

# Legal Update

## The UN Convention on the Assignment of Receivables in International Trade

### *Advancing Ratification and What This Means for Trade*

Ratification by the United States of the United Nations Convention on the Assignment of Receivables in International Trade<sup>1</sup> (the "Convention") in October 2019 marked an important and long-overdue step in advancing global adoption of this Convention. An apolitical and bipartisan technical solution to a series of commercial finance problems and not at all related to the current trade tensions, the Convention could have global, game-changing implications for businesses of all sizes to access more financing in support of international trade. This Legal Update discusses the potential impact of US ratification, the problems that the Convention addresses, its objectives, its key features, and next steps necessary for it to enter into force.

### Context

Global merchandise trade is US \$18-\$20 trillion per year, with fast-growing service sector trade representing an additional \$5 trillion in economic activity and value-creation. Eighty percent of cross-border merchandise flows, and an increasing percentage of service sector commercial activity, depends on some form of financing, according to the World Trade Organization.<sup>2</sup>

Trade activity is financed using a range of techniques and products, from documentary credits to supply chain finance (including factoring), to asset-based lending, trade finance securitization and for small businesses, even credit card debt. Globally, it is estimated that there is a persistent unmet demand for trade financing of about \$1.5 trillion annually,<sup>3</sup> with small- to medium-size business suppliers (SMEs) in Asia and elsewhere—critical to major supply chains everywhere—most challenged in accessing the trade financing they would require to do business in international markets.

### Why Is the Recent US Ratification a Potential Game Changer?

The UN General Assembly adopted the Convention in 2001. The Convention came under review in the United States during the Clinton administration in the 1990s, culminating in George W. Bush signing the Convention in 2003. After that, the Convention languished in the United States Congress for a decade and a half.<sup>4</sup> Ratification by the United States, completed on October 15, 2019, is expected to motivate other major trading partners to follow suit and has the potential to transform the trade finance landscape.

As it stands today, significant legal barriers and other factors impede robust growth in cross-border receivables financing. The Convention has the potential to reduce or eliminate many of these barriers by harmonizing and greatly simplifying the way in which receivables<sup>5</sup> are transferred and assigned, whether as collateral security for loans or other extensions of credit or in transactions in which receivables are sold. The Convention also provides the potential for improvements to commercial finance law in many jurisdictions around the world where such laws are antiquated or not fully developed.<sup>6</sup>

The Convention playbook is largely consistent with Article 9 of the Uniform Commercial Code ("UCC"). This is not by accident since many of the luminaries who played a role in drafting Article 9 of the UCC and supported the vision of modernizing commercial finance law across the globe were influential in drafting and promoting the Convention.<sup>7</sup> If broadly adopted, the Convention will facilitate far greater accessibility of receivables finance solutions in support of trade. By simplifying the global landscape through improved consistency across borders, the Convention will help incentivize financial institutions ("FIs") and fintechs alike to increase their activities in receivables-based financing. This includes both the origination of new lending deals and receivables sales transactions, the net effect of which is a significant increase in trade financing capacity.

Cross-border receivables financing and sale are likely—as a direct result of adoption of the Convention—to become a powerful complement to existing toolsets and techniques that support global trade today, materially increasing access to finance for companies of all sizes.

## What Are the Current Problems?

The Convention addresses many current problems in the global marketplace that stem from onerous and complex local law and regulatory requirements for receivables financing and sale, including laws and regulations imposed by countries throughout Central and South America, civil law jurisdictions in Europe, and under-developed legal frameworks for assigning receivables in the Middle East and beyond.

This red tape can include a variety of requirements, for example:

- a notary public must be involved in order for a receivables assignment to be valid and enforceable;
- any description of a receivable financed or sold must be specified in granular detail each time a transfer happens;
- notice to the account debtor has to be given in a particular way, at a particular time or in a certain language;
- receivables cannot be sold if there is an anti-assignment clause in the underlying sales contract; or
- receivables cannot be sold on a batch, future or undivided basis.

Other impediments can be:

- regulatory requirements which are protectionist in nature with the impact of strongly discouraging non-domestic FIs from purchasing trade receivables;
- exchange rate controls or other measures to support local currencies; or
- inconsistent adoption of European Union (EU) Directives among EU member states.

