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We Have to Tell Them What?: The New Corporate Transparency Act and Forming Business Entities in Massachusetts

James J. Wheaton
William & Mary Law School, jjwheaton@wm.edu

Gustavo De la Cruz Reynozo

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By James J. Wheaton and Gustavo De la Cruz Reynozo

The details and requirements of business entity formation have traditionally been the sole province of state law. Most states, like Massachusetts, maintain corporate annual report filing requirements that involve the public disclosure of corporate officers and directors, and some impose similar requirements for LLCs or other business entities. Those requirements focus on active managers of the entities, not information about the beneficial ownership of entities formed under their laws. However, the recently-enacted federal **Corporate Transparency Act (CTA)** will fundamentally change entity disclosure.[1]

By January 1, 2022, the Treasury Department will be promulgating regulations that will require every state filing creating a new business entity to be accompanied by a simultaneous transmission into a new federal database of the full name, street address, and an identification number of certain beneficial owners and of the "applicant" who forms the entity, who may be the attorney who handles the filing. Existing entities will have longer to comply, but will eventually be subject to similar disclosure.

I. Scope of the CTA

A. What Disclosure Does the CTA Require?

For each "beneficial owner" and "applicant" of a "reporting company," a filing must be made to Treasury's Financial Crimes Enforcement Network ("FinCEN") that includes:

- Each person's full legal name, date of birth, and current residential or street address; and
- Either (a) the identifying number from an acceptable identification document (i.e., valid passport, driver's license, or state, local or tribal identification document), or (b) a FinCEN identifier assigned to the person via a request from the person to FinCEN.

The CTA requires additional filings within one year of any change in the information included in the initial filing. This updating obligation applies not only to the identity of the beneficial owners, but also to changes in their address and even new numbers assigned to their licenses, ID cards, or passports upon renewal.

B. Who Will Have Access to the FinCEN Database?

The CTA limits access to the personal information in the database to:

- Any federal agency engaged in national security, intelligence, or law enforcement activity.
- State, local, and tribal law enforcement agencies if a court has authorized seeking the information in a criminal or civil investigation.
- Federal regulatory agencies for the purposes of their supervision.
- Foreign law enforcement agencies, prosecutors, or judges, upon a request by a federal agency on their behalf.
- A financial institution that has been authorized to make the request by the reporting company, for customer due diligence purposes.

The blanket "law enforcement category" includes immigration enforcement. This concern may be particularly relevant given the number of students, particularly in the Boston area, who engage in startup activity while studying in the United States. The disclosure to FinCEN that a student whose visa terms do not permit work[2] is a significant beneficial owner of an entity may create a presumption that customs and immigration officials could use to exclude a student from returning after travel outside the U.S. or to revoke the visa and expel the student from the country.

C. What Companies Are Covered by the CTA?

The CTA requires filings from all non-exempt corporations and LLCs, and any other "similar entity" that is either: (i) created by filing a document with a state or tribal filing agency, or (ii) formed in another country but registers to do business by filing a document with a state or tribe. The phrase "created by the filing of a document" means that an entity that exists irrespective of the making of a state filing should not be a CTA "reporting company." This means that several entity types may be CTA-exempt:

General Partnerships and LLPs. General partnerships are outside the CTA because they exist irrespective of a filing. Because an LLP is a general partnership that exists as an entity before it registers as an LLP,[3] an LLP should also be deemed outside the coverage of the CTA.[4]

Massachusetts Business Trusts. These trusts should be outside the CTA, while Delaware statutory trusts are likely to be deemed covered by the CTA. Massachusetts has long considered the state and local filings to be made by business trusts as administrative requirements, and not conditions of creation or existence.[5] By comparison, the filing itself creates a Delaware business trust.[6]

Entities Resulting from by Statutory Conversion. Most states have inter-entity conversion statutes that allow an entity to convert from one legal form to another. Such provisions typically make clear that the post-conversion entity is the same entity that existed before the conversion, just in a different legal form. *Entities Formed in Foreign Jurisdictions but Qualified or Registered to Do Business.* Foreign entities that register to do business in a state are required to make CTA filings. However, foreign entities that neglect or ignore state registration or qualification requirements are not included within the CTA, creating a gap in coverage.

