



INSTITUTE FOR FREE SPEECH

May 5, 2021

Mr. Michael Mosier
Acting Director
Financial Crimes Enforcement Network
P.O. Box 39
Vienna, VA 22183

**RE: Beneficial Ownership Information Reporting Requirements
(Docket Number FinCEN-2021-0005 and RIN 1506-AB49)**

Dear Mr. Mosier:

On behalf of the Institute for Free Speech,¹ I respectfully submit the following comments on the “advance notice of proposed rulemaking (ANPRM) … on the implementation of the Corporate Transparency Act” (CTA).

Our organization defends the free expression rights guaranteed by the First Amendment. As such, we wish to ensure that FinCEN works to faithfully implement the exemptions to the CTA that were placed in the law by Congress to protect First Amendment rights. The CTA’s exemptions eliminate or may reduce burdens that might otherwise be placed on civil society groups as they speak, publish, peacefully assemble, or petition the Government for a redress of grievances.

Question 6 of the ANPRM asks: “The CTA contains numerous defined exemptions from the definition of ‘reporting company.’ Are these exemptions sufficiently clear, or are there aspects of any of these definitions that FinCEN should clarify by regulation?”

Organizations Described in Section 501(c)

FinCEN should take care to ensure that the regulations implementing Section 5336(a)(11)(B)(xix) do not misinterpret the statute. The statute clearly states that the exemption applies to “any organization that is described in section 501(c) of the Internal Revenue Code of 1986.” An exemption also applies to “any political organization (as defined in section 527(e)(1) of such code).”

Many tax-exempt organizations under those provisions of the Internal Revenue Code are not required to obtain a determination of their tax-exempt status. *See, e.g.,* Internal Revenue Code § 508(c)(1)(B). Treas. Regs § 1.508-1(a)(4) provides –

(4) Voluntary filings by new organizations excepted from filing notice. *Any organization excepted from the requirement of filing notice under section 508(a) will be exempt from*

¹ The Institute for Free Speech is a nonpartisan, nonprofit § 501(c)(3) organization that promotes and protects the First Amendment political rights of speech, press, assembly, and petition.

taxation under section 501(c)(3) if it meets the requirements of that section, whether or not it files such notice. (emphasis added)

Others may file an IRS Form 8976, Notice of Intent to Operate Under Section 501(c)(4), but not an optional IRS Form 1024-A. Form 8976 permits a 501(c)(4) organization to operate without requesting a determination of status from the IRS.²

Those 501(c)(3) groups that are required to apply to the IRS for recognition of tax-exempt status must do so “within 15 months from the end of the month in which the organization was organized.” Organizations that apply for a determination may not receive it for many months or even years, yet such groups are still “described in section 501(c) of the Internal Revenue Code.”

Some may suggest that the statute implies that an organization must have formal recognition of a tax exemption because it may lose the exemption from the CTA 180 days after it “loses an exemption from tax.” Such a reading would clearly be contrary to the plain text of the statute. *See, e.g.* IRC § 508(c)(1)(B). If an organization is “described in section 501(c),” then it is exempt from the CTA reporting requirements. If the Internal Revenue Service or a reviewing court (see the next section of this comment) determines that the organization “loses an exemption from tax,” only then is the organization no longer “described in section 501(c).”

Therefore, the CTA regulations should not require formal IRS recognition of tax-exempt status, for the same reasons. The regulations should also clarify that an organization need not be described by any one particular subsection of IRC § 501(c) in order to qualify for CTA reporting exemption. Some nonprofit organizations have a mix of exempt purposes described in different portions of IRC § 501(c). For example, an organization might consist of a mix of activities between a 501(c)(4) entity, also known as a social welfare organization, and a 501(c)(7) entity, also known as a social club. Being described under any part of IRC § 501(c) should be sufficient for a reporting exemption.

Judicial Review of Tax-Exempt Status

Occasionally, organizations that apply for an IRS written determination of tax-exempt status are denied the request for exemption. In other circumstances, tax-exempt status is revoked. While IRS action calls into question whether the organization is “described in section 501(c),” it is not the final word. The difference is complicated, but significant for purposes of regulatory action and exemption under the CTA.

