

**NASS Summary: Treasury Department Incorporation Transparency Proposal
April 2010**

Overview: under the Treasury Department proposal, all legal entities formed in the state must have either a documentation agent or a licensed documentation agent. The main difference is that an entity with a documentation agent must provide the state with the beneficial ownership information, whereas an entity with a licensed documentation agent provides the beneficial ownership information to that licensed agent. If the state holds the beneficial ownership information (i.e. a documentation agent is designated), that information may not be disclosed except upon appropriate request, nor may information about the appropriate request be disclosed (except to state employees). These restrictions also apply to the licensed documentation agent if that licensed agent holds the beneficial ownership information.

Regardless of whether a legal entity has a documentation agent or a licensed documentation agent, the entity must provide that agent with a copy of photo identification for each beneficial owner. Each legal entity must file with the state the contact information and notarized signature for either the documentation agent or the licensed documentation agent (depending on which is designated).

The bill does not discuss who (or what entities) can serve as a licensed documentation agent, but it does specify that any state that licenses these agents under state law must subject the agent to (1) registration, (2) minimum licensing requirements for managers and beneficial owners of the agent (identification, criminal history, etc.), (3) ongoing compliance monitoring, and (4) sanctions for noncompliance.

Under the Treasury proposal, legal entities are split into two categories: covered legal entities (corporations, LLCs, LLPs, etc) and exempt legal entities (financial institutions, insurance companies, entities registered with the SEC, etc). Covered legal entities are subject to the procedures described above. While exempt legal entities do not have to provide beneficial ownership information, they still must designate either a documentation agent or a licensed documentation agent, and they must file with the state the contact information and signature of the documentation agent or licensed documentation agent (must be notarized if using a documentation agent). Also, any exempt entity must provide the documentation agent or licensed documentation agent with a copy of photo ID for an officer of the exempt entity.

The bill does not address federal funding for states to implement the new requirements, other than to acknowledge that states have asked for federal funding. Further, it concedes that Congress likely cannot compel states to implement the bill, so it anticipates withholding existing federal funding from any state that does not comply with the bill.

Summary of the Treasury Proposal

I. Definitions

Appropriate Request: an appropriate request is:

- a grand jury subpoena, or a civil, criminal or administrative subpoena;
- summons from a state or federal law enforcement agency;
- an order issued in response to a request for assistance from a foreign country;
- a written request made by the Financial Crimes Enforcement Network

Covered Legal Entity: Any legal entity that is not an exempt legal entity (see below)

Legal Entity: a legal entity is any:

- corporation;
- limited liability company (LLC);
- limited partnership (LP);
- limited liability partnership (LLP) ; or
- any non-US entity qualified to do business in any state

Effective Date: the bill would go into effect on October 1, 2012

Exempt Legal Entity: An exempt legal entity includes:

- an entity that issues securities registered with the SEC or files reports with the SEC;
- an entity formed a state, political subdivision of a state, interstate compact between two states, federal department or agency, or the US Congress;
- a financial institution registered with or regulated by a federal functional regulator or the Commodity Futures Trading Commission, any bank regulated by a State bank regulator, or any insurance company regulated by a state insurance department;
- any legal entity that: (1) has more than 20 full time employees, (2) files tax returns demonstrating more than ten million in annual receipts or sales, and (3) has a U.S. operating presence with a physical street address;
- any legal entity under Section 501(c), 527, or 4947(a)(1) [charitable trust] of US Code Title 26 that (1) has filed either an annual return with the IRS (if required) or (3) has filed an application for recognition of exemption from federal income tax with the IRS (if the exemption has not been denied and the due date for filing the first annual return has not yet passed).
- any entity in which any of the above exempt entities "holds at least a much interest as any other interest holder."

Beneficial Owner¹:

1. The beneficial owner of a covered legal entity includes:

- An individual who, directly or indirectly, has or shares the power to vote or direct the voting of "at least as much of any interest in such covered legal entity as any other individual." An interest in the covered legal entity includes an equity security (for corporations) a voting interest (for LLCs), or a voting right (for partnerships or LLPs).
- In determining the total amount of interest an individual has in the covered legal entity, all direct or indirect interests are combined, including interests held through another legal entity. Indirect interests held by trusts are attributed to the grantor (for revocable trusts) or the trustees (for irrevocable trusts) and indirect interests held by estates are attributed to the executor. Indirect interests held by general partnership are attributed to the general partners based on their right to vote.

and;

2. The individual with the greatest responsibility for managing or directing the regular affairs of the entity.

Documentation Agent: Any individual or entity who acts on behalf of a legal entity to meet the requirements of the bill.

