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FinCEN Seeks Comments on CTA Beneficial Ownership Regulations

On April 5, 2021, the Department of Treasury's Financial Crimes Enforcement Network ("FinCEN") published an advance notice of proposed rulemaking (the "Notice") in the Federal Register to request comments from the public about FinCEN's implementation of the Corporate Transparency Act ("CTA"). The CTA was passed by Congress on January 1, 2021 as part of the National Defense Authorization Act for Fiscal Year 2021 ("NDAA"). Although FinCEN is seeking comments on all aspects of the CTA, it specifically requested responses to a list of questions pertaining to definitions, beneficial ownership reporting, the creation of a unique FinCEN identifier, information security, and administrative matters. Comments in response to the Notice must be submitted on or before May 5, 2021.

As we wrote in July and December of last year, the CTA amends the Bank Secrecy Act ("BSA") to require U.S.-incorporated and U.S.-registered corporations, limited liability companies ("LLCs"), and similar entities ("Reporting Companies") to file information about their beneficial owner(s) and the applicants that helped incorporate or register the Reporting Company. A beneficial owner is defined as any individual who (1) exercises "substantial control" over the entity or (2) owns or controls not less than 25 percent of the ownership interests in the entity. The CTA requires a Reporting Company to report the names, dates of birth, addresses, and passport, driver's license, or other government-issued identification numbers of its beneficial owners and applicants. This disclosure requirement, however, is significantly narrowed by a long list of exceptions to the definition of Reporting Company.

In addition, the CTA requires FinCEN to store the beneficial ownership and applicant information reported to it in a non-public registry. FinCEN may share access to the non-public registry with state, local, or tribal law enforcement authorities if authorized by court order, and freely with federal agencies responsible for national security, intelligence, and law enforcement. In some circumstances, FinCEN may also share the beneficial ownership and applicant information with some federal financial regulators and even foreign authorities.



The CTA requires the Department of Treasury, through FinCEN, to issue regulations governing the procedures and standards for reporting beneficial ownership information, including the creation of a “FinCEN identifier” for each individual or entity that has submitted beneficial ownership or applicant information, by January 1, 2022. According to the Notice, FinCEN “intends to provide a reasonable timeframe for stakeholders to implement the regulations” after the regulations are issued.

As part of this rulemaking process, FinCEN is requesting public comments about the regulations it is drafting to implement the CTA, preferably in the form of responses to a specific list of questions set out in the Notice.

NOTICE OVERVIEW

FinCEN is seeking comments on the following topics for the reporting of beneficial ownership information:

- Prescribing procedures and standards governing reporting of beneficial ownership information and any FinCEN identifier;
- Specifying the information required to be reported and the reporting method;
- Specifying the method for reporting changes in beneficial ownership (for both entities and persons holding FinCEN identifiers); and
- Specifying reporting requirements for exempt subsidiaries and exempt grandfathered entities that cease to be exempt.

In addition, although they are not required to be released by the January 1, 2022 deadline, FinCEN is also seeking comments about the procedures, methods, and standards governing FinCEN’s disclosure of beneficial ownership to other entities (e.g., federal financial regulators or law enforcement agencies) and potential safe harbors. The topics for these procedures, methods, and standards include the following:

- The form and manner in which information shall be provided by FinCEN to a financial institution for customer due diligence, and to certain regulatory agencies for certain purposes;
- Protocols to protect the security and confidentiality of beneficial ownership information, to include obligations on requesting agencies; and
- Establishment of a safe harbor for persons seeking to amend previously submitted but inaccurate beneficial ownership information.

Finally, FinCEN is seeking comments on certain actions that the Secretary is required to take in the process of developing the regulations governing beneficial ownership and applicant information. These actions include:

- Reaching out to members of the small business community and other appropriate parties to ensure efficiency and effectiveness of the process for the entities subject to the requirements of the CTA;
- Establishing partnerships with State, Local, and Tribal governmental agencies;
- Collecting required identity information of beneficial owners through existing federal, state, and local processes and procedures;
- Minimizing burdens on Reporting Companies associated with the collection of the required information, in light of the private compliance costs placed on legitimate businesses, including by identifying any steps taken to mitigate the costs relating to compliance with the collection of information; and



- Collecting the required information in a form and manner that ensures the information is highly useful in (a) facilitating important national security, intelligence, and law enforcement activities, and (b) confirming beneficial ownership information provided to financial institutions in order to facilitate financial institutions' compliance with anti-money laundering (“AML”), countering the financing of terrorism (“CFT”), and customer due diligence (“CDD”) requirements under applicable law.

