The Daily Dish

A Head Fake on Beneficial Ownership

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If you are like me (and let us pray that you are not), you've been waiting for the financial services regulatory apparatus to spring to life. One might have thought that with the change of administration, there would be a flurry of activity, but thus far it has been quiet. So, I got an adrenaline rush when the AAF regulatory folks flagged a proposed rule from the Treasury on "Section 6403. Corporate Transparency Act." What could this be?

The complete answer is in Thomas Wade's pithily titled "Treasury Proposes Beneficial Ownership Reporting Requirements to Crack Down on Shell Companies." The short version is that the Department of Treasury's Financial Crimes Enforcement Network (FinCEN) is proposing a rule that requires (for the first time) some companies to report beneficial ownership data to FinCEN in order to help prevent bad actors from using shell companies in the course of tax evasion, terrorism financing, and other misdeeds.

For the unindoctrinated, "A beneficial owner is any person or group of people (not, however, a company) that enjoys the benefits of ownership even though the title to some form of property (for example, securities or real estate) is held in another's name. Beneficial ownership is distinct from legal ownership, although they will usually be the same person. … Beneficial ownership is typically defined as an individual who has 'substantial control' over an organization or who owns at least 25 percent."

I quickly envisioned an inordinately expensive, massive database at FinCEN that would be a target for hackers, a compliance nightmare, and a modest additional benefit over the existing systems for anti-money laundering (AML) regulations. (For a primer on AML regulation, see here.) But as Wade notes, the rule has exemptions that one can drive a truck through: "First, the rule would exclude 23 types of entities, including banks, insurers, brokers, and investment advisors; second, the rule would exclude entities with at least either 20 full-time employees in the Unites States or $5 million in gross receipts or sales," although as Wade points out this is perhaps not surprising given the target of the law is the bad faith owners and operators themselves rather than their financiers.

All the more strange, then, that despite the fact that the scope is quite narrow, the costs are significant. The first year cost is put at $1.26 billion and requires 33 million paperwork hours. That’s a lot of cost for a relatively small number of actors to provide their reports. Even worse, at this juncture we have no idea how FinCEN will use the reports, and since the reports are confidential, only FinCEN and law enforcement can use the reports.

So, after the long wait, and with the caveat that the rule will change in response to public comment, the proposed rule is full of surprises: surprisingly circumscribed, surprisingly costly, and potentially (un)surprisingly pointless.