Also the laws applicable to conflicts of priority among competing claims may be vague or uncertain.

The result is many FIs and other financiers are skittish about cross-border receivables financing and sale into certain countries—most notably in the asset-based lending and trade securitization space—given the administrative complexity and legal uncertainties regarding financiers'/FI purchasers' ability to collect the

receivables.<sup>8</sup> Those FIs who have ventured into the international markets with global supply chain programs have invested tremendous amounts of time, money and resources working with local counsel to navigate and comply with oftentimes tough local requirements for receivables financing and sale.

In many jurisdictions —throughout Latin America, the Middle East and Africa—extensions of credit are secured overwhelmingly by fixed assets such as land or other real property. The result is that credit is often tied up in illiquid assets, and other types of collateral are used with much less frequency and if used are at high transaction costs. This has broad social implications for businesses with fewer resources, including some SMEs, e.g., the local merchant who cannot access credit card financing. These smaller businesses as a practical matter may be unable to collateralize even a healthy volume of payment receipts in order to secure financing.<sup>9</sup>

If there were a mechanism that could support and help maintain the most effective characteristics of receivables finance (and related law) without up-ending certain appropriate elements of current local practice and legal standard, it would benefit global trade, help drive economic value and strengthen cross-border supply chains through improved liquidity. The Convention has the potential to provide this mechanism.

## What Are the Convention's Objectives?

As the preamble to the Convention provides, the Convention's goal is "to promote the availability of capital and credit at more affordable rates" and to establish a set of uniform rules that "would create certainty and transparency and promote the modernization of law relating to assignments of receivables."<sup>10</sup>

Uniform rules, where adopted, can override or simplify some of the local law complexities spelled out above, giving greater certainty for contracting parties and sharply reducing transactions costs and legal risk. The remarkable thing about this Convention is that it contains a general prohibition on any ratifying country modifying or nullifying its legal effect such that the goal of uniformity may be readily attainable.<sup>11</sup> Widespread adoption of the Convention has the potential to spur rapid growth and scaling up of a range of cross-border financing options, including global supply chain finance programs, factoring, asset-based lending and securitization, making these financings efficient and available to a broader and deeper customer base.

Successful implementation of the Convention will also facilitate cross-border financings that are more economically and geographically diverse, reaching into SMEs in developing countries.

## What Are the Convention's Key Features?

### SCOPE

The Convention is generally applicable only if the assignment<sup>12</sup> or the assigned receivable is "international," which means that the assignor and assignee must be located in different jurisdictions or the assignor and the debtor (a/k/a account debtor or obligor) on the receivable are located in different countries. In a typical receivables financing or sale transaction, the assignor will be the vendor selling goods or services, the debtor will be the buyer of those goods and services, and the assignee will be the FI that is financing or buying the receivable.

The Convention excludes assignments by consumers for consumer purposes.

### BULK ASSIGNMENTS; FUTURE RECEIVABLES

The Convention overrides local laws that would otherwise prohibit bulk assignments or transfers of receivables, present transfers of future receivables or undivided or partial transfers of receivables. By permitting assignments of receivables in bulk, the Convention eliminates the requirement that each

receivable be identified individually as is currently mandated in many countries. Under the Convention, general descriptions of receivables being assigned are effective so long as the receivables are described in such a way as to be identifiable to the contract of assignment. Likewise, future receivables can be assigned by one-off current assignment at the outset of the transaction so long as they can be identified as receivables to which such assignment relates.

### **ANTI-ASSIGNMENT CLAUSE OVERRIDE FOR TRADE RECEIVABLES**

The Convention partially invalidates contractual restrictions in the underlying sales contract or purchase order on assignment of “trade receivables” (meaning generally the purchase and sale of goods or services) along the lines of Article 9 of the Uniform Commercial Code.<sup>13</sup> Contractual restrictions on assignment are often a major legal barrier to the financing and sale of receivables outside of the United States and have spawned litigation in situations where vendors have sold receivables to FIs in contravention of their underlying sales contract with the debtor. Fortunately, Article 44 of the Convention specifically prohibits any ratifying country from using a reservation to block or change the Convention’s general annulment of anti-assignment clauses in the underlying sales contract.<sup>14</sup>

### **NOTICES OF ASSIGNMENT; DISCHARGE OF PAYMENT OBLIGATIONS**

The Convention provides that either or both of the assignor and assignee (financing party) can send the debtor notification of the assignment or a payment instruction. This innovation provides flexibility, lacking in certain jurisdictions, for the assignee to send a notice and demand to the obligor to receive payment directly.

