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# Goodbye Shareholder Anonymity, Hello Transparency

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Throughout US history, most businesses have been able to organize and operate without needing to disclose their ownership or management. This privacy afforded to businesses and their management, along with the protection of corporate shareholders and LLC members from liability beyond the capital they have contributed to the business, have encouraged formation and investment in businesses in the US and can be credited in large part to economic growth in the US.

That's about to change.

The federal Financial Crimes Enforcement Network (FinCEN), a branch of the Treasury Department, recently issued proposed rules to implement the Corporate Transparency Act (CTA). When final rules are issued, likely in early 2022, most domestic and foreign businesses in the United States will for the first time be required to disclose sensitive personal identifying information about their beneficial owners, senior officers and other control persons to a government agency.

## **Key Takeaways:**

- Most businesses will soon be required to report information on (and provide updates on changes to) their beneficial owners, senior management and certain other matters to FinCEN.
- Many of the rules about information required to be reported, and exemptions, require complex legal analysis to your business' particular situation. Consult with legal counsel who is very familiar with the CTA rules.
- It will be critical to ensure timely reporting and the accuracy and completeness of information reported to avoid significant potential civil and criminal sanctions.

**What is the Corporate Transparency Act?** After nearly two decades of failed attempts to pass similar legislation, Congress successfully enacted the CTA on January 1, 2021 (overriding then-President Trump's only veto while in office) by incorporating it into a much larger, must-pass defense department appropriations bill. The purpose of the CTA is to provide national security, intelligence and law enforcement authorities with beneficial ownership and other information on most US businesses, and foreign businesses doing business within the US, to enable them to identify and crack down on "shell" businesses and their controlling parties who are engaged in criminal activity, though it will impose a substantial new burdens and costs on most legitimate businesses as well.

**Who will be required to file reports?** Most corporations, LLCs and other business entities formed by the filing of a document with a secretary of state (or similar official or agency) of a State, US territory or possession, or Tribe, and foreign entities which file a document with such an official or agency to qualify to do business, must file beneficial ownership reports with FinCEN. Presumably, general partnerships, unincorporated associations and sole proprietorships will not have to file reports, but most other business entities will have to do so.

Exempt entities are generally heavily regulated and provide similar information to government officials already, including: businesses registered with the SEC (such as registered issuers, investment companies, investment advisers, and the like) or Commodity Futures Trading Commission (CFTC); federal- and state-chartered banks, savings banks and credit unions; bank- and savings-and-loan holding companies; state-regulated insurance companies and insurance producers; Fin-CEN registered money transmission businesses; registered accounting firms; regulated public utilities; and certain tax-exempt entities.

Certain large operating companies are exempt if they employ more than 20 full-time employees in the US, have an operating presence at a physical office in the US, and filed a federal income tax or information return in the US for the previous year demonstrating more than \$5 million in gross receipts or sales.

Inactive entities are exempt if they were in existence on or before January 1, 2020, aren't engaged in active business, aren't owned by a foreign person (whether directly or indirectly, wholly or partially), haven't experienced any change of ownership in the preceding 12-month period, haven't sent or received more than \$1,000 in funds (directly or through an affiliate) in the preceding 12-month period, and don't otherwise hold any kind or type of assets in the US or abroad (including ownership interests in another entity).

**What are the responsibilities of persons involved in filing reports?** The proposed rules state that any person who files a report with FinCEN must certify that it is accurate and complete (with no knowledge qualification) and that any person who willfully provides, or attempts to provide, false or fraudulent information to FinCEN or willfully fails to report complete or updated information or "directs or controls another person with respect to any...failure to report [complete or updated information to FinCEN]" is subject to civil and criminal penalties.

**When will reporting obligations commence?** The CTA mandated that FinCEN implement final rules and commence companies reporting obligations by January 1, 2022. However, FinCEN first published proposed rules (along with requests for comment and input on a number of questions) on December 7, 2021, with the comment period scheduled to end on February 7, 2022, so it is highly unlikely that final rules will be published (and reporting obligations commence) before early 2022.

