Updates

As discussed in our prior Update on the Corporate Transparency Act (CTA), anyone who owns or controls at least 25% of the ownership interests of a CTA reporting company must report their beneficial ownership to the Financial Crimes Enforcement Network (FinCEN).

However, the CTA reporting rule also provides that "beneficial ownership" includes an ownership interest through joint ownership with one or more other persons of an undivided interest in such ownership interest (*see* 31 CFR 1010.380(d)(2)(ii)(A)). This joint ownership language likely captures property, including ownership interests in legal entities, that is held jointly by spouses in a "community property" state. A community property state generally treats all assets and debts acquired during a marriage as equally owned by both spouses. Therefore, to the extent such ownership constitutes community property in the state where they reside, this will likely require the spouses of owners of at least 25% of the ownership interests of a CTA reporting company to report their beneficial ownership as a joint ownership interest.

FinCEN has not specifically addressed how the joint ownership provision in the CTA reporting rule covers "community property." However, it appears the issue was raised in comments to the proposed regulations governing CTA reporting, and FinCEN chose not to amend the definition of "joint ownership" triggering reporting. Additional clarity from FinCEN may be forthcoming, but for the time being, it seems that those responsible for reporting under the CTA should take care to include community property ownership as a potential trigger for inclusion of additional beneficial owners.

Where Do These Rules Apply?

As of the current publication date, there are nine states that observe community property laws: Arizona, California, Idaho, Louisiana, Nevada, New Mexico, Texas, Washington, and Wisconsin. In addition, there are several common-law states that permit limited adoption by agreement or trust into the community property system. Alaska, South Dakota, Tennessee, Florida, and Kentucky have adopted a community property system, but it is optional. In Alaska, spouses may create community property by entering into a community property agreement or by creating a community property trust.[1] In South Dakota, property held in a special spousal trust becomes community property if the trust expressly declares that property transferred is South Dakota special spousal property.[2] Tennessee also has adopted an optional community property system.[3] In addition, Florida and Kentucky permit spouses to opt into community property laws via trusts.[4]

There are four community property states (California, Nevada, New Mexico, and Washington) that specifically cover domestic partners that will similarly result in joint beneficial ownership reporting for domestic partners under the CTA reporting rule.

How Can CTA Reporting Companies Navigate Community Property Interests?

Given the complexity of these rules and the newness of the CTA reporting regime, the analysis of whether ownership interests constitute community property or joint ownership must be done on a state-by-state and case-by-case basis, as state laws, and circumstances, including joint ownership scenarios, vary widely. There are many exceptions and circumstances in which property can be owned in these states in ways that do not constitute "community property" or "joint ownership" for purposes of the CTA.

In light of the nuances, it is important to consider an individual's state of residence and status of the applicable ownership interests as community property when determining whether such individual and/or their spouse/domestic partner are required to be reported as beneficial owners for purposes of the CTA filing requirements. [T(4] [IL(5] [SA((6]

Notably, in many circumstances, it may be extraordinarily difficult for a CTA reporting company to come to a conclusion regarding whether or not community property rules apply to a particular scenario. As such, CTA reporting companies may need to rely on representations from beneficial owners regarding the status of their ownership interest under potentially applicable community property rules. In this regard, it may be prudent for CTA reporting companies to ask beneficial owners to certify the extent to which their ownership interests in the entity are held as community property. In the absence of any red flags suggesting such certification is false (or actual knowledge that it is or may be false), a confirmation of this nature will be a powerful tool to demonstrate good faith in reporting, particularly if regulators later question a CTA filing made in reliance on a beneficial owner's representation regarding joint ownership (through community property or otherwise).

Also, note that the joint ownership/community property analysis does not apply to the "substantial control" prong of beneficial ownership for purposes of the CTA. Therefore, if a person is a beneficial owner solely by virtue of being an executive officer, director, or other person with "substantial control" other than by ownership interest, their spouse or domestic partner **would not** also need to report as a beneficial owner under the CTA.

Where To Get More Information

For more information regarding CTA reporting, see our quick reference to the new beneficial ownership reporting requirements under the CTA and our more detailed Update on the subject. Also, see FinCEN's FAQs and Reference Materials on the CTA. Starting January 1, 2024, CTA reports can be filed, and FinCEN identifiers can be obtained on FinCEN's main CTA page.

Endnotes

[1] Alaska Stat. §§ 34.77.020 - 34.77.995.

[2] SD. ST. § 55-17.

[3] TN. ST. §[T(1] [IL(2] [SA((3] 35-17. *See*, IRS Internal Revenue Manual § sec. 25.18.1.2.3. (May 3, 2023).

[4] Fla. Stat. §§ 736.1501-1512, KY Rev. Stat. § 386.622.

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