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www.klgates.com

Authors:

Nanci L. Weissgold
nanci.weissgold@klgates.com
+1.202.778.9314

Kerri M. Smith
kerri.smith@klgates.com
+1.202.778.9445

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Third Party Loan Modification Companies and Foreclosure Consultants Subject to MARS' Orbit

A new law provides the Federal Trade Commission ("FTC" or "Commission") with additional rulemaking authority in the mortgage arena, and with this approval, the FTC has launched into the rulemaking process. The Omnibus Appropriations Act of 2009 ("Appropriations Act"), signed into law on March 11, 2009, contains a tiny provision that could potentially have far-reaching consequences to the mortgage industry, and may also extend to those third party entities assisting in foreclosure mediation efforts. Section 626 of the Appropriations Act mandates that the FTC "initiate a rulemaking proceeding with respect to mortgage loans in accordance with the Administrative Procedures Act" within 90 days from enactment, which has resulted in the FTC initiating the Mortgage Assistance Relief Services Rulemaking ("MARS Rulemaking" or "MARS"), as well as another rulemaking that addresses mortgage loan origination, appraisal, and servicing practices. Under MARS, the FTC is contemplating issuing final rules that would subject those offering mortgage assistance relief services, such as third party loan modification companies and foreclosure consultants, to new substantive requirements.

The Appropriations Act provided no guidance to the FTC regarding the type of rule it should issue, the topics to be addressed, or the types of entities subject to the rule. After its enactment, questions were raised as to whether this overly broad mandate would withstand constitutional challenge. Consequently, two months later, Congress tacked on the end of the Credit CARD Act of 2009 (the "Credit CARD Act")¹ provisions that amend the FTC's rulemaking authority on mortgage lending, in order to guide the rulemaking to address unfair and deceptive practices of the mortgage industry, and expressly limit the types of entities subject to the rule. While the Credit CARD Act was enacted on May 22, 2009, the provisions on the scope of the FTC's rulemaking authority became retroactively effective on March 12, 2009.

Congress not only gave the FTC a broad mandate in implementing regulations, it provides a strong set of teeth to enforce its new rules. The revised law provides that the FTC may enforce its rules "in the same manner, by the same means, and with the same jurisdiction, powers, and duties as though all applicable terms and provisions of the Federal Trade Commission Act (15 U.S.C. 41 *et seq.*)["FTC Act"] were incorporated into and made part of this section."² Thus, as stated in the MARS Rulemaking, a violation could be treated as a violation of a rule under Section 18 of the FTC Act, and the FTC could impose civil penalties.³ Moreover, Congress expands the authority of state attorneys general, providing that if he or she has "reason to believe that an interest of the residents of the state have been or is being threatened or adversely affected by the engagement of *any person subject to a rule ... in a practice that violates such rule,*" the state attorney general may "bring a civil action on behalf of its residents in an appropriate state or district court of the United States: (1) to enjoin the practice; (2) to enforce compliance with the rule; (3) to obtain damages, restitution, or other compensation on behalf of residents of the state;

or (4) to obtain penalties and relief provided by the FTC Act and such other relief as the court considers appropriate.”⁴

While the Appropriations Act authorizes the FTC to initiate “a” rulemaking proceeding, on June 1, 2009, the FTC initiated two such proceedings, or maybe one proceeding broken into two parts - the Mortgage Acts and Practices Rulemaking (“MAP Rulemaking”) and the MARS Rulemaking. This alert addresses the MARS Rulemaking, which reaches those providing mortgage assistance relief services, and an alert addressing the MAP Rulemaking, which focuses on those originating and servicing mortgage loans, will be forthcoming. Comments on the MARS Rulemaking must be received by July 15th.

