

## Substantial Assistance: the CFPB's Newest Tool

The Consumer Financial Protection Bureau's (CFPB) latest enforcement tool— "substantial assistance"—is becoming a common way for the agency to go after parties that might otherwise escape its reach. In the past year, the CFPB has started to bring such claims with increasing frequency. Below, we examine what "substantial assistance" is and how the CFPB has been relying on it.

In its first four years, the CFPB brought claims alleging unfair, deceptive or abusive acts or practices (UDAAPs) under various of its authorities—over covered persons, service providers, affiliates, and related persons. But the CFPB waited almost four years—until March 2015—before using its authority to bring claims against individuals and entities that provide "substantial assistance" to UDDAP violations. Based on its enforcement actions to date, the CFPB apparently intends to use substantial assistance claims both as a fallback if other claims fail and to extend its jurisdictional reach where other theories are unavailable. But key questions remain, including:

- What must the CFPB establish under the provision's scienter requirement?
- What constitutes substantial assistance under the provision?
- What violations may form the predicate of a substantial assistance claim?
- How does substantial assistance liability interact with other limitations on CFPB authorities?

The resolution of these questions will go a long way toward defining the scope of substantial assistance liability and, in turn, how frequently this authority is used by the CFPB going forward. Companies that assist in the marketing or delivery of consumer financial products or services, but do not themselves qualify as covered persons or service providers, will be particularly well served to monitor developments in this area and to consider the possible application of this provision to their operations.

### The Statutory Prohibition on Providing "Substantial Assistance" to a UDAAP

Section 1036(a)(3) of the Dodd-Frank Act makes it unlawful for:

*any person to knowingly or recklessly provide substantial assistance to a covered person or service provider in violation of the provisions of section 1031[’s prohibition on unfair, deceptive, or abusive acts or practices], or any rule or order issued thereunder, and notwithstanding any provision of this title, the provider of such substantial assistance shall be deemed to be in violation of that section to the same extent as the person to whom such assistance is provided.*<sup>1</sup>

Generally analogous to "aiding and abetting" prohibitions enforced by other federal agencies, this provision has significant textual limits on its scope, including a scienter requirement ("knowingly or recklessly"); a requirement that

any assistance be “substantial”; and a requirement that the recipient of the assistance itself be liable for a UDAAP. But the provision also has facets that suggest a potentially broad application: it applies to “any person”; it applies “notwithstanding any provision of this title”; and it allows imposition of liability equivalent to that imposed on the recipient of the assistance.

## The CFPB’s Use of its “Substantial Assistance” Authority To-Date

The CFPB did not use its substantial assistance authority in an enforcement action until early 2015, but subsequently has asserted substantial assistance claims with increasing frequency. The CFPB now has used that authority as a basis of liability in ten of the 67 enforcement actions it has filed since first bringing a substantial assistance claim in March 2015.

In the first case to allege substantial assistance, the CFPB brought a variety of claims against individuals and entities allegedly involved in a phantom debt collection scheme. In addition to bringing Fair Debt Collection Practices Act and UDAAP claims against the individuals and entities alleged to have been directly involved in the scheme, the CFPB brought substantial assistance claims against three groups of defendants: the individual defendants, for their alleged “substantial assistance” to the various LLCs they had established as part of the scheme by operating those entities; payment processors, for their alleged substantial assistance to the debt collectors by processing payments they collected from consumers; and a telephone broadcast service provider, for its alleged substantial assistance to the debt collectors by broadcasting collection calls. As discussed below, the claims against the individual defendants are part of a pattern that has emerged whereby the CFPB seeks to impose individual liability pursuant to the “substantial assistance” provision. On the other hand, the claims against the payment processors and phone broadcast service reflect the agency’s

apparent view that individuals and entities have an obligation to be aware of “red flags” in connection with services they provide to others. Although litigation in this case is ongoing, it has produced the only judicial opinion to date addressing the “substantial assistance” provision, discussed further below.<sup>2</sup>

Following this case, the CFPB’s substantial assistance cases can be grouped in two general categories: (1) claims against counterparties of entities alleged to have committed UDAAP violations, where the counterparty’s conduct in selling goods or providing services to the alleged UDAAP violator is alleged to constitute substantial assistance, and (2) claims against individual owners and managers of closely held companies, whose managerial involvement is alleged to constitute substantial assistance to those companies’ alleged UDAAP violations.

