PREMIUM

Treasury Stares Down Another Challenge To CTA After Michigan Plaintiffs File Suit

A second lawsuit challenging the Corporate Transparency Act (CTA) has been filed—this time, in a Michigan court. Small businesses are pushing back, citing compliance costs, estimated to be $21.7 billion in 2024.

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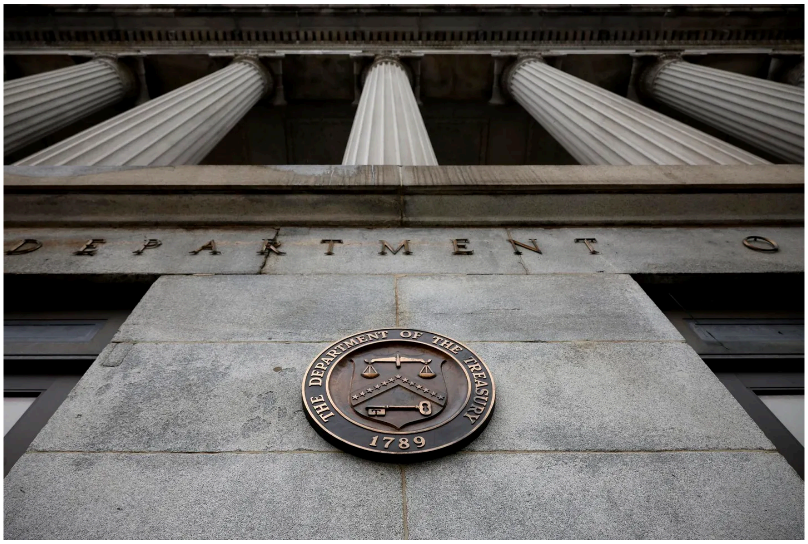

WASHINGTON, DC - MARCH 13: The exterior of the U.S. Department of Treasury building is seen on March 13, 2023 in Washington, DC. (Photo by Chip Somodevilla/Getty Images) GETTY IMAGES

A second lawsuit challenging the Corporate Transparency Act (CTA) has been filed—this time, in a Michigan court.

The Small Business Association of Michigan (SBAM) and other plaintiffs filed a federal lawsuit this week in the Western District Court of Michigan, Southern Division, seeking declaratory judgment and injunctive relief against the U.S. Treasury.

The legal challenge follows a similar case filed earlier this month. In that case, U.S. District Judge Liles C. Burke of the Northern District of Alabama, Northeastern Division, found the CTA unconstitutional "because it exceeds the Constitution's limits on Congress' power." The Alabama ruling resulted from a lawsuit filed by the National Small Business United (also known as the National Small Business Association, or NSBA) and Isaac Winkles, and bars the U.S.

Treasury from enforcing the CTA against the Plaintiffs—members of the NSBA—but does not enjoin enforcement against others. The federal government has since appealed the case.

Background

In 2021, Congress passed the Corporate Transparency Act—or CTA—as part of the National Defense Authorization Act for Fiscal Year 2021. The law requires certain companies to file reports that identify a company's beneficial owners with FinCEN, the Financial Crimes Enforcement Network. The stated goals of the CTA include to "better enable critical national security, intelligence, and law enforcement efforts to counter money laundering, the financing of terrorism, and other illicit activity." Secretary of the Treasury Janet L. Yellen has said about the CTA, "Corporate anonymity enables money laundering, drug trafficking, terrorism, and corruption. It harms American citizens and puts law-abiding small businesses at a disadvantage. Having a centralized database of beneficial ownership information will eliminate critical vulnerabilities in our financial system and allow us to tackle the scourge of illicit finance enabled by opaque corporate structures." For purposes of the CTA, reporting companies can be domestic companies created under the laws of a state or Indian tribe or entities formed under the law of a foreign country registered to do business in any state or tribal jurisdiction. This can include limited partnerships, limited liability partnerships (LLPs), business trusts, LLCs (including SMLLCs), and corporations—typically, any entity you would register with the state.

On January 1, 2024, the Department of the Treasury officially began accepting beneficial ownership information reports. A reporting company created or registered to do business before January 1, 2024, will have until January 1, 2025, to file its initial report, while a reporting company created or registered on or after January 1, 2024, and before January 1, 2025, will have 90 calendar days after receiving notice of the company's creation or registration to file its initial report. Reporting companies created or registered on or after January 1, 2025, will have 30 calendar days from actual or public notice that the company's creation or registration is effective to file their initial reports with FinCEN.

On March 26, 2024, the SBAM, together with the Chaldean American Chamber of Commerce, Steward Media Group, LLC, Power Connections Co, LLC, Derek Dickow, Semper Real Estate Advisors, LLC, and Timothy A. Eisenbraun, filed suit against Janet Yellen in her official capacity as the Secretary of the U.S. Department of the Treasury, the Treasury Department, and Himamauli Das, the Acting Director of FinCEN, tasked with carrying out the CTA.

Arguments

The plaintiffs argue in documents filed with the court that, instead of meaningfully advancing its stated goals, the CTA imposes significant burdens, especially on small businesses. Specifically, they note that the CTA's reporting requirements exempt any privately owned U.S. enterprise or business with over 20 full-time employees and more than $5 million in annual gross receipts or sales. That means, they argue, that "the CTA is aimed directly at small businesses, like the majority of the members of SBAM and the Chaldean Chamber," which may be inordinately burdened by the CTA's requirements.

