PREAPRING FOR THE CORPORATE TRANSPARENCY ACT

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I. OVERVIEW

A. Who is required to report under the new regulations issued by the Financial Crimes Enforcement Network (FinCEN) implementing the Corporate Transparency Act (CTA)?

1. FinCEN is a bureau of the U.S. Department of Treasury with the aim of investigating financial crimes.

B. What information is required to be reported?

C. Conducting an analysis of an entity's reporting obligations under the new regulations

D. Preparing your clients for the CTA

II. WHAT IS THE CTA? WHY DOES IT EXIST?

A. The CTA is a component of the Anti-Money Laundering Act of 2020

B. The law makes it "harder for bad actors to hide or benefit from their ill-gotten gains through shell companies or other opaque ownership structures."

The law was passed in 2021 on a bipartisan basis.

C. The CTA, along with the regulations promulgated by FinCEN to implement its provisions, take effect on January 1, 2024.

1. Most existing companies will have to make their first filing to comply by January 1, 2025.

III. WHO IS REQUIRED TO REPORT UNDER THE NEW CTA REGULATIONS?

A. An entity required to report under the act is a Reporting Company

1. Reporting Company is any corporation, limited liability company, partnership or other entity that is or has been created by filing a document with the secretary of state or any similar office under the law of a state or tribal jurisdiction, and any foreign entities that are registered to do business in any state or tribal jurisdiction.

a. Sole proprietorships and general or co-partnerships are formed at the county level and not the state level, and are generally not reporting companies.

2. Generally, family trusts will not be considered a Reporting Company because they are not typically created through the methods outlined above however, entities owned by trusts will be considered a Reporting Company.

3. If the entity is not a Reporting Company, it will not be subject to the reporting requirements of the CTA

B. Exemptions from Reporting

1. If the entity is a Reporting Company but is exempt from the CTA filing requirement, it will not be required to make the CTA filing.

2. The CTA exempts 23 different types of Reporting Companies from the CTA filing requirements, many of which are entities that are already subject to government reporting requirements (e.g., publicly traded companies, banks, credit unions, securities brokers or dealers, investment companies, insurance companies, state licensed insurance producers, tax exempt entities and registered public accounting firms).

3. Three of the most common exemptions under the CTA will be for: Large Operating Companies, Inactive Entities, and Tax-Exempt Entities

C. The Large Operating Company Exemption

1. In order to qualify for the Large Operating Company exemption, the entity must:

a. employ more than 20 full time employees in the United States

b. have an operating presence at a physical office within the United States; **and**

c. have filed a Federal income tax or information return in the United States for the previous year demonstrating more than $5,000,000 in gross receipts or sales.

D. Inactive Entity Exemption

1. An inactive entity exempt from reporting under the Act is any entity that:

a. was in existence on or before January 1, 2020;

b. is not engaged in active business;

c. is not owned by a foreign person, whether directly or indirectly, wholly or partially;

d. has not experienced any change in ownership in the preceding twelve-month period;

e. has not sent or received any funds in an amount greater than $1,000, either directly or through any financial account in which the entity or any affiliate of the entity had an interest, in the preceding twelve-month period; **and**

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f. does not otherwise hold any kind or type of assets, whether in the United States or abroad, including any ownership interest in any corporation, limited liability company, or other similar entity.

2. The inactive entity definition is a high bar to meet, and companies who believe they may meet the inactive entity definition should consider dissolution prior to 1/1/2024.

E. Tax-Exempt Entity Exemption

1. A tax-exempt entity exempt from reporting under the Act is any entity that:

a. is an organization that is described in section 501(c) of the Internal Revenue Code of 1986 (Code) (determined without regard to section 508(a) of the Code) and exempt from tax under section 501(a) of the Code;

b. is an organization that is described in section 501(c) of the Code, and was exempt from tax under section 501(a) of the Code, but lost its tax-exempt status less than 180 days ago;

c. is a political organization, as defined in section 527(e)(1) of the Code, that is exempt from tax under section 527(a) of the Code; **or**

d. is a trust described in paragraph (1) or (2) of section 4947(a) of the Code.

IV. WHAT INFORMATION ARE ENTITIES REQUIRED TO REPORT?

A. Beneficial Ownership Information (BOI)

1. Unless an exemption applies, the CTA creates a filing requirement for each Reporting Company to disclose:

   a. Entity information;

   b. beneficial ownership information ("BOI") for the beneficial owners of the entity and those in control (regardless of ownership interest), and:

   c. if the entity is formed on or after January 1, 2024, BOI for the persons involved in the formation of a Reporting Company (each, a "Company Applicant").

2. What is included in BOI?

   a. full legal name;

   b. date of birth;

   c. generally, a current residential address;

   d. unique ID number from a non-expired U.S. passport, state driver's license or other state or local government issued photo ID; and

   e. image of the document showing the unique ID number

3. BOI Reporting Deadlines

   a. **Existing Reporting Companies**: On or before January 1, 2025 (one year after the effective date of the CTA), for any Reporting Company that has been formed or registered before January 1, 2024;

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b. **<u>New Reporting Companies</u>:** Within 30 days after its date of formation (i.e., the filing date of its Articles or Certificate), for any Reporting Company <u>formed or registered on or after January 1, 2024</u>

c. **<u>Updates</u>:** Reporting Companies must update changes in beneficial ownership within 30 days after a change occurs

i. This would include address changes, adding new beneficial owners, or removing beneficial owners, among other things.

V. <u>CONDUCTING A BENEFICIAL OWNERSHIP ANALYSIS</u>

A. The Role of Accounting Firms in Reporting

1. One of the main functions for accounting firms under the Act will be assisting with or conducting an analysis of a Reporting Company's beneficial owners.