Types of Entities Subject to the Rule

The Appropriations Act did not specify the types of entities subject to this rulemaking initiative, thus many wondered if the FTC would assert jurisdiction over entities supervised by federal banking and credit union regulators. The Credit CARD Act clarifies the scope of the FTC’s authority, asserting that it cover only those entities over which the FTC has jurisdiction under the FTC Act. This includes entities other than banks, thrifts, federal credit unions and non-profits engaging in activities covered by the rules. While certain financial institutions will not be subject to any final rule, non-bank affiliates of banks, such as parent companies or subsidiaries, or entities that contract with banks to perform certain services on the bank’s behalf will be covered. The FTC acknowledges the scope of its authority in both its MARS Rulemaking and its MAP Rulemaking. So while the state attorneys general may enforce the rules promulgated by the FTC on mortgage matters, they cannot rely on this provision to bring an action against federally chartered banks and credit unions, as those entities will not be subject to the rule.

Mortgage Assistance Relief Services Rulemaking

While the Appropriations Act gave the FTC authority to issue rules related to unfair or deceptive practices with respect to mortgage loans, the Credit CARD Act adds that the rulemaking “may include unfair or deceptive acts or practices involving loan

modification and foreclosure rescue services.” So while Congress requires that the FTC engage in rulemaking for comprehensive rules with respect to mortgage services (and possibly other activities that occur through the life-cycle of a mortgage loan), it allows the FTC flexibility to discern whether rules are necessary in the modification or foreclosure context. This distinction may have played out in the MARS Rulemaking process, as the FTC appears tepid about whether it should specifically promulgate rules regulating “the practices of entities (other than mortgage servicers) who offer assistance to consumers in dealing with owners or servicers of their loans to modify them or avoid foreclosure,” but stands more assuredly that rules are required for the activities that occur through the life-cycle of a mortgage loan.

The FTC currently has authority to challenge practices that are unfair and deceptive under Section 5 of the FTC Act, and has used that authority to challenge the practices of companies engaging in loan modification and foreclosure rescue services at least ten times over the past few years.⁵ The Commission also has issued numerous publications to consumers warning of foreclosure rescue scams,⁶ sent warning letters to 71 companies for marketing potentially deceptive mortgage modification and foreclosure assistance programs,⁷ and joined forces with other federal and state regulators to crack down on loan modification and foreclosure rescue entities.⁸

Many of the states have initiated their own efforts to combat fraud in this area of loan modification and foreclosure rescue. Some states have enacted new laws regulating, and in some cases, licensing “foreclosure consultants.”⁹ States also have been reinterpreting existing law, including mortgage broker statutes, debt settlement or debt management law, or credit counseling and debt collection laws to regulate these practices.¹⁰ States also have initiated their own enforcement actions against these entities and have issued press releases announcing such efforts.¹¹ According to the FTC website, states have initiated or closed approximately 150 enforcement actions on foreclosure rescue as of March 31, 2009.¹² And this list only represents a “sampling of actions,” and does not include any recent enforcement activity over the last three months.

In light of all this ongoing activity in the area of loan modification and foreclosure rescue, the question the FTC is asking is whether additional rules are needed to address the conduct of those who provide or advertise loan modification and foreclosure rescue services given the proliferation in today's economy of third-party providers offering to assist homeowners in obtaining a loan modification or preventing foreclosure.

Need for FTC Rule

Recognizing the number of state laws that have been enacted or interpreted to regulate loan modification activities, and the number of enforcement actions that have been brought against unscrupulous foreclosure rescue and loan modification companies by both state attorneys general and the FTC itself, the Commission is asking for comments on whether the FTC should promulgate a rule to address these activities. If the answer to this question is yes, the following questions probe into the possible scope of such a rule.

Scope of Covered Entities

While the MARS Rulemaking states that any final rule will not apply to entities outside the FTC's jurisdiction, such as banks, thrifts, credit unions and non-profits, it nonetheless requests comments on the scope of loan modification and foreclosure rescue activities conducted by these exempt entities and the extent of competition between these exempt entities and those subject to any proposed rule.

The FTC also is concerned with attorneys. In light of the current economic climate, some foreclosure rescue firms allude to the fact that they are or may be law firms (which may not be the case). This is an area of concern for servicers as they may not know when they should communicate through the borrower directly or through his or her counsel. The FTC notes that attorneys may be exempt from state foreclosure consultant or debt settlement laws. The FTC has requested comment on whether attorneys should be exempt from any FTC proposed rule.

