

# U.S. District Court Rules the Corporate Transparency Act Unconstitutional: What is the Impact for Businesses?

## Corporate News: A Legal Update

By Karen Tobin on March 4, 2024

On March 1, 2024 in the case of *National Small Business United v. Yellen* 5:22-cv-01448-LCB the U.S. District Court for the Northern District of Alabama declared the Corporate Transparency Act (“CTA”) unconstitutional stating in part that it “exceeds the Constitution’s limits on the legislative branch and lacks a sufficient nexus to any enumerated power to be a necessary or proper means of achieving Congress’ policy goals.” (*Memorandum Opinion US District Court Northern District of Alabama Northeastern Division Case No. 5:22 cv 1448 – LCB at pg 3*)

The Corporate Transparency Act (31 CFR Section 1010.380) requires certain privately held companies to report the identities and other personal information of their owners (direct and indirect) and other individuals who exercise substantial control over the company to the U.S. Treasury’s Financial Crimes Enforcement Network (“FINCEN”).

Specifically, the court held in *National Small Business United v. Yellen* on March 1, 2024 that the CTA was not authorized under the Commerce Clause. The government offered three sources of constitutional authority for Congress’ enactment of the CTA. First, that it had power under its foreign affairs powers, because it has plenary power to conduct foreign affairs. Second, the government stated that it had the power to enact the CTA under the Commerce Clause. The government states that the act of corporate formation is enough to invoke the commerce power. Third, the government stated that the CTA is a necessary and proper exercise of Congress’ taxing power.

The court held that “formation has always been the province of the state. So, although the CTA does not directly interfere with or commandeer state incorporation practices, the CTA still convert[s] an astonishing amount of traditionally local...conduct into a matter for federal enforcement, and involve[s] a substantial extension of federal police resources.” *Memorandum at 22 citing Bond v. United States* 572 U.S. 844 (2014).

The court went on to note that the CTA cannot be justified as necessary and proper to carry out Congress' foreign affairs powers "because those powers do not extend to purely internal affairs, especially in an arena traditionally left to the States." *Memorandum at page 25.*

Further, the court stated that Congress can't look to international standards or agreements to extend those powers, no matter how praiseworthy the policy goal, because no agreement with a foreign nation can confer power on the Congress or on any other branch of government, which is free from the restraints of the Constitution." *Id at 25.*

Last, the court held that the CTA was not authorized under the Commerce Clause as "it did not regulate economic or commercial activity on its face." *Id at 49* "Submitting documents to the Secretary of State, does not implicate the Commerce Clause." *Id at 36.* "The connection between incorporation and criminal activity is far too attenuated to justify the CTA." *Id at 36.*

This ruling suspends the CTA reporting requirements for the plaintiffs in this case, however the District Court has not yet ruled on whether there will be a nationwide injunction. This case may be appealed and cases in other districts may be spawned by this litigation. Appeals in this case or a split between Federal Courts of Appeal may have to be resolved by the U.S. Supreme Court.

At this time, new entities formed on or after January 1, 2024 have 90 days to report under the CTA. In addition, to be conservative, businesses that were formed prior to January 1, 2024 should take steps to be prepared to report under the CTA by the deadline of December 31, 2024, as we monitor the situation. It may be wise to delay reporting for companies organized before January 1, 2024 until later in 2024 to see if there is more clarity under the CTA.

We will continue to monitor this and the impact for small business nationwide under the CTA.

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