FinCEN should not interpret an initial IRS administrative decision on tax-exempt status under IRC § 501(c) as controlling for an exemption from CTA reporting. Only a final determination revoking or denying tax-exempt status should result in denial of a CTA reporting exemption. Under IRC § 7428(c), some contributions remain generally tax-exempt during the pendency of judicial reviews.

Under IRC § 7428, an organization may file a pleading with “the United States Tax Court, the United States Court of Federal Claims, or the District Court of the United States for the District of Columbia” for judicial review of an initial qualification or continuing qualification of an

² See, e.g., Internal Revenue Service, Instructions for Form 1024-A, Jan. 2021, at <https://www.irs.gov/instructions/i1024a>.

organization's tax-exempt status. Any of those courts "may make a declaration with respect to such initial qualification or continuing qualification" for tax exemption. *See, e.g., Ritchie v. Amer. Council on Gift Annuities*, 943 F. Supp. 685, 690 (N.D. Tex. 1996) ("the Court cannot treat § 2(a)'s phrases — 'described in section 501(c)(3)' and 'exempt from taxation under section 501(a)' — as 'mere shorthand references' used by Congress, as Defendants urge. Instead, the Court will follow the law as written.") (cleaned up), *vacated and remanded*, *Amer. Bible Soc'y v. Richie*, 522 U.S. 1011, 118 S. Ct. 596 (1997), *dismissed*, *Ozee v. Amer. Council on Gift Annuities*, 143 F.3d 937 (5th Cir. 1998).

The petitioner to the court is required to have "exhausted administrative remedies available to it within the Internal Revenue Service." The statute states that the organization "shall be deemed to have exhausted its administrative remedies with respect to a failure by the Secretary to make a determination with respect to such issue at the expiration of 270 days."

FinCEN should therefore write the regulation to clarify that an exemption under the CTA also applies if the organization has a pending application, including any judicial review of the determination, for tax-exempt status. A CTA exemption should still apply in circumstances where an organization has filed an appeal of an initial qualification or continuing qualification of an organization's tax-exempt status either administratively within the IRS or to a federal court under IRC § 7428. The CTA exemption should continue until the appeal process has been completed.

Therefore, the 180-day period described in Section 5336(a)(11)(B)(xix) should only begin to run 90 days after receipt of a letter specified in IRC § 7428(b)(3) or a final determination by the courts, whichever occurs later.

Exemption Under Section 5336(a)(11)(B)(xxii)

This provision provides an exemption to "any corporation, limited liability company, or other similar entity of which the ownership interests are owned or controlled, directly or indirectly, by 1 or more entities described in clause ... (xix)."

To faithfully interpret the statute, any regulation interpreting this exemption, at least for organizations exempt under Section 5336(a)(11)(B)(xix), should only require that either a simple majority (more than 50%) of the ownership interest or of the voting rights be controlled by one or more CTA exempt entities.

Safe Harbor

Since the ownership or control concepts articulated under Section 5336(a)(11)(B)(xxii) do not apply as often or as clearly in the context of nonprofit entities as they do with for profit corporations and LLCs, we recommend the regulation also include a safe harbor specific to nonprofit entities that would simplify application of the law to tax-exempt organizations and ease administrative burdens for these groups and FinCEN. This can be done by providing a safe harbor for a CTA exemption to any entity listed on the IRS Form 990 Schedule R filed by a tax-exempt organization. If a tax-exempt corporation lists a related organization on its own Schedule R (Related

Organizations), then it would know that entity is also CTA exempt. Organizations that appear on schedule R clearly qualify for the exemption under Section 5336(a)(11)(B)(xxii).

Question 7 states: “In addition to the statutory exemptions from the definition of ‘reporting company,’ the CTA authorizes the Secretary, with the concurrence of the Attorney General and the Secretary of Homeland Security, to exempt any other entity or class of entities by regulation, upon making certain determinations. Are there any categories of entities that are not currently subject to an exemption from the definition of ‘reporting company’ that FinCEN should consider for an exemption pursuant to this authority, and if so why?”

We recommend that FinCEN exempt several types of nonprofit corporations from the CTA reporting requirement.