The CTA also contains a lengthy list of businesses exempt from its coverage, but only a few of these exemptions are likely to arise in typical legal practices:

- Public companies with securities registered under the Securities Act of 1934,
- Nonprofits and other organizations under IRC § 501(c),
- Certain regulated businesses,
- Accounting firms,
- Certain dormant companies, and
- Any company employing more than 20 employees in the US on a full-time basis, which filed a prior year federal tax return showing more than $5 million in gross receipts or sales, and which operates at a physical location in the U.S.

The last exemption is interesting for several reasons. First, a new entity could never use the exemption, because it will become available only in the year after a year in which the requisite revenue or sales were shown in a tax return. Second, the statute does not define what constitutes a physical office. Third, until better defined by Treasury, the 20-employee requirement remains unclear. What will constitute a full-time basis? Can multiple part-time employees comprise an FTE? Will members of an LLC, who for tax purposes are not considered "employees," be included in the count? Can persons treated as "independent contractors" be counted? When in the year will the number of employees be measured? Although the **Advanced Notice of Proposed Rulemaking issued by FinCEN in April 2021** did not address these issues, one would expect them to be clarified by the forthcoming regulations themselves.

D. Who is a "Beneficial Owner"?

The CTA's definition of a "beneficial owner" is simple but also inadequate. An entity's beneficial owners include every individual who "owns or controls" at least 25 percent of the entity's ownership interests, or who exercises "substantial control" over the entity.

The CTA neither defines what constitutes "owning or controlling" ownership interests[7] nor distinguishes among types of ownership interests with differing control and economic attributes. For

some purposes under the securities laws, beneficial ownership has been defined as voting power,[8] and a similar test based on aggregate affirmative voting rights would make sense for the CTA.

Will "substantial control" be defined by reference to the ability to cause the entity to take action, or will veto or blocking rights also be deemed to furnish control? Will persons serving as officers, directors and managers be "beneficial owners" because they "control" even if they own no equity? Massachusetts attorneys representing clients that are the beneficiaries of these kinds of "control" mechanisms must tread carefully to ensure that their clients do not unintentionally become beneficial owners.

E. Who is an "Applicant"?

Except in the provision that defines the term, the word "applicant" only appears twice more in the CTA, most importantly in the provision that specifies that the same information that must be filed about beneficial owners must also be filed about the applicant. There is no updating requirement for that information, and indeed, the personal information about the applicant is not even subject to the disclosure limitations and penalties of the CTA.

Will attorneys representing clients forming entities be considered applicants whose personal information must be submitted to FinCEN? The answer may depend on what it means to be an individual who "files an application to form a corporation, LLC, or other similar entity." An attorney (or law firm staff member) who physically or electronically tenders the document for filing would also seem to be one who has "filed an application," even if that filing is on behalf of another.

Removing the attorney from the direct action of filing, as by engaging a service company on the client's behalf to handle the filing, or by delegating electronic filing responsibilities to the client, should suffice to prevent the attorney from being considered someone who "filed."

F. Who is Responsible for Making CTA Filings?

The initial filing obligation for post-effective date formations is imposed on the company itself, and although the filed information must include personal information about the applicant (who, as observed above, might be the entity's attorney), the statute itself does not require the applicant to make the filing. For preexisting entities, and changes in beneficial ownership, the reporting company also has the filing obligation.

Failure to comply with the CTA's reporting requirements may lead to both civil and criminal liability. A "willful" failure to report complete or updated beneficial ownership information in a timely way, or a willful provision or attempt to provide false information, may result in a civil penalty of $500 per day of violation, as well as a criminal fine of $10,000 and imprisonment for up to two years.

II. Practice Implications

A. Should Attorneys Permit Themselves to Be "Applicants"?

Treasury regulations may better define "applicant" to clarify whether it includes anyone other than the person who actually signs the filing or delivers the filing to the state filing officer. Any effort by Treasury to impose "applicant" status on attorneys will surely face a legal challenge. Given the risk of liability and other penalties associated with CTA filings, and the ease of offloading the filing responsibility to others, attorneys should consider alternatives to what may have been their prior business entity formation practices.

Currently, the most common practice for attorneys is for the attorney (or a non-attorney colleague) to sign an initial corporate or LLC filing as the incorporator, organizer or authorized person.[9] For a Massachusetts entity, this process may happen entirely online, without direct client involvement. For non-Massachusetts entities, even where formation is handled by the Massachusetts attorney or firm, the need

for a registered agent in the other jurisdiction has necessitated the use of corporate service companies, some of which have national practices and others of which are based in and primarily serve Delaware.

