

# CORPORATE TRANSPARENCY ACT

Kinetic Law LLC

# Overview of CTA

- Passed into law on January 1, 2021
- Takes effect on January 1, 2024
- Designed to combat use of entities like LLCs and corporations for illegal activities
- Requires companies to report identities of control persons and beneficial owners to FinCEN
- Database will be available to law enforcement agencies, but not general public

# Compliance Estimates

## **Companies that are covered**

- FinCEN estimates at least 32.6 million entities will have to report
- FinCEN estimates at least 14.4 million will need to file updated reports in Year 2

## **Cost Estimates**

- Initial compliance for a complex entity structure - \$2,615, as estimated by FinCEN
- Updates estimated to cost \$561 per entity

# Who Must Report?

- Privately-owned corporations and LLCs
- Any other entity created by filing of a document with the state

# Who is Exempt?

- Sole proprietorships
- Most estate planning trusts and other trusts are not covered, unless they have beneficial ownership of a company that is required to report
- Companies with more than 20 full-time employees, AND more than \$5 million in gross sales (as measured by prior year tax return), AND a US physical presence, are exempt – these are “large operating companies”. Also, their wholly owned subsidiaries are exempt.
- Tax-exempt entities under 501(c) of the tax code
- Accounting firms
- Highly regulated companies – banks, insurance companies, etc.

# What Persons Must Be Reported?

- Senior officers – CEO, COO, CTO, CFO, VPs, and persons who have authority to appoint or remove senior officers or a majority of the board of directors
- Individual investors/shareholders with at least 25% of the ownership interests of the company Individual investors/shareholders with “substantial control” – this includes many common investor control features, such as the right to a board seat, or the right to approve certain transactions. Assume that many VC investors are included.

# What Persons Must Be Reported (cont'd)

- "Company applicants" – the person who files the certificate of incorporation or articles of organization for the company.
- However, reporting companies in existence prior to January 1, 2024 do not have to report information about their company applicants.
- If one of your investors is an entity, and you have to report on that investor, you will have to report information on individuals that own 25% or more of the investor, or that have substantial control over the investor

# What Persons Must Be Reported (cont'd)

- For trusts, the beneficial owners of the trust (grantors/settlors, beneficiaries, trustees) may be reportable if the trust directly or indirectly owns an interest of 25% of a reporting company.
  - A grantor or settlor who has the right to revoke the trust or otherwise withdraw the trust's assets
  - A beneficiary who is the sole permissible recipient of the trust's income and principal
  - A beneficiary who has the right to demand a distribution of or withdraw substantially all of the assets
  - Trustees
  - Any other person that has authority to dispose of trust assets



# What Persons Must Be Reported (cont'd)

- Creditors with a right to equity (through a convertible note or SAFE), if upon conversion they could hold 25% or more of the company or have substantial control
  - This may require some modeling to determine how much stock the convertible note or SAFE will convert into
  - If the convertible note or SAFE converts into preferred stock, ownership of that preferred stock may give substantial control

# Substantial Control

Substantial Control may be triggered by:

- Board representation
- Ownership of a majority or dominant minority of voting shares
- Rights associated with any financing arrangement or interest in the company
- Through arrangements of financial or business relationships, whether formal or informal, with other individuals or entities acting as nominees, or through any contract, arrangement, understanding, relationship, or otherwise

The ***right to control*** is what is important, not whether it is exercised

# What Information Must Be Reported?

For individuals

- Full legal name,
- Date of birth,
- Address,
- Government-issued identity document, such as a passport, drivers license, or state ID, and
- A photo of the government-issued identity document, showing the individual's photograph, jurisdiction of issuance, and identification number

# What Information Must Be Reported? (cont'd)

For the reporting company itself:

- Full name of the company
- Any trade names or DBAs
- Business street address
- Jurisdiction of formation
- IRS tax identification number (EIN)

# Filing Deadlines

- Existing entities must file initial reports by December 31, 2024
- New entities must file the initial report within 90 days of the date they are formed, for entities formed in 2024, and 30 days for entities formed in 2025 and after

# Updates

- Reporting companies must update information in a timely manner and correct any inaccurate information
- 30 days to file updates to report changes in beneficial ownership and any change with respect to the information reported for a beneficial owner
  - If you take on a new officer or shareholder/investor that meets the beneficial ownership requirements, you must file an update
  - If a beneficial owner's address changes, or gets a new drivers license or passport, you must file an update
  - You will need a mechanism to get this updated information from beneficial owners

# Updates (cont'd)

- If someone is no longer an officer or beneficial owner, you will need to file an update – for example, if a shareholder sells her stock or an officer leaves the company
- 14 days to correct inaccurate reports
- Reporting companies formed or registered after January 1, 2024 do not need to update company applicant information

# Penalties

- Any person who willfully fails to report complete or updated information faces fines of up to \$10,000 and/or imprisonment for up to 2 years
  - Now that you have watched this webinar and know what is required, if you fail to report it will likely be willful
- Same penalties apply to anyone who willfully provides (or attempts to provide) false or fraudulent beneficial ownership information
- Penalties apply to the reporting company as well as to responsible individuals and other entities, such as officers, directors, controlling shareholders



# Next Steps

- Determine whether your company is required to report – does it meet the large operating company exemption?
- Identify all persons that may need to be listed on the report – senior officers, directors, shareholders, investors, etc.
- Evaluate that list against the requirements described above to narrow the list – 25% ownership of stock, substantial control
- Contact each person on the list to obtain the necessary information. Explain why you are asking for the information, give them a deadline for compliance, and ensure that they understand this is mandatory.
- Also notify these persons about the requirement to provide updated information on a timely basis

# Next Steps (cont'd)

- Start compiling your initial report with the information provided
- Develop and implement a process for handling updates – new beneficial owners and changes to existing beneficial owners
  - Who will be responsible for this process? Someone needs to take ownership of it.
- Finally, look for states to act as well. The New York State Assembly recently passed a law, based on the CTA, that will be applicable to LLCs formed or registered in New York. Waiting to see if the governor signs it into law.

# CAUTION!!

- Watch out for official-looking mail solicitations offering to assist with your reporting
- The information you report is sensitive information
- Some solicitations may be from legitimate providers, but there may also be scammers trying to steal owners' identities

If you need assistance with complying with this new requirement, please contact us.

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