KIRKLAND & ELLIS

Private Investment & Family Office Insights

FinCEN Beneficial Ownership Reporting — Implications for Family Offices (Part 2 of 2)

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On January 1, 2024, the beneficial ownership information ("BOI") reporting provisions of the Corporate Transparency Act of 2020 (the "CTA") went into effect. This new rule, implemented by the Financial Crimes Enforcement Network ("FinCEN"), a U.S. Treasury unit tasked with safeguarding the financial system from illicit uses (e.g., money laundering), requires many U.S. domestic and certain non-U.S. legal entities to disclose information about their Beneficial Owners to FinCEN. Entities formed on or after January 1, 2024, have 90 days to make required filings, while entities in existence prior to such date have a full year to make the required filings.

Under the rule, "Beneficial Owners" are natural persons who directly or indirectly own or control at least 25% of an entity[1] or otherwise exercise "substantial control."[2] This information will be maintained in a confidential database that may only be accessed by law enforcement agencies and, with the reporting entity's consent, certain financial institutions seeking to comply with customer due diligence requirements. The rule clarifies which entities will be required to file a BOI report, the information that must be reported, and when such reports are due.

Family offices and their investment managers should be aware that BOI reporting requirements may apply to their structures and may require disclosure of natural person(s) that own 25% or more of their investment vehicles or otherwise control them.

Every entity organized under U.S. law or registered to do business in the U.S. will need to determine (i) whether it is able to make use of an exemption from reporting and (ii) if not, what information it must report. We discuss these considerations below.

U.S. domestic and non-U.S. entities are subject to reporting

Both U.S. domestic legal entities and certain non-U.S. entities may face BOI reporting requirements. Under the rule, domestic reporting entities include corporations, limited liability corporations ("LLCs"), or any other entity (e.g., limited partnership) created by filing a document with a secretary of state or analogous office. Non-U.S. reporting entities include corporations, LLCs, or other entities formed under the laws of a foreign jurisdiction that are **registered to do business** in any U.S. state or tribal jurisdiction.

Although a number of exemptions from reporting are available, it is not apparent that many family offices will qualify

The CTA exempts 23 types of entities from the BOI reporting requirements.[3] Importantly, each legal entity (LLC, limited partnership, etc.) must be looked at on a standalone basis for purposes of determining whether an exemption applies.

Generally speaking, exemptions from BOI reporting are available for regulated entities. Given that the majority of family office vehicles are not registered, it is unlikely family office entities will qualify for any of the below-detailed exemptions.

There are two main categories of BOI reporting exemptions for registered entities: (1) U.S.-domiciled entities if (a) the entity is an SEC-registered adviser or (b) a venture capital exempt reporting adviser;[4] and (2) private investment funds affiliated with exempt private fund managers, provided they qualify as "pooled investment vehicles" ("PIVs").[5] The CTA identifies two kinds of exempt PIVs:

- Any entity that qualifies as an investment company under Section 3(a) of the Investment Company Act of 1940 ("ICA") (e.g., registered funds or funds investing primarily in securities but relying on other exemptions such as ICA Section 3(c)(5) used by certain real estate funds); or
- Any entity (e.g., a private fund) that (i) relies on a Section 3(c)(1) or 3(c)(7) exemption from the ICA and (ii) is (or will be) identified by its legal name on an investment

adviser's Form ADV.[6]

BOI reporting exemption is available to any "bank" as defined in the Federal Deposit Insurance Act, ICA, or Investment Advisers Act of 1940. In addition, bank-type entities are also exempt from BOI reporting, such as state regulated private trust companies, or any bank holding company or savings and loan holding company as defined in the Bank Holding Company Act of 1956 or the Home Owners' Loan Act.

An additional BOI reporting exemption is available to "large operating companies." In order to qualify for this exemption, a family office must:

- maintain an operating presence in the U.S.;
- have more than 20 full-time employees in the U.S.; and
- have filed a U.S. tax return in the previous year reporting over $5 million in gross receipts.