## SUBSTANTIAL ASSISTANCE CLAIMS AGAINST COUNTERPARTIES

The CFPB has brought a number of substantial assistance claims against companies on the theory that their provision of certain goods or services to others constituted substantial assistance to the counterparties’ alleged UDAAP violations. The phantom debt collection case discussed above involved just such claims with respect to the payment processors and telephone broadcast service provider. Their provision of services to the other defendants in that case was alleged to constitute substantial assistance to the allegedly unfair debt collection scheme.

In the CFPB’s next substantial assistance case, the agency asserted substantial assistance claims in a consent order against various individuals and entities engaged in an alleged mortgage referral scheme that violated the Real Estate Settlement Procedures Act (RESPA). The agency brought RESPA claims against all the defendants – the individuals and entities who paid and received the kickbacks. It brought substantial assistance claims against various LLCs that had been established by some of the individual

defendants and that allegedly received the actual kickback payments. Although not elaborated in the Complaint, the CFPB's theory appears to be that those entities substantially assisted their individual owners by serving as conduits for the payments they received. As discussed below, this imposition of substantial assistance liability in a non-UDAAP case seems to be beyond the agency's authority.<sup>3</sup>

The CFPB next brought a substantial assistance claim against a party that provided credit monitoring services to customers of various banks. Many of the banks themselves had been subject to CFPB consent orders for billing their customers for credit monitoring services that the consumers did not receive. In an action against the banks' service provider, the CFPB alleged that it had provided substantial assistance to those UDAAP violations by instructing the banks to bill for services that were not received.<sup>4</sup>

In two separate cases, the CFPB alleged that the sale of delinquent debts with either incomplete or incorrect information about the debts constituted substantial assistance to UDAAPs committed in collecting on this debt, allegedly as a result of the incomplete or incorrect information.<sup>5</sup>

Finally in this regard, the CFPB also brought a separate substantial assistance case against a sole proprietor who sold consumer lead information to two of the defendants in the phantom debt case discussed above. The CFPB alleged that selling this information without conducting any due diligence concerning the purchaser or the uses for which it was buying the leads established the recklessness necessary for a substantial assistance claim.<sup>6</sup> The CFPB did not assert any UDAAP claims against the lead generator, presumably because he was not a "covered person" or "service provider" to whom the UDAAP prohibition applies directly. Interestingly, the CFPB appears to have exceeded its authority to bring administrative proceedings actions in this case, as the statutory provision authorizing such actions permits them

to be brought only against "covered persons" and "service providers."<sup>7</sup>

### **SUBSTANTIAL ASSISTANCE CLAIMS AGAINST INDIVIDUAL OWNERS & MANAGERS**

The second type of CFPB substantial assistance claim involves allegations that individual owners or managers of closely held companies have provided substantial assistance to, and thus are liable for, those companies' alleged UDAAP violations. As described below, these claims often appear to be intended to get around limitations on the CFPB's ability to assert individual liability pursuant to the statute's "related person" provision.

The phantom debt collection case discussed above itself involved substantial assistance claims against the individual defendants based on their conduct in setting up and operating various LLCs that allegedly were used in the debt collection scheme, although the CFPB also brought UDAAP claims against the individuals directly. The CFPB has also brought a series of cases alleging that certain individual defendants who were the owners or managers of a lead broker company substantially assisted that company's alleged UDAAP violations. The underlying UDAAP claims against the company focused on its purchase of consumer leads from lead generators who allegedly promised to find consumers the best rates or lowest fees and the resale of those leads to tribal and online payday lenders who allegedly charged higher rates and fees. The substantial assistance allegations focused solely on the individual defendants' role in founding and managing the defendant lead broker company.<sup>8</sup>

Finally, most recently, the CFPB alleged that two co-owners of a payment processor provided substantial assistance to that company's debiting of consumer bank accounts on behalf of clients allegedly engaged in unlawful practices, where the payment processor allegedly should have been aware of various red flags such as high return rates on its customers' transactions.