NOTICE QUESTIONS

The Notice sets out a total of forty-eight questions, many of which contain supplemental questions. Although FinCEN states that it invites comments on all aspects of the CTA, it is specifically seeking comments in response to the forty-eight questions listed in the Notice. The questions are broken into the following five topics:

- Definitions;
- Reporting of Beneficial Ownership Information;
- FinCEN Identifier;
- Security and Use of Beneficial Ownership and Applicant Information; and
- Cost, Process, Outreach, and Partnership.

The full list of questions can be viewed in the Notice or in the Annex to this alert.

NOTABLE QUESTIONS

We provide summaries of some notable questions from the Notice below. We recommend that all interested parties review all of the Notice's questions to assess whether they would like to submit comments.

Under the Definitions section, FinCEN asks several important questions relating to what constitutes a Reporting Company. In particular, FinCEN asks for comments about: (1) how to determine whether an entity is a “similar entity” to a corporation or LLC for purposes of determining whether the entity must report beneficial ownership; (2) whether the definition of “beneficial owner” needs further clarification, including the definition of “substantial ownership”; and (3) whether the numerous exemptions from the definition of “Reporting Company” need further clarification or if additional exemptions should be made. Significantly, FinCEN asks whether the definition of beneficial owner should be aligned with the beneficial ownership requirements that certain “covered financial institutions” must adhere to under current customer due diligence regulations.

Under the Reporting of Beneficial Ownership Information section, FinCEN asks for comments about: (1) the information that should be required as part of beneficial ownership information; (2) the burden of providing and updating the information; (3) how the information should be submitted to FinCEN; and (4) potential safe harbors for Reporting Companies that submit incorrect information.

Under the FinCEN identifier section, FinCEN asks for comments about: (1) the form and function of the FinCEN identifier; and (2) how best to protect the information of individuals and entities with FinCEN identifiers.

Under the Security and Use of Beneficial Ownership and Applicant Information section, FinCEN asks for comments about: (1) how to determine whether an entity is an “appropriate regulatory agency” that is eligible to receive beneficial ownership information from FinCEN; and (2) what measures should be put in place, including penalties, to prevent the misuse of beneficial ownership information.



Under the Cost, Process, Outreach, and Partnership section, FinCEN asks for comments about: (1) the burdens on small businesses caused by the beneficial ownership reporting requirements and how to mitigate those burdens; (2) how FinCEN should contact members of the small business community and financial institutions to “ensure the efficiency and effectiveness of the filing process”; and (3) how FinCEN should use existing federal, state, local, and tribal processes and procedures to acquire beneficial ownership information.

CONCLUSION

The Notice provides interested parties an important opportunity to comment on fundamental aspects of FinCEN's beneficial ownership regulations under the CTA. Interested parties should review the questions in the Notice and take advantage of this opportunity to help FinCEN devise an efficient and effective system to prevent the misuse of corporations, LLCs, and similar entities for illicit purposes while limiting the burdens placed on legitimate entities subject to the CTA's reporting requirements.

ANNEX

DEFINITIONS

1. The CTA requires reporting of beneficial ownership information by “reporting companies,” which are defined, subject to certain exceptions, as including corporations, LLCs, or any “other similar entity” that is created by the filing of a document with a secretary of state or a similar office under the law of a state or Indian tribe or formed under the law of a foreign country and registered to do business in the United States by the filing of such a document.
 - a. How should FinCEN interpret the phrase “other similar entity,” and what factors should FinCEN consider in determining whether an entity qualifies as a similar entity?
 - b. What types of entities other than corporations and LLCs should be considered similar entities that should be included or excluded from the reporting requirements?
 - c. If possible, propose a definition of the type of “other similar entity” that should be included, and explain how that type of entity satisfies the statutory standard, as well as why that type of entity should be covered. For example, if a commenter thinks that state-chartered non-depository trust companies should be considered similar entities and required to report, the commenter should explain how, in the commenter's opinion, such companies satisfy the requirement that they be formed by filing a document with a secretary of state or “similar office.”
2. The CTA limits the definition of reporting companies to corporations, LLCs, and other similar entities that are “created by the filing of a document with a secretary of state or a similar office under the law of a State or Indian Tribe” or “registered to do business in the United States by the filing of a document with a secretary of state or a similar office under the laws of a State or Indian Tribe.”
 - a. Does this language describe corporate filing practices and the applicable law of the states and Indian tribes sufficiently clearly to avoid confusion about whether an entity does or does not meet this requirement?
 - b. If not, what additional clarifications could make it easier to determine whether this requirement applies to a particular entity?
3. The CTA defines the “beneficial owner” of an entity, subject to certain exceptions, as “an individual who, directly or indirectly, through any contract, arrangement, understanding, relationship, or otherwise” either “exercises substantial control over the entity” or “owns or controls not less than 25 percent of the ownership interests of the entity.” Is this



