tribe.

Under the CTA, both types of reporting companies must report the following information to FinCEN:

1. The reporting company’s name, and any trade name or DBAs (if applicable);
2. The business street address (that cannot be a P.O. Box or a registered agent address); and
3. The formation jurisdiction.

### **Reporting Company Exemptions**

While some companies may meet the requirement of a “reporting company,” they may be exempt from reporting their information to FinCEN. Under the CTA, there are 23 types of exemptions. The most important exemption is the “large operating companies” exemption. An entity falls into this category if it:

1. Employs 21 or more full-time employees in the U.S.;
2. Has more than \$5 million in gross receipts or sales in the U.S. filed on a federal tax return; and
3. Has an operating presence at a physical office in the U.S.

If a company meets all three requirements, it does not need to report any information to FinCEN.

Some of the other exemptions apply to entities that are banks, insurance companies, or are registered with the SEC.

### **Beneficial Ownership Information**

The third type of information is beneficial ownership information. And a “beneficial owner” is someone who meets either one of two prongs.

The first prong relates to ownership interests. Under this prong, a “beneficial owner” is someone who owns at least 25 percent of the ownership interests of the company. An ownership interest can include not only equity in the company, but also capital or profit interests, convertible instruments, warrants, rights, options, and derivatives.

The second prong relates to management. Under this prong, a beneficial owner is someone who exercises “substantial control” over the company. This “substantial control” requirement is broad. It can include an individual who serves as a senior officer, has the authority to appoint or remove any senior officer, or has substantial influence over company decisions.

If someone is a beneficial owner under either prong, the company must submit the following pieces of beneficial ownership information to FinCEN:

1. The beneficial owner’s name;
2. The beneficial owner’s birthdate;
3. The beneficial owner’s residential or business street address; and
4. A “unique identifying number” from a passport or driver’s license (with an image).

### **Beneficial Ownership Exceptions**

Under the CTA, there are five exceptions to the definition of a beneficial owner. They are:

1. Minor children.
2. Nominees, intermediaries, custodians, and agents that act on behalf of another individual.
3. Company employees (who are not in a control position).
4. People who inherit an interest in the company.
5. Company creditors (unless they have control powers).

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Someone meeting one of these five exceptions does not need to report information to FinCEN.

## Obtaining a FinCEN Identifier

If your law firm forms many entities for your clients, you may be able to obtain a FinCEN Identifier. To get this identifier, you will need to report all of the same BOI to FinCEN. So, if you and/or your paralegal are “company applicants” who regularly form businesses, you will need to report all of the same company applicant information to FinCEN. But once you have that identifier, you will be able to report your BOI to FinCEN much more quickly.

## When to File BOI Reports

When do these BOI reports need to be filed? The timing to file these BOI reports depends upon when the reporting company was formed.

- If the reporting company was formed before January 1, 2024, they have one year (or until

December 31, 2024) to report their BOI to FinCEN. If the reporting company was formed between January 1, 2024, and December 31, 2024, they have 90 days to report their BOI to FinCEN.

- If the reporting company was formed after January 1, 2025, they only have 30 days to report their BOI to FinCEN.
- When there is a change in ownership, a new mailing address, a new driver’s license or passport, or someone discovers an error in a previous report, the reporting company has 30 days to file a corrected report.

## Penalties For Not Filing

If you do not file these BOI reports, the CTA imposes serious penalties. If a person either willfully provides false or fraudulent information, or they willfully fail to report complete or updated BOI to FinCEN, they can face up to two years in prison.

On top of this, that person can face up to \$10,000 in fines.

We already know that very few lawyers know about the CTA, and there has been little guidance from FinCEN on how lawyers are supposed to report this information.

However, none of these concerns change the fact that the CTA still became effective last month. And if you do not comply with it, you could expose yourself to unnecessary liability.

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