The CTA's (First, but Probably Not Last) Day in Court: While FinCEN Appeals the First CTA Case, Your Entity Must Still Comply with the CTA

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Much has been made about the burdensome impact of the Corporate Transparency Act (CTA) which was created under the 2021 National Defense Authorization Act but only took effect on January 1, 2024. Compliance with the CTA has required significant amounts of additional reporting work for individual investors, small businesses, and their advisors. Many have questioned the purpose of the policy, expressing opinions that Congress's intent with the CTA is to cut down on the use of shell corporations by drug dealers, terrorists, and others to launder money through the U.S. financial system and/or evade taxes.

Developments this month have created more confusion for small businesses. Within 60 days of the Corporate Transparency Act's effective date, a federal judge in Alabama stirred up hope that the CTA's existence would be short-lived by finding it "unconstitutional." But the U.S. Treasury Department's Financial Crimes Enforcement Network (FinCEN) is making it clear that the Alabama court's injunction in *National Small Business United et al v. Yellen et al* only applies to the plaintiff in that case. This means that for "beneficial owners" and "applicants" as defined by the CTA, compliance with the CTA is still mandatory.

Which Entities does the CTA Impact?

The CTA requires all "reporting companies" (i.e., corporations, limited liability companies, and other entities created by the filing of a document with a secretary of state or similar office under state law) to disclose to FinCEN the identity of any "beneficial owner" (i.e., an individual who exercises substantial control over the entity or who owns or controls not less than 25 percent of the ownership interests of the entity).

Companies formed after 2024 must also disclose the identity of any "applicants," generally defined as any individual who files an application to form a reporting company.

There are several exceptions to the definition of a "reporting company" including, but not limited to, banks, insurance companies, and entities with more than 20 employees, five million dollars in gross revenue, and a physical office in the United States.

For the millions of entities that do not fall under any exceptions to the general rule, the CTA requires a reporting company to provide FinCEN with the name, date of birth, current address, and identification number from a driver's license, passport or other government issued I.D. of each beneficial owner or applicant.

Is the CTA Constitutional?

On March 1, federal judge Liles C. Burke of the U.S. District Court for the Northern District of Alabama found that the CTA is unconstitutional. In the Court's opinion on *National Small Business United et al v. Yellen et al*, Judge Burke wrote, "The Constitution, in other words, does not allow judges to strike down a law merely because it is burdensome, foolish, or offensive. Yet the inverse is also true—the wisdom of a policy is no guarantee of its constitutionality. Indeed, even in the pursuit of sensible and praiseworthy ends, Congress sometimes enacts smart laws that violate the Constitution. This case, which concerns the constitutionality of the Corporate Transparency Act, illustrates that principle."

According to Judge Burke, Congress overstepped its boundaries by attempting to "regulate those millions of entities and their stakeholders the moment they obtain a formal corporate status from a state."

FinCEN Appeals the Alabama Court's Decision

Following Judge Burke's decision, FinCEN immediately published a notice on its website stating that the ruling applies *only to the plaintiff in that case and that everyone else remains subject to CTA enforcement*

. Shortly thereafter, the U.S. Department of the Treasury filed a Notice of Appeal in the U.S. Court of Appeals for the Eleventh Circuit. It remains to be seen whether the *National Small Business United* decision will hold up in higher courts. As such, we recommend that clients continue making plans for CTA compliance – and for those who have no such plans, now is not the time for further delay.

Please contact our Trusts & Estates department for questions regarding the CTA and your compliance with its reporting requirements.