Insights: Alerts

National Defense Authorization Act for Fiscal Year 2021 - New Beneficial Ownership Reporting Requirements

JANUARY 20, 2021

On January 1, 2021, the National Defense Authorization Act for Fiscal Year 2021 (the "Defense Act") was enacted. The Defense Act includes the Anti-Money Laundering Act of 2020 and the Corporate Transparency Act ("CTA"). The CTA requires "Reporting Companies" to disclose their beneficial ownership information to the Financial Crimes Enforcement Network ("FinCEN") and authorizes FinCEN to share such information with domestic and foreign law enforcement authorities, with the intent of reducing the money laundering activities of "shell" entities in the United States.

The CTA's requirements, a summary of which follows, are of particular interest to the real estate industry given the near universal use of single purpose entities in the ownership of commercial real estate.

I. Definition of "Reporting Companies", "Beneficial Ownership", and Compliance

The CTA broadly defines "reporting companies" as corporations, limited liability companies, other similar entities, and entities that are formed by or registered to do business under the laws of a state or commonwealth of the United States or an Indian Tribe, as well as foreign companies that are registered to do business in the United States.[i]

The CTA specifically excludes twenty-three types of entities, including entities already subject to other anti-money laundering requirements or that must report to other regulatory bodies (for example, credit unions, banks, bank holding companies, broker-dealers, exchanges and clearing agencies), and entities that are identified as low risk as determined by the Departments of the Treasury and Justice as well as Homeland Security. Also excluded are entities owned or controlled directly or indirectly by other exempt entities.

The CTA defines a beneficial owner as an individual who directly or indirectly, through any contract, arrangement, understanding, relationship or otherwise: (a) exercises substantial control over the Reporting Company (the CTA does not define "substantial control"); or (b) owns or controls not less than twenty-five percent of the Reporting Company. A beneficial owner does not include: (a) a minor child (the information of the parent or guardian must be reported instead); (b) an individual acting as a nominee, intermediary, custodian or agent on behalf of another individual; (c) an individual acting solely as an employee of a Reporting Company; (d) an individual whose only interest in the Reporting Company is through inheritance; or (e) a creditor of a Reporting Company.

"Reporting companies" are required to identify to FinCEN each of their beneficial owners by disclosing the beneficial owner's: (a) full legal name; (b) date of birth; (c) current residential or business address; and (d) unique identifying number from an acceptable identification document (such as a driver's license or passport number) or FinCEN identifier. Additionally, upon a change in beneficial ownership (including name and address changes of the originally

identified beneficial owners), a Reporting Company must update the information provided to FinCEN within one year of such change. It is not clear if a change to the percentage of beneficial ownership, rather than a transfer to a new beneficial owner, must also be reported.

II. Disclosure by FinCEN

The information disclosed to the FinCEN will be held for a period ending five years after the Reporting Company is terminated, will not be made publicly available, and may only be used for: (a) national security, intelligence and law enforcement activities, or (b) confirming beneficial information provided to financial institutions.

The FinCEN may, upon request, disclose such information provided to (a) a local, tribal, State (subject to court approval), or Federal law enforcement agency for use in furtherance of the such national security, law enforcement or intelligence purposes; (b) a foreign law enforcement agency provided the information is requested through an agency of the Federal government, or (c) subject the consent of the Reporting Company, a financial institution for customer due diligence purposes.

FinCEN is required to provide any person that submits an ownership statement with a FinCEN identification number upon request from such person. The CTA does not make clear that issuance of a FinCEN identification number is proof of compliance with the CTA and there is no separate requirement that FinCEN provide a certification that a Reporting Company has complied with the requirements of the CTA. The CTA prohibits the issuance of a certificate evidencing ownership interest in a Reporting Company. In addition, any party that unlawfully discloses any beneficial information shall be liable for fines of up to $500 per day and up to $250,000 in the aggregate, and up to ten years in prison.

III. Penalties for Non-Compliance/Safe Harbor

Any person or entity that files an application for the formation of a Reporting Company that intentionally fails to comply with the CTA will be liable for fines of no more than $500 for each day that there is a willful failure to report complete beneficial ownership information, and such parties may be subject to aggregate fines of up to $10,000 or a prison term of up to two years. Significantly, attorneys helping with corporate-registration paperwork on behalf of a client may be included as parties subject to penalty. Merely negligent non-intentional violations are not subject to penalty. In addition, the CTA does not provide that the acts of a non-complying company are void solely because of non-compliance with the CTA. As such, non-compliance with reporting requirements should not result in the dissolution of the entity or prevent it from otherwise conducting business in the normal course.

The CTA provides safe harbor rules for any person that submits inaccurate beneficial ownership information provided that such person (a) had no knowledge of the inaccuracy, (b) was not trying to evade the reporting requirement, and (c) corrects the information no later than 90 days after the initial report was submitted.

IV. Effective Date

The CTA will become effective on the date that the regulations of the CTA are prescribed and issued by the US Secretary of the Treasury, which shall be no later than one year after the enactment of the CTA.

Footnotes

[i] The CTA does not define or otherwise clarify as to what is intended by "other similar entities" but likely includes partnerships and trusts that are formed or registered within the United States.