The FTC also broadly asks what other class of persons or entities should be exempt. The FTC appears primarily concerned with foreclosure rescue and loan modification entities that solicit consumers, often by reviewing publicly available default or

foreclosure notices, or market their services through mail, email, radio, television or Internet; however, it is not clear if the FTC could also include other entities within the purview of a new rule. A number of companies are starting to fill a niche by assisting servicers process loan modifications. These companies are typically hired and compensated by the lender or servicer. Although these types of companies do not appear to be the primary target of the FTC's proposed rulemaking, absent express guidance, it may not be clear whether or not such third party vendors would be covered by any final rule. As a result, those interested in this issue may want to submit comments to the FTC before the July 15th deadline.

Scope of Covered Practices

The FTC cites to a number of practices that it views as unfair or deceptive. For example, the FTC has brought actions against companies that claim they could stop a borrower's foreclosure action or bring about a modification, and similarly claim a certain success rate without being able to substantiate their claim.¹³ Similarly, the FTC found that companies that have represented that they are affiliated with government or nonprofit agencies when they were not were being unfair or deceptive.¹⁴ Further, companies that charged significant up-front fees and promised refunds if their loss mitigation efforts were successful but failed to deliver on their promise were subject to the FTC's enforcement authority.¹⁵ The FTC brought actions against foreclosure rescue companies that advise consumers, including those consumers that are still current on their loan, to stop making payments and cease communicating with their servicer whom the company claims they will communicate with on their behalf.¹⁶ These practices allegedly have the opposite effect of increasing the chance of foreclosure.

If the FTC were to adopt a rule regulating loan modification and foreclosure rescue servicer providers, the FTC is soliciting comments on what practices should be addressed in the rule such as whether the rule should:

- Require written contracts and specific disclosures;
- Provide consumers with a right to cancel a contract, and if so, what those rights should be;

- Ban advance fees until the servicers contracted for or promised are completed, or otherwise restrict the type, amount and timing of the fees charged; and
- Otherwise regulate fees and refund practices, and if so, what types of fee restrictions should be imposed.

The Commission also seeks advice on:

- When the protections of a proposed rule should take effect: before the consumer receives a notice of default, after such a notice is received, or when foreclosure proceedings actually begin.
- What other state restrictions or challenged conduct should or should not be covered in a proposed rule.
- Whether there are other deceptive acts or practices of loan modification and foreclosure

rescue servicers that neither the FTC nor the states have addressed that the FTC should address.

Conclusion

It would be unlikely that any new rule would grant the FTC any expansive pull over those third party entities helping borrowers avoid foreclosure beyond those powers which the FTC currently holds.

However, state attorneys general may benefit from expanded enforcement authority. What other activities the FTC may address in its rulemaking is yet to be seen. We will be looking at how this rule could interplay with existing law, and what its impact will be on servicers, or those entities assisting servicers, in loss mitigation efforts. While once a tiny star not quite on the radar screen, servicers should continue to follow MARS' orbit.

¹ Pub. L. No. 111-24, Title V, § 511(a), 123 Stat. 1763 (effective Mar. 12, 2009); see amended FTC provisions at 15 U.S.C.S. § 1568.

² See *id.*

³ See 15 U.S.C. §§ 57a and 57b.

⁴ Before initiating an enforcement action, the state must notify the primary federal regulator, at least 60 days in advance, and the primary federal regulator may intervene in the action. See Credit CARD Act § 511(a) (which substituted the term "primary federal regulator" for "Commission," as used in the Appropriations Act.) We also note that the Credit CARD Act amended the provision so that attorneys general may not bring civil actions on behalf of their states for violations of section 128 of the Truth in Lending Act ("TILA") or any other provision of TILA, as originally enacted in the Appropriations Act.