Commencing on the effective date of the final rules:

- Non-exempt domestic companies *organized on or after the effective date of the final rules* (and foreign companies which first register to do business in a State on or after such effective date) must file their initial report within 14 calendar days of formation or registration.
- Non-exempt domestic companies *organized before the effective date of the final rules* (and foreign companies which first registered to do business in a State before such effective date) must file their initial report within one year of the effective date of the final rules.

**What must be reported?** The report must provide identifying information on:

- the reporting company (including the entity name, any trade name or d/b/a name, street address, and taxpayer identification number (including EIN));
- each beneficial owner of the reporting company (including the full legal name, date of birth, complete current address, and passport, driver's license or similar identification) (***note that many businesses do not have, know or have the legal right to obtain this information***); and
- each individual who files organizational (or registration) documents for the reporting company or who directs or controls the filing of such document by another person (including the full legal name, date of birth, complete current address, and passport, driver's license or similar identification) (such a person is a "company applicant").

In lieu of including this information on a person or entity in a report, a unique FinCEN-issued identifier number may be used in the report. However, such information about the person or entity must be provided to FinCEN to obtain such identifier.

Reports must be updated or corrected if any information changes or is (or becomes) incorrect or incomplete, including by changes of name, trade names, addresses, or beneficial owners. Failure to file an updated report within 30 days of the change could result in civil and/or criminal liability under the CTA.

**Who is a "beneficial owner"?** In general, a beneficial owner is one of the following:

- An individual who has direct or indirect ownership or control of at least 25% of the ownership interests of the reporting company on a fully diluted basis (including non-voting ownership interests); or
- An individual who exercises, or has the right or ability to exercise, substantial control over the reporting company (including all senior officers).

This information may change due to a number of factors, including mergers and acquisitions, issuances of (or subscriptions to purchase) new shares or membership interests, sales of shares or membership interests, issuance of warrants, options or convertible debt, changes in

organizational documents, new or changed significant contractual arrangements, and changes in the composition of management.

**Who will have access to reported information?** All reported information will be housed in a massive, newly-created database controlled by FinCEN. The CTA limits access to reported information to federal national security agencies, federal intelligence agencies, federal law enforcement personnel, state or Tribal law enforcement personnel (with a court order), federal functional regulators (e.g., banking regulators and the Securities and Exchange Commission), foreign law enforcement agencies in certain circumstances (upon a request from a federal agency), and financial institutions subject to customer due diligence requirements (with the consent of the reporting company). While leaks or hacks of such information is prohibited by law, that prohibition will be cold comfort if sensitive non-public information about a business, its beneficial owners, its senior management or its “company applicant” is publicly released or ends up in the wrong hands.

**What are the possible civil and criminal sanctions for a violation of the CTA?** Possible sanctions include:

- Civil penalties of up to \$500 per day that the violation continues or has not been remedied; and
- Fines of up to \$10,000, imprisonment of up to two years, or both.

**Your Next Steps.** Our CTA team is keeping abreast of all developments and will report back with updates. While the proposed rules may change before final adoption, you can start preparing now:

- Many businesses won't currently know all of the information on beneficial owners and company applicants that will need to be reported. Before the rules become effective and initial reports are due, businesses should reach out to shareholders or members and enlist their assistance in gathering information that must be reported.
- Businesses, beneficial owners and company applicants should consider applying for a FinCEN identifier when it is available.
- Consult with legal counsel to verify whether a business is exempt from reporting requirements and to confirm specific information needed for reporting, such as who is a beneficial owner, senior management, or a company applicant.
- Changes in the identity and ownership by direct and indirect shareholders or members of your business, and the effect of corporate transactions and contracts, need to be monitored to quickly identify changes which must be reported.

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