Generally speaking, the Convention clarifies that after the debtor receives notification of the assignment, the debtor is discharged only by paying the assignee. The Convention further provides that “notification of the assignment” requires a “writing that reasonably identifies the assigned receivable and the assignee” and that notice will be effective when received by the debtor if it is in a language that is reasonably expected to inform the debtor about its contents.

This is significant because the Convention—in contrast to prevailing law in many jurisdictions—places no restriction on the timing or manner in which the notice must be sent. In fact, the Convention allows for notification of the assignment or a payment instruction to relate to receivables arising after the notification. The Convention is also silent on the oftentimes onerous requirement in many jurisdictions that receipt of the notice be confirmed each time in writing by the debtor or by a return receipt. In many jurisdictions, if the debtor does not receive notice of the assignment at the right time or in the right way, or if there is no solid evidence confirming the debtor’s receipt, the assignment will be unenforceable against the debtor: not an optimal outcome for the receivables purchaser or financing party. Through silence, the Convention appears to eliminate local law notice confirmation requirements (although this is not entirely clear).

### **CHOICE OF LAW FOR DETERMINING PRIORITY OF CLAIMS**

One of the most important parts of the Convention addresses the impact of assignment on “competing claimants” which the Convention defines as including competing assignees, other creditors of the assignor and the administrator in the insolvency of the assignor.<sup>15</sup> The Convention provides that the priority of an assignee’s interest in a receivable as against competing claimants is determined by the law of the jurisdiction where the assignor is located. That law also determines whether the assignment is a “true sale” or a secured financing. If a challenge to the priority of an assignment is made in a court outside of that jurisdiction, the court must nonetheless apply the laws of the jurisdiction where the assignor is located unless those laws are “manifestly contrary to the public policy” of the jurisdiction where the challenge is being made.<sup>16</sup> Because an assignor’s assets may not be sufficient to satisfy all creditors, this issue is of considerable importance.<sup>17</sup>

## **ESTABLISHMENT OF A FILING AND REGISTRATION SYSTEM**

The Annex to the Convention provides the potential for a global registry to enable the filing and searching of assignments of receivables. The searchable registry will enable any party to obtain search results which will, in most cases, be binding proof of registration along the line of Uniform Commercial Code Secretary of State filing systems in the United States. Such a registry is voluntary, not mandatory under the Convention. A ratifying country can agree on a voluntary basis to sign onto the registry by declaration and should be encouraged to do so given that a filing and registration system is by far the best means to provide notice to third parties of receivables collateral assignment or sale. Once a ratifying country signs on by declaration, it will be bound by the registry's governing rules.<sup>18</sup>

## **WHAT ARE THE IMPLICATIONS OF THESE KEY FEATURES?**

As explained above, the Convention and its key features, taken holistically, make the assignment of receivables across jurisdictions and legal traditions easier. The administrative complexity as well as the cost and risk of assigning receivables will be reduced if countries adopt the Convention without material deviation from its terms; at the same time, the financing and commercial practices linked to the assignment of receivables in transactions with a cross-border component will benefit from greater consistency and materially improved certainty.

The Convention's enablement of bulk assignments, simplified account debtor notice procedures and choice of law provisions, and partial override of anti-assignment clauses in the underlying sales contracts, are a clear recognition of the imperative around increased global capacity for receivables-based financing and sale. The Convention effectively circumvents legal limitations extant in certain jurisdictions, that have the unintended consequences of discouraging the use of assignments of receivables in support of international commerce.

## **Forward View; Next Steps**

In October 2019, the United States became the second country after Liberia to ratify the Convention. The Convention requires ratification by five countries before it enters into full force and effect between and among the adopting countries.

