



FinCEN Finalizes Rule Implementing Beneficial Ownership Reporting Requirements

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On September 30, 2022, the U.S. Department of the Treasury's Financial Crimes Enforcement Network (FinCEN) published a highly anticipated rule (the "Final UBO Rule" or the "Final Rule") that implements the beneficial ownership information reporting requirements of the Corporate Transparency Act (the CTA).¹ The CTA, which is part of the Anti-Money Laundering Act of 2020 and enacted into law as a part of the National Defense Authorization Act for Fiscal Year 2021, establishes ultimate beneficial ownership (UBO) information reporting requirements for the vast majority of privately held corporations, limited liability companies and other similar entities created in, or registered to do business in, any of the states of the United States.

As we previously [reported](#), the hotly contested issue over how and whether to track beneficial ownership of privately held entities operating in the United States dates back to at least 2006, and debates have primarily centered around the value in providing law enforcement with such information against privacy and cost concerns. While the early focus had been on requiring the states to collect and protect the data, the CTA focuses on a centralized federal approach to UBO data collection. Also, as we previously [reported](#), in December 2021, FinCEN issued a Notice of Proposed Rulemaking allowing the public an opportunity to review and comment on its proposed rule. In issuing the Final Rule, FinCEN considered the public comments and made some adjustments, but largely adopted the proposed rule as previewed. Acting FinCEN Director Himamauli Das described the Final Rule as a "significant step forward in our efforts to support national security, intelligence, and law enforcement agencies in their work to curb illicit activities,"^[2] and Treasury Secretary Janet Yellen provided similar sentiments, noting that the Rule "mak[es] it more difficult for oligarchs, terrorists, and other global threats to use complex legal structures to launder money, traffic humans and drugs, and commit other crimes that threaten harm to the American people."^[3]

Key Takeaways:

- **Compliance Dates.** The Final UBO Rule becomes effective January 1, 2024. Existing reporting companies and those formed before January 1, 2024 will have until January 1, 2025 to file their initial reports. Companies incorporated or formed after January 1, 2024 must file their initial reports within 30 days of their creation or registration.

- **Reporting Companies & Exempt Companies.** The Final UBO Rule requires entities that are considered reporting companies to file reports that identify themselves and provide UBO information on the entities' "beneficial owners" and "company applicants." Many key entities are exempt from the Final Rule's reporting requirements, including inactive entities, some subsidiaries, banks and credit unions, and Securities and Exchange Commission ("SEC") reporting issuers.
- **CDD Rule Differences.** The Final UBO Rule does not replace FinCEN's existing customer due diligence ("CDD") rule requiring U.S. financial institutions to collect UBO information from their legal entity customers, although FinCEN will be revising the CDD rule to align it with the CTA. The Final UBO Rule provides a broader definition of "beneficial owner" than the previous CDD Rule but exempts more companies. Thus, reporting companies can expect that they may have to provide more information to FinCEN and/or identify additional persons as UBOs than previously required to disclose/provide to their banks. Likewise, at least until the CDD rule is amended, financial institutions may continue to collect UBO information from customers that may not otherwise be required to report to FinCEN.

Background

Winston previously reported that the debate over how and whether to track beneficial ownership of privately held entities operating in the United States dates back to at least 2006 where the issue was the topic of hearings and investigations spearheaded by the Senate Permanent Sub Committee on Investigations. Proponents of sharing such information with the government (at the state level) largely cite the concern that anonymity allows bad actors to use shell companies to engage in certain illicit activity, including money laundering, terrorist financing, and other financial crimes. On the other hand, sharing such information presents real concerns from a privacy standpoint and cost perspective and efforts to impose legislation had been met with strong opposition from various groups, including the American Bar Association. Of primary note was the expense of maintaining databases that would be adequately protected from cyber-attacks—an equally valid concern in 2022.

In 2016, FinCEN issued a Final Rule relating to customer due diligence (CDD) which amended the Bank Secrecy Act (BSA) regulations requiring covered financial institutions to identify and verify the identity of the natural persons (known as "beneficial owners") of certain legal entity customers. Then, on December 11, 2020, as part of the National Defense Authorization Act (NDAA), the U.S. Senate passed the CTA, which established new reporting requirements to FinCEN, among other things. On December 7, 2021, FinCEN published a proposed rule to implement the beneficial ownership information reporting requirements as set forth in Section 6403(a) of the CTA and to welcome public comment. FinCEN considered public comment and on September 30, 2022, FinCEN issued the Final UBO Rule.

Final UBO Rule

Under the Final UBO Rule, effective January 1, 2024, certain legal entities will be required to submit to FinCEN a report containing certain information relating to the entity, its UBOs, and Company Applicants (as such term is defined below). Below we summarize: (1) which entities are required to report UBO information to FinCEN; (2) what information the entities must report to FinCEN; (3) when an entity must report UBO information; (4) the definition of "Beneficial Owner" under the Final UBO Rule; and (5) the penalties for non-compliance with the Rule.

