Your New Reporting Obligations under the Corporate Transparency Act: What Healthcare Providers Need to Know

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CTA Overview

- The Corporate Transparency Act (CTA) was enacted January 1, 2021, after several decades of failed efforts to pass similar legislation.
- Included in "must pass" Department of Defense reauthorization/funding legislation.
- Then-President Trump vetoed it, but Congress then overrode his veto (the only Trump veto overridden by Congress).

CTA Overview

- CTA is being implemented by the Financial Crimes Enforcement Network (FinCEN), a division of the Department of the Treasury.
- FinCEN issued rules to implement the CTA, which became effective January 1, 2024.

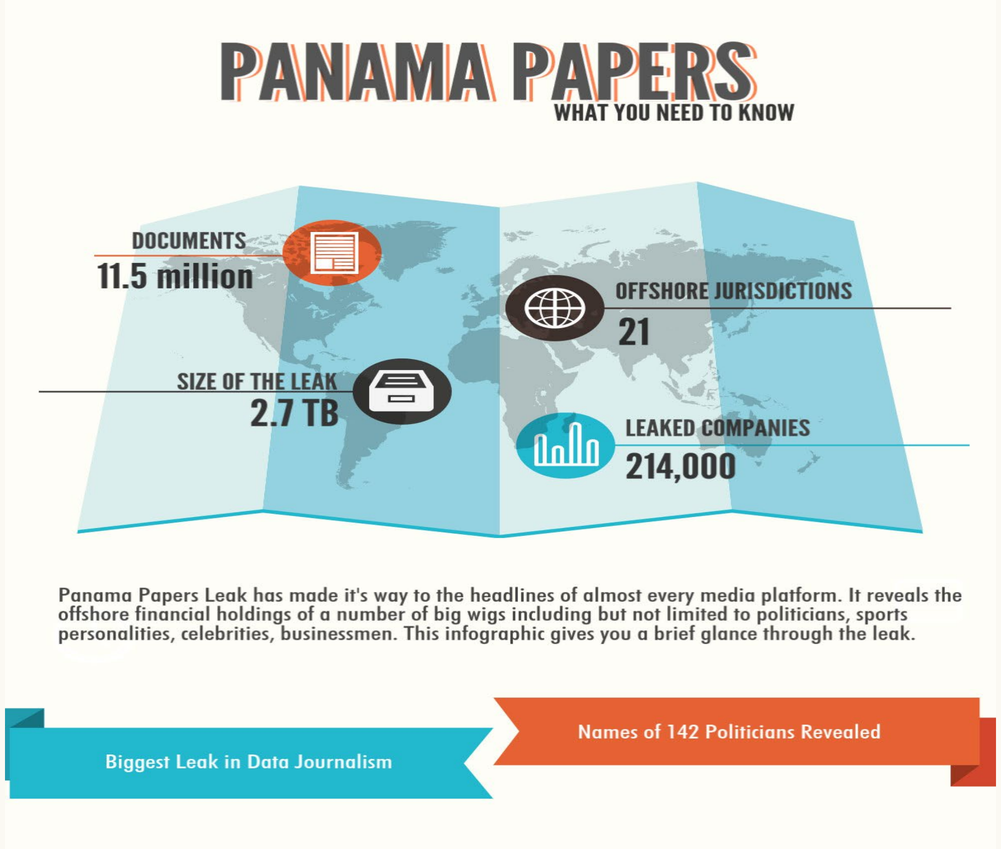
Why Do We Now Have the CTA?

- Longstanding concern in the federal government and internationally that law enforcement and intelligence lack the information and tools to pursue criminal activity.
  - Most European countries require reporting of beneficial ownership information.
  - Financial Action Task Force, an international, intergovernmental task force, found US practices deficient.

Past Efforts Fell Short

- Then-Senator Barack Obama and others tried and failed to establish a beneficial ownership reporting regime.
- The Panama Papers scandal created an opportunity:
  - Documents leaked from a Panamanian law firm (Mossack Fonseca) in 2016 revealed rampant use of shell companies by wealthy elites and oligarchs around the world (including many politicians, celebrities, rogue nations, terrorist and criminal organizations) to hide assets, engage in money laundering, tax fraud, narco trafficking, human trafficking and other crimes.

Panama Papers



- Credit for graphic: Viewpoints: Panama Papers Explained, Worldpress.org, June 12, 2016.

Panama Papers

- **The New York Times, 5/29/16:** "In the United States, the revelations of hidden wealth have resonated amid growing public concern about economic inequality; the word yacht appears in the documents 19,380 times. President Obama has deplored how the rich and some companies are "gaming the system," as he said the documents showed, and has proposed multiple reforms. …**In fact, some experts believe the "Panama" label is misleading, obscuring the central role of several states, including Delaware, Wyoming and Nevada, in registering companies with hidden ownership**. Mossack Fonseca probably represents just 5 or 10 percent of the industry creating anonymous companies."