After languishing for sixteen years, the advocacy efforts of various industry groups and professional and trade associations<sup>19</sup> propelled forward momentum, and in 2016, President Obama sent the Convention for advice and consent by the United States Senate. These groups thoughtfully positioned the Convention as a technical, apolitical solution to a very specific finance-driven global problem, culminating in a successful outcome when the Convention was ratified in October 2019.<sup>20</sup>

## **WHAT EFFORTS ARE AFOOT TO RATIFY THE CONVENTION ACROSS THE GLOBE?**

It is the mission of the United Nations Commission on International Trade (UNCITRAL), which prepared the draft of the Convention in 2001, to advance the ball for its adoption by countries around the world, and the hope is that the United States' ratification will accelerate this process.<sup>21</sup> UNCITRAL will actively engage with various countries to promote the benefits of the Convention and persuade them to join, highlighting the advantages to SMEs of doing so.<sup>22</sup> Other countries that are likely to jump on the bandwagon are those who have already participated in secured transactions reform: the UAE, Colombia, the Philippines, Zambia and Kenya, among others.<sup>23</sup> Also promising candidates for ratification are the group of 73 countries who ratified the Cape Town Convention on International Interests in Mobile Equipment aircraft protocol, which facilitates the efficient cross-border purchase, sale and financing of aircraft equipment and likewise rests on UCC Article 9 principles.<sup>24</sup> These countries could be open and receptive to the very similar package of economic stimuli which

the Convention offers. Additionally, it is expected that the World Bank and other international organizations will get the message out to governments about the benefits of the Convention.

### **WHAT FACTORS MIGHT IMPEDE PROGRESS?**

The Convention languished for some 20 years, and there are very specific reasons why there was little forward momentum. Throughout Europe and elsewhere, there is no one consistent approach to the laws of proprietary title transfer, i.e., what constitutes a valid assignment of receivables. There are also significant variances in local bankruptcy and insolvency law and procedure. The bespoke approach of each jurisdiction is built on decades, if not centuries, of case law precedent and customary practices and local biases. This means the most formidable challenge to the Convention's widespread and consistent adoption is overcoming the underlying disparities in the laws of title transfer, bankruptcy and insolvency. For example, it is possible that the Convention can achieve the laudable goal of facilitating a clear and more common understanding of a "true sale." Greater consensus around this concept is fundamentally important to increasing FI and fintech activity as providers of supply chain finance and, in particular, payables finance programs, where questions about the legal and accounting character of these structures have been an impediment to broader uptake and deployment. (See the "Accounting and Rating Agency Treatment of Supply Chain and Other Trade Payables Programs" [post](#) on Mayer Brown's Retained Interest Blog.) The problem is, the concept of "true sale" varies widely from jurisdiction to jurisdiction—even as between the United States and England—if such concept is recognized at all.

These local law disparities will likely manifest themselves in the form of declarations filed by various countries who move forward to adopt the Convention. Under the Convention, countries have the option to limit the application of certain sections or to exclude the application to certain types of assignments or to specific types of receivables by declaration.<sup>25</sup> The Convention allows for such declarations<sup>26</sup> except in the case of the anti-assignment clause override provision as explained above. This means that a country could ratify the Convention but retain laws that would not recognize certain aspects of the Convention.<sup>27</sup>

Although the Convention contains a general prohibition on changing or invalidating the legal effect of its provisions, the challenge is to persuade governmental decision-making bodies to join the Convention whole cloth, without deviation, unless in direct conflict with local law practice and policy. Otherwise the result will be a patchwork of inconsistent and potentially conflicting approaches to interpretation and implementation of Convention principles and provisions.

Another challenge is that even if factoring, trade finance or other industry groups fully understand the importance of the Convention, each country ultimately becoming a party to the Convention would need to involve its ministry of foreign affairs, who may not be receptive to the benefits. Additionally, some countries are undergoing a more comprehensive reform of their secured transactions laws and may prefer to wait until they have completed those reforms.