1) Which Entities Must Comply with the Final UBO Rule? And Which Are Exempt from Compliance?

The Final UBO Rule applies to Reporting Companies. Reporting Companies are U.S. domestic companies and certain non-U.S. foreign companies:

- **Domestic Reporting Companies:** Any corporation, limited liability company or other similar entity created by the filing of a document with a secretary of state or any similar office under the law of a State (including U.S. territories and possessions) or Indian tribe (unless exempt).

- **Foreign Reporting Companies:** Any entity that is formed under the laws of a non-U.S. jurisdiction but is registered with a secretary of state or similar office to do business in that State or tribal jurisdiction in the United States (unless exempt).

Despite the broad definition of Reporting Companies under the CTA, the Final UBO Rule exempts 23 types of entities from the reporting requirements, including:

- **Entities already required to disclose beneficial ownership information** publicly or to federal regulators (g., U.S. banks and credit unions, U.S. branches and agencies of non-U.S. banks, securities broker-dealers, investment advisers registered with the U.S. Securities and Exchange Commission, and money services businesses registered with FinCEN);
- **Large operating companies** that (1) have 21 or more full-time employees, (2) filed federal income tax returns with the United States in the previous year that demonstrated more than \$5,000,000 in gross receipts or sales in the aggregate, and (3) have an operating presence at a physical office within the United States;
- **Inactive entities** that existed on or before January 1, 2020 but, among other requirements, are not engaged in active business and have not received or sent funds in an amount greater than \$1,000; and
- Subject to exceptions, **subsidiaries** whose ownership interests are controlled or wholly owned, directly or indirectly, by one or more exempt entities.

FinCEN made it clear that any ambiguities in exemptions should be interpreted “reasonably narrowly,” as the “exemptions for twenty-three specific categories of entities are carefully circumscribed.”

2) What Information Must be Reported to FinCEN?

Initial reports made to FinCEN must include the following information about the Reporting Company, its Beneficial Owners, and Company Applicants:

Reporting Company Information

- Full legal name and fictitious names (e., “doing business as” names);
- Address of the reporting company’s principal place of business;
- Jurisdiction of incorporation or formation (for both domestic and foreign reporting companies) and initial registration in the United States (for foreign reporting companies); and
- Taxpayer Identification Number (TIN).

Beneficial Owners & Company Applicant Information

- Full legal name;
- Date of birth;
- Current residential address; and
- Unique identifying number from an acceptable identification document (or, if information has already been provided to FinCEN, by a FinCEN identifier).

The definition of “Beneficial Owner” is discussed below in more detail.

A “Company Applicant” is the individual who directly files the document that creates a domestic reporting company or first registers a foreign reporting company, as well as the individual who is primarily responsible for directing or controlling such filing (if there is more than one individual involved in the filing or registering). Information must be provided for the Beneficial Owners as well as the Company Applicants.

3) When Are Reports Due?

Any reporting company formed or registered before January 1, 2024 must submit an initial report to FinCEN before January 1, 2025.

Reporting companies formed or registered on or after January 1, 2024 must submit an initial report to FinCEN within 30 days of the reporting company receiving actual notice that its creation has become effective, or a secretary of state or similar office first providing public notice of the reporting company's creation or registration. If a previously exempt entity ceases to be exempt, the entity must file a report within 30 days of losing its exempt status.

Additionally, the Final UBO Rule requires reporting companies to file reports with FinCEN that update outdated information or correct inaccurate information within 30 days after a change occurs or after the reporting company becomes aware of the inaccuracy.

In a change from the proposed rule, the timeframes and timing events for initial, updated, and corrected reports were "harmonized" in the Final UBO Rule at 30 days to "ease administration for reporting companies and service providers that may support reporting companies."

4) Who are the "Beneficial Owners" That Must Be Disclosed?

Beneficial Owner

Under the CTA, a "beneficial owner" of a reporting company is "**any individual, who, directly or indirectly, either exercises substantial control over such reporting company or owns or controls at least 25 percent of the ownership interests of such reporting company.**"^[4] This definition is broader than the definition under the existing CDD rule in that the "control prong" under the CDD rule calls for the identification of a *single* individual with such control, whereas the Final UBO Rule calls for *any* (i.e., all). Thus, a corporation with four 25% equity holders would, for Final UBO Rule reporting purposes, report all four equity holders as UBOs. Moreover, the Final Rule implements broader definitions for what constitutes "substantial control" and an "ownership interest," as discussed below.