Groups Subject to Automatic Revocation and Eligible for Retroactive Reinstatement of Tax-Exempt Status

It is not unusual for a small volunteer-run nonprofit organization to have its tax-exempt status automatically revoked for failure to file one of the Form 990 series of tax returns for three consecutive years. Fortunately, the IRS has provided a streamlined process for retroactive reinstatement of tax-exempt status. This process is described in IRS Revenue Procedure 2014-11.³

The regulation providing for a CTA exemption should accommodate this process for retroactive reinstatement of tax-exempt status by providing a retroactive CTA reporting exemption for organizations that successfully complete the reinstatement process. This process may occur well after the 180-day window described in Section 5336(a)(11)(B)(xix). We think such organizations are suitable “for an exemption pursuant to this authority.”

Nonprofit Corporations That Have Lost Their Tax-Exempt Status

Small nonprofit corporations that lose their tax-exempt status through automatic revocation are sometimes unaware of the revocation. For example, the notice of revocation may have been sent to a former officer who has since moved so that none of the current officers are aware of the revocation. Yet the organization may continue to operate at the same scale that it has done historically. Below, we recommend that FinCEN exempt all nonprofit corporations. If it is unwilling to do so, we recommend that nonprofit corporations that have lost their tax-exempt status through automatic revocation retain a CTA reporting exemption if they spend no more than \$5,000 in a calendar year.

Incorporated Nonprofits That Are Not Tax-Exempt

Nonprofit status is a State-level determination, while federal tax exemption is a federal-level determination. While most nonprofit corporations are eligible for tax-exempt status, not all of them desire to operate with a tax exemption. These corporations are usually organized to promote a

³ Available at: https://www.irs.gov/irb/2014-03_IRB#RP-2014-11.

cause or serve a community need. Those that try to serve a community need will often charge for their products or services but wish to do so at the lowest possible cost.

These organizations pose little risk of “money laundering, the financing of terrorism, proliferation finance, serious tax fraud, or other crimes” and appear suitable for such an exemption. In any event, most states have a public database listing officers and directors of such nonprofit corporations.

Alternatively, if FinCEN is unwilling to extend a CTA reporting exemption to all nonprofit corporations, we strongly recommend that it do so for those that spend no more than \$5,000 in a calendar year. Under IRS guidance, such organizations are often treated as tax-exempt even if they have not applied for tax-exempt status.

B Corps

We urge that FinCEN issue regulations that would provide an exemption to public benefit corporations that are Certified B Corporations by the nonprofit organization known as B Lab.

According to the B Lab website:⁴

Certified B Corporations are businesses that meet the highest standards of verified social and environmental performance, public transparency, and legal accountability to balance profit and purpose. B Corps are accelerating a global culture shift to redefine success in business and build a more inclusive and sustainable economy.

Society’s most challenging problems cannot be solved by government and nonprofits alone. The B Corp community works toward reduced inequality, lower levels of poverty, a healthier environment, stronger communities, and the creation of more high quality jobs with dignity and purpose. By harnessing the power of business, B Corps use profits and growth as a means to a greater end: positive impact for their employees, communities, and the environment.

B Corps form a community of leaders and drive a global movement of people using business as a force for good. The values and aspirations of the B Corp community are embedded in the B Corp Declaration of Interdependence....

Certified B Corporations achieve a minimum verified score on the B Impact Assessment—a rigorous assessment of a company’s impact on its workers, customers, community, and environment—and make their B Impact Report transparent on bcorporation.net. Certified B Corporations also amend their legal governing documents to require their board of directors to balance profit and purpose.

The combination of third-party validation, public transparency, and legal accountability help Certified B Corps build trust and value. B Corp Certification is administered by the non-profit B Lab.

⁴ Available at: <https://bcorporation.net/about-b-corps>.

Section 5336(a)(11)(B)(xxiv) indicates that “any entity... should be exempt from the requirements of subsection (b) because requiring beneficial ownership information from the entity... (I) would not serve the public interest; and (II) would not be highly useful in national security, intelligence, and law enforcement agency efforts to detect, prevent, or prosecute money laundering, the financing of terrorism, proliferation finance, serious tax fraud, or other crimes.”

The B Lab certification process is highly rigorous and appears to only certify organizations that operate ethically and lawfully. These organizations appear well-qualified for an exemption.

Question 9 states, in part, as follows: “How should a company’s eligibility for any exemption from the reporting requirements, including any exemption from the definition of ‘reporting company,’ be determined?