Licensed Documentation Agentⁱⁱ: Any individual or entity that acts on behalf of a legal entity to meet the obligations of the bill and that is licensed under a state law or regulation that subjects the licensed documentation agent to: (1) registration; (2) licensing requirements of the managers and beneficial owners (including identification, physical presence; and absence of certain convictions); (3) effective and regular monitoring for compliance; and (4) sanctions for noncompliance.

II. Covered Legal Entities

After the bill is in effect, any covered legal entity formed in the state must have either a documentation agent or a licensed documentation agent within the US at all times. The information that the covered legal entity must file with the state (including beneficial ownership information) varies depending on which type of agent the covered entity uses.

A. Filing by Covered Entities With a Documentation Agent

If the covered entity designates a documentation agent, the covered entity must provide the state with a beneficial ownership statement that:

- identifies each beneficial owner by name and street address;
- identifies the documentation agent by name and street address; and
- contains a notarized signature of the documentation agent and signatures of each beneficial owner certifying compliance with identification requirements

The state must dissolve any covered entity that fails to comply with the above obligations for 60 consecutive days.

The state must maintain the beneficial ownership information statement for at least 5 years after a covered entity terminates.

B. Filing by Covered Entities with a Licensed Documentation Agent

If the covered entity uses a licensed documentation agent, the covered entity must provide the state with a licensed documentation agent information statement that:

- identifies the licensed documentation agent by name and address and contains his notarized signature; and
- contains a statement signed by the licensed documentation agent certifying compliance with identification requirements

The covered entity must provide the licensed documentation agent with a statement of beneficial ownership signed by each beneficial owner. The licensed documentation agent must sign and notarize the beneficial ownership statement, and must maintain the statement for five years after the covered entity dissolves, or the licensed documentation agent resigns

C. Beneficial Ownership Identification Held by Documentation Agents and Licensed Documentation Agents

Regardless of whether a covered entity uses a documentation agent or licensed documentation agent, the covered entity must provide the agent with a copy of government issued photo ID for each beneficial owner. If the beneficial owner is not a US citizen or permanent US resident, the agent must obtain a copy of the beneficial owner's passport photo and identification number. The agent must maintain the identification documentation for 5 years after the covered entity dissolves, or the agent resigns.

D. Disclosure of Beneficial Ownership Information

Neither the state, the documentation agent, or the licensed documentation agentⁱⁱⁱ may disclose the beneficial ownership information, except upon receipt of an appropriate request. Neither the state nor any its employees may disclose the existence of an appropriate request for beneficial ownership information (except to other employees of the state). Neither the documentation agent nor the licensed documentation agent may disclose the existence of any appropriate request for beneficial ownership information (except as necessary to an agent or employee of the documentation agent).

III. Exempt Legal Entities

After the bill is in effect, any exempt legal entity formed in the state must have a documentation agent or licensed documentation agent within the U.S at all times. All exempt entities must provide the state with an exempt entity statement.

A. Filing by Exempt Entities

The exempt entity must provide the state with an exempt entity statement that:

- identifies the documentation agent or licensed documentation agent by name and address; and
- contains the signature of the documentation agent or the licensed documentation agent stating that the certification and identification requirements have been met [note: if using a documentation agent, the signature must be notarized].

The state must dissolve an exempt entity that fails to comply with the above obligations for 60 consecutive days.

The state must maintain the exempt entity statement for at least 5 years after an exempt entity terminates.

B. Exempt Entity Officer Certification and Identification

The exempt entity must provide the documentation agent or the licensed documentation agent with a notarized certification from an officer of the entity stating the basis for the exemption, and a copy of government issued photo ID. The documentation agent or licensed documentation agent must maintain the certification and identification documentation for at least five years after the exempt entity dissolves or the agent resigns.

IV. Entity Compliance and Updating of Information

A. Legal Entities Formed Before the Effective Date

Each legal entity formed before the effective date of the bill must comply with the requirement of the bill no later than two years after the effective date.

B. Updating of Beneficial Ownership Information

Each covered legal entity must update its beneficial ownership information statement within 60 days of any change in beneficial ownership or beneficial ownership information by providing an amended beneficial ownership information statement to the state (if using a documentation agent) or, if using a licensed documentation agent, to that licensed agent. The covered legal entity must also provide the documentation agent or the licensed documentation agent with updated identification documentation.

C. Transfer of Interest

If a covered legal entity is formed and controlled by a person who has formed ten or more covered legal entities in the state before the effective date of the bill, any transfer by that person of an interest in the covered entity after the effective date is considered a formation of the entity, subject to immediate filing and information requirements (section B above notwithstanding).