Interestingly, unlike in the phantom debt case, the CFPB did not bring substantial assistance claims against the payment processor itself, but only against the individual owners.<sup>9</sup>

## KEY ISSUES RAISED BY THE CFPB'S SUBSTANTIAL ASSISTANCE CLAIMS TO-DATE

### *The Scierter Requirement*

The CFPB's assertion of substantial assistance claims to date has raised questions about how the CFPB must establish the knowledge or recklessness required for substantial assistance liability. The phantom debt collection case discussed above has seen the first judicial opinion on this point.

In response to a motion to dismiss by three defendants, the CFPB urged the district court to conclude that the Dodd-Frank Act did not incorporate the "severe recklessness" standard that had been applied by the Eleventh Circuit in related statutory contexts. The court rejected this argument in a September 1, 2015 order. It concluded instead that the recklessness standard under Section 1036(a)(3) is equivalent to the standard of "severe recklessness" previously adopted in aiding and abetting claims under the securities laws. Liability is limited under this standard to "those highly unreasonable omissions or misrepresentations that involve not merely simple or even inexcusable negligence, but an extreme departure from the standards of ordinary care, and that present a danger of misleading buyers and sellers which is either known to the defendant or is so obvious that the defendant must have been aware of it."<sup>10</sup>

The district court applied that standard and concluded that the CFPB had alleged "facts which, taken as true, plausibly allege that [the defendant payment processor] was 'highly unreasonable' in ignoring obvious signs of debt-collection fraud amounting to 'an extreme departure from the standards of ordinary care,' thus presenting an obvious danger of debt-collection fraud for consumers of which [the

defendant] must have been aware."<sup>11</sup> The Court went on to find that allegations against two other payment processors also satisfied the "severe recklessness" standard.

While the CFPB ultimately prevailed under the test employed by the district court, the court's ruling confirms that Section 1036(c)(3)'s scierter requirement provides a significant limitation on the CFPB's substantial assistance authority. Litigation of the precise contours of this limitation seems likely, in part because the CFPB continues to base substantial assistance claims on alleged failure to heed "red flags."<sup>12</sup> There may even be more litigation over the scope of that requirement in the phantom debt collection case itself. One defendant, the telephone broadcast service alleged to have provided substantial assistance by broadcasting the debt collectors' collection calls even after having received a civil investigative demand (CID) from the CFPB, did not move to dismiss, but filed an answer denying that it had the requisite scierter or otherwise had violated the substantial assistance prohibition.<sup>13</sup> In fact, in an affirmative defense, it specifically rejected the theory, implicit in the CFPB's complaint, that receipt of a CID about a covered person's behavior can be enough to establish knowledge of a UDAAP.<sup>14</sup> Whether the CFPB will prevail on this and other applications of its "red flag" theory remains to be seen.

### *Substantial Assistance*

The CFPB's enforcement actions also raise questions about what constitutes "substantial assistance" under Section 1036(a)(3), including whether the provision of routine commercial services can meet that definition.

The phantom debt collection opinion also addressed this point. That district court chose to adopt a test that looked to the acts and motives of the defendant, rather than one that looked at how significantly the assistance contributed to the wrongful conduct. Specifically, the district court adopted the standard employed by the

Second Circuit in securities fraud cases. It thus explained that “to plead substantial assistance against a defendant, the SEC must allege ‘that he in some sort associated himself with the venture, that the defendant participated in it as in something that he wished to bring about, and that he sought by his action to make it succeed.’”<sup>15</sup> The district court rejected the defendants’ argument that the CFPB must establish that the assistance proximately caused the wrongful conduct, concluding that a causal relationship was “relevant but not required.”<sup>16</sup>

