

FinCEN Beneficial Ownership Rules Require Private Fund Reporting

By Melissa Goldstein, Michael Didiuk, and Jessica Romano2024-04-08T04:30:33000-04:00

- Schulte Roth & Zabel attorneys clarify CTA private fund rules
- Many US businesses need to report information to FinCEN

The government's latest effort to make it harder for bad actors to hide ill-gotten gains through shell companies or other complicated ownership structures is poised to significantly impact the private fund industry.

The Beneficial Ownership Information Reporting [Rule](#), effective this year, was adopted by the Treasury's Financial Crimes Enforcement Network as part of Corporate Transparency [Act](#) implementation. According to the Treasury, as a result of the BOI rule, "many companies are required to report information to FinCEN about the individuals who ultimately own or control them."

Separately, on March 1, the US District Court for the Northern District of Alabama found the CTA unconstitutional in *Nat'l Small Bus. United v. Yellen*. While the court's [final judgment](#) permanently enjoins the government from enforcing the CTA against the two plaintiffs, the CTA continues to be effective as to all reporting companies other than the plaintiffs.

The government [appealed](#) this ruling to the 11th Circuit. Fund managers should continue to focus on complying with the CTA rather than pause compliance efforts pending future litigation.

Under the BOI rule, reporting companies—generally, legal entities formed or registered to do business in the US—must submit detailed beneficial ownership information to FinCEN. A beneficial owner, in turn, is an individual who exercises substantial control or owns or controls 25% or more of the reporting [company](#).

Beneficial owners of reporting companies need to provide FinCEN with a full legal name, birth date, current residential address, and a unique identifying number from an acceptable document, such as a passport or driver's license.

Company applicants—individuals involved in forming or registering the reporting company to do business in the US—must also provide identifying information to FinCEN.

Failing to comply with the rule can produce both civil and criminal penalties for the reporting company and any individual that causes such reporting company's failure.

Of particular interest to the private fund industry is that not all legal entities are reporting companies: The rule provides 23 express exemptions from the definition of reporting company. Determining whether an exemption applies requires an entity-by-entity analysis that is fact-specific and time-consuming.

Many fund managers appreciate that Securities and Exchange Commission-registered investment advisers and certain private funds they advise are exempt. It can be surprising to learn that most upper-tier entities in an organizational structure, for example, are likely reporting companies.

In these six key steps, fund managers can properly identify reporting companies and determine whether reorganization or restructuring might help entities within the enterprise qualify for one or more exemptions, and also streamline reporting.

First, prepare a comprehensive organizational chart. Identify all entities, including management entities, holding companies, trusts, investment vehicles, joint venture vehicles, blockers, and special-purpose vehicles.

An organizational chart should identify all upstream entities with direct or indirect ownership, or control interests over the listed entities and any downstream entities in which listed entities have direct or indirect ownership or control interests. Identify each legal entity, including those that are non-US.

Second, determine if any listed entities are in-scope for BOI reporting—that is, whether such entities are formed or registered to do business in the US.

It's common that Cayman Islands-based pooled investment vehicles aren't registered to do business in the US, but this should be verified now while there is still time before the Jan. 1, 2025 compliance deadline for entities that were formed or registered to do business prior to Jan. 1, 2024.

Third, analyze each would-be reporting company individually to determine whether it qualifies for an exemption from the rule. The answer isn't always obvious. For example, recent FinCEN [guidance](#) significantly narrowed the availability of the "subsidiary exemption."

Although FinCEN defines a subsidiary as an entity whose "ownership interests are controlled or wholly owned, directly or indirectly," by one or more certain exempt entities, a subsidiary qualifies for the exemption only if its ownership interests are "fully, 100 percent owned or controlled by an exempt [entity](#)."

Specifically, in this context, "control of ownership interests means that the exempt entity entirely controls all of the ownership interests in the reporting company, in the same way that an exempt entity must wholly own all of a subsidiary's ownership interests for the exemption to [apply](#)."

The term "control" as used in the subsidiary exemption isn't defined, and FinCEN declined to consider any other definitions of "control" under other federal regulatory or statutory provisions as dispositive.

Fourth, compile the information necessary to complete the BOI report for each reporting company. This would include identifying which individuals have a 25% or more ownership interest in the reporting company and which individuals exercise substantial control over the reporting company.

In addition, each reporting company must provide its own:

- Legal name
- Any trade or "doing business as" name
- Principal place of business in the US Jurisdiction of formation or registration
- Taxpayer identification number

Fifth, develop record-keeping systems to track BOI reporting information. This includes tracking ownership structures and any information disclosed to FinCEN in a BOI report.

The BOI Rule requires reporting companies to update or correct BOI reports within 30 days of any change to previously reported information or becoming aware of an inaccuracy in previously reported information.

The system should also keep track of exempt entities and the exemption applicable to each one. If, in

the future, the entity no longer qualifies for an exemption, it will become subject to BOI filing requirements.

Finally, fund managers should implement a CTA compliance policy to devote adequate resources to CTA compliance. This includes dedicated persons who are responsible for CTA compliance and monitoring FinCEN's [FAQs](#) and Small Entity Compliance [Guide](#) for continuing guidance on the BOI Rule.

Fund managers should also implement procedures for creating new entities given the reporting obligations that are triggered under the BOI rule once a new entity is formed.

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