definition, including the specified exceptions, sufficiently clear, or are there aspects of this definition and specified exceptions that FinCEN should clarify by regulation?

- a. To what extent should FinCEN's regulatory definition of beneficial owner in this context be the same as, or similar to, the current CDD rule's definition or the standards used to determine who is a beneficial owner under 17 CFR 240.13d-3 adopted under the Securities Exchange Act of 1934?
 - b. Should FinCEN define either or both of the terms "own" and "control" with respect to the ownership interests of an entity? If so, should such a definition be drawn from or based on an existing definition in another area, such as securities law or tax law?
 - c. Should FinCEN define the term "substantial control"? If so, should FinCEN define "substantial control" to mean that no reporting company can have more than one beneficial owner who is considered to be in substantial control of the company, or should FinCEN define that term to make it possible that a reporting company may have more than one beneficial owner with "substantial control"?
4. The CTA defines the term "applicant" as an individual who "files an application to form" or "registers or files an application to register" a reporting company under applicable state or tribal law. Is this language sufficiently clear, in light of current law and current filing and registration practices, or should FinCEN expand on this definition, and if so how?
 5. Are there any other terms used in the CTA, in addition to those the CTA defines, that should be defined in FinCEN's regulations to provide additional clarity? If so, which terms, why should FinCEN define such terms by regulation, and how should any such terms be defined?
 6. The CTA contains numerous defined exemptions from the definition of "reporting company." Are these exemptions sufficiently clear, or are there aspects of any of these definitions that FinCEN should clarify by regulation?
 7. In addition to the statutory exemptions from the definition of "reporting company," the CTA authorizes the Secretary, with the concurrence of the Attorney General and the Secretary of Homeland Security, to exempt any other entity or class of entities by regulation, upon making certain determinations.[53] Are there any categories of entities that are not currently subject to an exemption from the definition of "reporting company" that FinCEN should consider for an exemption pursuant to this authority, and if so why?
 8. If a trust or special purpose vehicle is formed by a filing with a secretary of state or a similar office, should it be included or excluded from the reporting requirements?
 9. How should a company's eligibility for any exemption from the reporting requirements, including any exemption from the definition of "reporting company," be determined?
 - a. What information should FinCEN require companies to provide to qualify for these exemptions, and what verification process should that information undergo?
 - b. Should there be different information requirements for operating companies and holding companies, for active companies and dormant companies, or are there other bases for distinguishing between types of companies?
 - c. Should exempt entities be required to file periodic reports to support the continued application of the relevant exemption (e.g., annually)?