The plaintiffs point to a FinCEN estimate that, in 2024, the aggregate cost of compliance with the CTA will be approximately $21.7 billion. Much of that cost, they claim, "will be borne by small businesses alone." The plaintiffs cite FinCEN estimates that 32,556,929 entities will meet the definition of a reporting company under the CTA as of 2024, excluding entities who are exempted from reporting—an additional 4,998,468 new entities will be required to report in each subsequent year.

The cost of compliance with the CTA has been estimated to be between $85.14 and $2,614.87, depending upon the complexity of the entity. That works out to $21.7 billion in costs for 2024 and approximately $3.3 billion each year afterward.

As in the Alabama case, the plaintiffs argue that the CTA is unconstitutional—a point that they reference in their pleading, noting "at least one federal court has already ruled that the CTA is not a proper exercise of Congress's authority over foreign affairs and national security interests, the Commerce Clause, or the taxation power."

The plaintiffs argue that the requirements of the CTA result in the treatment of "millions of law-abiding United States citizens as if they are criminals, except without any reason to suspect that any of them have engaged in wrongdoing." Key to that is the collection of private information—including copies of licenses and passports—that the plaintiffs fear can be leveraged against them in any future criminal investigation "regardless of whether the investigation is related to the money-laundering and terrorism-related impulses that gave rise to the CTA." That, the plaintiffs say, is an overreach not permitted by the Fourth Amendment. The filing notes, "The Fourth Amendment does not allow the warrantless, suspicionless searches of American citizens and companies that the CTA authorizes wholesale."

Some business owners have suggested that the CTA rules are too confusing, and the plaintiffs agree. They say that "[t]he CTA is too indefinite for ordinary people to know precisely when they are required to report an interest or not—that is, to know whether their conduct is criminal or not." And they say that is potentially damaging since the statute carries criminal penalties. Ultimately, they say, "the CTA bears all the hallmarks of an unconstitutionally vague statute."

And, they say, the law requires small businesses to report far more information than is needed at the state level. For example, they note that Michigan law does not require birth dates or active passports, driver's licenses, or other personal identification information for individuals who form an entity. When it comes to LLCs, Michigan law does not require disclosure of the identity of the LLC's members, and Michigan law also does not require disclosure of the identity of the shareholders of corporations. That is an extra burden many small businesses may not have contemplated when they opened their businesses.

The bottom line? The CTA is, they say, an overreach and unconstitutional.

Remedies

Among other things, the plaintiffs are asking for declaratory judgment and injunctive relief. Declaratory judgment is a resolution to a matter when there's legal uncertainty—and is often pursued before the lawsuit is fully developed. While courts typically require that a party demonstrate that they've been injured before relief can be granted, a declaratory judgment is a little different in that it allows a party to a suit to seek a judgment before an injury has happened. Put another way, it allows a court to determine the rights and obligations of the parties without finding damages.

Injunctive relief also applies to the future—it's intended to stop a wrong from happening. An injunction prevents a party from acting if harm will result otherwise. Here, the plaintiffs seek to bar the U.S. Treasury and other government agencies from enforcing the CTA.

A request for comment made to the U.S. Treasury was not immediately returned.

Plaintiffs

SBAM, located in Lansing, Michigan, is a statewide and state-based association that focuses on serving the needs of Michigan's small business community. The organization, which has been active since 1969, is comprised of small businesses registered to do business in Michigan—it currently has more than 32,000 small business members. SBAM has been hosting webinars and other educational efforts to get the word out about the CTA. But, they argue that the federal government isn't doing its part, saying that "[t]he federal government has not extensively educated the public about the CTA or its disclosure requirements." The Chaldean American Chamber of Commerce is a non-profit organization with a principal place of business in Farmington Hills, Michigan. The Chaldean Chamber advocates and promotes small businesses and economic opportunities, particularly in the context of businesses and individuals who are affiliated with the Chaldean American community. According to the organization's website, Chaldeans are Aramaic-speaking, Eastern Rite Catholics indigenous to Iraq. Metro Detroit is home to the largest Chaldean population outside the Middle East, with an estimated 160,000 members.

The Chaldean Chamber claims that it is using a disproportionate share of its resources to explain the CTA to its members—resources, they say, that could have been used for advocacy, promotion, and education efforts on other issues of importance to its members that did not involve the CTA. Other plaintiffs involved in the suit are business owners subject to the CTA. Brian Calley, President & CEO of the Small Business Association of Michigan, said, in a statement to *Forbes*, "The Corporate Transparency Act is an overreach that creates a complex yet vague compliance structure that adds further administrative and financial burdens to small businesses. Non-compliance or an incomplete filing is a felony that comes with heavy fines and up to two years in prison. It's entirely possible that millions of people will unintentionally violate this law and face severe consequences that endanger their livelihood."

He concluded, "An Act that was created by Congress to identify egregious criminals could instead create millions of accidental ones. This unconstitutional and burdensome overreach by

Congress must be corrected by the judicial system – precisely as checks and balances was intended."

The case is *Small Business Association of Michigan et al v. Yellen* (1:24-cv-00314), District Court, W.D. Michigan.

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