

**OMG!**  
**Here Comes the CTA!**





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## Digesting the Alphabet Soup That is the Corporate Transparency Act

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### IDK, What is the CTA?

The Corporate Transparency Act (the “CTA”) was passed in Fiscal Year 2021 as part of the National Defense Authorization Act (“NDAA”) in an effort to “better enable critical national security, intelligence, and law enforcement efforts to counter money laundering, the financing of terrorism, and other illicit activity.”<sup>1</sup> Prior to the enactment of the CTA, the United States did not have a uniform system requiring individuals or entities to disclose information regarding those who establish or beneficially own entities that are formed or operate within the country. Times have changed. Pursuant to the CTA and the final regulations issued by the US Department of the Treasury’s Financial Crimes Enforcement Network (“FinCEN”) on September 30, 2022<sup>2</sup> (the “Regulation”), every “reporting company” will soon be required to submit a report to FinCEN disclosing, among other things, certain beneficial owner information (“BOI”), or will face possibly significant consequences for noncompliance.<sup>3</sup> Although much remains uncertain regarding the implementation and enforcement of this massive program, disclosure obligations will become effective in 2024, so it is time to become familiar with the CTA and the Regulation, and how this may affect you, your clients and customers.

## Will This Affect My BFFs?

The obligations imposed by the CTA apply to each so-called “reporting company.” A reporting company is defined as an entity that is created by filing a document with a secretary of state or similar office under the law of a State or Indian Tribe, or is formed in a foreign country and registered to do business in the United States by the filing of a document in such office.<sup>4</sup> Entities that may qualify as reporting companies include, but are not limited to, corporations, LLCs, LLPs, and business trusts (or, as they are called in Delaware, statutory trusts).<sup>5</sup> Although the CTA casts a wide net, twenty-four entity categories are exempted from the statute, including banks, tax-exempt entities, large operating companies, and inactive entities.<sup>6</sup> Additionally, trusts that are not created pursuant to a filing with the secretary of state or similar office (e.g. Delaware common law trusts) do not fall within the definition of reporting company.<sup>7</sup> However, many trusts hold interests in entities that will qualify as reporting companies, so certain trustors, trustees, fiduciary and nonfiduciary officeholders, powerholders and beneficiaries will be affected by the CTA.

Under the CTA, each reporting company is obligated to provide information regarding its “beneficial owners” and, depending on when it was formed, its company “applicants.” The CTA and the Regulation describe two categories of beneficial owners: (1) those who exercise “substantial control” over a reporting company, and (2) those with at least 25% of the ownership interests of a reporting company.<sup>8</sup> While the ownership test should, theoretically, be relatively easy to apply (and the rules that apply to beneficiaries of trusts are described in more detail below), determining whether someone possesses substantial control appears to be a more amorphous standard. An individual is deemed to exercise substantial control over a reporting company if the individual serves as a senior officer; has authority over the appointment or removal of any senior officer or a majority of the board of directors; directs, determines, or has substantial influence over important decisions made by the reporting company (e.g., important decisions regarding the nature of the business, major expenditures or investments, issuances of any equity and incurrence of any significant debt, compensation schemes, etc.); or has any other form of substantial control over the reporting company.<sup>9</sup> FinCEN intended this broad definition to “close loopholes that allow corporate structuring that obscures owners or decision-makers,” but it may cause some uncertainty among reporting companies, especially until additional guidance and standard practices are developed.<sup>10</sup>

Notwithstanding the breadth of the CTA and the Regulation, the following five categories of individuals and entities are excepted from the definition of a beneficial owner:

- minor children (whose parent or parents’ information is reported);
- individuals who are acting as nominees, intermediaries, custodians, or agents on behalf of other individuals;
- an individual acting as an employee for a corporation, LLC, or other entity and “whose control over or economic benefits from such entity is derived solely from the employment status of the person”;
- an individual with a right of inheritance interest in a corporation, LLC, or other entity; or

- a creditor of a corporation, LLC, or other entity unless they exercise substantial control or own more than 25% of the ownership interests of the entity.<sup>11</sup>

In regard to company applicants, the term “applicant” includes both the individual filing the document that creates the entity (or that registers it for business in the United States) and the individual who has directed or controlled another individual to file such a document.<sup>12</sup> Consequently, a variety of service providers that help facilitate the formation of entities, but who are otherwise unaffiliated with or have limited involvement with such entities, will be captured by the statute.