REPORTING OF BENEFICIAL OWNERSHIP INFORMATION

10. What information should FinCEN require a reporting company to provide about the reporting company itself to ensure the beneficial ownership database is highly useful to authorized users?
11. What information should FinCEN require a reporting company to provide about the reporting company's corporate affiliates, parents, and subsidiaries, particularly given that in some cases multiple companies can be layered on top of one another in complex ownership structures?
12. Should a reporting company be required to provide information about the reporting company's corporate affiliates, parents, and subsidiaries as a matter of course, or only when that information has a bearing on the reporting company's ultimate beneficial owner(s)?
13. What information, if any, should FinCEN require a reporting company to provide about the nature of a reporting company's relationship to its beneficial owners (including any corporate intermediaries or any other contract, arrangement, understanding, or relationship), to ensure that the beneficial ownership database is highly useful to authorized users?
14. Persons currently obligated to file reports with FinCEN overwhelmingly do so electronically, either on a form-by-form basis or in batches using proprietary software developed by private-sector technology service providers.
 - a. Should FinCEN allow electronic filing of required information about reporting companies (including the termination of such companies), beneficial owners, and applicants under the CTA?
 - b. Should FinCEN allow or support any mechanisms other than direct electronic filing?
 - c. Should FinCEN allow or support direct batch filing of required information?
 - d. Should there be any differences among the mechanisms used for different types of information or different types of filers?
 - e. Should any additional or alternative reporting system involve the collection of information from the states and Indian tribes, and if so how?
 - f. Should the filing mechanisms for reporting companies be different for entities that were previously exempt for one reason or another (including exempt subsidiaries and exempt grandfathered entities under section 5336(b)(2)(D) and (E)) and lose that exemption? If so how?
15. Section 5336(b)(2)(C) requires written certifications to be filed with FinCEN by exempt pooled investment vehicles described in section 5336(a)(11)(B)(xviii) that are formed under the laws of a foreign country.
 - a. By what method should these certifications be filed?
 - b. What information should be included in these certifications?
 - c. Should there be a mechanism through which such filings could be made to foreign authorities and forwarded to FinCEN, or should such filings have to be made directly to FinCEN?
 - d. What information should be included in these certifications (e.g., what information would allow authorities to follow up on certifications containing false information)?
 - e. Should these certifications be accessible to database users, and if so, should they be accessible on the same terms as beneficial ownership information of reporting companies?



16. What burdens do you anticipate in connection with the new reporting requirements? Please identify any burdens with specificity, and estimate the dollar costs of these burdens if possible. How could FinCEN minimize any such burdens on reporting companies associated with the collection of beneficial ownership information in a manner that ensures the information is highly useful in facilitating important national security, intelligence, and law enforcement activities and confirming beneficial ownership information provided to financial institutions, consistent with its statutory obligations under the CTA?
17. Section 5336(e)(1) requires the Secretary to take reasonable steps to provide notice to persons of their reporting obligations.
 - a. What steps should be taken to provide such notice?
 - b. Should those steps include direct communications such as mailed notices, and if so to whom should notices be mailed?
 - c. What type of information should be included in such a notice, for example, the purposes and uses of the data, and how to access and correct the information?
 - d. Should the notice be followed by an explicit acknowledgement of the reporting company, or consent of the beneficial owner or applicant if the owner or applicant is submitting the information, to the handling of beneficial ownership information as stated in the notice and applicable law?
18. Section 5336(e)(2) requires states and Indian tribes, as a condition of receiving certain funds, to have their Secretary of State or a similar office in each state or Indian tribe periodically provide notice of reporting obligations and a copy of, or internet link to, the reporting company form created by FinCEN.
 - a. How should this requirement be implemented?
 - b. What form should the notice take?
 - c. Should this notice be provided yearly, or on some other periodic schedule?
19. What should reporting companies or individuals holding FinCEN identifiers be required to do to satisfy the requirement of section 5336(b)(1)(D) that they update in a timely manner the information they have submitted when it changes, such as when beneficial owners or holders of FinCEN identifiers (i) transfer substantial control to other individuals; (ii) change their legal names or their reported residential or business street addresses; or (iii) die; or (iv) when a previously acceptable identification document expires? For example, should the reporting companies or individuals be required to file a new report, or provide notice only of the information that has changed?
20. Should reporting companies be required to affirmatively confirm the continuing accuracy of previously submitted beneficial ownership information on a periodic basis (e.g., annually)? How should such confirmation be communicated to FinCEN?
21. For those reporting companies without FinCEN identifiers, what should be considered a “timely manner” [54] for updating a change in beneficial ownership?
 - a. Should this period differ based on the type of reporting company?
 - b. What factors should be taken into account in determining this period?
 - c. How much time should reporting companies be given to update beneficial owner information upon a change of ownership?
 - d. What are the benefits or drawbacks of allowing a longer period to report a change of beneficial ownership?