### **WHAT IS THE BEST WAY FORWARD?**

In the United States, ratification happened because the Convention was positioned as a technical, apolitical solution. This approach, if replicated in the effort to drive further global ratification and adoption, should prove successful in persuading governments that the Convention solves a major commercial, financial and inclusion problem in a non-political way. While UNCITRAL is leading the charge on widespread adoption without deviation, supportive messaging from corporates, chambers of commerce and other interested/influential stakeholders in various jurisdictions could be effective in complementing the advocacy efforts of UNCITRAL. These stakeholders and influencers could help to strongly reinforce the recommended apolitical positioning of the ratification process to governmental bodies. Additionally, past

similar exercises, like the 73-country adoption of the Aircraft Protocol in connection with the Cape Town Convention on International Interests in Mobile Equipment, can be leveraged. Also key is persuading the critical decision-makers—governmental ministries of foreign affairs—of the risks of diluting the power of the Convention through qualifiers, including local laws and statutes that may continue to disregard certain provisions. The Convention’s strength is in its uniformity, and a unified text and unified rules without dilution should be the preeminent goal as the ratification process continues. The flexibility to buy, sell and finance receivables free of elaborate account debtor notice requirements, restrictions on bulk or future sales of receivables and worries about anti-assignment clauses is critical to the global growth of accounts receivable financing as an essential complement to the global trade finance toolset.

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*For more information about the topics raised in this Legal Update, please contact either of the authors:*

**Rebecca Fruchtman**

Counsel

Mayer Brown LLP

[rfruchtman@mayerbrown.com](mailto:rfruchtman@mayerbrown.com)

**Alexander R. Malaket**

President

OPUS Advisory Services International Inc.

[ar.malaket@opus-advisory.com](mailto:ar.malaket@opus-advisory.com)

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## Endnotes

- <sup>1</sup> United Nations Convention on The Assignment of Receivables in International Trade.  
<https://www.uncitral.org/pdf/english/texts/payments/receivables/ctc-assignment-convention-e.pdf>
- <sup>2</sup> Trade Finance and SMEs: Bridging the Gap in Provision, 2016, P.6.  
[https://www.wto.org/english/res\\_e/booksp\\_e/tradefinsme\\_e.pdf](https://www.wto.org/english/res_e/booksp_e/tradefinsme_e.pdf)
- <sup>3</sup> Asian Development Bank, Trade Finance Gaps, Growth and Jobs Survey 2019.  
<https://www.adb.org/sites/default/files/publication/521096/adb-brief-113-2019-trade-finance-survey.pdf>
- <sup>4</sup> Aside from the United States signing in 2003, little happened after the 2002 publication of Harry Sigman's (now deceased) and Edwin Smith's seminal article on the Convention in *The Business Lawyer*, the opening paragraph of which seemed to anticipate (or hope for) rapid adoption or accession: "In July 2001, after a six-year process, the United Nations Commission on International Trade Law (UNCITRAL) completed its work on the multilateral 'Convention on the Assignment of Receivables in International Trade.' The Convention was adopted by the United Nations General Assembly on December 12, 2001 and is now open for signature and ratification or accession by countries." Harry C. Sigman and Edwin M. Smith, *Toward Facilitating Cross-Border Secured Financing and Securitization: An Analysis of the United Nations Convention on the Assignment of Receivables in International Trade*, 57 BUS. LAW. 727 (2002). However, when the United States itself did not move to ratify, other countries that may have had interest also deprioritized it according to Hal Burman, a former official with the United States Department of State, Office of Legal Adviser who was instrumental in promoting the Convention through the United States ratification process.
- <sup>5</sup> Receivables can be defined as contractual rights to payment arising from goods sold or services rendered.
- <sup>6</sup> As explained by Mr. Burman (former official with the US Department of State, Office of Legal Adviser).
- <sup>7</sup> Including Messrs. Sigman and Smith, the *Toward Facilitating Cross-Border Secured Financing and Securitization* co-authors who were members of the drafting committee that revised Article 9 of the Uniform Commercial Code from 1993 to 1998. The Uniform Commercial Code is in the process of being revised to reference the Convention in the appropriate Official Comment.
- <sup>8</sup> As the December 12, 2017, letter to the Senate Committee on Foreign Relations from a coalition of organizations, including BAFT (Bankers Association for Finance and Trade), the Commercial Finance Association, the U.S. Chamber of Commerce, and the National Law Center for Inter-American Free Trade, among others, supporting the ratification of the Convention states: "US lenders often are unable or unwilling to extend credit to US companies seeking to borrow against their receivables owed by customers in other countries because the laws in many foreign countries make it difficult or cost-prohibitive to use foreign receivables as collateral for loans." The same challenge is faced by lenders based in other jurisdictions.
- <sup>9</sup> Quoting Mr. Burman.
- <sup>10</sup> Convention, *Preamble*.
- <sup>11</sup> *Article 44* of the Convention generally prohibits "Reservations" by ratifying countries (except with respect to the conflicts of laws principles set forth in *Chapter V* thereof). Reservations enable ratifying countries to modify or nullify the legal effect of certain provisions of a convention in their application to that country. (The definition for the term "Reservations" is in Article 2(d), Vienna Convention on the Law of Treaties of 1969.)
- <sup>12</sup> *Article 2(a)* of the Convention defines "Assignment" as the transfer by agreement from one person ("assignor") to another person ("assignee") of all or part of or an undivided interest in the assignor's contractual right to payment of a monetary sum ("receivable") from a third person (the "debtor").
- <sup>13</sup> The Convention's general nullification of anti-assignment contractual clauses in the underlying sales contract applies to "trade receivables," which are broadly defined in the Convention as receivables arising from a contract for the sale or lease of goods or services other than financial services or certain types of contracts. For more specifics on how the Convention's "anti-assignment clause" override works, see Explanatory Note of UNCITRAL secretariat on the Convention, page 34, note 27.
- <sup>14</sup> See Footnote 11.
- <sup>15</sup> Explanatory Note of UNCITRAL secretariat on the Convention, page 41, note 49.
- <sup>16</sup> As summarized by the American Bar Association in its *Resolutions* adopted by the House of Delegates dated February 4-5, 2002, recommending that the United States sign and ratify the Convention.
- <sup>17</sup> Explanatory Note of UNCITRAL secretariat on the Convention, page 28, note 4.
- <sup>18</sup> According to a member of the UNCITRAL Secretariat, the creation of the Registry was one of the unresolved aspects within the Convention and thus placed in the Annex. The Convention also does not necessarily envisage an "international" registry. The 2016 UNCITRAL Model Law on Secured Transactions, which applies to both outright transfers and transfers for security purposes (art. 1(2)), foresees registration as a way to make such transactions effective against third parties (art. 18) and has provisions pertaining to a domestic registry.

