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Portfolio Company Reporting Under the Corporate Transparency Act

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In Private Equity, a Portfolio Company (PortCo) is a company in which an investing entity, such as a private equity fund, venture capital firm, buyout firm, or holding company owns or has the right to acquire equity. The use of an operating company or PortCo is a standard method for private equity and venture capital funds, and fundless sponsors to deploy capital.

Beginning in 2024, PortCos will need to understand and be ready to add new reporting requirements to their list of deliverables once the Corporate Transparency Act (CTA) and its implementing regulations take effect (31 U.S.C. §§5336 and 31 C.F.R. §1010.380).

The Corporate Transparency Act

As part of the National Defense Authorization Act of 2020, Congress passed the CTA to increase visibility into entity structures and ownerships, in order to foster the public policy objectives of combatting money laundering, tax fraud and other nefarious activities.

Are portfolio companies “reporting companies” under the CTA?

By way of overview, the CTA intends for the creation of a semi-private database maintained by the Treasury Department’s Financial Crimes Enforcement Network (FinCEN). This database is to be populated with information submitted by legal entities themselves, if they are a “reporting company,” identifying the entities, such entity’s beneficial owners and its associated company applicants as we describe below.

A “reporting company” is a corporation, limited liability company, or other entity created by the filing of a document with a secretary of state or any similar office under the law of a state or Indian tribe. Foreign entities also can be reporting companies.

While the CTA's scope is purposefully broad, there are numerous statutory exemptions. As a rule of thumb, most entities already regulated by a prudential regulator, such as the U.S. Securities and Exchange Commission (SEC), will be exempt from the CTA's disclosure requirements, while most small to medium-sized businesses must comply with the CTA and thus shoulder the burden of disclosing.

Many PortCos will be reporting companies under the CTA. A typical PortCo will fall within the CTA's broadly thrown statutory net covering legal entities and many are structured such that one of the CTA's exemptions will not apply, although all the exemptions should be examined carefully. There are 23 statutory exemptions and a couple of informal ones. By way of examples, two statutory exemptions are noteworthy.

Noteworthy statutory exemption

One is the "large operating company" exemption which covers PortCos with 20 or more employees operating at a physical location in the United States and whose prior year's tax filings reported gross receipts or sales in excess of \$5 million. There also are statutory exemptions for certain investment companies, provided they are SEC-registered and meet Section 3's definition under the Investment Company Act of 1940 (the "Act"), and for venture capital fund advisers, provided they have filed Form ADV (or a successor of that form) with the SEC.

By way of "indirect" exemptions, a PortCo wholly owned and operated by another CTA-exempt entity should be able to avoid disclosure to FinCEN under the CTA. Further, an inactive PortCo, as described in the Act's implementing regulations, also may be excused from disclosure. The devil is in the details, of course, so careful study of the details of each exemption is warranted.

While this related topic warrants more discussion in a subsequent article, we foresee that opinion practice is likely to change as counter-parties revise their requirements covering CTA compliance, including potential warranties from legal advisors of an exemption's applicability should a PortCo not disclose.

Who must report? What is reported?

Each reporting company will be required to make its CTA disclosures to FinCEN. FinCEN announced the filings will be electronically (only) submitted through the BOSS system (Beneficial Ownership Secure System), which is currently in development. The three categories of disclosures relate to information about the entity itself, the entity's beneficial owners and, as applicable, the associated company applicant(s).

A "Beneficial Owner" is defined as any individual who directly or indirectly (a) exercises substantial control over a reporting company; or (b) owns or controls at least 25% of the ownership interests of a reporting company.

Interpretation of this aspect of the CTA remains in flux; however, "substantial control" generally means those individuals who:

- serve as a senior officer;
- have authority over the appointment or removal of senior officers (or similar authority concerning a majority of the entity's governing directors);
- direct or has material influence over the entity's important decisions; and
- have any other form of substantial control over the reporting company.

As can be imagined, this "substantial control" inclusion is a rabbit hole that remains for further development, implementing regulations and FAQs, all of which are promised by FinCEN. But importantly, unlike the Bank Secrecy Act's beneficial ownership analysis which limits the "control" person to a single individual, the CTA envisions the disclosure of multiple persons whenever each has substantial control.

For those beneficial owners of a reporting company, the following five items must be disclosed to FinCEN:

- The individual's name;
- Date of birth;

- Current residential or business street address (which cannot be a P.O. Box or registered agent address);
- A unique identifying number and issuing jurisdiction of an acceptable form of personal identification, such as a driver's license or passport; and
- An image of the identification document used for the above supplied information.

Reporting companies also must disclose to FinCEN its "company applicants" if the reporting company is formed after Jan. 1, 2024. A "company applicant" will be either, or both, the individual who created the documents governing the entity and individual who filed the formation documents. This can mean that the attorney who drafted the articles of incorporation, for example, and the paralegal who files the articles with a secretary of state's office, so that both will be company applicants. However, if a reporting company was formed prior to Jan. 1, 2024, the company applicant does not need to be disclosed.

Since PortCos rarely have language in place in their governance documents or equity purchase agreements that create an obligation to provide the information now required by the CTA, amendments should be made to allow the PortCo to be fully compliant with the filing requirements.

When to file and how often?

For reporting companies formed prior to Jan. 1, 2024, the CTA requires the FinCEN filing to be made during the calendar year of 2024, but no later than Jan. 1, 2025. If a reporting company is formed after Jan. 1, 2024, then its disclosures must be made within 30 days of its formation, generally the date of its filing with a secretary of state's office. Please note, however, that FinCEN has applied to extend this 30-day deadline for newly formed entities to 90 days.

The CTA imposes continuous compliance burdens. Specifically, if any of the information previously reported to FinCEN changes, then a revised (updated) filing must be made by the reporting company

within 30 days. For example, if a PortCo, which is a reporting company, experiences a change in executive leadership or should a material investor change addresses or their name, then FinCEN updated filings must be timely made.

Conclusion

Ready or not, the CTA will soon impose material new compliance burdens on many businesses. Per FinCEN's estimates, over 36 million reporting companies are expected to file in 2024 alone. Unlike many other federal business statutes, the compliance burden largely will be borne by small to medium-sized businesses, as the larger entities likely will find a qualifying exemption. While the CTA is now the law of the land, the very important matters of the creation of its implementing regulations remain a work in progress. For PortCos, the CTA warrants close attention as its deadlines draw near.

For more information, contact the authors or any attorney with Frost Brown Todd's [Private Equity](#) or [Corporate Transparency Act](#) teams.

Frost Brown Todd's Corporate Transparency Act Team is staying up to date on the important rule changes that will likely have significant impacts on your business operations. Click below to read the latest information about the Corporate Transparency Act.

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- [**Reporting Under the Corporate Transparency Act – Is My Company Exempt?**](#)
- [**FinCEN Announces Proposed Solution to Disclosure Dilemma in the Corporate Transparency Act**](#)
- [**Portfolio Company Reporting Under the Corporate Transparency Act**](#)

- [***The Corporate Transparency Act: Considerations for Effectively Using the FinCEN Identifier***](#)
- [***The Corporate Transparency Act's Impact on the Real Estate Industry: What You Need to Know to Comply***](#)
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