It is also important to note that certain tax-exempt entities and charitable trusts are entitled to BOI reporting exemptions. Given the recent increased use of tax-exempt entities in family office structures, it may be possible for a family office to qualify under this BOI reporting exemption if the family office entity is:

- a non-profit organization (including charities and private foundations, described in Section 501(c) of the Internal Revenue Code);
- a political organization[7]; or
- a charitable or split-interest trust described in Section 4947 of the Internal Revenue Code.

Finally, subject to a few important exceptions, subsidiaries of any exempted entity are also exempt from the reporting requirements. This "subsidiary exemption" removes from the BOI reporting obligations entities controlled or wholly owned, directly or indirectly, by an enumerated list of owners who are themselves exempt from BOI reporting. Notably, subsidiaries of PIVs are not exempt from reporting requirements under the subsidiary exemption, but other exemptions may apply.

Reporting entities must disclose "Beneficial Owners" and "Company Applicants"

Domestic and foreign entities that do not benefit from a reporting exemption will be required to file reports with FinCEN that identify:

- the entity's Beneficial Owners; and
- individuals who have filed applications with government authorities to form the entity or register it to do business ("company applicants") — though this company applicant prong only applies to entities formed after January 1, 2024.

As noted above, "*Beneficial Owners*" include any *natural person* who (i) exercises substantial control over a reporting entity or (ii) owns or controls at least 25% of the ownership interests of a reporting entity. The rule sets out a list of actions demonstrating "substantial control" of a reporting entity and captures anyone who can make significant decisions on behalf of the entity. This includes, for example, "senior officers" of a reporting entity.

The following persons constitute "Beneficial Owners" in the context of a trust:

- trustees and each other person that has authority to dispose of trust assets;
- trust beneficiaries who are the sole permissible recipient of income and principal from the trust;
- trust beneficiaries who have a right to demand a distribution from the trust; and
- trust settlors and grantors who have the right to revoke or withdraw trust assets.

"*Company Applicants*" are the individuals who file the documents forming the entity (for domestic entities) or the individuals who file the document that first registers the entity to transact business in the U.S. (for non-U.S. entities). In either case, Company Applicants include anyone directing or controlling the filing of the relevant document. There can be up to two such Company Applicants for each filer. One applicant will be an employee of the service provider that actually makes the "last mile" filing with the relevant Secretary of State. The other company applicant could be a lawyer, paralegal, or client contact that causes the formation of a legal entity.

For each Beneficial Owner or Company Applicant covered by the regulation, the BOI report must disclose:

- name;
- date of birth;
- residential street address (business address in the case of company applicants); and
- a unique identifying number from an identification document, such as a passport, or a unique FinCEN identifier.

Access to BOI database

On December 21, 2023, FinCEN issued a final rule implementing the access and safeguard provisions of the CTA (the "Access Rule"). The Access Rule prescribes the circumstances under which BOI reported to FinCEN may be disclosed to authorized BOI recipients, and how it must be protected. Under the Access Rule, FinCEN limits BOI access to (i) federal agencies engaged in national security, intelligence, or law enforcement activity; (ii) state, local, and tribal law enforcement agencies with court authorization; (iii) foreign law enforcement agencies, judges, prosecutors, and other authorities that meet specific criteria; (iv) financial institutions with customer due diligence requirements and regulators supervising them for compliance with such requirements; and (v) U.S. Department of the Treasury officers and employees. Each category of authorized recipients is subject to security and confidentiality protocols aligned with applicable access and use provisions. According to FinCEN, reported BOI "will be stored in a secure, non-public database using rigorous information security methods and controls typically used in the Federal government to protect non-classified yet sensitive information systems at the highest security level."

Looking ahead

The final rule became effective on January 1, 2024. By January 1, 2025, FinCEN will also revise its Customer Due Diligence rule (applicable to "financial institutions" under the Bank Secrecy Act) to ensure consistency with the final rule regarding BOI. Companies in existence prior to the BOI rule's effective date and now subject to the new reporting requirements will have until one year after the effective date (until January 1, 2025) to file initial BOI reports. Reporting entities created in 2024 will have to file their initial reports within 90 days after their formation (for U.S. domestic entities) or their initial registration to do business in the U.S. (for non-U.S. entities). Starting on January 1, 2025, newly formed entities will have to make such filings within 30 days of formation. Reports may be filed using FinCEN's BOI E-Filing website, or in a form and manner to be set forth in subsequent rulemaking.