⁵ 74 Fed. Reg. 26135, fn 44 and 45 (June 1, 2009). These two footnotes provide cases that the FTC has initiated and include *FTC v. New Hope Property LLC*, Case No. 1:09-cv-01203-JBS-JS (D.N.J. filed Mar. 17, 2009); *FTC v. Hope Now Modifications, LLC*, Case No. 1:09-cv-01204-JBS-JS (D.N.J. filed Mar. 17, 2009); *FTC v. National Foreclosure Relief, Inc.*, Case No. SACV09-117 DOC (MLGx) (C.D. Cal. filed Feb. 2, 2009); *FTC v. United Home Savers, LLP*, Case No. 8:08-cv-01735-VMC-TBM (M.D. Fla. filed Sept. 3, 2008); *FTC v. Foreclosure Solutions, LLC*, No. 1:08-cv-01075 (N.D. Ohio filed Apr. 28, 2008); *FTC v. Mortgage Foreclosure Solutions, Inc.*, Case No. 8:08-cv-388-T-23EAJ (M.D. Fla. filed Feb. 26, 2008); *FTC v. National Hometeam Solutions, Inc.*, Case No. 4:08-cv-067 (E.D. Tex. filed Feb. 26, 2008); see also *FTC v. Federal Loan Modification Law Center, LLP*, Case No. SACV09-401 CJC (MLGx) (C.D. Cal. filed Apr. 3, 2009); *FTC v. Thomas Ryan*, Civil No. 1:09-00535 (HHK) (D.D.C. filed March 25, 2009); *FTC v. Home Assure, LLC*, Case No. 8:09-CV-00547-T-23T-SM (M.D. Fla. filed Mar. 24, 2009).

⁶ See FTC Publication, A Note to Homeowners, available at: <http://www.ftc.gov/bcp/edu/pubs/consumer/homes/rea16.pdf>; see also FTC Publication, Mortgage Payments Sending You Reeling? Here's What to Do, available at:

<http://www.ftc.gov/bcp/edu/pubs/consumer/homes/rea04.shtm>; see also FTC Publication, Foreclosure Rescue Scams: Another Potential Stress for Homeowners in Distress, available at:

<http://www.ftc.gov/bcp/edu/pubs/consumer/credit/cre42.shtm>.

⁷ See, e.g., <http://ftc.gov/os/2009/04/090406warningletter.pdf>.

⁸ See Press Release *Federal, State Partners Announce Multi-Agency Crackdown Targeting Foreclosure Rescue Scams, Loan Modification Fraud* (April 6, 2009).

⁹ See, e.g., Cal. Civ. Code §§ 2945 *et seq.*; Colo. Rev. Stat. §§ 6-1-1101 *et seq.*; 6 Del. C. §§ 2400B *et seq.*; D.C. Code Ann. §§ 42-2431 *et seq.*; Fla. Stat. Ann. § 501.1377; Haw. Rev. Stat. Ann. §§ 480E-1 *et seq.*; Ill. Comp. Stat. Ann., Ch. 765 §§ 940/1 *et seq.*; Ind. Code Ann. § 24-5.5-1-1 *et seq.*; Iowa Code §§ 714E.1 *et seq.*; Md. Real Property Code Ann. §§ 7-301 *et seq.*; Code Mass. Reg., 940 CMR §§ 25.01 *et seq.*; Minn. Stat. Ann. §§ 325N.01 *et seq.*; Mo. Ann. Stat. §§ 407.935 *et seq.*; Neb. Rev. Stat. Ann. §§ 76-2701 *et seq.*; NH Rev. Stat. §§ 479-B:1 *et seq.*; NY CLS Real Prop. § 265-b; RI Gen. Laws §§ 5-79-1 *et seq.*

¹⁰ See e.g., Washington Interpretative Letter 2009-01, stating that those providing loan modification or negotiating residential mortgage loan terms are acting as mortgage brokers or loan originators and must be licensed under the Mortgage Broker Practices Act or the Consumer Loan Act unless specifically exempt from those Acts, available at:

http://www.dfi.wa.gov/cs/interpretive_statements/mortgage/IS-2009-01.pdf; see also N.J. Stat. Ann. § 17:16G-1c(1), which provides that a person engaged as a third party in mortgage loan modification activities in New Jersey must be licensed as a debt adjuster pursuant to N.J.S.A. 17:16G-1 *et seq.*, unless exempt from the licensing requirement; see also Maryland Advisory 09-08, providing that businesses which provide loss mitigation consulting, foreclosure prevention, mortgage loan modification, and/or similar services likely will be subject to the Maryland Credit Services Businesses Act, available at:

<http://www.dllr.state.md.us/finance/advisories/advisory9-08.htm>.