The advent of the CTA may change these filing practices in at least two ways. First, attorneys will be much less sanguine about simply signing the initial filing document, and may request that a client representative do so instead. First, for Massachusetts companies, having a client representative (a) sign the formation document, if the representative is willing to be in the public record, and (b) handle the filing on the Secretary of the Commonwealth's website with step-by-step instructions from counsel, may eliminate the risk that the attorney is deemed a CTA applicant. For the client, any concern about public disclosure has less relevance for Massachusetts LLCs and corporations. The LLC's filing must already name the managers or an authorized member, one of whom could be the signatory. Massachusetts corporations must file an annual report providing the names and addresses of directors and officers, and so while disclosure does not occur at filing, it does happen within the ensuing year.

Second, for companies formed in Delaware and other jurisdictions, corporate service companies may step in to either fill two roles in the filing process: (1) replacing the attorney (or her employee) as the person who effects the filing, or (2) also signing the filing document itself as incorporator, organizer or authorized person. This may result in more substantial service fees and obligations on the client's part to execute documents to protect the service company and its employee handling the filing from the CTA risks associated with incomplete or false information.

B. Due Diligence and Legal Opinion Questions

The mechanics of the FinCEN beneficial owner database will become known once the Treasury regulations are finalized and the reporting scheme launches, but the non-public nature of the filings means that it will not be possible for the public to use the database to confirm the CTA compliance status of a particular entity. For this reason, in transactions involving covered entities, it may fall to the legal profession to conduct due diligence regarding CTA compliance, to maintain records of prior filings made as "applicants" or otherwise on behalf of clients, and to advise clients making their own initial or ongoing ownership change filings to maintain sufficient records to evidence up-to-date compliance.

Transactions involving representations by covered business entities will likely include new representations, covenants and closing conditions related to the CTA compliance status of those companies. Lawyers on both sides of transactions should be expected to include proof of compliance in due diligence checklists and pre-transaction "cleanup" projects.

Whether CTA compliance status should also be a subject of closing legal opinions is a subject for future consideration by both practitioners and the bar-related organizations that attempt to set the standard for legal opinion practice. Arguably, CTA compliance will be as relevant in a closing opinion as presently expected or demanded opinions regarding existence, good standing, or even foreign qualification, subjects that are addressed in the most commonly referenced opinion forms.

Opinion-issuers may ultimately resist CTA-related opinions, but as practice evolves, attorneys should anticipate that they may be asked to serve another gatekeeper role. Even if they avoid serving as "applicants," counsel may be asked to opine, even if qualified by client fact certificates or knowledge, as to the existence and accuracy of required CTA filings.

C. Amending and Adapting Document Forms

Once an entity is formed, whose duty will it be to maintain the ongoing accuracy of the company's FinCEN information? For entities existing before the Treasury regulations become effective, who will have the duty to make the initial filing? What responsibility will a person nominally charged with making the filings have if through omissions or misinformation, the CTA requirements are not met, or the filings contain inaccurate information? The forthcoming regulations may address some of these concerns, but interpretive gaps will likely remain.

Each of these questions leads to the conclusion that the responsibility for filing, and for accuracy, will need to be allocated among an entity's beneficial owners and those (if not the owners themselves) making the filings. An officer, manager or general partner charged with transmitting a filing to FinCEN should likely indemnify the entity against a false filing, and in turn be indemnified against the consequences of false information provided by others. The governing documents of the company should establish responsibility for making CTA filings, and obligate beneficial owners to provide the necessary information on a timely basis.

This likely need for changes to a substantial library of business entity forms also raises the issue of how best to handle entities formed before the effective date of the CTA regulations. All attorneys who have been involved previously in forming entities for their clients will need to consider not only how to communicate and assist current clients, but also whether and how to reach out to former clients, who may have received business-entity services as one-off or since-ended engagements.**[10]** In-house counsel will need to take on, or delegate to in-house or outside counsel colleagues, responsibility for CTA filings for each entity, however insignificant, that appears in the corporate family tree.