- a. What information should FinCEN require companies to provide to qualify for these exemptions, and what verification process should that information undergo?

- c. Should exempt entities be required to file periodic reports to support the continued application of the relevant exemption (e.g., annually)?”

Our comments regarding this question are limited to organizations exempt under Section 5336(a)(11)(B)(xix), 5336(a)(11)(B)(xx), and 5336(a)(11)(B)(xxii).

The statute does not provide any authority for FinCEN to obtain any information from nonprofit tax-exempt corporations to determine the organization’s eligibility for a CTA reporting exemption. Any such requirement would clearly contravene the intent of the nonprofit exemption language in the statute, which is to protect privacy under the First Amendment, “the right of the people peaceably to assemble.” The CTA exemption also eliminates reporting burdens for civil society organizations so they can focus their resources on achieving their mission.

If FinCEN were to collect information to verify the CTA exemption for tax-exempt corporations, there is risk it would leak from hacking of a database where this information is stored. Leaks or misuse of the data may also come from rogue government or financial industry employees. Such leaks or misuse could do irreparable harm to the civil society organizations exempted by the CTA.

Such insider leaks are not hypothetical concerns. FinCEN has had instances of misuse and wrongful dissemination of data it already collects under safeguards as exacting as those imposed by the CTA. Similar leaks of protected confidential data by errant employees have also occurred at other government agencies. Just last year a senior adviser at FinCEN, Natalie Edwards, pled guilty to conspiring to unlawfully disclose to a news reporter confidential protected personal information and business information from the agency’s Suspicious Activity Reports database.⁵ Ms. Edwards insisted that her actions were not wrong and that she merely “brought issues that she thought were important, compelling issues to the press so that the press could bring them to the people. She didn’t trust that the government was doing the right thing with these issues.”⁶ Congress

⁵ <https://www.justice.gov/usao-sdny/pr/former-senior-fincen-employee-pleads-guilty-conspiring-unlawfully-disclose-suspicious>.

⁶ <https://www.politico.com/news/2020/01/13/treasury-official-pleads-guilty-to-leaking-financial-documents-098333>.

was aware of the Edwards case when it inserted the nonprofit exemption in the CTA and when it omitted authority for FinCEN to collect information on exempt entities and cabined the agency’s data gathering to four specific datapoints on beneficial owners.

Hackers regularly access and disclose confidential government information. For example, in 2015, we learned that “U.S. government databases holding personnel records and security-clearance files exposed sensitive information on about at least 22.1 million people, including not only federal employees and contractors but their families and friends,” according to an article in *The Washington Post*.⁷

Last December, we learned that Russia hacked the IT company SolarWinds. According to *Wired* magazine, “a cascading number of victims have been identified, including the U.S. Departments of State, Homeland Security, Commerce, and the Treasury, as well as the National Institutes of Health. The nature of the attack—and the tremendous care taken by the hackers—means it could be months or longer before the extent of the damage is known. The impact is already devastating....”⁸

An amicus brief to the U.S. Supreme Court filed this year by the China Aid Association⁹ (known as ChinaAid) provides more evidence that authoritarian regimes seek to infiltrate U.S. government databases to obtain private information that can be used to help suppress criticism of the regimes:

China has acted to harass, threaten, and intimidate ChinaAid, which, along with its supporters, China has labeled “anti-China forces.” Recently, China unleashed a proxy in the United States who repeatedly urged his hundreds of thousands of social media followers to “kill” ChinaAid’s founder, Bob Fu, along with another democracy activist in California.

One of China’s key means of attacking critics abroad is by hacking into their accounts and organizational systems. Hundreds of entities have been penetrated—from technology firms, to universities, to nonprofits, to religious institutions. Another favorite target is government agencies, including, most notoriously, the U.S. Office of Personnel Management. In past years, China employed primitive techniques, but now shows skills exceeding those of the Federal Bureau of Investigation (“FBI”). Recently, for example, China hacked into the iPhone, when the FBI could not.

Such threats are not mere hypotheticals. Last year, Bloomberg News reported¹⁰ the following:

An internal breach at Twitter Inc. a half decade ago yielded data that was later used by Saudi Arabia to harass or arrest people critical of the government, according to lawsuits, human rights groups and the relative of a person apprehended in 2018.

