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## FinCEN’s Proposed Rule Would Broadly Expand Beneficial Ownership Reporting Requirements

On December 8, the Financial Crimes Enforcement Network (“FinCEN”), within the U.S. Department of the Treasury, published proposed regulations, *Beneficial Ownership Information Reporting Requirements* (the “Proposed Rule”),<sup>1</sup> to implement the beneficial ownership information reporting provisions of the Corporate Transparency Act (“CTA”).

**Attorneys**  
[Ama A. Adams](#)  
[James P. Dowden](#)  
[Brendan C. Hanifin](#)  
[Emerson Siegle](#)  
[S.J. Tilden](#)

The CTA, enacted as part of the Anti-Money Laundering Act of 2020, is intended to expand and modernize the U.S. government’s ability to collect beneficial ownership information (“BOI”) to deter money laundering, corruption, tax evasion and fraud, and other financial crime. The CTA requires FinCEN to, *inter alia*, (1) implement rules for the reporting of BOI of legal entities organized or registered to conduct business in the United States; (2) develop protocols for access to, and the sharing of, reported BOI; and (3) amend the current Customer Due Diligence (“CDD”) Rule applicable to financial institutions to account for the new requirements of the CTA. The Proposed Rule addresses only the reporting of BOI, with the remaining requirements to be addressed through future rulemaking.

The Proposed Rule would require “reporting companies” to file reports with FinCEN that (1) identify themselves; and (2) provide BOI of their “beneficial owners” and “company applicants,” each as discussed in greater detail below. FinCEN has solicited further public comment on the Proposed Rule until February 7, 2022, but there is currently no firm timeline for final implementation.

### Reporting Companies

The Proposed Rule would apply to “reporting companies,” which include both domestic and foreign companies, as described below:

- Domestic Reporting Companies, including any (a) corporation; (b) limited liability company; or (C) other entity that is 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 (which FinCEN has previewed would likely include limited liability partnerships, limited liability limited partnerships, business trusts, and most limited partnerships); and
- Foreign Reporting Companies, meaning any (a) corporation, limited liability company, or other entity; that is (b) formed under the law of a foreign country; and (c) 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 under the law of a State or Indian tribe.

The Proposed Rule sets forth 23 exemptions to the definition of reporting company, consistent with the CTA’s approach of “target[ing] generally smaller, more lightly regulated entities that may not be subject to any other BOI reporting requirements.” Key categories of exempted legal entities include:

- SEC reporting issuers;
- Banks;
- Money transmitting businesses;
- Broker-dealers;
- Investment companies and investment advisers;
- Venture capital fund advisers.

<sup>1</sup> See Beneficial Ownership Information Reporting Requirements, 86 Fed. Reg. 69,920 (Dec. 8, 2021).

Also exempted are:

- Large operating companies that (1) employ more than 20 full time employees in the United States; (2) have an operating presence at a physical office within the United States; and (3) filed a Federal income tax or information return in the United States for the previous year demonstrating more than \$5,000,000 in gross receipts or sales;
- Subsidiaries whose ownership interests are controlled or wholly owned, directly or indirectly, by one or more entities exempt from the definition of reporting company; and
- Pooled investment vehicles<sup>2</sup> operated or advised by a qualifying bank, credit union, broker-dealer, investment company or investment adviser, or venture capital fund adviser.

The Proposed Rule clarifies that one potentially large exempt category—“dormant entities” that have not engaged in active business or held material assets in the preceding 12 months—is merely a grandfathering provision, applying only to entities that were dormant for a year or more prior to the CTA’s enactment.

## Subjects of FinCEN Reports

In addition to identifying information of the reporting company, the Proposed Rule would require the reporting of BOI concerning: (1) beneficial owners; and (2) company applicants.

### *Beneficial Owners*

Similar to the CDD Rule, the term “beneficial owner” is defined in terms of both ownership and control: any individual (*i.e.*, natural person) who, directly or indirectly, either (x) exercises substantial control over a reporting company or (y) owns or controls at least 25% of the ownership interests of a reporting company. Limited exceptions exist to the definition, including for minor children, nominees, employees, inheritors, and creditors.

The Proposed Rule’s definition of “substantial control” includes:

- Acting as a senior officer of the reporting company;
- Authority over the appointment or removal of any senior officer or a majority or dominant minority of the board of directors (or similar body);
- Direction, determination, or decision of, or substantial influence over, important matters affecting the reporting company (*e.g.*, the selection of business lines or ventures, major expenditures or investments, fulfillment of substantial contracts, amendments to material governance documents, and others); or
- Any other form of substantial control over the reporting company.

In addition, in contrast to the CDD Rule, which requires legal entity customers to identify only a single individual under the “control prong” of the definition of beneficial owner, the Proposed Rule would require reporting of BOI for each individual deemed to exercise substantial control over a reporting company.

The Proposed Rule’s definition of “ownership interest” is broader than the CDD Rule’s “ownership prong,” as it is defined to include not only purely equity interests but also categories such as capital or profit interests (including partnership interests), convertible interests, options, and debt instruments in certain cases. While acknowledging that

<sup>2</sup> Under the Proposed Rule, “pooled investment vehicle” means (1) any investment company, as defined in section 3(a) of the Investment Company Act of 1940 (15 U.S.C. 80a-3(a)); or (2) any company that: (A) would be an investment company under that section but for the exclusion provided from that definition by paragraph (1) or (7) of section 3(c) of that Act (15 U.S.C. 80a-3(c)); and (B) is identified by its legal name by the applicable investment adviser in its Form ADV (or successor form) filed with the Securities and Exchange Commission.

application of this broader ownership interest standard could create additional burden for smaller reporting companies with complex ownership structures, FinCEN reasons that such “burden is justified because these are the entities most at risk for abuse of the corporate form.”