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1. A natural person must own 25% of the total outstanding "ownership interests" of a reporting entity. "Ownership interests" are defined to include (i) any equity, stock, or other similar instrument establishing ownership without regard to whether it confers voting power or voting rights; (ii) any capital or profit interest in an entity; or (iii) any other instrument or arrangement used to establish ownership. ↩

2. The rule defines a number of relationships and circumstances (formal and informal) that may establish "substantial control." In short, senior officers, those who control a majority of the board, and those who direct or have substantial influence over important business decisions may be considered to have substantial control for purposes of the reporting requirement. ↩

3. For the complete list of exempted entities, see 31 U.S.C. § 5336(a)(11)(B)(i)-(xxiii). FinCEN has the statutory authority to expand the list of exempted entities. ↩

4. A relying adviser identified as such on the Form ADV of an SEC-registered adviser is exempt from beneficial ownership reporting under the Final Rule. The SEC, pursuant to a regime known as "umbrella registration," permits an RIA and its affiliated advisory entities to register under the Advisers Act on a single Form ADV – subject to certain conditions – rather than requiring the affiliates (i.e., a relying advisers) to complete multiple Forms ADV that would reflect a shared business with the main RIA (i.e., the filing adviser). The SEC formally recognized umbrella registration in 2016 by codifying into Form ADV, one of the conditions of which was that any relying adviser be independently eligible to register with the SEC. As a result, relying advisers are investment advisers registered with the SEC. *See* Form ADV and Investment Advisers Act Rules, 81 Fed. Reg. 60418, 60433, 60436 (September 1, 2016). Thus, if not for umbrella registration under a filing adviser's Form ADV, each relying adviser identified as such would separately register with the SEC. An RIA's relying advisers are considered by the SEC to be registered advisers, and it is clear these relying advisers are themselves "investment adviser[s] as defined in section 202" of the Advisers Act that are "[r]egistered with the [SEC] under the [Advisers Act]" for purposes of the beneficial ownership reporting exemption for RIAs in the Final Rule. FinCEN has taken the position that general partnerships are generally not created through the filing of documents with a secretary of state or analogous office, nor is any registration for a business license or similar permit an act "creating" the entity. ↩

5. Because most sponsors list their GPs on a Form ADV, those GPs are deemed "registered" with the SEC. Although FinCEN declined to provide categorically that the exemption for RIAs "encompasses vehicles used by an investment adviser that serve as general partners or managing members of pooled investment vehicles advised by the investment adviser," FinCEN specifically acknowledged that these entities used by an exempt adviser could themselves satisfy the criteria for an exemption. 87 Fed. Reg. at 59544-45. To the extent an entity serving as a GP or managing member is in scope under the Final Rule, there are multiple potentially applicable exemptions from the reporting obligation. Ownership vehicles that sit above the GPs may not enjoy an exemption, however. ↩

6. Recognizing that the timeframe between the creation of a PIV and its identification on an investment adviser's Form ADV can exceed the Beneficial Ownership disclosure deadline that applies to new entities, FinCEN's final rule expressly exempts PIVs that will be identified on an investment adviser's next annual updating amendment form ADV. ↩

7. The CTA's definition of "political organization" is derived from Section 527(e)(1) of the Internal Revenue Code, which defines political organizations as "a party, committee, association, fund, or other organization (whether or not incorporated) organized and operated **primarily for the purpose of directly or indirectly accepting**

contributions or making expenditures, or both, for an exempt function." An "exempt function" is "the function of influencing or attempting to influence the selection, nomination, election, or appointment of any individual to any Federal, State, or local public office or office in a political organization, or the election of Presidential or Vice-Presidential electors, whether or not such individual or electors are selected, nominated, elected, or appointed." ↩

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Suggested Reading

- 20 July 2023 Award Chambers High Net Worth 2023
- 07 June 2023 Private Investment & Family Office Insights FinCEN Beneficial Ownership Reporting — Implications for Family Offices
- 19 January 2023 Award Top 100 Family Influencers 2022