



The Corporate Transparency Act (CTA) became law on January 1, 2021, and requires companies formed and/or operating in the United States to disclose beneficial ownership information through a database that will be maintained by the U.S. Department of the Treasury's Financial Crimes Enforcement Network (FinCEN).

The CTA was designed to combat the use of shell companies for illegal activities and to bring the United States into alignment with international corporate transparency standards.

Beginning January 1, 2024, the CTA will require most entities formed in the United States to disclose to FinCEN information describing their "beneficial owners," which include owners, officers, and control persons. The disclosed information is referred to as "beneficial ownership information" (BOI). There are 23 exemptions to the CTA's reporting requirement. One important exemption applies to large operating companies that have

more than 20 full-time employees, a physical operating presence in the United States, and more than \$5 million in gross receipts or sales in the prior year. Other key exemptions involve regulated entities such as public companies, investment advisers, venture capital fund advisers, pooled investment vehicles, tax-exempt entities, and many types of banks and financial institutions. For a broader analysis of the CTA and its exemptions, please see our Update [here](#).

This controversial new reporting regime carries significant compliance obligations and potential civil and criminal liability implications for individuals managing companies that are required to report under the CTA. This Update discusses how the CTA rules will affect directors and senior officers of CTA reporting companies, in particular. All senior officers, directors and their advisers, and counsel should be aware of these rules and potential implications.

## **Beneficial Ownership Information Disclosure Requirements**

The CTA defines "beneficial owner" to mean any individual who, directly or indirectly, either exercises "substantial control" over or owns or controls at least 25% of the ownership interests of a CTA reporting company. In their CTA reports, reporting companies will be required to provide FinCEN with the following information for each beneficial owner and company applicant:

- Full legal name.
- Date of birth.
- Current residential street address.
- Unique identifying number from a passport, state identification, or driver's license and an image of that document.

This information must be updated within 30 days of any change (except for the document image, which only needs to be updated if the address, name, or identifying number changes).

## **FinCEN Identifiers**

The beneficial ownership information is obviously highly sensitive private information, so in lieu of providing this information directly to a CTA reporting company, individuals will have the option to obtain a "FinCEN Identifier" by providing this information directly to FinCEN and keeping FinCEN updated as to changes. This FinCEN Identifier can then be provided to reporting companies to include in their CTA reports instead of the details typically required. We expect that beneficial owners will prefer to obtain FinCEN Identifiers, especially if they are beneficial owners of multiple CTA reporting companies.

## **"Substantial Control" and Senior Officers and Directors as Beneficial Owners Under the CTA**

FinCEN has defined the term "beneficial owners" broadly to include individuals who "substantially control" the entity, as well as those who own or control at least 25% of the ownership interests of the CTA reporting company.

An individual exercises "substantial control" under the CTA if they: (1) serve as a "senior officer" of the CTA reporting company; (2) have authority over the appointment or removal of any senior officer or a majority of the board of directors (or similar body); (3) direct, determine, or have substantial influence over important decisions made by the CTA reporting company; or (4) have any other form of substantial control over the CTA reporting company.

- A senior officer of a CTA reporting company is defined to include the president, chief executive officer, chief financial officer, chief operating officer, general counsel/chief legal officer, as well as "any other person, regardless of title, who performs similar functions." Individuals who perform ministerial functions like a secretary or treasurer do not typically have the requisite control to be considered a senior officer.
- Many other individuals may have the requisite control over a CTA reporting company to meet the definition of "beneficial owner." For example, FinCEN explicitly highlights in the rule that an individual may exercise direct or indirect control over a company through representation on the board of directors. Unlike senior officers, however, individual directors will only be reportable when their authority over the CTA reporting company rises to the level of "substantial control" or "substantial influence over important decisions," phrases that remain vague as applied in the context of a particular business.
- Many LLCs appoint a "manager" with the power and authority to manage the business and affairs of the entity. LLC managers also fall within the definition of a beneficial owner that exercises substantial control under the final rule.
- Beneficial owners of a parent reporting company, including its senior officers, may also be beneficial owners of certain downstream subsidiary reporting companies that are owned or controlled by the parent. The final rule provides that an individual may exercise substantial control over a reporting company if the individual has control over one or more intermediate entities that exercise substantial control over a reporting company. In situations involving multiple downstream subsidiaries, an analysis of the corporate organization ownership structure and control structure must be undertaken to determine which senior officers exercise substantial control over these subsidiaries.
- Notably, many other categories of individuals who may exercise "substantial control" or "substantial influence over important decisions" will be exempted from reporting, as the CTA exempts any person (with the exception of senior officers) whose control over the company stems exclusively from their employment by the reporting company.