22. Section 5336(h)(3)(C) contains a safe harbor for persons who seek to correct previously submitted but inaccurate beneficial ownership information pursuant to FinCEN regulations. How should FinCEN's regulations define the scope of this safe harbor? Should the nature of the inaccuracy (e.g., a misspelled address versus the complete omission of a beneficial owner) be relevant to the availability of the safe harbor?
23. What steps should reporting companies be required to take to support and confirm the accuracy of beneficial ownership information?
 - a. Should reporting companies be required to certify the accuracy of their information when they submit it?
 - b. If so, what should this certification cover?
 - c. Should reporting companies be required to submit copies of a beneficial owner's acceptable identification document?
24. What steps should FinCEN take to ensure that beneficial ownership information being reported is accurate and complete?
 - a. With respect to other BSA reports, FinCEN e-filing protocols prohibit filings from being made with certain blank fields, and automatically format certain fields to ensure that letters are not entered for numbers and vice versa, etc. The filing protocols, however, do not involve independent FinCEN verification of information filed. Should FinCEN take similar or additional steps in connection with the filing of beneficial ownership information?
 - b. If so, what similar or additional steps should FinCEN take?
25. Should a reporting company be required to report information about a company's "applicant" or "applicants" (the individual or individuals who file the application to form or register a reporting company) in any report after the reporting company's initial report to FinCEN? Why or why not?

FINCEN IDENTIFIER

26. In what situations will an individual or entity wish to use the FinCEN identifier? How can FinCEN best protect both the privacy interests underlying an individual's or entity's desire to use the FinCEN identifier, and the identifying information that must be provided to FinCEN by an individual or entity wishing to obtain and use the FinCEN identifier?
27. What form should the FinCEN identifier take?
 - a. How long should it be?
 - b. Should it be alphabetical, numeric, or alphanumeric?
 - c. Should it contain embedded information such as a filing year, a geographic code, a sequential number, or numbers shared among related persons or entities, or should it be generated independently for each individual or entity?
 - d. Should it resemble or be derived from another identifier provided by another authority?
 - e. Should it resemble the document numbers of other reports filed with FinCEN under the BSA?
 - f. Should the form of FinCEN identifiers for individuals and legal entities be different? If so, how and why?



28. How can FinCEN best ensure a one-to-one relationship between individuals or entities and their FinCEN identifiers, in light of the possibility that individuals and entities may mistakenly or intentionally attempt to apply for more than one FinCEN identifier? [55]
29. How can FinCEN best protect FinCEN identifiers from being used without individuals' and entities' authorization? Should protections include specific regulatory requirements or prohibitions?
30. As noted in the CTA, in some cases multiple companies can be layered on top of one another in complex ownership structures. Given that there may be multiple entities within an ownership structure of a reporting company that are identified by FinCEN identifiers, how can FinCEN implement the FinCEN identifier in a way that reduces the burden to financial institutions of using the FinCEN database when reporting companies with complex ownership structures seek to open an account?
31. What should the process be to obtain a FinCEN identifier?
 - a. Should the FinCEN identifier be secured by an applicant or beneficial owner prior to filing an application to form a corporation, LLC, or other similar entity under the laws of a state or Indian tribe?
 - b. How, if at all, should FinCEN verify an individual's identity before providing a FinCEN identifier?
 - c. If an applicant or beneficial owner chooses not to apply for a FinCEN identifier, should FinCEN create any limitations—in addition to those in the statutory definition of “acceptable identification document”—on the types of unique identifying numbers that can be submitted?

SECURITY AND USE OF BENEFICIAL OWNERSHIP AND APPLICANT INFORMATION

32. When a state, local, or tribal law enforcement agency requests beneficial ownership information pursuant to an authorization from a court of competent jurisdiction to seek the information in a criminal or civil investigation, how, if at all, should FinCEN authenticate or confirm such authorization?
33. Should FinCEN provide a definition or criteria for determining whether a court has “competent jurisdiction” or has “authorized” such an order? If so, what definition or criteria would be appropriate?
34. As a U.S. Government agency, FinCEN is subject to strict security and privacy laws, regulations, and other requirements that will protect the security and confidentiality of beneficial ownership and applicant information. What additional security and privacy measures should FinCEN implement to protect this information and limit its use to authorized purposes, which includes facilitating important national security, intelligence, and law enforcement activities as well as financial institutions' compliance with AML, CFT, and CDD requirements under applicable law? Would it be sufficient to make misuse of such information subject to existing penalties for violations of the BSA and FinCEN regulations, or should other protections be put in place, and if so what should they be?
35. How can FinCEN make beneficial ownership information available to financial institutions with CDD obligations so as to make that information most useful to those financial institutions?
 - a. Please describe whether financial institutions should be able to use that information for other customer identification purposes, including verification of customer information program information, with the consent of the reporting company?
 - b. Please describe whether FinCEN should make financial institution access more efficient by permitting reporting companies to pre-authorize specific financial institutions to which such information should be made available?