Although FinCEN received comments to its proposed rule reflecting a preference that the definitions under the CDD rule and Final UBO Rule match, ultimately, FinCEN concluded that adopting the CDD rule's "numerical limitation" would be inconsistent with the CTA's "objective of establishing a comprehensive" UBO "database for all beneficial owners of reporting companies."^[5] Specifically, FinCEN explained that "limiting reporting of individuals to one person would "artificially restrict the reporting of beneficial owners who may exercise substantial control over an entity ... and become a means of evasion or circumvention."^[6] We note this is a rejection of the compromise proposed in the early Senate debates over UBO information to provide law enforcement with access to a natural person who had access to the ownership and control structure of an entity. As such, the Final UBO Rule largely adopts the "substantial control" language of the proposed rule but modifies some language to "clarify and streamline application of the rule in general, to focus the applicability of the senior official element of the definition of 'substantial control,' and clarify the issue of substantial control through trust arrangements."

Substantial Control

The Final UBO Rule's broad definition of "substantial control" states that an individual exercises substantial control over a reporting company if the individual:

- (A) Serves as a senior officer of the reporting company;
- (B) Has authority over the appointment or removal of any senior officer or a majority of the board of directors (or similar body);
- (C) Directs, determines, or has substantial influence over important decisions made by the reporting company, including decisions regarding:
 - 1. The nature, scope, and attributes of the business of the reporting company, including the sale, lease, mortgage, or other transfer of any principal assets of the reporting company;
 - 2. The reorganization, dissolution, or merger of the reporting company;

3. Major expenditures or investments, issuances of any equity, incurrence of any significant debt, or approval of the operating budget of the reporting company;
4. The selection or termination of business lines or ventures, or geographic focus, of the reporting company;
5. Compensation schemes and incentive programs for senior officers;
6. The entry into or termination, or the fulfillment or non-fulfillment, of significant contracts; or
7. Amendments of any substantial governance documents of the reporting company, including the articles of incorporation or similar formation documents, bylaws, and significant policies or procedures.

In addition, the broad definition of “substantial control” is also circular in that it captures “additional forms of control”—without explaining what that means—as an indicator of “substantial control”

The Final UBO Rule also provides clarity on what constitutes an exercise of “direct or indirect” substantial control. Specifically, an individual may directly or indirectly, **including as a trustee of a trust or similar arrangement**, exercise substantial control over a reporting company through:

- A. Board representation;
- B. Ownership or control of a majority of the voting power or voting rights of the reporting company;
- C. Rights associated with any financing arrangement or interest in a company;
- D. Control over one or more intermediary entities that separately or collectively exercise substantial control over a reporting company;
- E. Arrangements or financial or business relationships, whether formal or informal, with other individuals or entities acting as nominees; or
- F. Any other contract, arrangement, understanding, relationship, or otherwise.

Ownership Interests

The Rule provides that an ownership interest includes not only equity interests but also categories such as convertible interests, capital or profit interests, convertible instruments, and a catchall category for any other instrument, contract, arrangement, understanding, or mechanism used to establish ownership. Debt instruments would also be included if they enable the holder to exercise the same rights as one of the specified equity or other interests. Importantly, ownership interests of the individual are calculated at the present time, and any options or similar interests of the individual are treated as exercised.

An individual may own or control an ownership interest through joint ownership with other persons; through a nominee, intermediary, custodian, or agent; through certain trust arrangements; or through ownership or control of intermediary entities that separately or collectively own or control ownership interests of the reporting company. The Final UBO Rule provides for a special exception for reporting companies with ownership interests held by exempt entities. Such reporting companies need not provide UBO information for individuals that are beneficial owners in the reporting company exclusively by virtue of the individuals’ ownership interests in the intermediate exempt entities. Instead, these reporting companies may list the exempt entities. Because FinCEN declined to extend this special exception to beneficial owners qualifying under the substantial-control prong, an analysis must still be undertaken to confirm whether those with ownership interests exercise substantial control over the reporting company.

With respect to the definition of “ownership interest,” FinCEN explained its reasoning for not making changes to the rule that identified specific individuals in trust arrangements whom a reporting company could treat as owners of 25% of the ownership interests: First, to “ensure that any individual or entity that establishes an ownership interest in a reporting company through a contractual relationship” is subject to the reporting requirements, the Final UBO Rule adds a catch-all provision to the definition of ownership interest to include “[a]ny other instrument, contract, arrangement, understanding, relationship, or other mechanism used to establish ownership.” Second, the Final UBO Rule amends paragraphs now entitled “Ownership or Control of Ownership Interest” by adding more specific,

straightforward language to address means through which a beneficial owner can “own or control” an ownership interest. FinCEN acknowledged comments that expressed concerns about whether the list of individuals who may own or control an ownership interest held in trust is illustrative or exhaustive and which parties in trust arrangements should be reported as beneficial owners. While FinCEN considered these concerns, it ultimately decided to adopt the proposed rule without change. FinCEN justified the non-changes by noting that the Final UBO Rule identifies trustees who are considered to have ownership interests in a reporting company and circumstances in which ownership interests held in trust will be considered as owned or controlled by a beneficiary.

