

Who Owns It Anyway? Implications of the Beneficial Ownership Requirements on Structuring Real Estate Transactions

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In this article, the authors explore the implications on structuring real estate transactions in light of the final rule issued on the reporting of beneficial ownership information to FinCEN.

The Financial Crimes Enforcement Network (FinCEN), a bureau of the United States Department of the Treasury, has issued the Final Rule¹ regarding implementation of the reporting of beneficial ownership information to FinCEN under the Corporate Transparency Act of 2019 (the CTA), which is part of the Anti-Money Laundering Act of 2020 (the AMLA). These Regulations,² scheduled to go into effect on January 1, 2024, will affect clients in the real estate investment space who may need to make a report of beneficial ownership information (BOI) for their new as well as their existing investment vehicles.³ In conjunction, FinCEN has released a helpful FAQ guide, which provides further information regarding the requirements.⁴

While real estate companies are generally accustomed to providing beneficial ownership and other sensitive information to financial partners, banks and other lenders to satisfy “know your customer” a/k/a “KYC” requirements, as well as title companies⁵ for the

purpose of “Covered Transactions,”⁶ the CTA regulations may capture a broader number of reporting persons.

WHAT REAL ESTATE VEHICLES WILL BE SUBJECT TO THE RULES?

Starting January 1, 2024, all business entities⁷ are required to report BOI information to FinCEN, including entities formed under the law of a foreign jurisdiction that is registered to do business within the United States, unless one of the 23 entity type exemptions⁸ applies.

Therefore, numerous real estate companies, including those who form individual special purpose entities (SPEs) to acquire, develop, lease and finance real property, may be affected. Unless a specific exemption applies, each such entity will be required to provide BOI to FinCEN.

Many private real estate companies may fall into the “large operating company” exemption

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which provides that entities with a physical U.S. office, more than 20 “full-time” employees and which reported more than \$5 million in gross receipt or sales on its last U.S. federal tax return are exempt. Importantly for real estate companies, the Final Rule notes that companies are not allowed to consolidate employee headcount across affiliated entities, although the revenue test may be calculated on a consolidated basis.

WHO IS A “BENEFICIAL OWNER” UNDER THE CTA?

A “beneficial owner” is defined as someone who directly or indirectly “exercises substantial control over an entity” or owns or controls at least 25% of the reporting entity’s ownership interests. The Final Rule provides three indicators of substantial control:

- (i) Service as a senior officer;
- (ii) Authority over the appointment or removal of any senior officer or dominant majority of the board of directors (or similar body); and
- (iii) Direction, determination, decision-making functions, or substantial influence over important matters of a reporting company.⁹

FinCEN has provided a list of examples of “important decisions,” including, without limitation: compensation, approval of equity issuances or operating budgets and changes to governing documents; the later often being matters reserved to capital joint venture partners and preferred equity providers in real estate private equity transactions. Of note, control can also be found not only through broad representation and ownership, but also

through “rights associated with any financing arrangement or interest.”

Further, the Final Rule specifically includes an expansive definition of “ownership interests,” including, without limitation: equity interests, capital and profit interests, convertible instruments, options, warrants, arrangements related to voting, proprietorship interests, “future conversion of ownership interests” and a catch-all provision which includes “any other instrument, contract, arrangement, understanding, relationship or other mechanism to establish ownership.” Several of the ownership interest categories are relatively straightforward; a few, however, are rather broad and require further guidance from FinCEN so that reporting companies can make an accurate decision regarding which “beneficial owners” to disclose.

WHAT INFORMATION MUST BE REPORTED?

A reporting company’s report to FinCEN must include details of each beneficial owner and each “company applicant” (if applicable) as well as details on the reporting company itself. Specifically, the required reports must include each beneficial owner and each company applicant’s (if applicable) full legal name, date of birth, current residential or business address and a unique identifier from either an acceptable identification document or a previously-assigned FinCEN identifier. The filing must also contain an image of the identification document. Newly formed reporting companies must also provide reports on “company applicants,” which are individuals who file documents that form entities or register them to do business in the United States and “any individual who directs or controls the

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filing of such document by another person.” Again, such matters are often reserved to capital partners in the joint venture context.