- c. In response to requests from financial institutions for beneficial ownership information, pursuant to 31 U.S.C. 5336(c)(2)(A), what is a reasonable period within which FinCEN should provide a response? Please also describe what specific information should be provided.
36. How should FinCEN handle updated reporting for changes in beneficial ownership when beneficial ownership information has been previously requested by financial institutions, federal functional regulators, law enforcement, or other appropriate regulatory agencies?
- a. If a requestor has previously requested and received beneficial ownership information concerning a particular legal entity, should the requester automatically receive notification from FinCEN that an update to the beneficial ownership information was subsequently submitted by the legal entity customer?
- b. If so, how should this notification be provided?
- c. Should a requesting entity have to opt in to receive such notification of updated reporting?
37. One category of authorized access to beneficial ownership information from the FinCEN database involves “a request made by a Federal functional regulator or other appropriate regulatory agency.” [56] How should the term “appropriate regulatory agency” be interpreted? Should it be defined by regulation? If so, why and how?
38. In what circumstances should applicant information be accessible on the same terms as beneficial ownership information (i.e., to agencies engaged in national security, intelligence, or law enforcement; to non-federal law enforcement agencies; to federal agencies, on behalf of certain foreign requestors; to federal functional regulators or other agencies; and to financial institutions subject to CDD requirements). If financial institutions are not required to consider applicant information in connection with due diligence on a reporting company opening an account, for example, should a financial institution's terms of access to applicant information differ from the terms of its access to beneficial ownership information?

COST, PROCESS, OUTREACH, AND PARTNERSHIP

39. What specific costs would CTA requirements impose—in terms of time, money, and human resources—on small businesses? Are those costs greater for certain types of small businesses than others? What specifically can FinCEN do to minimize those costs, for all small businesses or for some types in particular?
40. Are there alternatives to a single reporting requirement for all reporting companies that could create a less costly alternative for small businesses?
41. How can FinCEN best reach out to members of the small business community to ensure the efficiency and effectiveness of the filing process for entities subject to the requirements of the CTA?
42. Are there other business constituencies to which FinCEN should reach out, and if so, who are they?
43. How can FinCEN best reach out to financial institutions to ensure the efficiency and effectiveness of the process by which financial institutions could potentially access the beneficial ownership information held by FinCEN?
44. What burdens would CTA requirements impose on state, local, and tribal governmental agencies? In particular, what additional time, money, and human resources would state, local, and tribal governments have to secure and expend—or reallocate from other duties, and if the latter what duties would be compromised or services impaired? How, if at all, would any of these burdens or allocations of time or money vary according to the size or other characteristics of a jurisdiction—would smaller jurisdictions find it easier or harder to handle the costs associated with CTA requirements?



45. How should FinCEN minimize any burdens on state, local, and tribal governmental agencies associated with the collection of beneficial ownership information, while still achieving the purposes of the CTA?
46. How can FinCEN best partner with state, local, and tribal governmental agencies to achieve the purposes of the CTA?
47. How can FinCEN collect the identity information of beneficial owners through existing Federal, state, local, and tribal processes and procedures?
 - a. Would FinCEN use of such processes or procedures be practicable and appropriate?
 - b. Would FinCEN use of or reliance on existing processes and procedures help to lessen the costs to state, local, and tribal government agencies, or would it increase those costs?
 - c. Would FinCEN use of existing Federal, state, local, and tribal processes and procedures help to lessen the costs to small businesses affected by CTA requirements, or would it increase those costs?
48. The process of forming legal entities may have ramifications that extend beyond the legal and economic consequences for legal entities themselves, and the reporting of beneficial ownership information about legal entities may have ramifications that extend beyond the effect of mobilizing such information for AML/CFT purposes. How can FinCEN best engage representatives of civil society stakeholders that may not be directly affected by a beneficial ownership information reporting rule but that are concerned for such larger ramifications?

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