In bringing substantial assistance claims against payment processors and a telephone broadcast service, as well as against various lead generators, the CFPB has suggested that even the delivery of routine commercial services may be sufficient in its view to support “substantial assistance” liability. The district court addressed this issue in the phantom debt collection case. It cited to Eleventh Circuit case law in other contexts and reasoned that “common business practices could . . . substantially assist unlawful conduct if there are ‘atypical’ factors involved in the common practice.”<sup>17</sup> The order then treated the failure to heed “obvious red flags” and “obvious warning signs” as a basis for substantial assistance claims against the various defendants, essentially collapsing the inquiry into scienter and substantial assistance by focusing on “red flags” in both instances.<sup>18</sup> The court summarized: “innocuous business practices in one context could amount to substantial assistance to unfair, deceptive, and abusive practices in another, as long as the aider and abettor knows of or is reckless to the risk of the primary violation.”<sup>19</sup> In other words, the court seemed to read the requirement that assistance be “substantial” so that it has little, if any, force independent of the scienter requirement. It remains to be seen whether other courts adopt this reading or conclude that it inappropriately renders the requirement of “*substantial* assistance” surplusage.

### ***Predicate Violations for Substantial Assistance Claims***

Congress made clear that substantial assistance claims must be based on UDAAP violations. The CFPB, however, has sought to stretch its substantial assistance authority to reach other violations of federal consumer financial law.

In the RESPA enforcement action discussed above, the CFPB claimed that a title company and various loan officers had engaged in an illegal kickback scheme related to real-estate settlement services. The CFPB alleged that the various defendants violated RESPA and that they thereby violated Section 1036 of the Dodd-Frank Act, which renders any violation of Federal consumer financial law a violation of that section of the Dodd-Frank Act. On this basis, the CFPB alleged that the entities established by the individual defendants to accept the alleged kickback payments knowingly or recklessly provided substantial assistance to those individual defendants and the alleged payor of the kickbacks.

While the CFPB successfully settled the case, its substantial assistance claims exceed the agency’s authority. By its terms, the substantial assistance provision applies only to conduct prohibited under Section 1031 of the Dodd-Frank Act or to a rule implementing that section.<sup>20</sup> Section 1031 permits the CFPB to take regulatory or enforcement actions against UDAAPs. By contrast, Section 1036 makes violations of RESPA or other Federal consumer financial laws a violation of the Dodd-Frank Act. By limiting substantial assistance claims to violations of Section 1031, Congress made a clear choice to apply substantial assistance liability only to UDAAPs – not to violations of RESPA or the other Federal consumer financial laws that the CFPB enforces. By treating a RESPA violation as a basis for a substantial assistance claim, the CFPB exceeded its substantial assistance authority. While this case can be seen as an aberration, the agency’s willingness to settle

claims beyond its authority is troubling and surprising. Respondents in CFPB investigations should resist any efforts by the agency to assert substantial assistance claims outside the UDAAP context.

### ***Substantial Assistance and Limits on Other CFPB Authorities***

The CFPB repeatedly has used substantial assistance claims as one of multiple bases for asserting jurisdiction in an enforcement action. For example, in the case against a company that provided credit monitoring services to bank clients, the CFPB alleged that the company was liable not only under the substantial assistance provision, but also as a covered person and as a service provider.

The CFPB also has used its substantial assistance authority to extend its authority to reach entities otherwise outside its jurisdiction. In the cases against the owners and operators of a lead broker, the CFPB has alleged that the individual defendants provided substantial assistance to the company's alleged unfair and abusive practices.<sup>21</sup> The CFPB has treated company founders and managers of non-bank entities as "related persons" in the past, and sought to impose individual liability on such individuals based on their ownership or management role. (Indeed, the CFPB alleges a "related person" theory, in addition to a substantial assistance theory, against the individual defendants in its most recent payment processor action.<sup>22</sup>) In order to assert that an individual is a "related person" of a company under the Dodd-Frank Act, however, that company itself must be a "covered person" (i.e., one who offers or provides a consumer financial product or service).<sup>23</sup> Because the lead generator at issue in these cases did not provide any consumer financial products or services – and thus was not itself a "covered person" – a related-person theory of individual liability was unavailable against the individual defendants. The CFPB's use of a substantial assistance theory

(and nothing else) against these individuals thus appears to be an attempt to circumvent the limitations set forth in the statute with respect to the imposition of individual liability on those alleged to materially participate in an entity's affairs. As all three cases are currently in litigation, the courts may have an opportunity to opine on the validity of this approach.

