

Corporate Transparency Act Update: Texas Court Issues Preliminary Injunction Halting Enforcement

By: John Fuchs, Rachel Sterbenz, Nida Rais, and Tate Thompson

As previously reported, the Corporate Transparency Act (“CTA”) took effect on January 1, 2024, requiring many businesses to file a beneficial ownership information report (“BOIR”), including general information about the company and sensitive personal information of its “company applicants” and “beneficial owners.” Under the CTA, companies formed prior to 2024 have until January 1, 2025, to submit their initial BOIR; and entities formed during 2024 have only 90 days after the date of formation to submit an initial BOIR. Any “willful” failure to comply with the CTA gives the Financial Crimes Enforcement Network (“FinCEN”) the authority to impose significant civil and criminal penalties.

On Tuesday, December 3, 2024, in *Texas Top Cop Shop, Inc. v. Garland*, the U.S. District Court for the Eastern District of Texas issued a preliminary injunction against the CTA and its implementing regulations, determining the CTA’s reporting requirements are “likely unconstitutional.” The injunction applies nationwide, halting the initial BOIR deadline. In short, the District Court’s decision provides that “[n]either the [CTA nor the Reporting Rule] may be enforced, and reporting companies need not comply with the CTA’s January 1, 2025, BOI reporting deadline pending further order of the Court.” However, as explained further in the “What Now?” section below, this is not a final decision, and businesses should be aware that the reporting deadline could be reinstated if the Court’s order is overturned, or a permanent injunction is not awarded on the merits.

Prior CTA Litigation

To date, there have been numerous lawsuits across the country challenging the constitutionality of the CTA. In March, the Northern District of Alabama held that the CTA was unconstitutional in *Nat'l Small Business United v. Yellen*, deciding the CTA exceeded Congress’s constitutional authority. Notably, however, the Alabama ruling was limited to the plaintiffs involved in that case. That decision is currently on appeal before the Eleventh Circuit.

Other District Courts have reached the opposite conclusion, finding the CTA is within Congress’ broad powers to regulate interstate commerce. In *Firestone et al. v. Yellen et al.*, the U.S. District Court for the District of Oregon denied the plaintiffs’ request for injunctive relief, ruling that the constitutional challenges were unlikely to succeed on the merits as the CTA was within Congress’ constitutional powers. The U.S. District Court for the Eastern District of Virginia reached the same conclusion in *Comm. Ass’ns. Inst., et al. v. Yellen, et al.*, denying a preliminary injunction and finding that the CTA is within Congress’ Article I powers and does not violate the plaintiffs’ First or Fourth Amendment rights.

Texas Top Cop Shop, Inc. v. Garland

In *Texas Top Cop Shop*, the plaintiffs challenged the CTA on the same grounds, claiming the CTA exceeds Congress’ Article I powers and that the law violates the First and Fourth Amendment. In a 79-page opinion, the U.S. District Court for the Eastern District of Texas ruled in favor of the plaintiffs, holding that the CTA “likely” exceeds Congress’ constitutional powers under the Commerce Clause and

the Necessary and Proper Clause. The Court did not reach the First or Fourth Amendment claims.

The Court's reasoning focused on the commercial activity regulated by the CTA, which the government described as "the anonymous existence and operation of corporations." The Court emphasized that, among other issues, the CTA "does not regulate a pre-existing activity, but instead compels a new one, [thus] the CTA exceeds Congress's commerce power." And, even assuming the "anonymous existence and operation of corporations" is an activity that may be regulated by Congress, the Court stated, "[t]he fact that a company is a company does not knight Congress with some supreme power to regulate them in all aspects—especially through the CTA, which does not facially regulate commerce." The Court rejected the government's remaining claims under the Necessary and Proper Clause, finding all of them insufficiently tied to an enumerated congressional power under the Constitution.

The Court acknowledged that "[w]hether the CTA and the Reporting Rule are absolutely unconstitutional is a question for another day." Still, it found the CTA is "likely unconstitutional" and issued a preliminary injunction. Importantly, unlike the Alabama decision, the preliminary injunction was not limited to the plaintiffs in the case and, citing authority from the Fifth Circuit, the Court's injunction applies nationwide. It is rare for a District Court to issue a nationwide injunction, particularly where other District Courts throughout the country have reached the opposite conclusion. The Court acknowledged this but determined "[t]he extent of the constitutional violation Plaintiffs have shown is best served through a nationwide injunction."

Government Appeal and FinCEN's Response

On Thursday, December 4, the federal government submitted its Notice of Appeal to the Fifth Circuit. The government may also seek an emergency stay of the district court's preliminary injunction in full or in part during the pendency of the appeal.

Over the weekend, FinCEN released a statement addressing the injunction:

"While this litigation is ongoing, FinCEN will comply with the order issued by the U.S. District Court for the Eastern District of Texas for as long as it remains in effect. Therefore, reporting companies are not currently required to file their beneficial ownership information with FinCEN and will not be subject to liability if they fail to do so while the preliminary injunction remains in effect. Nevertheless, reporting companies may continue to voluntarily submit beneficial ownership information reports."

Accordingly, so long as the injunction is in place, FinCEN will not be enforcing the CTA. Notably, however, the alert does not specify whether the initial reporting deadlines will be enforced in the event the injunction is lifted.

What Now?

In short, the CTA is unenforceable while the preliminary injunction remains in place. Reporting companies and their individual beneficial owners and company applicants (if applicable) are not obligated to submit BOIRs or otherwise comply with the CTA. Likewise, businesses that have already submitted an initial BOIR, and individuals who have obtained FinCEN IDs, are not obligated to update any information previously provided under the CTA.

However, given the current split among the District Courts on the constitutionality of the CTA, it is uncertain whether the CTA will ultimately be upheld. It seems likely that the issue will appear before the Supreme Court, where the CTA's fate will be decided.

In the interim, businesses are left somewhat in limbo as it is unclear how long the preliminary injunction will remain in effect. While the decision may serve as a reprieve for many business owners, the

preliminary injunction is only temporary.

Given the uncertainty surrounding the CTA, it is up to each business to decide whether to continue compliance efforts with the CTA. At this time, obtaining a FinCEN ID or submitting a BOIR is entirely voluntary. However, the conservative approach is to assume the CTA will eventually be enforced and, at minimum, identify individual beneficial owners and company applicants (if applicable) and gather all the information that will need to be included in any BOIRs. Business owners should remain diligent and be prepared to file in the event the injunction is stayed or the CTA is deemed constitutional. Further, in such case, reporting companies may need to move swiftly to make the required filings and may not have enough time to do so as FinCEN may or may not extend the filing deadline.

Please contact the Seigfreid Bingham Corporate Law Practice Group or your regular Seigfreid Bingham contact with any questions.

This article is general in nature and does not constitute legal advice. The authors of this article are members of Seigfreid Bingham's Corporate Law Practice Group and Corporate Transparency Act Task Force and routinely represent clients in corporate structuring and other general business matters. If you or your organization have questions about the impact of these developments, please contact John Fuchs, Rachel Sterbenz, Emily Crane, Nida Rais, or Tate Thompson at 816.421.4460.