2. The ownership, control, revenue, and other organizational information maintained by accounting firms will be instrumental to assisting entities and determining beneficial ownership.

3. It is important for accounting firms to develop a process for asking clients the right questions to help them gather the necessary information regarding beneficial owners and company applicants (if applicable).

B. Definitions

1. A beneficial owner is any individual who, directly or indirectly, <u>either</u>:

a. exercises <u>substantial control</u> over a Reporting Company, or

b. owns or controls at least 25 percent of the <u>ownership interests</u> of a Reporting Company.

2. An individual might be a beneficial owner through substantial control, ownership, or both.

3. There must be at least one (1) beneficial owner, and there is no maximum number of beneficial owners who must be reported.

C. Identification Steps

1. Identify individuals who exercise <u>substantial control</u> over the entity

2. Identify the types of <u>ownership interests</u> in the entity and the individuals that hold those ownership interests

3. Calculate the percentage of <u>ownership interests</u> held directly or indirectly by individuals to identify those who own or control, directly or indirectly, at least 25 percent of the ownership interests of the entity

D. Definitions (con't)

1. **<u>Substantial Control</u>:** An individual exercises substantial control over a Reporting Company if the individual meets **<u>any</u>** of four general criteria: (1) the individual is a senior officer; (2) he 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; <u>or</u> (4) the individual has any other form of substantial control over the Reporting Company

2. **<u>Ownership Interest</u>:** Any of the following may be an ownership interest: 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. A Reporting Company may have multiple types of ownership interests.

E. Exceptions

1. When an individual who would otherwise be a beneficial owner of a Reporting Company qualifies for an exception, the Reporting Company does not have to report that individual as a beneficial owner in its CTA filing. The five exceptions are any one of the following:

   a. The individual is a minor child

   b. The individual merely acts on behalf of an actual beneficial owner as the beneficial owner's nominee, intermediary, custodian, or agent

   c. The individual is an employee of the Reporting Company such that all three of the following apply;

      i. The individual is subject to the will and control of the employer in what and how to do work, and that the employer may discharge the individual from work

      ii. The individual's substantial control over, or economic benefits from, the Reporting Company are derived solely from the employment status of the individual as an employee; and

      iii. The individual is not a senior officer of the Reporting Company. The term "senior officer" means an individual holding the position or exercising the authority of a president, chief financial officer, general counsel, chief executive office, or chief operating office, or any other office, regardless of official title, who performs a similar function

   d. The individual's only interest in the Reporting Company is a future interest through a right of inheritance, such as through a will providing a future interest in a company

   e. The individual is a creditor of the Reporting Company

VI. PREPARING YOUR CLIENTS FOR COMPLIANCE

A. WHAT YOU CAN DO

1. Become familiar with and stay up to date with the CTA and its requirements

2. Make clients aware of the CTA and assist in determining whether they are a Reporting Company and, if so, whether they are exempt from the reporting requirements. Otherwise, a CTA filing will be necessary

3. Advise on the timing for the initial filing and any continued compliance

4. Know and advise your clients on the penalties for noncompliance

5. File the required reports on behalf of clients with FinCEN regarding the Reporting Company, the beneficial owners and the company applicants (if applicable)

6. Assist with the client's continued compliance with the CTA

VII. MADDIN HAUSER'S ROLE

A. WHAT WE'RE DOING

1. Analyzing client businesses to determine whether it is a Reporting Company required to make disclosures under the CTA

2. If a client's business is a Reporting Company, analyzing whether it is exempt from the CTA reporting requirements

3. Analyzing and compiling who are the beneficial owners of the Reporting Company

4. Analyzing and compiling who are the company applicants (if applicable) of the Reporting Company

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5. Analyzing and compiling the beneficial ownership information (BOI) information for the beneficial owners and the company applicants (if applicable) of the Reporting Company

6. Advising on the timing for the initial filing and any continued compliance

7. Filing the required reports with FinCEN regarding the Reporting Company, the beneficial owners and the company applicants (if applicable)

8. Assisting with continued compliance with the CTA

9. Preparing necessary corporate resolutions

10. Preparing or amending governance documents that appoint a CTA compliance officer and contain other relevant language, including that relating to compliance/indemnification for failure of a beneficial owner to comply

11. Drafting or reviewing language in contracts regarding CTA compliance (i.e., lenders and potential buyers may require assurances of compliance or exemptions with the CTA)

B. ASSISTING ACCOUNTING FIRMS

1. We would be happy to speak with you about the CTA and its impact on your clients and/or your accounting firm.

2. We can assist you and your clients with anything you might need to help comply with the CTA.

3. We are regularly monitoring these matters, have established a CTA resource blog page on our website and will be adding to and updating our CTA blog page as needed.

4. We encourage you to monitor our firm's CTA blog page for such information and updates.

VIII. A NOTE ON INTERNAL COMPLIANCE

A. WHAT YOU CAN DO

1. In addition to your clients, many accounting firms may be a non-exempt Reporting Company also subject to, and required to file the required reports under, the CTA.

2. An analysis should be undertaken as to whether your firm would be considered exempt as a large reporting company or a public accounting firm registered under Section 102 of the Sarbanes-Oxley Act of 2002.

IX. UNANSWERED QUESTIONS

A. WHAT WE DON'T KNOW

1. What does a filing form look like?

2. What does enforcement look like?

3. Will there be any sort of warning or safe harbor issued for first time violators?

4. What if a company cannot locate its BOI? Should it file an incomplete report?

5. *Is this really going to happen?*

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