### **Will Senior Officers and Directors Be Subject to Liability?**

As noted above, the CTA provides for both civil and criminal liability. Violations may result in civil penalties of up to \$500 for each day that the violation continues, and criminal penalties of imprisonment for up to two years and/or a fine of up to \$10,000.

Importantly, we expect that CTA enforcement will relate primarily to the underlying misconduct involving reporting companies or significant systemic failures in CTA reporting, and not to technical reporting violations. In fact, there is no provision for liability for negligent failures to report. Violations of the CTA can be enforced only when committed willfully or by extension under circumstances where the violator was "willfully blind" or "consciously disregarded" a high risk that they were violating the CTA.

While the responsibility for reporting under the CTA falls to the reporting company itself, liability for failure to report or false information provided to FinCEN can run to "any person" involved in the filing or omission. Under the final rules, it is unlawful for "any person to willfully provide, or attempt to provide, false or fraudulent beneficial ownership information" or fail to provide information required to be filed with a CTA report. With a clear eye toward senior officers, directors, and other potential "beneficial owners" whose information will be required in CTA reports by companies with which they are associated, the final rules note that a person may still be liable even if they provide false information to FinCEN indirectly, including by providing it to another person for purposes of reporting.

Notably, the rule also specifically provides for liability where a person (willfully or with willful blindness) fails to report complete or updated beneficial ownership information if: (1) the entity is required to report information to FinCEN; (2) the reporting company fails to report such information to FinCEN; and (3) such person either

"causes the failure" or is "a senior officer of the entity" at the time of the failure. Again, this demonstrates FinCEN's intention to target senior officers—and others involved in decision-making around CTA compliance—who shirk responsibility for ensuring CTA reporting or refuse to provide required information for purposes of reporting under the CTA.

### **Liability Exposure of Senior Officers**

Senior officers face risks under the CTA in two primary circumstances. First, because senior officers expressly fall within the definition of beneficial owners, a reporting company must always report the beneficial ownership information of its senior officers. Therefore, to the extent that a senior officer willfully provides or attempts to provide false or fraudulent BOI—or willfully fails to report complete or updated BOI—as part of that process, the senior officer will be liable for the reporting violation.

But beyond failures relating to the information they provide, senior officers may also be exposed to liability for the reporting company's broader CTA compliance failures. As described above, the final rules expressly state that a person is considered to have failed to report complete or updated beneficial ownership information if such person is a senior officer of the entity at the time of the failure. Accordingly, senior officers could be subject to liability where their reporting company fails to report complete or updated information for its beneficial owners if the failure/false information was the result of a willful (or willfully blind) act. For example, if a reporting company (or a company that should have been reporting under the CTA) is associated with money laundering or sanctions evasion by its ultimate beneficial owners, we may see charges against senior officers uninvolved in the underlying misconduct for failures under the CTA insofar as CTA reports may have omitted or obscured the ownership of the entity, and the senior officer may have overlooked red flags suggesting the information they received may be false.

### **Liability Exposure of Directors**

The liability of directors under the final rules is more ambiguous because a director's position as a beneficial owner is a facts-and-circumstances determination related to the director's control of the reporting company. On September 29, 2023, [FinCEN published an FAQ](#) on its website confirming that whether a particular director meets any of these criteria for beneficial ownership on the basis of their "substantial control" or "substantial influence over important decisions" of the reporting company is a question that the reporting company must consider on a director-by-director basis.