D. Updating of Documentation Agent or Licensed Documentation Agent Information

If there is a change by the legal entity, or resignation by a documentation agent or licensed documentation agent, the legal entity must, within 30 days, provide the state with an amended beneficial ownership information statement (if using a documentation agent), an amended licensed documentation agent information statement (if using a licensed documentation agent), or an amended exempt information statement (in the case of an exempt legal entity). A covered entity must provide the new documentation agent or licensed documentation agent with the beneficial owner identification documentation.

In addition to the above requirements, if the documentation agent or licensed documentation agent resigns or changes his name or address, the agent must provide the Secretary of State with a signed statement of change that includes the agent's new name or address, or a statement that he resigns.

E. Updating of Exempt Entity Officer

An exempt legal entity may change the certifying officer by submitting to the documentation agent or licensed documentation agent (1) an amended exempt entity statement, containing the notarized signature of the new certifying officer and (2) a copy of the officer's government photo ID.

F. Compliance Obligations of Non-US Entities

Any non-US entity qualified to do business under the laws of any state is only required to comply with the obligations of the bill in one state.

G. Penalties for Non-Compliance with Beneficial Ownership Requirements

Any person who affects interstate or foreign commerce in any of the ways below is liable for civil penalties of up to ten thousand dollars and up to three years of incarceration:

- knowingly providing false or fraudulent beneficial ownership information to the state, the documentation agent, or the licensed documentation agent
- knowingly providing a copy of false or fraudulent identification to a documentation agent or a licensed documentation agent
- willfully failing to provide updated beneficial ownership information to a state, documentation agent, or licensed documentation agent
- in the case of a documentation agent or licensed documentation agent, willfully failing to obtain or maintain a credible and legible copy of government issued identification of the beneficial owner(s)
- knowingly disclosing the existence of an appropriate request for information except as authorized by the bill

V. Studies and Report

A. State Compliance Report

No later than June 1, 2013, the US Comptroller General must provide Congress with a report identifying states not in compliance with the bill, and identifying what measure must be taken by the states to achieve compliance.

B. Report on Trusts and Uncovered Legal Entities

No later than one year after the enactment of the bill, the Comptroller General must submit a study to the Secretary of the Treasury, the Attorney General, and the Secretary of Homeland Security that includes the following:

- identifies each state with unregistered partnerships, trusts, or other legal entities not addressed in the bill, and the procedures for forming or registering those entities.
- identifies each state that requires partnerships, trusts, or other entities to provide beneficial ownership information
- evaluates whether the lack of available beneficial ownership information for partnerships, trusts, or other legal entities (1) raises concerns about the involvement of these entities in terrorism, money laundering, tax evasion, securities fraud, or other misconduct; and (2) has impeded investigations into entities suspect of such misconduct

- evaluates whether the failure of the US to require beneficial ownership information for partnerships and trusts formed or registered in the US has elicited international criticism and what steps, if any, the US has taken or is planning in response.

C. Report on Effectiveness of Transparent Incorporation Practices

No later than June 1, 2013, the Comptroller General must provide Congress, the Secretary of the Treasury, the Attorney General, and the Secretary of Homeland Security, with a study on the effectiveness of transparent incorporation practices implemented under this bill as it relates to improving the ease of access to and quality, quantity, reliability, and operational security of information required by law enforcement during their investigations.

VI. Explanatory Notes on Funding

The bill notes that states and other stakeholders have argued for federal funding to implement the bill, and that, preliminary estimates of implementation cost average approximately one million dollars per state. The bill also notes that because Congress is generally not constitutionally permitted to compel states to enact or administer a regulatory program, the bill will identify a federal program that provides funding to the states and specify that states that do not comply with the bill will lose a portion of that funding.

VII. Record Keeping and Statistics

Any state or federal law enforcement agency requesting access to beneficial ownership information under this bill must maintain a record of these requests and the results for five years after the request. The Secretary of State must maintain a record of all requests received for a period of five years after the request was received.

COMMENTS

ⁱ Does this mean the individual who has the largest interest, and any other individual who has the same amount? Example: If A has 45%, B has 45%, and C has 10%, A and B would be beneficial owners. Alternatively, does this mean anyone but the smallest investor? Example: If A and B each have 40%, C has 15%, and D has 5%, A, B, and C would be beneficial owners since that have at least as much as D.

ⁱⁱ Does this mean that a lawyer, regulated by the state in this manner, could be considered licensed documentation agents without having to meet any other requirements? Also, if the above is true, does that mean that states would have to establish new rules and procedures to allow someone other than an attorney (e.g. registered agents) to become a Licensed Documentation Agent?

ⁱⁱⁱ Assuming that an attorney could serve as the licensed documentation agent, would this violate confidentiality obligations to a client?