Exemptions

There are five types of individuals who are considered “exempt” from the definition of “beneficial owner”:

- A minor child (as defined under the state law where the reporting company is formed or first registered);
- An individual acting as a nominee, intermediary custodian, or agent on behalf of another individual;
- Certain employees of a reporting company, acting solely as an employee and not as a senior officer;
- An individual whose only interest in a reporting company is a future interest through a right of inheritance; and
- Certain creditors of a reporting company.

5) What are the Penalties for Violations of the Final UBO Rule?

The Final UBO Rule adopts the CTA’s penalty framework and clarifies that liability can be for indirect or direct violations, and for acts or omissions. The CTA provides that any willful violation of UBO reporting requirements may result in civil penalties of up to \$500 each day a violation goes unremedied and criminal penalties of up to \$10,000 and/or imprisonment for up to two years.

The Final UBO Rule significantly expands the scope of information that legal entities must disclose under U.S. law and signals Treasury’s prioritization of corporate disclosure. To minimize confusion during the implementation of this Rule, FinCEN will likely publish Frequently Asked Questions (FAQs) to clarify common points of confusion and questions about the reporting requirements.

FinCEN’s changes to the Anti-Money Laundering (“AML”) regulatory scheme do not end with the implementation of the Final UBO Rule. FinCEN also intends to issue two sets of rules that would potentially impact how financial institutions comply with regulatory requirements under a number of anti-money laundering/countering terrorism financing laws. FinCEN is likely to issue a rule to implement protocols for access to, and disclosure of, beneficial ownership information and another rule to revise the existing CDD rule requirements that apply to depository institutions, credit unions, mutual funds, and securities broker-dealers.

If you have any questions or need assistance with navigating the UBO reporting requirements in light of the Final UBO Rule, please contact **Carl Fornaris** (Partner and Co-Chair of the Financial Services Practice), **Cari Stinebower** (Partner, White Collar, Regulatory Defense, and Government Investigations), or your Winston & Strawn relationship attorney. You can also contact **Suzanne Jaffe Bloom**, Co-Chair of our White Collar, Regulatory Defense, and Government Investigations practice group, or visit our practice group webpage **here**, for more information on this and related subjects.

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¹¹ See Beneficial Ownership Information Reporting Requirements, 87 Fed. Reg. 59,498 (Sept. 30, 2022), available at <https://www.federalregister.gov/d/2022-21020>.

FinCEN issued its proposed rule to implement the CTA’s beneficial ownership reporting requirements on December 8, 2021. See Beneficial Ownership Information Reporting Requirements, 86 Fed. Reg. 69,920 (Dec. 8, 2021), available at <https://www.federalregister.gov/d/2021-26548>.

² Press Release, FinCEN, FinCEN Issues Final Rule for Beneficial Ownership Reporting to Support Law Enforcement Efforts, Counter Illicit Finance, and Increase Transparency (Sept. 29, 2022), available at <https://www.fincen.gov/news/news-releases/fincen-issues-final-rule-beneficial-ownership-reporting-support-law-enforcement>.

³ Press Release, Statement by Secretary of the Treasury Janet L. Yellen on New Rule Under the Corporate Transparency Act (Sept. 29, 2022), available at <https://home.treasury.gov/news/press-releases/jy0979>.

⁴ 31 U.S.C.A. § 5336 (3)(A)(i)-(ii).

⁵ See Beneficial Ownership Information Reporting Requirements, 87 FR 59498, Sept. 30, 2022 (amending 31 C.F.R., § 1010.380), at <https://www.federalregister.gov/d/2022-21020/p-378>.

⁶ *Id.*

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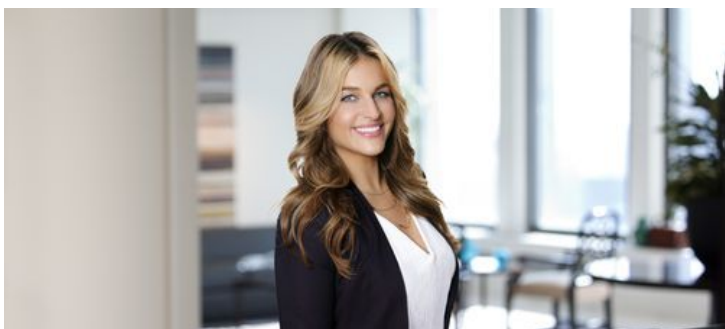
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