Preparing Your Company for FinCEN's Beneficial Ownership Reporting Requirements

By Diana Ingallinera Faillace, Scott H. Moss, Jimmy Kang, Samantha Sigelakis-Minski, and Sabrina N. Jorge

On September 29, 2022, the U.S. Treasury's Financial Crimes Enforcement Network (FinCEN) issued a final rule implementing the Corporate Transparency Act's (CTA) beneficial ownership information (BOI) reporting requirements (Final Rule).[1] The CTA was initially enacted into law as part of the National Defense Authorization Act for Fiscal Year 2021 in January 2021, with an effective date of January 1, 2024 (Effective Date). It requires identification of both BOI (described in further detail below) and the identity of the individual who directly files or manages filing of the document that creates the company (Company Applicant). The Final Rule was implemented after years of bipartisan efforts to bolster corporate transparency in order to help prevent money laundering, terrorist financing, fraud, corruption, and other illicit activities in the U.S.

On March 24, 2023, FinCEN issued additional guidance to the Final Rule to clarify reporting deadlines and requirements and to facilitate compliance by reporting entities, in particular small businesses that may have never before interacted with FinCEN.[2] In the guidance, FinCEN advised that BOI will not be accepted until the Effective Date and clarified that reporting companies will not have to report their Company Applicants if the reporting company was created or registered before the Effective Date.

This Client Alert will address who will be required to report under the Final Rule and associated guidance, common exemptions that may apply, what information will be required to be reported, and how you can prepare. If you do not fit into any of the exemptions and will be required to report, this Client Alert will inform you about how to plan ahead of the Final Rule's Effective Date.

I. Who Must Report?

The Final Rule mandates that any entity that meets the definition of a "reporting company" must identify and report BOI to FinCEN. As defined, reporting company includes corporations, limited liability companies, limited liability partnerships, and any other entity created by a filing with the secretary of state or any similar office under the laws of its domicile state or Indian tribe. This covers both domestic and foreign entities in the event that the foreign entity is registered to do business in any U.S. state pursuant to a state filing.[3]

The Final Rule includes 23 exemptions from the definition of reporting company. Certain exemptions of note are the following:[4]

- Pooled investment vehicles
- Certain issuers, brokers, or dealers of securities that are registered or required to file periodic information under the Securities Exchange Act of 1934
- Registered investment advisers and companies

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[1] Federal Register Vol. 87, Nov. 189, Beneficial Ownership Information Reporting Requirements (Sept. 30, 2022), https://www.govinfo.gov/content/pkg/FR-2022-09-30/pdf/2022-21020.pdf.

[2] *FinCEN Issues Initial Beneficial Ownership Information Reporting Guidance,* https://www.fincen.gov/news/news-releases/fincen-issues-initial-beneficial-ownership-information-reporting-guidance.

[3] FinCEN's Office of Strategic Communications, *Beneficial Ownership Information Reporting Rule Fact Sheet*, (Sept. 29, 2022), https://www.fincen.gov/beneficial-ownership-information-reporting-rule-fact-sheet ("The rule identifies two types of reporting companies: domestic and foreign. A domestic reporting company is a corporation, limited liability company (LLC), or any entity 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. A foreign reporting company is a corporation, LLC, or other entity formed under the law of a foreign country that is registered to do business in any state or tribal jurisdiction by the filing of a document with a secretary of state or any similar office.").

[4] 31 CFR § 1010.380(c)(2).

- Tax-exempt entities (notably certain nonprofit entities that are subject to 501(c) of the IRS Code)
- Licensed money service businesses
- Companies demonstrating more than $5 million in gross receipts/sales that have (i) a physical office in the U.S. and (ii) more than 20 full-time U.S. employees

All 23 exemptions are subject to certain conditions, and not every entity will fit into an exemption despite the exemption initially appearing to be applicable. Moreover, some entities may qualify for multiple exemptions. An analysis of each entity and its subsidiaries/affiliates is required in order to determine the appropriate exemption. Once an exemption is identified, companies should be prepared to justify the exemption applied, as FinCEN has yet to issue guidance on what may be required of exempt entities, including reporting of such exemption. The authors of this Client Alert are prepared to assist with this exemption analysis.

II. What Information Must Be Reported?

The following information is required to be reported if the entity is determined to be a reporting company (Company Information).[5]

- Legal name of the entity
- Trade name or "doing business as" name of the entity
- Principal place of business in the U.S.
- Formation jurisdiction
- Tax number (employer identification number or taxpayer identification number)
- BOI for the beneficial owners of the entity

"Beneficial owners" are defined as "any individual who, directly or indirectly, either (1) exercises substantial control over a reporting company, or (2) owns or controls at least 25 percent of the ownership interests of [the] reporting company."[6] An individual exercises substantial control over a reporting company if they are empowered to act on the entity's behalf. For instance, a company's Chief Executive Officer (CEO), due to their decision-making authority, would qualify as a beneficial owner despite owning, if any, less than 25 percent of the reporting company. If a company's Chief Financial Officer is a nominal position with little decision-making authority, the reporting company may opt not to report such Chief Financial Officer in favor of an individual with a different title but with increased actual authority. As highlighted by the foregoing, actual authority is the prevailing consideration in the analysis of substantial control, not any titles with perceived authority.[7]

"Ownership interest" is broadly defined to include, among other things, equity, stock, and any other "mechanism used to establish ownership."[8] It is important to note that, unlike FinCEN's current Customer Due Diligence Rule, all individuals who qualify as beneficial owners, either by control or ownership, are required to be reported. As an example, both a CEO with substantial control and an individual with a 26 percent equity ownership stake would have to be reported. Despite the wide range of potential beneficial owners, the term does not include minors, agents, creditors, or future interest holders.[9]

Once a reporting company's beneficial owners are identified, the company must report the Company Information and BOI to FinCEN. BOI includes the beneficial owner's:

- Full legal name
- Date of birth
- Residential address
- A unique identifying number from a passport or accepted identification card

In addition, reporting companies created after the Effective Date must provide a scanned image of the document depicting the unique identifying number of the beneficial owner(s). Willful failure to report accurate BOI may result in civil and criminal penalties. Companies should implement controls to ensure reports are updated within regulatory timelines.