## OMG, I Have To File What? And What if the Information Is Incorrect or I Fail to File?

Initial reports are required to include the following information regarding the reporting company: (1) the company’s full legal name, (2) the company’s trade name or “doing business as” name, (3) the company’s complete current address of its domestic principal place of business for companies with a principal place of business in the US and for all other cases, the US address of the primary location where the reporting company conducts business, (4) the company’s formation jurisdiction, (5) for a foreign reporting company only, the jurisdiction where it first registered, and (6) the IRS Taxpayer Identification Number (“TIN”) that includes the reporting company’s Employer Identification Number of if a foreign reporting company does not have a TIN, such TIN that has been issued by its foreign jurisdiction.<sup>13</sup> BOI reports are also required to include four categories of information about each beneficial owner: (1) name, (2) date of birth, (3) address, and (4) some form of unique identifying number, such as a driver’s license number, with an image of the document containing such number.<sup>14</sup> The CTA also requires this same information be provided about the company applicant; provided, however, that company applicant information will only need to be reported for entities formed after January 1, 2024.<sup>15</sup> Furthermore, an individual may provide the required information directly to FinCEN and may obtain a FinCEN identifier, which can then be used in lieu of the above information on future BOI reports.<sup>16</sup> FinCEN received comments during the rulemaking process expressing concerns over entities’ use of a FinCEN identifier, and pledged to “address them before the effective date.”<sup>17</sup>

A reporting company discovering that a BOI report includes inaccurate information, or realizing that once-accurate information has since changed, has 30 days from the time the information changed or from the time it became aware or should have been aware that information was inaccurate to report changes to FinCEN.<sup>18</sup> Those willfully providing false or fraudulent information, willfully failing to report, or willfully failing to update inaccurate information,<sup>19</sup> could face criminal or civil penalties,<sup>20</sup> including a civil penalty of not more than \$500 for each day inaccurate information remains unfixd and may also be fined not more than \$10,000 and/or face two years of jail time.<sup>21</sup> Having received many comments regarding penalties through the rulemaking process, FinCEN stated that “any

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assessment as to whether false information was willfully filed would depend on all of the facts and circumstances surrounding the certification and reporting of the BOI, but as a general matter, FinCEN does not expect that an inadvertent mistake by a reporting company acting in good faith after diligent inquiry would constitute a willfully false or fraudulent violation.<sup>22</sup> Nevertheless, those with reporting obligations should be vigilant about reporting information accurately in the first instance and about keeping information up to date, or will potentially face serious adverse ramifications.

### What's the ETA?

Starting January 1, 2024, reporting companies will have disclosure obligations with respect to BOI and, depending on when they were formed, company applicants. Companies established before January 1, 2024 (“previously existing companies”) will have a different deadline and filing requirements than companies created or registered to do business in the United States on or after January 1, 2024 (“later created companies”). Specifically, previously existing companies will have until January 1, 2025 to file a BOI report and will not be required to disclose information regarding the company applicant.<sup>23</sup> Later created companies, however, will have 30 days after receiving notice of their creation or registration to file their initial BOI reports and will be required to provide company applicant information when the BOI report is filed.<sup>24</sup>

Importantly, both previously existing companies and later created companies will have an obligation to ensure their information remains up to date. If a reporting company discovers that reported information is inaccurate, or if control or ownership changes in a manner that causes previously-accurate information to become incorrect, the reporting company has 30 days from the time it become aware or should have become aware of such inaccuracy to report the changes.<sup>25</sup>

### BTW, How Will This Affect Trusts?

Notwithstanding that most trusts will not fall within the definition of a reporting company under the CTA, many trusts own one or more entities that will qualify as a reporting company, which may cause a trustor, trustee, fiduciary or nonfiduciary officeholder, powerholder or trust beneficiary to qualify as a “beneficial owner” within the meaning of the CTA if such person is deemed to beneficially own at least 25% of the entity or possess substantial control over the entity.

In determining whether an individual has substantial control of a reporting company held by a trust, in addition to the general control factors described above, the Regulation provides that an individual, including a trustee, may directly or indirectly exercise substantial control over a reporting company through: “(A) [b]oard representation; (B) [o]wnership or control of a majority of the voting power or voting rights of the reporting company; (C) [r]ights associated with any financing arrangement or interest in a company; (D) [c]ontrol over one or more intermediary entities that separately or collectively exercise substantial

control over a reporting company; (E) [a]rrangements or financial or business relationships, whether formal or informal, with other individuals or entities acting as nominees; or (F) any other contract, arrangement, understanding, relationship, or otherwise.”<sup>26</sup> Indeed, FinCEN stated that a trustee, depending on the circumstance, can exercise substantial control over a reporting company “through the exercise of his or her powers as a trustee over the corpus of the trust, for example, by exercising control rights associated with shares held in trust.”<sup>27</sup>