⁷ Ellen Nakashima, “Hacks of OPM databases compromised 22.1 million people, federal authorities say,” *The Washington Post* (Jul. 9, 2015), at <https://www.washingtonpost.com/news/federal-eye/wp/2015/07/09/hack-of-security-clearance-system-affected-21-5-million-people-federal-authorities-say/>.

⁸ Brian Barrett, “Security News This Week: Russia’s SolarWinds Hack Is a Historic Mess,” *Wired* (Dec. 19, 2020), at <https://www.wired.com/story/russia-solarwinds-hack-roundup/>.

⁹ Available at: <https://www.supremecourt.gov/docket/docketfiles/html/public/19-251.html>.

¹⁰ Ryan Gallagher, “Spies in Silicon Valley: Twitter Breach Tied to Saudi Dissident Arrests,” *Bloomberg* (Aug. 19, 2020), at <https://www.bloomberg.com/news/articles/2020-08-19/twitter-security-breach-blamed-for-saudi-dissident-arrests>.

In 2015, two Twitter employees allegedly accessed more than 6,000 accounts while acting as spies for the government of Saudi Arabia. Some details of the incident have been disclosed by U.S. prosecutors, who charged the two men last November, and in recent lawsuits by people who alleged their accounts were among those breached. But few other details have emerged about what the Saudi government may have done with the data.

Now, the sister of a Saudi man who ran an anonymous Twitter account said her brother's disappearance resulted from the activities of the alleged Twitter spies. Abdulrahman al-Sadhan was working at his office in Riyadh on March 12, 2018 when Saudi Arabia's secret police showed up and took him away, according to his sister, Areej al-Sadhan. His family hasn't seen him since, and until he was permitted to make a short phone call to a relative in February, they worried that he might have been killed....

The Saudi operation underscores the stakes involved. Government critics in Saudi Arabia have been jailed and even executed, as in the case of the former Washington Post columnist Jamal Khashoggi, who was murdered in 2018 in the Saudi consulate in Istanbul.

FinCEN can easily confirm the tax-exempt status of the vast majority of organizations that qualify for a CTA exemption without having to collect sensitive data about many of these organizations. The IRS publishes an online "Exempt Organizations Business Master File."¹¹ The IRS also publishes an online database of political organizations that have filed Forms 8871 and 8872.¹²

Still, not all tax-exempt organizations will be listed on the IRS databases. New organizations and those that must apply for recognition of their tax-exempt status will not immediately appear in the database. Also, as noted below, political organizations that "reasonably expect their annual gross receipts to always be less than \$25,000" do not have to file forms with the IRS. A few organizations tax-exempt under section 501(c)(3) with receipts no greater than \$5,000 are exempt from filing requirements.¹³ Such smaller organizations could not be reasonably expected to know of any FinCEN CTA exemption reporting process.

We strongly urge that FinCEN not require any tax-exempt corporation to file any information or undergo any verification process to prove their eligibility for a CTA exemption. In addition to the strong statutory arguments against such a regulation, many if not most of the organizations exempt under these provisions are run completely by volunteers or have limited staff. They may initially be unaware of such requirements and, should they be imposed by regulation, would struggle to fulfill them. They may initially be unaware of such requirements and, should they be imposed by regulation, would struggle to fulfill them. Some may ultimately be dissuaded from engaging in

¹¹ Available at: <https://www.irs.gov/charities-non-profits/exempt-organizations-business-master-file-extract-eo-bmf>.

¹² Available at: <https://forms.irs.gov/app/pod/dataDownload/dataDownload>.

¹³ IRC § 504(c)(1)(B). This section of the code is explained in the following Instructions for Form 1023-EZ:

Note. Most organizations seeking exemption from federal income tax under section 501(c)(3) are required to complete and submit an application. However, the following types of organizations may be considered tax exempt under section 501(c)(3) even if they do not file Form 1023 or Form 1023-EZ:

- Churches, including synagogues, temples, and mosques.
- Integrated auxiliaries of churches and conventions or associations of churches.
- Any organization that has gross receipts in each taxable year of normally not more than \$5,000.

Available at: <https://www.irs.gov/instructions/f1023ez>.

protected activity out of concern about confidential information stored at a government agency, which could connect them to an unpopular cause.

