

# The NAPPA Report

April 2021  
Volume 35, Number 1



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## Must Corporations Whose Shares are Owned by Government Retirement Systems Report Such Ownership Under the New Corporate Transparency Act?

By: *Marc Lieberman and Lisa Sarver*

Congress recently passed the Corporate Transparency Act (“Act”) which, with a few exceptions, requires corporations and limited liability companies (and similar entities) to disclose certain information about their beneficial owners.<sup>1</sup> The Act is aimed at cracking down on bad actors who use anonymous shell companies to launder money or commit other bad acts. The Act combats these illicit actions by requiring corporations and limited liability companies to disclose their true beneficial owners.

The Act is an effort by the United States to match international disclosure standards. For example, the European Union’s 27 country members are required to have corporate registries that contain beneficial owner information.<sup>2</sup> In the United States, more than two million corporations and limited liability companies are formed annually.<sup>3</sup> A person forming a company is often required to provide less information than what is required to obtain a bank account or driver’s license.<sup>4</sup> As a result, criminals have exploited State formation laws and concealed their true identities from law enforcement. The Act is designed to redress these concealment efforts. It is the first major reform of America’s money laundering laws in over a decade.<sup>5</sup>



*The Act is aimed at cracking down on bad actors who use anonymous shell companies to launder money or commit other bad acts.*

### What the Act Requires:

The Act requires companies to disclose four data points:

1. The name of each beneficial owner of the company;
2. The birthdate of each beneficial owner of the company;
3. The current residential or business street address of each beneficial owner of the company; *and*
4. The driver’s license or passport of each beneficial owner of the company.<sup>6</sup>

Remarkably, the Act does not require any beneficial owner to disclose financial information.

### Who is a Beneficial Owner?

The Act defines a “beneficial owner” subject to the disclosure provisions of the Act as a *natural person* who directly or indirectly through any contract or understanding exercises “substantial

control” over the company or owns or controls not less than 25% of the ownership interests of the company.<sup>7</sup> The term “beneficial owner” does not include minor children (as defined by the State where the company is formed), persons acting as nominees, intermediaries, custodians, or agents, employees, persons whose only interest is through inheritance, or creditors.<sup>8</sup>

Unfortunately, the Act does not define what constitutes “substantial control” over the company. It is anticipated that the Secretary of the Treasury will issue clarifying regulations and guidance regarding this key term and others used in the Act.

### What Types of Companies Must Report?

The Act applies to entities formed under the laws of any State or Indian Tribe or under the laws of a foreign country and are registered to do business in any State or before an Indian Tribe (each defined as a “Reporting Company”).<sup>9</sup> The Act defines “Reporting Company” broadly to include entities “similar to” corporations and limited liability companies,<sup>10</sup> but absent clarifying guidance from the Treasury Department, the exact meaning of “similar to” remains unclear.

### To Whom are Reports Made?

All disclosures required by the Act are to be filed with the Secretary of State where each company is formed or registered to do business and will then be transmitted by the Secretary of State to the Financial Crimes Enforcement Network (FinCEN).<sup>11</sup>

### What are the Penalties for Non-Compliance?

Penalties for individuals or companies who violate the Act’s requirements are severe. For example, the provision of false information or failure to provide complete or updated information can result in a civil penalty of up to \$500/day for each day the violation continues and a fine of up to \$10,000 plus a prison term of up to two years.<sup>12</sup> However, the Act also contains a safe harbor provision whereby a person who submits inaccurate information can amend the inaccuracy within 90 days of the filing.<sup>13</sup>

## Must Corporations Whose Shares are Owned by Government Retirement Systems Report Such Ownership Under the New Corporate Transparency Act? *(continued)*

### The Exemptions:

Most government retirement systems own interests in both publicly traded and privately traded corporations and limited liability companies. The question then becomes whether the companies whose shares are owned by such systems must report the systems' beneficial ownership under the Act. In our view, such disclosure is *not* required for at least two reasons.

The Act expressly excludes certain types of companies from the definition of Reporting Company. There are 24 separate exemptions,<sup>14</sup> but the most pertinent to government retirement systems and the entities they own is the exemption for an entity that is “established under the laws of the United States, a State, a political subdivision of a State or an Indian Tribe” which “exercises governmental authority on behalf of the United States or any such State, political subdivision or Indian Tribe.”<sup>15</sup> It is likely that government retirement systems will be deemed to exercise governmental authority on behalf of their respective States and/or political subdivisions or Indian Tribes and, therefore, be subject to this exemption. There is another exemption for an entity owned or controlled, directly or indirectly, by an entity subject to the exemption referenced above (amongst other exemptions), which would then apply to the entities owned by the governmental retirement system.

To confirm this, we *urge* plans to form a task force dedicated to lobbying Treasury to clearly specify in the Act's implementing regulations that companies are not required to report the interests of government retirement systems under the Act. The Act requires Treasury to promulgate regulations no later than one year after enactment of the Act,<sup>16</sup> so no time should be wasted in forming a task force to address the exemption issue.

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### ENDNOTES:

<sup>1</sup>See *The William M. (Mac) Thornberry National Defense Authorization Act ("NDAA") for Fiscal Year 2021*, H.R.6395 (Enrolled Bill), 116th Congress (2020) Sec. 6401-6403.

<sup>2</sup>See H.R. 2513, 116th Congress (2019) Sec. 2 (8).

<sup>3</sup>NDAA Sec. 6402, p. 1217.

<sup>4</sup>H.R. 2513, Sec. 2 (3).

<sup>5</sup>Marc-Alain Galezzi, *et al.*, *The Anti-Money Laundering Act of 2020*, JDSUPRA (January 13, 2021), <https://www.jdsupra.com/legalnews/the-anti-money-laundering-act-of-2020-4339719/> (The Corporate Transparency Act is “the first major reform

of the 50-year-old United States anti-money laundering (AML) framework since the 2001 USA PATRIOT Act was enacted after 9/11”).

<sup>6</sup>NDAA, Section 6403, p. 1218.

<sup>7</sup>*Id.* at Section 6403 § 5336(a)(3)(A), p. 1219.

<sup>8</sup>*Id.* at Section 6403 § 5336(a)(3)(B), p. 1219.

<sup>9</sup>*Id.* at Section 6403 § 5336(a)(11)(A), p. 1220.

<sup>10</sup>*Id.*

<sup>11</sup>See *id.* at Section 6403 § 5336(b).

<sup>12</sup>*Id.* at Section 6403 § 5336(h)(3)(A), p. 1234.

<sup>13</sup>*Id.* at Section 6403 § 5336(h)(3)(C), p. 1234-35.

<sup>14</sup>See *id.* at Section 6403 § 5336(a)(11)(B), p. 1220-23.

<sup>15</sup>*Id.* at Section 6403 § 5336(a)(11)(B)(ii), p. 1220. Also exempt from reporting obligations are companies whose shares are listed for sale on or required to file reports to a domestic securities exchange. Section 6403 § 5336(a)(11)(B)(i), p. 1220.

<sup>16</sup>*Id.* at Section 6403 § 5336(b)(5), p. 1227.

