

How a new federal law will affect more than 30 million small US businesses

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On Jan. 1, 2024, The Corporate Transparency Act comes into effect, requiring more than 30 million small and medium-sized businesses to report ownership information to the federal government. (iStockphoto via Getty Images)

By [Teresa J Rhyne](#) | Teresa@trlawgroup.net | TR Law Group

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On Jan. 1, 2024, a new federal law comes into effect, requiring more than 30 million small and medium-sized businesses to report ownership information to the federal government.

The law is far-reaching and may affect you in unexpected ways. Failure to timely file the report could result in fines of \$500 per day, up to \$10,000 maximum, or two years' jail time. This is not something you can ignore if you own a business or maintain a business entity.

What is It?

The Corporate Transparency Act was passed in 2021 to eliminate anonymity in business ownership that previously allowed bad actors to hide illicit financial dealings and launder money, which they sometimes used in terrorist activities.

You might think that means the law doesn't apply to you, but you might be wrong. The CTA casts a very wide net.

The law directs the Financial Crimes Enforcement Network (a unit of the Department of Treasury, known as "FinCEN") to create a massive database of business "beneficial" ownership information for use by the government in identifying the individual owners of privately held assets.

FinCEN will be gathering that data from business owners and family companies, including that limited liability company you formed to hold your vacation home or rental property.

Who must report?

With 24 very narrow exceptions (which will be covered in a later article but are mostly financial institutions and industries already heavily regulated by the US government), the CTA reporting requirements apply to any business that is created by "filing a document" with a state or Indian tribe.

This includes LLCs, corporations (S and C), limited partnerships, other closely held businesses, and in some circumstances, trusts. The CTA refers to these as "reporting companies," and FinCEN estimates there will be more than 32 million of them required to act in 2024.

Your LLC that holds rental properties, your S corporation from which you operate your small business, the corporation owned and operated by generations of your family, the LLC you formed to sell T-shirts or eBay items, and your S corporation management entity that owns a C corporation operating entity that leases equipment from that LLC you own, all are likely "reporting companies."

Start gathering the data now.

What has to be reported?

Reporting Companies must report to FinCEN certain information — the kind we generally work hard to keep private — with respect to the "company applicant" and the "beneficial owners" of the company.

Although FinCEN has yet to release the specific forms, the reporting company must provide the following information for each "company applicant" and "beneficial owner" and must keep the information current: full legal name; date of birth; a copy of a valid photo ID (driver's license, state ID, or passport) that has the same name and date of birth); residential address (no PO boxes, no business address, no using your lawyer or accountant's office address).

Reporting companies will have to collect this information from each “beneficial owner” — a term not as straightforward as it sounds — and then file the required report with FinCEN.

Reporting companies formed on or after Jan. 1, 2024, will need to report “company applicants,” as well.

Also, anytime there is a change in the beneficial ownership or in the information provided by the company applicant or beneficial owners (e.g., someone moves or renews their driver’s license), the reporting company has 30 days to file an updated report.

After the initial filing, the filing requirements are event-driven, rather than on a specific timeline, which effectively puts the burden on the reporting companies to regularly check with their beneficial owners as to when an update is needed.

Who is a company applicant

A “company applicant” is the person who files the application to form an entity.

In my office, that would be me, my associate attorney and/or my paralegal. Each reporting company for whom we file entity formation documents after this year will be required to include our information in their report. (No, we’re not happy about this, either.)

Who is a “beneficial owner”?

The term “beneficial owner” is more complicated.

In general, a beneficial owner is someone who owns or controls, directly or indirectly, 25% or more of the entity’s ownership interest, or exercises “substantial control” over the entity. What constitutes “substantial control” is the kind of thing litigators love to argue about.

And here, the proposed regulations included a lengthy list of non-exclusive examples and then chased its tail by saying “and any other forms of substantial control over the reporting company.” See your lawyer. And good luck, folks.

When must the report be filed?

Reporting companies formed before Jan. 1, 2024, will have until Jan.1, 2025, to file the required report.

Reporting companies formed on or after Jan. 1, 2024, will have 90 days from the date of formation to file the report. This means newly formed entities will be the test subjects for this new, far-reaching, untested, privacy-invading law. If you are planning to create a new business entity, consider forming it in 2023.

What now?

The next few articles in our columns will continue to cover the CTA, what companies are exempt from reporting, the FinCEN ID number that can be used by company applicants and beneficial owners in lieu of providing personal information to every company with which they are affiliated, discussing the term “beneficial owners,” and updates as to when the form for filing the report is available and who can file it. (Still unknown is whether your lawyer, once retained, can do it for you.)

In the meantime, if you own a business entity, whether the business is active or not, whether it’s in California or elsewhere in the U.S., and whether you’re a small, medium or large business, be proactive.

See your attorney about what your CTA reporting requirements are, if any. This is a new law — preparation of the filing is not likely covered by any retainer agreement you have with your attorney, and it would be impossible for attorneys to reach out to every business entity they’ve formed or worked with over the years.

Your CPA is likely not going to be handling CTA matters. The AICPA advised its members that handling CTA matters is likely the unauthorized practice of law and may not be covered by their professional liability insurance.

New year, new law, new headaches. Here we go again, folks.

Teresa J. Rhyne is an attorney practicing in estate planning and trust administration in Riverside and Paso Robles, CA. She is also the #1 New York Times bestselling author of “The Dog Lived (and So Will I)” and “Poppy in The Wild.” You can reach her at Teresa@trlawgroup.net