At least one officer is listed in publicly available filings for political organizations filed either with the IRS or the Federal Election Commission or equivalent state agency. As noted in the instructions to IRS Form 8871:

Every political organization that is to be treated as a tax-exempt political organization under the rules of section 527 must file Form 8871, except for:

- An organization that reasonably expects its annual gross receipts to always be less than \$25,000,
- A political committee required to report under the Federal Election Campaign Act of 1971 (2 U.S.C. 431 et seq.),
- A political committee of a state or local candidate,
- A state or local committee of a political party, or
- A tax-exempt organization described in section 501(c) that is treated as having political organization taxable income under section 527(f)(1).

Question 17 states: “Section 5336(e)(1) requires the Secretary to take reasonable steps to provide notice to persons of their reporting obligations. a. What steps should be taken to provide such notice? b. Should those steps include direct communications such as mailed notices, and if so to whom should notices be mailed? c. What type of information should be included in such a notice, for example, the purposes and uses of the data, and how to access and correct the information?”

Our comments are limited to civil society groups. As noted elsewhere in these comments, we recommend that FinCEN expand the categories eligible for an exemption. Not only will expanded exemptions prevent small civil society groups from inadvertently violating the reporting requirement, it would lower FinCEN’s costs “to provide notice to persons of their reporting obligations.”

The two classes of civil society groups most likely to incur reporting obligations but not be aware of them are: small tax-exempt organizations that fail to file their Form 990 for three consecutive years and have their tax exemption automatically revoked; and nonprofit organizations that do not seek or do not operate with tax-exempt status.

For the first group, FinCEN may wish to explore whether it is possible to partner with the IRS to provide notice to organizations that have lost their tax-exempt status. If not, FinCEN could provide its own notice by mail to such organizations.

The second group is more difficult to locate. While the states have information on nonprofit organizations incorporated in their states, to our knowledge, such lists do not indicate which ones are tax-exempt.

Question 37 states: “One category of authorized access to beneficial ownership information from the FinCEN database involves ‘a request made by a Federal functional regulator or other

appropriate regulatory agency.’ How should the term ‘appropriate regulatory agency’ be interpreted? Should it be defined by regulation? If so, why and how?”

Question 37 does not address a more fundamental underlying issue. Section 5336(c)(2)(B) includes permission for FinCEN to disclose certain beneficial ownership information to “a Federal agency engaged in national security, intelligence, or law enforcement activity, for use in furtherance of such activity.”

A regulation implementing this provision should consider when such federal agencies are entitled to receive such information. In the case of the Federal Election Commission (FEC), by law the agency does not have free rein to obtain confidential information from other federal agencies. Under 52 U.S. Code Section 30109, the FEC may not commence law enforcement activity on an organization or person until “the Commission … determines, by an affirmative vote of 4 of its members, that it has reason to believe that a person has committed, or is about to commit, a violation.”

Therefore, the regulations implementing this section should only authorize disclosure of confidential information on an individual or organization to the FEC when it obtains verification that the Commission has authorized “an investigation of such alleged violation” of the individual or organization. The law does not authorize FEC commissioners or staff to obtain access to confidential information maintained by FinCEN without the vote required by law.

Miscellaneous Comments

Beneficial Owner Reporting Requirement for Nonprofit Organizations

As noted elsewhere in our comments, FinCEN should work to minimize the number of nonprofit corporations subject to the reporting requirements. Even with additional exemptions, a few may still need to report under the CTA.

It is unclear how the definition of beneficial owner under Section 5336(a)(2) should be applied to a nonprofit corporation. FinCEN should clarify that the reporting individual or individuals should be limited to the chief executive officer of the corporation. Alternatively, it could be limited to those individuals who remain as directors or officers of the corporation and have authority to write checks or transfer money for the organization.

Exemption Under Section 5336(a)(11)(B)(xix)

A CTA reporting exemption is provided to corporations that appear to have limited or no activity. FinCEN may wish to clarify by regulation that the requirement that such an entity “not engaged in active business” also applies to a nonprofit corporation even though such corporations do not typically conduct “business” operations.

* * *

Thank you for your consideration. Should you have any further questions, please contact the Institute for Free Speech at (202) 301-3300 or via email at info@ifs.org.

Sincerely,

A handwritten signature in blue ink, appearing to read "DK".

David Keating
President