



New Law Will Require Millions of Corporations, LLCs, and Other Entities to Disclose Beneficial Owners and Those Individuals with “Substantial Control”

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The Corporate Transparency Act, enacted in 2021, will soon require millions of corporations, limited liability companies, and other entities formed in the U.S. or doing business here to make new filings with U.S. law

Most common business entities, including corporations, limited partnerships and limited liability companies, are subject to the law.

enforcement disclosing details of “beneficial owners” in a beneficial ownership information report. Because the law is very broad in scope but has many exemptions, we are notifying clients about this law without regard to whether we anticipate that the client will be subject to the law. In multi-entity structures, one or more companies

may be exempt from reporting while others are not, so each entity should be analyzed separately. This Client Alert is not a comprehensive analysis of the requirements or guidance on how to comply. Because the law is broad and carries potential criminal penalties for non-compliance, we encourage every client to become familiar with the general scope of the law and then consult a knowledgeable attorney for further analysis as needed.

A “beneficial owner” can include a trustee of a trust and someone who does not have direct ownership, such as a beneficiary or settlor of a trust or someone who holds an interest through an agent, nominee, or custodian.

One might think that dissolving an entity would mean it would no longer have a reporting obligation, but the regulators have declined to give clear guidance on the effect of terminating an entity, stating they believe, “the variety in types of termination and degrees of finality under state laws would require numerous special rules for small variations, and would still result in confusion if any circumstance were inadvertently unaddressed.” We suggest, therefore, that attention be given even to those entities that have been dissolved. For example, a Delaware corporation generally exists for three years after it has filed for dissolution, and an Ohio corporation generally exists for five years after it files for dissolution.

The law and related rules apply, subject to certain exemptions, to every entity formed by filing with a state office or registered to do business in a state. This means most common business entities, including

A report will disclose those individuals who directly or indirectly either exercise substantial control over the entity or own or control at least 25 percent of its ownership interests.

corporations, limited partnerships, and limited liability companies, are subject to the law. Each such entity must file a report disclosing the identities of its beneficial owners. “Beneficial owner” means any individual who, directly or indirectly, either exercises substantial control over the entity or owns or controls at least 25 percent of its ownership interests. A “beneficial owner” can include an individual serving in a fiduciary capacity, such as a trustee of a trust. It can also include someone who does not have direct ownership, such as a beneficiary or settlor of a trust or someone who holds an

interest through an agent, nominee, or custodian. The rule provides specific guidance for analyzing those relationships.

The report must provide each beneficial owner’s name, birthdate, and address, as well as a unique identifying number and issuing jurisdiction from an acceptable identification document (and an image of such document), such as a driver’s license or a passport. The information in the filed report is intended to be available only to law enforcement agencies and regulators, but the exact scope of its availability is as yet uncertain.

For entities first formed or registered on or after January 1, 2024, the initial report will be due within 30 days after formation. For entities formed before January 1, 2024, the initial report will be due on or before January 1, 2025.

After an initial report has been filed, a reporting entity will be required to file updated reports, generally within 30 days, if reported information changes, the reporting entity discovers an error in a filed report, or the reporting entity becomes subject to an exemption.

Entities formed after January 1, 2024 must file within 30 days. Entities formed before January 1, 2024 must file on or before January 1, 2025.

Any person who willfully fails to file a required report or willfully files false information is subject to a civil penalty of up to \$500 per day that the violation continues and may be fined not more than \$10,000, imprisoned for not more than two years, or both.

Exemptions

More than 20 types of entities are exempted from the reporting requirements. Some of the more generally applicable exemptions include:

- Any company that has securities registered under the Securities Exchange Act of 1934 or files reports as a result of section 15(d) of that act;
- Any “large operating company,” meaning any entity that:
 - Employs more than 20 full time employees in the United States (not counting employees of subsidiaries or affiliates unless also actually employed by the subject company);
 - Has an operating presence at a physical office within the United States; and
 - 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 on a consolidated basis;
- Any entity that exercises governmental authority of the U.S. or of any state or political subdivision of a state;
- Any bank (as specifically defined in the regulations), credit union, bank holding company, or savings and loan holding company;
- Any entity registered with the SEC as a securities broker-dealer, investment company, or investment adviser;
- Any insurance producer licensed by a state and having a physical operating presence in the U.S. and any insurance company;
- Any PCAOB-registered accounting firm;
- Certain tax-exempt entities; and
- Any entity with ownership interests that are controlled or wholly owned, directly or indirectly, by one or more entities described above.

