The Corporate Transparency Act Compliance Deadline Looms—Lenders, Are Your Customers Ready? Are YOU Ready?

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The **January 1, 2025,** deadline imposed by the Corporate Transparency Act (CTA) for all "reporting companies" formed prior to 2024 to file their initial beneficial ownership reports with FinCEN is rapidly approaching. Given the potential civil and criminal penalties for violation of the CTA, it is essential that reporting companies make compliance a high priority and establish protocols for collecting and reporting the required information. Lenders and private equity sponsors should carefully evaluate their customers and portfolio investment structures to assess the potential impact of the CTA.

What is the CTA?

Enacted on January 1, 2001, the CTA went into full effect on January 1, 2024.The new law is a groundbreaking change in the way the federal government tracks those who have beneficial ownership of U.S. companies (and foreign companies registered to conduct business in the U.S.) or otherwise possess the ability to control them. The CTA requires business owners to file beneficial ownership information (BOI) reports, with the ultimate goal of assisting federal law enforcement agencies in combatting crimes such as financing terrorism, wire fraud, and money laundering.

The CTA places significant responsibilities on the business community for collecting and reporting beneficial ownership information to the Financial Crimes Enforcement Network (FinCEN), a federal agency under the U.S. Department of Treasury, with an imminent year-end deadline for pre-2024 reporting companies to file their initial BOI reports. Yet millions of companies *still* need to comply with the law's requirements, which include disclosing specified information about their beneficial owners, which can include those who own and/or have the right to acquire 25% or more of any class of the company's ownership interests (e.g., stock, membership interests, equity, etc.), as well as anyone who has substantial control over the business (whether or not they own any equity).

Key Takeaways:

- "Reporting companies" formed (or foreign reporting companies which first qualified to do business in any U.S. state) prior to January 1, 2024, have until January 1, 2025, to file their initial BOI reports, while businesses created or registered on or after January 1, 2025, must file reports within 30 days of creation or registration (or within 90 days if formed or registered during 2024).

- Failure to fully and timely comply with the CTA's requirements may result in significant civil and criminal penalties to the reporting company as well as its senior officers and directors.

- The CTA covers any domestic entity formed (or foreign entity registered to conduct business in any US jurisdiction) by a filing with a Secretary of State or similar office (e.g., corporations or LLCs), unless subject to a specific exemption under the CTA.

- Additional controls, procedures, and protocols should be developed and implemented by companies, lenders, and investors to account for obligations now imposed by the CTA and to require significant equity holders, senior officers, directors, and other persons with "significant control," to provide the companies with timely, correct, and complete information to enable them to fulfill their BOI reporting obligations.

Impact on Financial Sector:

Financial institutions are separately subject to information collection requirements in connection with federal "know your customer" (KYC) due diligence requirements. These requirements are primarily intended to ensure that financial institutions know their customers and are thereby better able to prevent their institutions from being used to facilitate illicit activities.

FinCEN has also given banks and other financial institutions guidance on the interplay between the CTA and existing due diligence requirements, noting in December 2023 that the CTA "does not create a new regulatory requirement" for banks or non-bank financial institutions to access BOI reported by their customers "or a supervisory expectation that they do so."

However, the financing community, including banks and private equity firms, still needs to be mindful about the law's requirements and recognize that a vast majority of their customers will be required to comply with the CTA. Educating customers and portfolio companies regarding the law's requirements and taking steps to encourage their compliance with the CTA now is advisable and is consistent with FinCEN's vision for the implementation of the law.

Recommended Considerations:

Reporting companies, financial institutions, and private equity firms need to be well versed in the new legal requirements imposed by the CTA which, notably, include an ongoing obligation for reporting companies to update their BOI reports within 30 days of any changes (as opposed to just a "one-and-done" reporting obligation).Financial institutions and private equity firms should consider taking proactive measures for CTA compliance, such as the following:

- **Review FinCEN Filings.** All BOI reports delivered by a reporting company to FinCEN, or at least the filing confirmations received from FinCEN upon the filing of such reports, should be obtained and reviewed by lenders and private equity sponsors as a standard component of due diligence in connection with any financing or acquisition process.