Given the ambiguity as to when a director must be reported under the CTA, many reporting companies may wish to adopt a conservative approach when determining whether to report their directors. In some cases, companies may choose to report information for all directors. FinCEN contemplated the potential for overreporting throughout the rule and explicitly permits filings including any person who "may" be a beneficial owner to encourage this approach.

Where companies do not draw a bright line of this nature, they will need to adopt guiding principles that can be consistently applied in determining when to report directors under the CTA. For instance, where a reporting company is managed by a small board of directors, it is more likely that FinCEN would conclude that each director exercises substantial control, such that they must be reported under the CTA. By contrast, where a reporting company is managed by a larger board of directors, the question will be whether each of those directors otherwise exercises substantial control or substantial influence over the reporting company, such that they would be beneficial owners. Within this context, the analysis turns on factors similar to those enumerated more broadly under the rule for determining substantial control (e.g., substantial influence over important decisions made by the reporting company, control of a majority of the voting power or voting rights of a

reporting company, or special reservations of rights such as veto powers).

If a reporting company determines that a director is a beneficial owner under the CTA, then the director (akin to the senior officer analysis above) will be liable if they willfully provide or attempt to provide false or fraudulent BOI, or willfully fail to report complete or updated information.

## **The Role of Reporting Companies**

Some reporting companies may update their bylaws and agreements with senior officers and directors to clarify these requirements and ensure that these individuals are required by contract to provide either BOI or a FinCEN identifier for use in the reporting company's CTA compliance. However, this is not strictly necessary; as set out above, senior officers and directors will have independent potential civil and criminal liability for failure to provide required information/provision of false information under the CTA.

To the extent that any beneficial owner refuses to provide such information, a reporting company will have the option to submit their CTA report naming that person and checking a box indicating that the information was not available. Reporting companies should be sure to document their diligence in making reasonable attempts to obtain this information before filing such a report. But, ultimately, a report including this reference will flag for FinCEN that the named beneficial owner may have shirked their responsibilities under the CTA.

In light of the ambiguities under these rules, particularly as to the reporting of directors, there may be genuine disagreements between individuals and reporting companies as to whether the reporting of a particular individual is required. As noted above, the most conservative approach will likely be to report in the absence of certainty. In circumstances where there is genuine, good faith disagreement between the reporting company and an individual potential "beneficial owner" under the rule as to the reporting requirements, both will be best protected by maintaining robust documentation of their analysis, information on which they relied, and the basis for their ultimate conclusion in the event that FinCEN questions a CTA report down the road.

## **Key Takeaways**

### **Ambiguities Remain**

Although FinCEN has defined who qualifies as a beneficial owner required to be reported under the CTA, many ambiguities remain, particularly with respect to how these rules apply to senior officers and directors and, in particular, in the case of downstream subsidiary entities within complex corporate organization structures. The rules are more explicit with respect to senior officers, specifically stating that they exercise the substantial control required to be considered beneficial owners and are more exposed to liability for reporting violations due to the positions they hold. When it comes to directors, however, the analysis is more fact dependent and less clear. In turn, whether liability attaches to a director will depend on reporting companies and directors agreeing on the outcome under this case-by-case approach.

### **Consistent Policies and Record Keeping Will Be Important**

With regard to CTA reporting, as with any high-stakes and complex compliance regime, it will be critical for all parties—reporting companies as well as their individual senior officers and directors—to keep detailed records regarding CTA compliance decisions and to adopt *and consistently apply* organizationwide policies regarding how remaining ambiguities under the rule will be addressed. Even if FinCEN disagrees with a reporting company's approach, records of this nature will help to demonstrate good faith in reporting and to rebut allegations that anyone willfully violated the CTA's reporting requirements.

## Where To Get More Information

For more, see our [quick reference](#) to the new beneficial ownership reporting requirements under the CTA and our more detailed [Update](#) on the subject. Also, see FinCEN's [FAQs](#) and [Reference Materials](#) on the CTA. Starting January 1, 2024, CTA reports can be filed and FinCEN identifiers can be obtained on [FinCEN's main CTA page](#).

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