III. Next Steps

Reporting companies created or registered before the Effective Date will have until January 1, 2025, to file their initial BOI reports. Reporting companies created or registered after the Effective Date will have 30 days from creation/registration to file their initial BOI reports. All reporting companies are required to file updated reports within 30 days of any change to BOI or Company Information.

The Final Rule is the first of multiple anticipated rulemakings that will implement the CTA's reporting requirements. FinCEN is expected to issue guidance on (1) access to reporting companies' BOI and safeguards intended to maintain the highest levels of data protection and oversight and (2) amendments to its existing rules to better align with the Final Rule's requirements. The BOI and Company Information will be housed in FinCEN's Beneficial Ownership Secure System (BOSS). Current prevailing guidance indicates that the BOI will be confidential and the information will not be accessible through Freedom of Information Act requests. Reporting companies

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[5] *Id.* § 1010.380(b)(1)(i) (the reporting company itself must report its full legal name, address, jurisdiction of formation or registration, and Taxpayer Identification Number).
[6] *Beneficial Ownership Information Reporting Rule Fact Sheet*, https://www.fincen.gov/beneficial-ownership-information-reporting-rule-fact-sheet.
[7] *Id.*
[8] 31 CFR § 1010.380(d)(2)(i)(E).
[9] *Id.* § 1010.380(d)(3).

should expect their BOI and Company Information to be accessed only via the BOSS, in limited circumstances, and by limited parties as follows:

- Federal agencies, only when furthering national security, intelligence, or law enforcement activities
- State, local, and tribal agencies, as part of criminal or civil investigations if authorized by a court of competent jurisdiction
- Foreign governments, only to the extent requests are made by a foreign law enforcement agency, prosecutor, or judge and such request is approved by FinCEN
- Certain financial institutions seeking to comply with customer due diligence requirements if they have permission from the reporting company in question

The foregoing is subject to change as new final rules are issued.

IV. How to Prepare Prior to the Effective Date

The following are steps that potential reporting companies should consider taking prior to the Effective Date of the Final Rule:

1. Companies that have multiple subsidiary entities/fund families should analyze their organizational structure to identify each potential reporting company and begin the exemption analysis on an entity-by-entity basis. An analysis of each individual entity within the fund family is required in order to determine any applicable exemption, since there is no blanket exemption for entities falling within a fund's particular structure.
2. Once the entities are identified, an action plan for registration and reporting is recommended. Companies with entities incorporated prior to the Effective Date have one year from the Effective Date to register and report. Therefore, companies with a large organizational footprint should consider implementing a phased review of each entity, collating relevant information regarding applicable exemptions or reporting obligations.
3. With an action plan in place, companies should consult with internal stakeholders and in-house/outside counsel regarding applicable exemptions or reporting obligations. To the extent an exemption is applicable, the company should be prepared to support the designated exemption in the event of regulatory inquiries.
4. Where exemptions are not available, the reporting company must prepare the required BOI and Company Information for the FinCEN report. Special attention should be given to determining beneficial ownership. Ownership determination may require detailed analysis from multiple sources to establish ownership percentage, in addition to determining individuals with actual authority to substantially control the reporting company. Depending upon ownership complexity, the foregoing analysis may require significant time and resources.
5. Once all owners/controllers are identified, their BOI will need to be collected for reporting purposes and maintained in a secure manner in accordance with relevant privacy and cybersecurity laws.
6. Companies should document the foregoing processes in their anti-money laundering programs and include protocols for filing with the BOSS and conducting periodic reexaminations of each entity's claimed exemptions or reporting obligations. If any entity in a company's structure ceases to qualify for an exemption and therefore becomes a reporting company, such entity is required to file a report with FinCEN within 30 days of this change. Failure to report such changes may result in civil and criminal penalties.

V. Conclusion

Lowenstein Sandler is available to assist our clients with determining the applicability of any exemptions to the definition of reporting company, identifying beneficial owners, and otherwise preparing for the implementation of the Final Rule, including offering training to your compliance and operations teams. We encourage our clients to review the Final Rule and additional guidance, begin discussions to determine exemption status and/or prepare for reporting, and assess how FinCEN's Final Rule may otherwise impact your operations. Please contact the authors of this article at LSAMLTeam@lowenstein.com or your regular Lowenstein Sandler contact for further information.

Contacts

Please contact the listed attorneys for further information on the matters discussed herein.

DIANA INGALLINERA FAILLACE
Senior Counsel
T: **646.414.6953**
dfaillace@lowenstein.com

SCOTT H. MOSS
Partner
Chair, Fund Regulatory & Compliance
T: **646.414.6874**
smoss@lowenstein.com

JIMMY KANG
Associate
T: **646.414.6916**
jkang@lowenstein.com

SAMANTHA SIGELAKIS-MINSKI
Associate
T: **646.414.6934**
ssigelakisminski@lowenstein.com