The CFPB has also sought to use its substantial assistance powers to navigate other limitations on its authority in the phantom debt collection case. The CFPB alleged there that a telecommunications company provided substantial assistance by broadcasting allegedly abusive messages to consumers on behalf of the debt collector defendants.<sup>24</sup> Such a service is arguably exempt from the CFPB's jurisdiction under the support services exception or the electronic conduit exception.<sup>25</sup> The CFPB likely will take the view that any inquiry into the application of those exceptions is unnecessary, however, because substantial assistance liability may attach "notwithstanding any provision of [Title X of the Dodd-Frank Act]." Judicial acceptance of such a theory could have significant implications for a wide range of companies and individuals otherwise exempted from the CFPB's jurisdiction by the Dodd-Frank Act.

The CFPB has also sought to use its substantial assistance authority to regulate industries not otherwise within its purview. Last year, the agency sought to wade further into regulating the for-profit college industry by going after the institutions that accredit for-profit schools. Clearly, such accreditation is *not* a financial product or service within the CFPB's purview. To get over this hurdle, the CFPB sought to assert that by accrediting for-profit schools, the accrediting body was providing substantial assistance to potential UDAAPs committed by those schools in connection with private student loans. The issue arose in connection with a CID the CFPB issued to such an accrediting body, which refused to comply on the grounds that the

CFPB had no authority to conduct such an investigation. In discussing this issue, CFPB Director Richard Cordray commented that “[i]f an accrediting agency is *facilitating* for-profit colleges’ misleading consumers, treating them unfairly and deceptively, then that’s something that we should look at” (emphasis added).<sup>26</sup> Similarly, the CFPB argued in federal court that its CID was appropriate, among other reasons, because the CFPB is empowered to take action against those who “knowingly or recklessly provide substantial assistance to a covered person” who engages in UDAAPs. The district court dismissed the CFPB’s case seeking to enforce the CID, finding that the CFPB’s argument was “a bridge too far!”<sup>27</sup> The CFPB has appealed this order, meaning that the Court of Appeals will have an opportunity to opine on the scope of the substantial assistance provision, at least insofar as the CFPB’s investigatory authority is involved.

### **Disfavored Industries**

The survey of cases above suggests that the CFPB is particularly likely to use its substantial assistance authority in cases involving debt collection and payday lending, two industries that the agency appears to view with particular suspicion. Of the ten cases involving substantial assistance claims to date, four have involved substantial assistance claims related to debt collection and four have involved substantial assistance claims ultimately related to payday lenders. While this is a small data set from which to draw broad conclusions, it suggests that the CFPB is especially likely to pursue any avenue it thinks available to it to address conduct it is concerned with in these industries.

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After initially leaving this tool unused, the CFPB has begun to make regular use of its substantial assistance authority. While this authority is subject to clear textual limits, the CFPB’s actions to date strongly suggest that it expects this authority to play a significant role in its

regulation of the consumer financial services market in the years ahead. Companies and individuals not otherwise subject to the CFPB’s UDAAP authority should pay particular attention to the development of the law in this area, as the CFPB seems intent on using this provision to expand its reach.