### *Company Applicants*

The term “company applicant” means:

- Domestic reporting company: any individual who files the document that creates a domestic reporting company; and
- Foreign reporting company: any individual who files the document that first registers a foreign reporting company.

The above definitions also encompass any individual who directs or controls the filing of a creation or registration document by another person. FinCEN clarifies that this requirement is in place because “in many cases, the company applicant may be an employee of a business formation service or law firm” and FinCEN does not wish for “the individual directing or controlling the formation of a legal entity [to] remain anonymous simply by directing another individual to file the requisite paperwork.” As such, where a company uses a service provider to file the relevant documentation, both the filer *and* the person who directed or controlled the filing must provide BOI.

## Information to be Reported

### *Reporting Companies*

Initial reports to FinCEN must include the following information concerning the reporting company:

- Full name, and any trade name or “doing business as” names;
- Business street address;
- Jurisdiction of formation (for domestic reporting companies) or initial registration (for foreign reporting companies); and
- Taxpayer Identification Number (TIN), or if a TIN has not yet been issued, a Dun & Bradstreet Data Universal Numbering System (DUNS) Number or Legal Entity Identifier (LEI).

### *Beneficial Owners and Company Applicants*

The following information must be reported for each beneficial owner and company applicant:

- Full legal name;
- Date of birth;
- Current residential address for tax residency purposes (except in the case of company applicants who file such applicants as part of a business, for which a business address is required);
- Unique identifying number from a non-expired U.S. passport, state identification document, or state driver’s license (or a foreign passport, if the individual does not possess any of the foregoing); and
- Image of the document showing the unique identifying number and recognizable photo (which FinCEN reasons will help deter fraud and misreporting).

In addition to the above information, reporting companies have the option of submitting TINs of beneficial owners and company applicants with the individuals' advance consent.

### *Unique FinCEN Identifier*

Under the Proposed Rule, reporting companies and individuals may apply to FinCEN for issuance of a “FinCEN identifier” that, upon issuance, may be submitted to FinCEN in lieu of the above-described information. Individuals and entities that obtain FinCEN identifier numbers would be required to update and correct information submitted to FinCEN in the same manner as reporting companies that submit normal-course BOI reports to the bureau.

### **Timing for Reports and Reporting of Updated/Corrected Information**

For any reporting company that has been formed or registered before the effective date of the reporting regulations, FinCEN proposes to require submission of an initial report, along with beneficial owner and company applicant information, not later than one year following the effective date of the Proposed Rule. Meanwhile, for both (1) domestic reporting companies that are formed on or after the effective date; and (2) foreign reporting companies that become foreign reporting companies (*i.e.*, by registering to do business in a State or tribal jurisdiction), submission of an initial report (along with beneficial owner and company applicant information) within 14 days of the initial incorporation or registration filing. Finally, if an exempt entity ceases to become exempt, a report would need to be filed within 30 days after the exemption criteria no longer applied.

In addition to requiring the submission of BOI, the CTA also requires reporting companies to update information in a timely manner (and to correct any inaccurate information filed with FinCEN). The Proposed Rule would give reporting companies (1) 30 days to file updates to previously filed reports (including, *inter alia*, changes to BOI and changes to exempt status); and (2) 14 days to correct inaccurate reports, if any of the information previously filed was incorrect in any respect.

### **Violations**

The CTA provides that any willful violation of BOI reporting requirements can lead to civil or criminal penalties, including (1) civil penalties of up to \$500 per day a violation has not been remedied; and (2) criminal penalties of up to \$10,000 and/or imprisonment of up to two years. The Proposed Rule adopts this penalty framework from the CTA, clarifying that liability can be for direct or indirect violations, and for acts (*i.e.*, reporting of inaccurate information) or omissions (*i.e.*, failure to provide or update any required information).

### **Effective Date**

FinCEN does not in the Proposed Rule identify a proposed effective date, but does indicate that “FinCEN is committed to identifying the soonest possible effective date after publication of the final rule,” as FinCEN stresses “that the collection of beneficial ownership information is critical to protecting U.S. national security and other interests and will advance efforts to counter money laundering, terrorist financing, and other illicit activity.”

FinCEN notes that the agency will be required to undertake various steps—including the development of its Beneficial Ownership Secure System, or BOSS, for storing and processing of BOI reported pursuant to the final regulations—before the effective date, and that FinCEN will “move expeditiously to the execution phase of the project[.]”

For now, FinCEN has provided sixty days—or until February 7, 2022—to provide comments. After FinCEN receives comments, the agency has committed to finalizing the Proposed Rule as expeditiously as possible. When the Proposed Rule is finalized, FinCEN will also provide guidance as to the effective date.

## Conclusion

The Proposed Rule reflects another step in FinCEN's efforts to modernize and strengthen the U.S. anti-money laundering regime. While the Proposed Rule may develop and change as FinCEN receives comments and assesses the best way to implement its mandate under the CTA, it is likely that the framework set forth in the Proposed Rule will be adopted in largely the form previewed by FinCEN. Assuming that occurs, the Proposed Rule would meaningfully increase the amount of BOI that companies and other entities would be required to report, and domestic and foreign companies alike would be well-served to track the Proposed Rule and ensure they are aware of and prepared to comply with the new reporting requirements.