

THOUGHT LEADERSHIP

LEGAL UPDATES

PUBLISHED: MARCH 12, 2024

Services

Corporate
Corporate
Transparency Act
(CTA)

Professionals

YUEFAN WANG
DENVER:
303.749.7200
YUEFAN.WANG@
HUSCHBLACKWELL.COM

MATTI MORTIMORE
MILWAUKEE:
414.978.5659
MATTI.MORTIMORE@
HUSCHBLACKWELL.COM

The Corporate Transparency Act Is Unconstitutional—But Not for You

On Friday March 1, 2024, the U.S. District Court for the Northern District of Alabama in *NSBA v. Yellen* ruled that the Corporate Transparency Act (CTA) is unconstitutional because it cannot be justified as an exercise of Congress' enumerated powers. The Financial Crimes Enforcement Network (FinCEN), which administers the CTA, responded on Monday, March 4, 2024, by issuing a notice emphasizing the narrow applicability of the court's ruling.

The ruling in *NSBA v. Yellen* represents a major and timely disruption to the ongoing rollout of the CTA, the first deadline of which arrives at the end of March for some entities. FinCEN estimates more than 32 million entities will need to report this year with millions each year afterwards.

For more information on the CTA, please see our Guide to the Corporate Transparency Act.

The case

The plaintiffs in *NSBA v. Yellen*, the National Small Business Association (NSBA), a small business advocacy group, sued the U.S. Treasury Department, claiming that the CTA's mandatory reporting requirements violate the First, Fourth, and Fifth Amendments of the Constitution and exceed Congress's authority under Article I of the Constitution. However, because the court agreed that the CTA exceeds Congress's legislative authority, it declined to rule on whether it also violates the First, Fourth, and Fifth Amendments.

It should be noted that the CTA has an outsized effect on small businesses, since there is an exemption to the CTA for "large operating entities," which is why the NSBA was an ideal plaintiff to bring this case. More information on the exemptions under the CTA are available in our Guide to the Corporate Transparency Act.

In its defense, the government argued that Congress has the power to enact the CTA for three reasons:

Foreign Affairs and National Security

Commerce Clause Authority

Taxing Powers

Foreign affairs and national security

Treasury argued that both Congress and the executive branch agree that the collection of Beneficial Ownership Information, as elaborated in the CTA, is to “better enable critical national security, intelligence, and law enforcement efforts to counter money laundering, the financing of terrorism, and other illicit activity.” Although the court noted this was a laudable goal, it held that “even in the pursuit of sensible and praiseworthy ends, Congress sometimes enacts smart laws that violate the Constitution.” The court found that Congress cannot regulate state-created entities under the Foreign Affairs powers “absent a clear indication from Congress,” which in this case does not exist.

Commerce clause authority

Although Treasury argues the CTA regulates the channels and instrumentalities of interstate commerce, the court notes that the CTA applies to reporting companies that are created by the filing of a document with the secretary of state or similar office, and nowhere in the CTA does the word “commerce,” or references to any channel or instrumentality, appear. The court also noted that the U.S. Supreme Court has always held that Congress does not have the authority under the Commerce Clause to regulate non-commercial, intrastate activity even when certain entities use commerce in their operations to “affect interstate and foreign commerce.” Finally, the Court also held that the CTA lacks the jurisdictional hook that Congress knows how to include when it intends legislation to deal with matters “affecting commerce.” Here the complete lack of that phrase or a similar one makes it impossible for a court to read that language into the CTA.

Taxing powers

The government argued that the CTA is constitutional because the regulations are sufficiently “incidental” to the taxing power. The Court found that such “unfettered legislative power ‘is in no way an authority that is ‘narrow in scope,’ or ‘incidental’ to the exercise of the commerce power...’ [and even if] the CTA’s provisions were ‘necessary,’ ‘such an expansion of federal power is not a ‘proper’ means for making those [policy goals] effective.’”

FinCEN response

On March 4, 2024, FinCEN issued an official notice responding to the ruling in the case. The notice provides that FinCEN will comply with the court's order and "is not currently enforcing the [CTA] against the plaintiffs in the action...*those individuals and entities* [emphasis added] are not required to report beneficial ownership information to FinCEN at this time."

The notice implies, but does not explicitly state, that FinCEN will continue enforcing the CTA against everyone else not specifically a plaintiff in *NSBA v. Yellen*.

U.S. Treasury appeals

On March 11, 2024, Treasury appealed the court's ruling to the United States Court of Appeals for the Eleventh Circuit. We will continue to monitor and provide updates as this case develops.

What this means to you

As of now, the CTA is only unconstitutional as applied to members of the NSBA as of March 1, 2024. (FinCEN's position in its notice seems to imply that entities or persons that become members of the NSBA after the date of the March 1, 2024, ruling would be subject to the CTA.) Time will tell whether this decision gains national traction, given the near certainty of copycat suits to follow, or whether it can make its way up to the Supreme Court (which we note may come to a similar conclusion given its current composition).

However, despite the court's unfavorable reading of the CTA, it also provides a roadmap for how Congress may amend the CTA to make it constitutional. It could have, for example, imposed the reporting requirements on state entities as soon as they engage in commerce, rather than before.

While we recommend a wait-and-see approach for entities created prior to January 1, 2024 (for which the reporting deadline under the CTA is December 31, 2024), we recommend that entities created on or after January 1, 2024, begin preparing their reports, including undergoing the potentially complicated exercise of identifying their beneficial owners.

Contact us

Husch Blackwell is ready to help with all of your CTA needs, including assessing whether you are subject to the CTA or qualify for an exemption, as well as identifying your beneficial owners and preparing a report. We will continue to provide updates as the law progresses. Contact our CTA team for more information.