Address AML/CFT Deficiencies

- Following Panama Papers, efforts in Congress to pass federal legislation gained bipartisan traction.
- Congress found that the federal government's failure "to mandate collection of beneficial ownership information of corporate entities in the United States has been a vulnerability in the US anti-money laundering/countering the financing of terrorism (AML/CFT) framework."
- Creates opportunities for criminal actors and groups to act anonymously and evade investigation and prosecution.

More Recent Events

- In its rulemaking, FinCEN has pointed to actions taken by the Russian Federation and Russian oligarchs following the onset of the war in Ukraine in February 2022, to use US and foreign shell companies to evade sanctions.
- 255-foot superyacht "Tango", owned by shell companies used to conceal real ownership by Viktor Vekselberg, was seized due to alleged violations of bank fraud, money laundering and sanctions.

More Recent Events

- Shell companies used to make fraudulent applications for Paycheck Protection Program loans (COVID relief for small businesses).
  - Hasan Hakim Brown pled guilty to using shell companies and synthetic identities to apply for and obtain over $24 million in PPP loans.

How Has This Happened?

- Until CTA, there was no federal registry of businesses and beneficial owners.
- States have not required registration of beneficial owners or, in most cases, direct owners.
  - A few states have now enacted (or are attempting to enact) their own versions of CTA, requiring state registration.
- No such registry has existed.

How Has This Happened?

- The status quo in many:
  - Corporations' articles of incorporation and annual reports do not require listing of direct or beneficial owners, directors or officers.
  - LLCs need not disclose managers, members or direct or beneficial owners.
  - The same is true for professional corporations (PCs) and professional limited liability companies (PLLCs) used by many healthcare providers.

Purpose of CTA

- Mandate reporting of "beneficial ownership" information (broader than it sounds) for corporations, LLCs, professional corporations, professional limited liability companies, and similar entities.
- Create a federal database of beneficial ownership information, available to law enforcement, national security, intelligence and certain other authorities.
- Bring US into compliance with international AML/CFT standards (such are in place in Europe).

CTA's Mandate

- Most small and newly formed US businesses and foreign businesses registered to do business in a state must report (and update to report changes to) sensitive personal identifying information about:
  - Beneficial owners (25% or more)
  - Senior officers
  - Directors?
  - Other parties with significant control by contract, organizational documents, or under law
  - "Company applicants"

When Does It Start?

- Entities formed before January 1, 2024: must file initial report by January 1, 2025.
- Entities formed on or after January 1, 2024: reporting obligation commences immediately, with the first report due within 30 days following formation (receipt of actual notice of effectiveness or provision of public notice, e.g., through an online registry).
  - FinCEN extended the period to file for entities formed in 2024 but not later to 90 days after formation.

Who Must Report?

- Most smaller corporations, LLCs, professional corporations, professional limited liability companies, and other business entities formed by the filing of articles or another document with a Secretary of State (or similar office) of a State, US territory, or Tribe.
  - Limited partnerships? Limited liability partnerships? Depends on state law
- Foreign entities which file a document with such an office to qualify to do business.

Who Is Exempt?

- Certain types of entities are exempt from CTA's reporting requirements so long, but only so long, as they continue to meet the exemption requirements.
- If an exempt entity ceases to meet all requirements for an exemption, they must commence reporting.
- A reporting entity may become exempt and cease reporting.

Exempt Larger Entities

- Large businesses and their subsidiaries
  - Employ more than 20 full-time employees in the US; and
  - Have an operating presence at a physical office in the US; and
  - Filed federal income tax return or information return in the US for the previous year demonstrating more than $5 million in gross receipts or sales (net of returns and allowances), excluding gross receipts or sales from non-US sources.
    - <u>Newly formed entities will not be able to meet this requirement during their first year of existence.</u>

Exempt Inactive Entities

- In existence on or before January 1, 2020 (exemption unavailable for more recently formed entities); <u>and</u>
- Not engaged in any active business; <u>and</u>
- No amount of direct or indirect ownership by a foreign person; <u>and</u>
- No change of ownership in the preceding 12-month period; <u>and</u>
- Hasn't sent or received more than $1,000 in funds (directly or through an affiliate) in the preceding 12-month period; <u>and</u>
- Doesn't hold any kind or type of asset (including equity) in the US or abroad.

Exempt Regulated Entities

- Public companies (registered with the Securities and Exchange Commission or the Commodity Futures Trading Commission)
- Financial institutions (banks, savings banks, credit unions, holding companies)
- Insurance companies
- Registered money transmitters (e.g., PayPal, Western Union)
- Regulated public utilities
- Certain tax-exempt entities
- Subsidiaries of certain categories of exempt entities

When Is the Initial Report Due?