Conclusion

The adoption of final Treasury regulations may clarify some ambiguities, and may even close potential loopholes that would otherwise allow some business entities to evade the CTA's dragnet. Those changes, however, will not allow Massachusetts practitioners to avoid the substantial professional responsibility, structuring and practical issues created by this new law, which will change the way we have approached business entity formation for many decades.

APPENDIX

Existing Massachusetts Filing Requirements**[11]**

Entity Type	*Formed by Filing?*	*Filing Information Required*	*Annual Report Information Required*
Corporations	Yes. Ch. 156D, § 2.01.	Name and address of each incorporator (only one required). Ch. 156D, § 2.02(a)(3).	Names and business addresses of every director as well as of the president, treasurer and secretary, and of any CEO and CFO, if different. Ch. 156D, § 16.22(a)(4).
LLCs	Yes. Ch. 156C, § 12(b).	Name and address of every manager if LLC has managers when formed, plus name and address of any other person authorized to execute and file documents with the Secretary of the	Same information is required in an annual report, which effectively imposes an annual updating requirement. Ch. 156C, §§ 12(c).

		Commonwealth (including the person signing the filing if there are no managers). Ch. 156C, §§ 12(a)(5), 12(a)(6).	
LPs	Yes. Ch. 109, § 8(b).	Name and business address of every general partner. Ch. 109, § 8(a)(4).	Updated general partner information must be contained in an annual report that became a required filing in 2008. Ch. 109, § 63.
LLPs	No. An LLP is a general partnership that has opted into limited liability partnership status, and so the filing of the documents needed to make the partnership an LLP do not actually constitute a filing that creates the entity.	For an LLP that is not a professional LLP, the registration filing need not include any general partner information other than the name of the general partner signing the registration form. Ch. 108A, § 45(2).	Annual report requirement requires no partner identifying information. Ch. 108A, § 45(2).
Professional LLPs	No. Same as LLP.	Must list the name and business address of every general partner rendering the professional service in Massachusetts in the LLP registration filing. Ch. 108A, § 45(7).	Same information is required in an annual report, which effectively imposes an annual updating requirement. Ch. 108A, § 45(7).
Business Trusts	No. Required filings are not linked to the trust's creation or continued	Must file a copy of its instrument or declaration of trust with the clerk of every city and town where it has a usual	No annual report requirement.

	existence; rather, the Massachusetts trust statute simply recognizes the existence of the trust and imposes administrative requirements, such as the filing requirement.[12]	place of business, and with the Secretary of the Commonwealth. Ch. 182, § 2. Presumably, that document will, at minimum, name the trustees.	

[1] Pub. L. 116-283 (Jan. 1, 2021) tit. LXIV, now codified primarily at **31 U.S.C. § 5336**.
[2] See **https://www.uscis.gov/working-in-the-united-states/students-and-exchange-visitors/students-and-employment** (last accessed Sept. 19, 2021).
[3] See Appendix.
[4] See Del. Code tit. 6, § 15-201(b); Mass. Gen. L. c. 108A, §45.
[5] See Appendix.
[6] Del. Code tit. 12, § 3810(a)(2).
[7] Ownership or control cannot be through bearer interests, which are prohibited by the CTA. *See* § 5336(f).
[8] Exchange Act Rule 13d-3, 17 C.F.R. § 240.13d-3.
[9] By definition, unless a general partner, the attorney could not sign limited partnership certificates of LLP registration forms, and unless a trustee, could not be the signer of a trust instrument.
[10] The CTA ties some state and tribal funding to periodic notifications by filing agencies of reporting company requirements under the CTA. *See* § 5336(e)(2)(A).
[11] All statutory references are to Massachusetts General Laws.
[12] *See* **Letter Ruling 91-2**, Mass. Dep't of Rev. (Jul. 1, 1991).

Professor James Wheaton is Clinical Associate Professor and Director of the Startup Law Clinic at Boston University School of Law, Research Director of the Uniform Laws Commission/ABA Joint Editorial Board for the Uniform Unincorporated Organizations Acts, and a former Chair of the ABA Section of Business Law LLCs, Partnerships and Unincorporated Entities Committee. The views expressed in this article are solely those of Professor Wheaton and Mr. Reynozo, and are not made on behalf of any of Boston University, the ABA, or the Uniform Laws Commission.

Gustavo De la Cruz Reynozo is a third-year law student at Boston University School of Law and a former staff editor of the Journal of Science and Technology Law.