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### **Endnotes**

- <sup>1</sup> 12 U.S.C. § 5536(a)(3) (emphasis added).
- <sup>2</sup> See Complaint, *CFPB v. Universal Debt & Payment Solutions, LLC*, No. 15-cv-0859 (N.D. Ga. March 26, 2015).
- <sup>3</sup> See Complaint, *CFPB v. Genuine Title, LLC*, No. 15-cv-1235 (D. Md. April 29, 2015).
- <sup>4</sup> See Complaint, *CFPB v. Intersections Inc.*, No. 15-CV-0835 (E.D. Va. July 1, 2015).
- <sup>5</sup> See *In re Chase Bank, USA N.A.*, 2015-CFPB-0013 (July 8, 2015); *In re Citibank, N.A.*, 2016-CFPB-0003 (Feb 23, 2016).
- <sup>6</sup> See *In re Eric V. Sancho*, 2015-CFPB-033 (Dec. 17, 2015).
- <sup>7</sup> See 12 U.S.C. § 5563(b)(1)(A). Although section 5563(a) authorizes administrative proceedings with respect to “any person,” 12 U.S.C. § 5563(a), all the details concerning the conduct of such proceedings are contained in section 5563(b), which governs cease-and-desist proceedings and is limited in scope to “covered persons” and “service providers.” It is unclear whether the CFPB actually may bring enforcement actions under section 5563; the action against the lead generator appears to be a cease-and-desist proceeding subject to section 5563(b).
- <sup>8</sup> See Complaint, *CFPB v. D&D Marketing*, No. 15-cv-09692 (C.D. Cal. Dec. 17, 2015); *CFPB v. Fomichev*, No. 16-cv-2724 (C.D. Cal. April 21, 2016); *CFPB v. Gasparyan*, No. 16-cv-2725 (C.D. Cal. April 21, 2016).
- <sup>9</sup> See Complaint, *CFPB v. Intercept Corp.*, No. 16-cv-0144 (D.N.D. June 6, 2016)

- <sup>10</sup> See Order at 22, Dkt. 149, 15-cv-0859 (N.D. Ga. Sept. 1, 2015) (“Universal Debt Order”) (citing *Woods v. Barnett Bank of Ft. Lauderdale*, 765 F.2d 1004, 1010 (11th Cir. 1985)).
- <sup>11</sup> See Universal Debt Order at 26-27.
- <sup>12</sup> See, e.g., Complaint ¶¶ 114, 133, *CFPB v. Intercept Corp.*, No. 16-cv-0144 (D.N.D. June 6, 2016).
- <sup>13</sup> See Answer of Global Connect LLC, Dkt. 79 at ¶ 338, 15-cv-0859 (N.D. Ga. May 7, 2015).
- <sup>14</sup> See *id.* at ¶ 102; Complaint, Dkt. 1 at ¶¶ 118-19, 15-cv-0859 (N.D. Ga. Sept. 1, 2015).
- <sup>15</sup> See Universal Debt Order at 38.
- <sup>16</sup> *Id.*
- <sup>17</sup> See Universal Debt Order at 40-41.
- <sup>18</sup> *Id.* at 41, 43.
- <sup>19</sup> *Id.* at 41.
- <sup>20</sup> 12 U.S.C. § 5536(a)(3).
- <sup>21</sup> See, e.g., Complaint ¶¶ 47, 59, *CFPB v. Fomichev*, 16-cv-2724 (C.D. Cal. April 21, 2016).
- <sup>22</sup> See Complaint ¶¶ 16, 23, *CFPB v. Intercept Corp.*, 16-cv-0144 (D.N.D. June 6, 2016).
- <sup>23</sup> See 12 U.S.C. § 5481(25).
- <sup>24</sup> Complaint ¶¶ 337-39, Dkt. 1, 15-cv-0859 (N.D. Ga. Mar. 26, 2015).
- <sup>25</sup> See generally 12 U.S.C. § 5481(15)(C)(ii) (electronic conduit exception); 12 U.S.C. § 5481(11) (defining “electronic conduit services”); 12 U.S.C. § 5481(26)(B)(i) (support services exception). The defendant has asserted the “support services” exception as an affirmative defense to service provider liability. See Answer of Global Connect, LLC, Dkt. # 79 at ¶¶ 100-01, 15-cv-0859 (N.D. Ga. Mar. 26, 2015).
- <sup>26</sup> <https://www.insidehighered.com/quicktakes/2015/10/29/cfpb-chief-defends-investigation-involving-college-accreditation>
- <sup>27</sup> Slip Op. at 6, *CFPB v. ACICS*, No. 15-1838 (D.D.C. April 21, 2016), *appeal filed*, No. 16-5174 (D.C. Cir.).

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