- Entities formed before January 1, 2024: Initial report is due on or before January 1, 2025.
- Entities formed on or after January 1, 2024 but before January 1, 2025: Within 90 days of formation.
- Entities formed on or after January 1, 2025: Within 30 days of formation.

What Must Be Reported?

- Identifying information about the reporting company:
  - Entity name
  - Any trade name or d/b/a name
  - Street address
  - Taxpayer identification number (EIN)

What Must Be Reported?

- Identifying information on each "company applicant":
  - Each individual who files organizational or registration documents for the reporting company <u>or</u> who directs or controls the filing of such document by another person
  - Full legal name
  - Date of birth
  - Complete current address
  - Copy of passport, driver's license or similar identification
  - Alternatively, FinCEN identifier

What Must Be Reported?

- Identifying information on each “beneficial owner” of the reporting company:
  - Full legal name
  - Date of birth
  - Complete current address
  - Copy of passport, driver’s license or similar identification
  - Alternatively, FinCEN identifier

Who Is a "Beneficial Owner"?

- Any individual who has direct or indirect ownership or control of at least 25% of the ownership interests of the reporting company on a fully diluted basis (including non-voting ownership interests).
  - Assumes exercise of all options, warrants, subscriptions, conversion of debt.
  - Individual who exercises, or has the right or ability to exercise, substantial control over the reporting company, including all senior officers, directors, LLC managers.

FinCEN Identifier Number

- In lieu of including the sensitive personal information on company applicants and beneficial owners in a report, a unique FinCEN-issued identifier number may be used in the report.
- The individual must apply to FinCEN and provide FinCEN with the information required to obtain an identifier number.
- Once obtained, the individual may provide it to multiple reporting companies.
- FinCEN has proposed, but not finalized, rules for collection of information from individuals and issuance of identifier numbers.

When Must a Report be Updated?

- Reports must be updated or corrected if any reported information changes or is (or becomes) incorrect or incomplete.
- Must be filed within 30 days of the change.
- Examples:
  - Change of entity name
  - Change or addition or cessation of trade name or d/b/a name
  - Transfers or gifting of direct or indirect ownership interests
  - Changes in senior management or board
  - Issuance of new equity, convertible debt, warrants, options or subscriptions
  - Redemption or cancelation of equity, debt convertible into equity, or warrants, options or subscriptions to acquire equity

Certifications

- The person who submits a report on behalf of a reporting company makes a certification that it is accurate or complete.
  - *No knowledge or materiality qualification*
- Any person who willfully provides, or attempts to provide, false or fraudulent information to FinCEN or willfully fails to report complete or updated information or "causes the failure, or is a senior officer of the entity at the time of the failure" is subject to civil and criminal penalties.
- A person provides or attempts to provide beneficial ownership information to FinCEN if they do so directly or indirectly, including by providing such information to another person for purposes of a report or application.

What Happens with Reports?

- FinCEN is creating a massive database to house all reported information.
  - Data to be held for at least five (5) years beyond the date on which the reporting company terminates.
- The CTA limits access to reported information to:
  - Federal national security agencies
  - Federal intelligence agencies
  - Federal law enforcement personnel
  - State or Tribal law enforcement personnel (with a court order)
  - Federal functional regulators (e.g., FDIC, OCC, NCUA, SEC, CFTC)
  - Foreign law enforcement agencies in certain circumstances
  - Financial institutions subject to customer due diligence requirement, with the consent of the reporting company (much of the information has previously had to be collected by financial institutions)

Sanctions for Violations

- Civil penalties of up to $500 per day.
- Criminal penalties:
  - Fines up to $10,000, up to two (2) years imprisonment, or both.
- Other penalties for unauthorized use or disclosure of reports or beneficial ownership information.

Legal Challenges

- A federal court in Alabama recently ruled that the CTA, as written, is unconstitutional. *National Small Business Association v. Yellen*.
- The ruling applies only to the NSBA and one person named as a plaintiff.
- The government is appealing the decision, and is likely to succeed in reversing it.

What You Can Do Now?

- Analyze whether your company, and any subsidiaries, are exempt.
- Obtain, understand and update your organizational chart and registry of shareholders, members, and holders of convertible debt, options and warrants.
- Understand which officers, directors, managers or others, through position of control or contract, exercise control over the company and are “beneficial owners” even if they are not equityholders.
- Amend your organizational documents or enter into agreements with equityholders to promptly provide and update information on beneficial owners.
- Provide “beneficial owners” with the opportunity to apply for and provide FinCEN identifier numbers.

Questions

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