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The Impact of FinCEN's Beneficial Ownership Regulation on Investment Funds

Client Alert | August 10, 2023

In January 2021, the Corporate Transparency Act came into effect. The law, passed as part of the National Defense Authorization Act, requires millions of U.S. and non-U.S. companies to file information with the Financial Crimes Enforcement Network ("FinCEN") regarding identity of the beneficial owner(s) of the company.[1] In September 2022, FinCEN promulgated a final rule laying out further details of which companies need to report, what information needs to be reported, and by when.[2]

In less than six months, millions of corporate entities in the United States will be required to file beneficial ownership information directly with FinCEN.[3] Specifically, FinCEN's beneficial ownership regulation comes into effect on January 1, 2024. Companies that were in existence prior to that time have one year to comply (*i.e.*, by January 1, 2025), and new companies formed after January 1, 2024 will have 30 days to comply with this new regulation.[4] Further, there are potential civil penalties of $500 per day and criminal penalties of up to $10,000 or 2 years in prison for failure to comply.[5]

While we expect that private investment funds and potentially their subsidiaries will generally be exempt from these reporting requirements pursuant to one of the exemptions set forth below, the existence of these new regulations means that each sponsor should undertake a thorough review of its entire structure, including upper tier parent company entities, special purpose vehicles, special accounts, and other entities which exist within the sponsor's overall corporate structure to identify an applicable exemption for each (if available) or prepare to comply with the new regulation.

The breadth of companies covered by this regulation is quite broad. The regulation covers (a) any domestic corporation or LLC or entity which has filed a document with a Secretary of State (or similar office) and (b) any foreign corporation, LLC, or similar entity that has registered to business in a U.S. state or jurisdiction.[6] Companies that are required to report will have to provide for their "beneficial owners" (defined as those who exercise substantial control over, or own and control at least 25% of the company) information such as legal name, date of birth, address, and an image of a government identification document.[7] And companies created after January 1, 2024 will have to provide similar information for "company applicants," meaning those directly involved in or primarily responsible for the filing that creates the company.[8]

Notably, however, the beneficial ownership regulation contains 23 exemptions for various types of entities. **Some of the exemptions which may be most relevant to our investment funds clients include**:

- Certain SEC Registered Entities—The regulation exempts various entities that have registered with the SEC, including certain securities issuers, broker dealers, and entities registered under the '34 Act.[9]

- Fund Advisers—The regulation also exempts an individual entity that meets the

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definition of an investment advisor or investment company, as well as venture capital fund advisers.[10]

- Pooled Investment Vehicles ("PIVs")—Another exemption covers PIVs operated by, among other entities, broker dealers, investment advisers, and venture capital fund advisers.[11]

- Subsidiaries—Any entity "whose ownership interests are controlled or wholly owned, directly or indirectly," by some—but critically not all—of the other entities that are exempt are also exempt.[12] Notably, for instance, subsidiaries of PIVs are not included as part of this exemption, although PIV subsidiaries may be exempt under other exemptions.

- Large Operating Companies—Another important exemption is for "large operating companies," which are defined as employing more than 20 full time employees in the United States, having an operating presence at a physical office within the United States, and having more than $5 million in gross receipts or sales from sources inside the United States.[13]

Determining whether the beneficial ownership regulation applies requires an entity-by-entity analysis, including for large and complicated corporate structures. For example, while many portfolio and operating companies of a fund may be exempt (e.g., as a large operating company), a holding company that sits above these companies may not qualify for any of the exemptions in the rule. **Because this regulation comes into effect in less than six months, we recommend that our clients begin evaluating which of their entities are required to report and, for those entities, who qualifies as a beneficial owner**.

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Gibson Dunn's lawyers are available to assist with any questions you may have regarding the issues and considerations discussed above, including assisting your organization in conducting the entity-by-entity analysis required by the new rules. Gibson Dunn's Anti-Money Laundering practice group provides legal and regulatory advice to all types of financial institutions and nonfinancial businesses with respect to compliance with federal and state anti-money laundering laws and regulations, including the U.S. Bank Secrecy Act as amended by the USA PATRIOT Act. The group's members have experience as government lawyers with the Department of the Treasury, the U.S. Department of Justice (DOJ), the U.S. Securities and Exchange Commission (SEC), and the U.S. Attorneys' Offices, as well as private practitioners.

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[1] William M. (Mac) Thornberry National Defense Authorization Act for Fiscal Year 2021, H.R. 6395, § 6403.

[2] 31 C.F.R. § 1010.380.

[3] 31 C.F.R. § 1010.380.

[4] 31 C.F.R. § 1010.380(a)(1).

[5] 31 U.S.C. § 5336(h).

[6] 31 C.F.R. § 1010.380(c)(1).

[7] 31 C.F.R. § 1010.380(b)(1).

[8] 31 C.F.R. § 1010.380(b)(1)(iv).

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[9] 31 C.F.R. § 1010.380(c)(2)(i), (vii), (ix).

[10] 31 C.F.R. § 1010.380(c)(2)(x)-(xi).

[11] 31 C.F.R. § 1010.380(c)(2)(xviii).

[12] 31 C.F.R. § 1010.380(c)(2)(xxii).

[13] 31 C.F.R. § 1010.380(2)(xxi).

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