- **Obtain Consent Rights.** Consents granting a lender a broad right to obtain future BOI reports directly from the FinCEN database should be a standard expectation for reporting company borrowers.

- **Perform Due Diligence.** Increased due diligence by lenders and private equity firms considering an acquisition should include cross-checking governing documents, meeting minutes, and written consents delivered by borrowers or target companies, as applicable, against BOI reports and addressing any inconsistencies prior to closing the financing or transaction.

- **Assess Policies and Procedures.** A review of borrower or target company policies and procedures for addressing CTA compliance should be undertaken as part of standard due diligence.

- **Examine Template Documents.** Lenders should also examine their template loan documents and other customer-interfacing agreements to determine whether additional representations, warranties, and covenants should be included to address the CTA specifically (or money laundering generally).

- **Capture Defaults.** A failure by a reporting company to timely file CTA reports with FinCEN, or to provide false or inaccurate information to FinCEN, should be an event of default in credit agreements.

- **Confirm CTA Compliance.** All lenders will want to consider how to obtain confirmation of compliance from existing borrowers. Even if loan documents do not explicitly address the CTA, it is typical for loan documents to include general requirements for the borrower to remain in compliance with applicable laws, which may provide an opportunity to confirm a borrower's compliance with the CTA's reporting requirements.

- **Understand Interplay between KYC and FinCEN Rules.** Financial institutions will still need to collect KYC information from their business customers, independent of the CTA's reporting requirements, but FinCEN plans on extending access to the BOI database to financial institutions in Spring 2025, subject to supervisory requirements that have not yet been defined. Lenders should stay informed about such access rules for financial institutions as they roll out, as the BOI database information on a customer is likely to become an additional source of diligence information when developing a customer risk profile.

- **Monitor Developments.** The interpretive guidance from FinCEN relating to the CTA is ongoing and developing. It will therefore be important to monitor developments. Lenders and private equity firms should also stay informed about potential state legislation similar to the CTA rolling out in the jurisdictions in which they operate. For example, the New York LLC Transparency Act (NYLTA) was signed into law on December 23, 2023 (effective in 2026) and similar legislation is under consideration in California, Massachusetts, and other states. To the extent loan transactions involve borrowers or guarantors formed (or registered to do business) in these states, or secured assets located in these jurisdictions, additional inquiries and due diligence may be necessary to ensure compliance with such laws as they come into effect.

- **Amend Governing Documents.** Reporting companies should (1) include provisions in their operating agreements, subscription agreements, shareholder agreements, and similar governing documents requiring timely cooperation, disclosure, and indemnification by beneficial owners for CTA reporting purposes; and (2) assess whether they need to address any potential conflicting provisions under existing indemnification and exculpation provisions covering directors, officers, and beneficial owners so the reporting company is not required to cover them for willful noncompliance with the CTA.

- **Conduct CTA Impact Analysis.** Lenders, businesses, and investors should assess the potential impact of the CTA (and any applicable state-law equivalents) on their processes and procedures for entity formation, acquisition transactions, financing activities, and capitalization matters. Issues relative to timing, jurisdiction, allocation of beneficial owners, and any control granted to third parties will all be more material now that the CTA has come into effect.

- **Perform Portfolio Analysis.** Private equity sponsors should carefully evaluate their own corporate portfolios and investment structures to assess potential CTA filing obligations. While exemptions may apply to the operating entities and certain pooled investment vehicles, there is no stand-alone CTA exemption for holding companies or special purpose vehicles. This means that management company holding entities, ultimate general partner entities, and other similar upper-tier entities may be subject to CTA reporting obligations.

Final Thoughts:

The CTA has created significant uncertainty for businesses in many ways. FinCEN has issued bulletins, alerts, and advisories providing interpretive guidance with to try to address some of this uncertainty, but many questions remain. In addition, challenges to the CTA are pending in various federal courts, adding to the sense of unease. Understanding the CTA and following developments regarding the legislation is necessary for a reporting company to ensure it is CTA-compliant and positioned for success in a regulatory environment that prioritizes accountability and transparency. Lenders and private equity firms should also take account of the CTA and its impact on their customers and/or portfolio companies and any changes that may be necessary to ensure their compliance.