WHEN DO REPORTS NEED TO BE FILED?

Reporting companies already in existence prior to January 1, 2024, have one year to file the BOI with FinCEN (i.e., by January 1, 2025). However, all reporting companies newly formed or registered after January 1, 2024, must submit an initial report to FinCEN within 30 calendar days after the date of formation or registration but such report is not only with respect to itself, but also its “company applicants.” It should also be noted that if a previously exempt entity no longer satisfies the exemption criteria, such entity is required to file its report within 30 calendar days after the date on which it no longer meets such criteria (or within the remaining days left in the one-year filing period if it ceases to be exempt during the first year after the effective date, whichever period is longer).

The Final Rule also provides that companies have 30 days “after the date on which there is any change with respect to any information previously submitted to FinCEN.”¹⁰ This 30-day deadline appears to start on the day the change occurs regardless of whether the reporting company has actual or constructive knowledge of the change.

WHAT HAPPENS TO THE INFORMATION?

FinCEN¹¹ is only authorized to disclose BOI collected for two purposes: (i) to facilitate important national security, intelligence and law enforcement activities, and (ii) to confirm BOI provided to financial institutions to facili-

tate their compliance with anti-money laundering and customer due diligence requirements. There are a few instances when FinCEN may disclose BOI to financial institutions to assist with compliance with the existing Customer Due Diligence Rule¹² for financial institutions, but such disclosure requires the reporting company’s consent. Otherwise, BOI is not available to the public and may not be disclosed by FinCEN.

CONCLUSION

Starting January 1, 2024, FinCEN reporting will need to be a checklist item for all new non-public entities or non-exempt entities with the practice of tracing and reporting beneficial ownership being a regular part of the due diligence process for all real estate transactions irrespective of funding sources. However, consideration should start to be given now to ensure reporting companies receive and are able to obtain the specific information required (including for any “company applicants”) to allow compliant reporting under any relevant governance documentation that is put in place on a go-forward basis, and consideration should be given to modifications to existing reporting requirements in real estate joint venture and other entities governance documents.

NOTES:

¹<https://www.federalregister.gov/documents/2022/09/30/2022-21020/beneficial-ownership-information-reporting-requirements>.

²The CTA is found at 31 U.S.C.A. § 5336; the Final Rule will be at 31 C.F.R. § 1010.380 once effective.

³Beneficial ownership reports on entities existing prior to January 1, 2024, are due on January 1, 2025.

⁴https://www.fincen.gov/sites/default/files/shared/BOI_FAQs_FINAL_508.pdf.

⁵Geographic Targeting Order Covering Title Insurance Company, April 29, 2021.

⁶Where residential real property is purchased for an amount of \$300,000 or more without external financing in certain counties of certain U.S. states.

⁷This includes corporations, limited liability companies, limited partnerships and other legal entities created by the filing of a document with a Secretary of State or similar office of a jurisdiction within the United States.

⁸31 C.F.R. § 1010.380(c)(2) once effective.

⁹FinCEN has noted that it broadly defines this last indicator so that an individual who has “substantial influence” over “important decisions” will be deemed to be a

beneficial owner.

¹⁰31 C.F.R. § 1010.380(a)(2) once effective.

¹¹FinCEN is developing a secure cloud-based system for storage of all BOI, which must meet the highest Federal security level.

¹²31 C.F.R. §§ 1010, 1020, 1023, 1024 and 1026; The Customer Due Diligence Rule (CDD Rule) requires covered financial institutions (U.S. banks, mutual funds, brokers or dealers in securities, futures commission merchants and brokers in commodities) to identify and verify the identity of the beneficial owners of legal entity customers who own, control and profit from companies when those companies open accounts.