In determining whether an individual is deemed to own at least 25% of the ownership interests in the reporting company held in a trust, the Regulation provides that an individual may directly or indirectly own or control an ownership interest of a reporting company through “any contract, arrangement, understanding, relationship, or otherwise,” including, in part “(1) [a] trustee of the trust or other individual (if any) with the authority to dispose of trust assets; (2) [a] beneficiary who: (i) [i]s the sole permissible recipient of income and principal from the trust; or (ii) [h]as the right to demand a distribution of or withdraw substantially all of the assets from the trust; or (3) [a] grantor or settlor who has the right to revoke the trust or otherwise withdraw the assets of the trust.”<sup>28</sup> Notably, the Regulation provides that an individual’s total ownership will be considered, so the various capacities in which an individual may be deemed to own an interest must be considered.<sup>29</sup> Furthermore, more than one person can qualify as a beneficial owner of a trust’s interest in a reporting company, so all of the different individuals who possess interests and powers must be considered for reporting purposes.

Given the incredible flexibility of Delaware trusts and the number of roles and powers often possessed by trustors, trustees, fiduciary and nonfiduciary officeholders, powerholders and beneficiaries, the potential fact patterns are limitless, which makes it very difficult to establish general rules that will apply in every situation. Based on published guidance, however, it is clear that certain trustors, trustees, officeholders, powerholders and beneficiaries will fall within the definition of beneficial owner provided they possess the powers and ownership thresholds generally described above and in further detail in the Regulation. Consequently, a reporting company should understand the governing instrument for trusts that hold an interest to assess whether someone may qualify for mandatory disclosure under the CTA. All of this can, of course, be complicated greatly by factors such as limitations upon rights to information in silent trusts and bifurcation of trust powers among co-trustees and advisers. In light of the myriad designs of trust instruments and relationships in jurisdictions like Delaware, interesting questions are certain to arise. Members of the trust industry and their advisers will certainly be monitoring developments closely for additional guidance regarding CTA application in unique circumstances.





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#### Notes

- 1- Corporate Transparency Act, Pub. L. No 116-283, § 6403, 134 Stat. 4604, 4605-06 (2021). The NDAA includes the Department of Defense's plans for the coming fiscal year, and gathering information regarding those who create and own entities in the United States is one of the latest security measures the Department of Defense is taking.
- 2- 31 C.F.R. § 1010.380.
- 3- See generally, FINCEN, BENEFICIAL OWNERSHIP INFORMATION REPORTING RULE FACT SHEET (2022), <https://www.fincen.gov/beneficial-ownership-information-reporting-rule-fact-sheet>.
- 4- 31 U.S.C. 5336(a)(11).
- 5- FINCEN, supra note 3.
- 6- 31 U.S.C. § 5336(a)(11)(B).
- 7- FINCEN, supra note 3.
- 8- 31 U.S.C. § 5336(a)(3)(A).
- 9- 31 C.F.R. § 1010.230(d).
- 10- FINCEN, supra note 3.
- 11- 31 U.S.C. § 5336(a)(3)(B).
- 12- 31 U.S.C. § 5336(a)(2).
- 13- 31 C.F.R. § 1010.380(b)(1)(i).
- 14- 31 C.F.R. § 1010.380(b)(1)(ii).
- 15- 31 C.F.R. § 1010.380(b)(2)(iv).
- 16- 31 C.F.R. § 1010.380(b)(4).
- 17- Beneficial Ownership Information Reporting Requirements, 87 Fed. Reg. 59,525 (Sept. 30, 2022) (to be codified at 31 C.F.R. pt. 1010).
- 18- 31 C.F.R. § 1010.380(iv)(2).
- 19- 31 C.F.R. § 1010.380(g).
- 20- 31 U.S.C. § 5336(h)(1)(A)-(B).
- 21- 31 U.S.C. § 5336(h)(3)(A).
- 22- Beneficial Ownership Information Reporting Requirements, 87 Fed. Reg. 59,515.
- 23- 31 C.F.R. § 1010.380(a)(1)(iii), (b)(2)(iv).
- 24- 31 C.F.R. § 1010.380(a)-(b).
- 25- 31 C.F.R. § 1010.380(a)(2).
- 26- 31 C.F.R. § 1010.380(d)(1)(ii).
- 27- Beneficial Ownership Information Reporting Requirements, 87 Fed. Reg. 59,529.
- 28- 31 C.F.R. § 1010.380(d)(2)(ii).
- 29- 31 C.F.R. § 1010.380(d)(3).

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