Any person who willfully fails to file a required report or willfully files false information is subject to a civil penalty of up to \$500 per day that the violation continues and may be fined not more than \$10,000, imprisoned for not more than two years, or both.

An exemption may apply to one or more entities without applying to all related companies, so each entity should be analyzed separately.

An “inactive entity” exemption applies if the entity:

- Existed on or before January 1, 2020;
- Is not engaged in active business;
- Is not owned, directly or indirectly, wholly or partially, by a foreign person;
- Has not had a change in ownership in the preceding 12 months;
- Has not sent or received more than \$1,000 in funds in the preceding 12 month period; and
- Does not otherwise hold any type of asset.



We believe that this exemption may allow some entities to avoid reporting, especially for companies that are no longer needed, but only if they are fully and formally wound up by the end of December 2023. We hope regulators will provide timely clarification on this point.

Meaning of “Substantial Control”

If none of the exemptions applies, the entity will need to analyze and report on those individuals who directly or indirectly either exercise substantial control over the entity or own or control at least 25 percent of its ownership interests. The regulations do not fully define “substantial control,” but the regulations are clear that control can exist without actual ownership and can exist in more than one person. The determination of what individuals exert substantial control are fact-specific and can be very subjective. There may be unexpected results as to the number and the identity of “beneficial owners” to be reported.

The regulations do not fully define “substantial control.” Control can exist without regard to ownership and can exist in more than one person.

Examples of a person with “substantial control” include any individual who:

- Serves as a senior officer;
- Has authority over the appointment or removal of any senior officer or a majority of the board of directors (or similar body); or
- Directs, determines, or has substantial influence over important decisions, including decisions regarding:
 - The nature, scope, and attributes of the business of the entity, including the sale, lease, mortgage, or other transfer of any principal assets of the entity;
 - The reorganization, dissolution, or merger of the entity;
 - Major expenditures or investments, issuances of any equity, incurrence of any significant debt, or approval of the operating budget of the entity;
 - The selection or termination of business lines or ventures, or geographic focus, of the entity;
 - Compensation schemes and incentive programs for senior officers;
 - The entry into or termination, or the fulfillment or non-fulfillment, of significant contracts; or
 - Amendments of any substantial governance documents of the entity, including the articles of incorporation or similar formation documents, bylaws, and significant policies or procedures.

Prepare Soon

There are nuances to many of the exemptions noted above. Moreover, because the beneficial ownership information reporting regulation is subject to further guidance and interpretation, we may need to adjust our positions as new information becomes available. The analysis of who must be reported by an entity as a

A detailed organization chart, including every entity, even inactive ones, would be a useful tool for this purpose.

“beneficial owner” is complex and, in some cases, subjective. If a report must be filed, it will include details, including photo identification, for each beneficial owner. It may take time to obtain all the information to comply with the reporting requirements. We recommend that every client

conduct at least a preliminary analysis and then consult legal counsel about the details. A detailed organization chart, including every entity – even seemingly inactive ones – would be a useful tool for this purpose. As further guidance is issued by the regulators, it may become clear that fully terminating or merging entities by December 31, 2023 may reduce or eliminate reporting requirements that would otherwise exist, making now the time to consider if any entities are unnecessary or duplicative. Analysis and planning should also be a high priority for anyone who may form a new entity in 2024 because there will be only 30 days to file a beneficial ownership report after forming that entity. In all cases, it will be necessary to monitor ongoing circumstances, because there is a continuing obligation to file updated reports.



Additional Information

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