[https://uncitral.un.org/sites/uncitral.un.org/files/media-documents/uncitral/en/19-08779\\_e\\_ebook.pdf](https://uncitral.un.org/sites/uncitral.un.org/files/media-documents/uncitral/en/19-08779_e_ebook.pdf)

- <sup>19</sup> See Footnote 8 above.
- <sup>20</sup> As explained by Mr. Burman.
- <sup>21</sup> Press release of UNCITRAL (24 October 2019) available at <http://www.unis.unvienna.org/unis/en/pressrels/2019/unisl286.html>
- <sup>22</sup> As explained by a member of the UNCITRAL Secretariat. Quoting Mr. Burman, "It is the approach of some in the UN system to encourage concurrent adoption of the UNCITRAL model law on secured finance negotiated after the Convention, so that a participating jurisdiction's laws are compatible both with modern commercial finance practices as well as the Convention. Adoption of both would be ideal."
- <sup>23</sup> Quoting Robert Trojan, prominent financial professional and CEO of Financial Services Insights. Mr. Trojan was also a key player in the Convention's United States ratification process.
- <sup>24</sup> As explained by Messrs. Trojan and Burman.
- <sup>25</sup> Convention, *Articles 41 and 44*.
- <sup>26</sup> A declaration (unlike a reservation, which is not generally permitted under *Article 44* of the Convention except with respect to conflicts of law principles) clarifies a country's position but does not purport to modify the legal effect of the treaty. Raising permitted declarations and excluding the applicability of certain treaty provisions ensures that there is no conflict with domestic law.
- <sup>27</sup> The United States filed a lengthy declaration in connection with its ratification of the Convention which contains a number of understandings and interpretive provisions.

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