¹¹ See FTC Publication, "State Foreclosure Rescue Enforcement Actions - Sampling of Actions (March 31, 2009)," available at: <http://www.ftc.gov/os/2009/04/090406foreclosurerescue.pdf>

¹² *Id.*

¹³ See, e.g., *FTC v. Federal Loan Modification Law Center, LLP*, Case No. SACV09-401 CJC (MLGx) (C.D. Cal. filed Apr. 3, 2009); *FTC v. National Foreclosure Relief, Inc.*, Case No. SACV09-117 DOC (MLGx) (C.D. Cal. filed Feb. 2, 2009); *FTC v. Foreclosure Solutions, LLC*, No. 1:08-cv-01075 (N.D. Ohio filed Apr. 28, 2008); *FTC v. Mortgage Foreclosure Solutions, Inc.*, Case No. 8:08-cv-388-T-23EAJ (M.D. Fla. filed Feb. 26, 2008). Additionally, some entities claim to be associated with or to have good relationships with the consumer's mortgage servicer. *FTC v. Home Assure, LLC*, Case No. 8:09-CV-00547-T-23T-SM (M.D. Fla. filed Mar. 24, 2009).

¹⁴ For example, in two cases the Commission charged defendants for falsely advertising themselves to be associated with the HOPE NOW Alliance, and then breaking promises to secure loan modifications or alternatively, to refund the money of consumers whose loans could not be modified. See *FTC v. New Hope Property LLC*, Case No. 1:09-cv-01203-JBS-JS (D.N.J. filed Mar. 2009); *FTC v. Hope Now Modifications, LLC*, Case No. 1:09-cv-01204-JBS-JS (D.N.J. filed Mar. 2009).

¹⁵ See, e.g., *FTC v. Home Assure, LLC*, Case No. 8:09-CV-00547-T-23T-SM (M.D. Fla. filed Mar. 24, 2009) (alleging that defendant promised "100% SATISFACTION GUARANTEE OR YOUR MONEY BACK"); *FTC v. United Home Savers, LLP*, Case No. 8:08-cv-01735-VMC-TBM (M.D. Fla. filed Sept. 3, 2008); *FTC v. National Hometeam Solutions, LLC*, Case No. 4:08-cv-067 (E.D. Tex. filed Feb. 26, 2008).

¹⁶ See, e.g., *FTC v. Home Assure, LLC*, Case No. 8:09-CV-00547-T-23T-SM (M.D. Fla. filed Mar. 24, 2009); *FTC v. National Hometeam Solutions, LLC*, Case No. 4:08-cv-067 (E.D. Tex. filed Feb. 26, 2008).

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For more information, please contact one of the professionals listed below.

LAWYERS

Boston

R. Bruce Allensworth	bruce.allensworth@klgates.com	+1.617.261.3119
Irene C. Freidel	irene.freidel@klgates.com	+1.617.951.9154
Stephen E. Moore	stephen.moore@klgates.com	+1.617.951.9191
Stanley V. Ragalevsky	stan.ragalevsky@klgates.com	+1.617.951.9203
Nadya N. Fitisenko	nadya.fitisenko@klgates.com	+1.617.261.3173
Brian M. Forbes	brian.forbes@klgates.com	+1.617.261.3152
Andrew Glass	andrew.glass@klgates.com	+1.617.261.3107
Phoebe Winder	phoebe.winder@klgates.com	+1.617.261.3196

Charlotte

John H. Culver III	john.culver@klgates.com	+1.704.331.7453
--------------------	-------------------------	-----------------

Los Angeles

Thomas J. Poletti	thomas.poletti@klgates.com	+1.310.552.5045
-------------------	----------------------------	-----------------

Miami

Paul F. Hancock	paul.hancock@klgates.com	+1.305.539.3378
-----------------	--------------------------	-----------------

New York

Philip M. Cedar	phil.cedar@klgates.com	+1.212.536.4820
Elwood F. Collins	elwood.collins@klgates.com	+1.212.536.4005
Steve H. Epstein	steve.epstein@klgates.com	+1.212.536.4830
Drew A. Malakoff	drew.malakoff@klgates.com	+1.216.536.4034

San Francisco

Jonathan Jaffe	jonathan.jaffe@klgates.com	+1.415.249.1023
----------------	----------------------------	-----------------

Seattle

Holly K. Towle	holly.towle@klgates.com	+1.206.370.8334
----------------	-------------------------	-----------------

Washington, D.C.

Costas A. Avrakotos	costas.avrakotos@klgates.com	+1.202.778.9075
Melanie Hibbs Brody	melanie.brody@klgates.com	+1.202.778.9203
Daniel F. C. Crowley	dan.crowley@klgates.com	+1.202.778.9447
Eric J. Edwardson	eric.edwardson@klgates.com	+1.202.778.9387
Anthony C. Green	anthony.green@klgates.com	+1.202.778.9893
Steven M. Kaplan	steven.kaplan@klgates.com	+1.202.778.9204
Phillip John Kardis II	phillip.kardis@klgates.com	+1.202.778.9401
Rebecca H. Laird	rebecca.laird@klgates.com	+1.202.778.9038
Laurence E. Platt	larry.platt@klgates.com	+1.202.778.9034
Phillip L. Schulman	phil.schulman@klgates.com	+1.202.778.9027
Nanci L. Weissgold	nanci.weissgold@klgates.com	+1.202.778.9314
Kris D. Kully	kris.kully@klgates.com	+1.202.778.9301
Morey E. Barnes	morey.barnes@klgates.com	+1.202.778.9215
David L. Beam	david.beam@klgates.com	+1.202.778.9026
Emily J. Booth	emily.booth@klgates.com	+1.202.778.9112

Holly Spencer Bunting	holly.bunting@klgates.com	+1.202.778.9853
Krista Cooley	krista.cooley@klgates.com	+1.202.778.9257
Elena Grigera	elena.grigera@klgates.com	+1.202.778.9039
Melissa S. Malpass	melissa.malpass@klgates.com	+1.202.778.9081
David G. McDonough, Jr.	david.mcdonough@klgates.com	+1.202.778.9207
Stephanie C. Robinson	stephanie.robinson@klgates.com	+1.202.778.9856
Kerri M. Smith	kerri.smith@klgates.com	+1.202.778.9445
David Tallman	david.tallman@klgates.com	+1.202.778.9046

**Director of Licensing
Washington, D.C.**

Stacey L. Riggin	stacey.riggin@klgates.com	+1.202.778.9202
------------------	---------------------------	-----------------

**Regulatory Compliance Analysts
Washington, D.C.**

Dameian L. Buncum	dameian.buncum@klgates.com	+1.202.778.9093
Teresa Diaz	teresa.diaz@klgates.com	+1.202.778.9852
Jennifer Early	jennifer.early@klgates.com	+1.202.778.9291
Robin L. Gieseke	robin.gieseke@klgates.com	+1.202.778.9481
Allison Hamad	allison.hamad@klgates.com	+1.202.778.9894
Brenda R. Kittrell	brenda.kittrell@klgates.com	+1.202.778.9049
Dana L. Lopez	dana.lopez@klgates.com	+1.202.778.9383
Patricia E. Mesa	patty.mesa@klgates.com	+1.202.778.9199
Jeffrey Prost	jeffrey.prost@klgates.com	+1.202.778.9364

Anchorage Austin Beijing Berlin Boston Charlotte Chicago Dallas Dubai Fort Worth Frankfurt Harrisburg Hong Kong London
Los Angeles Miami Newark New York Orange County Palo Alto Paris Pittsburgh Portland Raleigh Research Triangle Park
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