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REPORT ON THE MOST RELEVANT TAX ISSUES FOR CORPORATIONS IN URUGUAY

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1. TERRITORIAL PRINCIPLE

The Uruguayan Tax System is ruled by the territorial principle.

Under this principle, the corporate income tax levies Uruguayan-source income, while capital taxes levy the assets located, placed or economically used in Uruguay, regardless of the nationality or domicile of taxpayers.

2. TAXES THAT LEVY CORPORATIONS' ACTIVITIES

The most important taxes to be considered by Corporations in Uruguay are the following:

- Corporate Income Tax (IRAE)
- Income Tax to Non- Residents (IRNR) on dividends
- Capital Tax (IP)
- Corporations Control Tax (ICOSA)
- Value Added Tax (IVA)
- Excise Tax (IMESI)

2.1 Corporate Income Tax (IRAE)

IRAE levies net income from Uruguayan source generated by the company at a rate of 25%.

o Determination of the Net Income

Net income is determined annually by deducting from the company's total revenues for the fiscal year, all the expenses needed to generate and maintain the income, as long as they are accrued within the fiscal year in which the tax is determined and are also dully documented.

In order to deduct expenses, it is also required for the counterpart who invoices such costs to be an IRAE, IRNR (Non Residents' Income Tax) or IRPF (Personal Income Tax) payer in Uruguay. If we are dealing with a foreign entity, it is required to be taxed by Income Tax in the country of residence.

There is also a limitation on the deduction of expenses when the counterpart who is invoicing those expenses, is levied by IRNR (Non Residents' Income Tax) or for capital income by the IRPF (Personal Income Tax). In these cases, the expenses' deduction is limited to its 48% (proportional deduction). This 48% rises from considering, as appropriate, the relationship between the maximum rate of IRPF or IRNR (12% in both cases) and the IRAE rate (25%).

Consequently, when expenses are to be deducted from IRPF (for capital income) or IRNR taxpayers it will only be deductible 48% of the amount of expenses (48% is the result of proportioning the rates of 12% of IRPF/IRNR and 25% of IRAE).

It must also be considered that when expenses constitute, for the counterpart, taxable income in its country, the expenses' deduction will be 100% of the amount but only if the foreign tax rate equals or exceeds 25%. If the foreign tax rate is lower than 25%, a proportion of rates should be applied as detailed in the preceding paragraph. If the foreign supplier is taxed in its country of origin and also in Uruguay by IRNR, the proportion of rates is made by considering the IRNR (12%) plus the foreign Income Tax rate.

- o **Fiscal Losses**

Fiscal losses from previous fiscal years are deductible from net income provided that no more than 5 years have gone through from the fiscal year in which the loss occurred. The amount of tax losses is updated by an inflation index.

- o **Annual and Advance Payments**

IRAE is settled by an annual tax return. This tax return is submitted to the Tax Office (DGI) on the fourth month following the closing date of the company's fiscal year, together with the tax balance payment if corresponds.

From the second fiscal year on, and when IRAE taxable income was obtained in the immediately preceding fiscal year, the company must make IRAE monthly payments on account for the current fiscal year. The monthly amount of these advance payments is determined by applying to the amount of monthly gross revenues taxable by IRAE, a coefficient which arises from considering the quotient between the total IRAE tax amount from the previous fiscal year and the amount of gross revenues taxed by IRAE in the previous fiscal year (relation between the tax and the taxable revenues of the previous fiscal year). At the time of paying the annual tax, the advance tax payments made according to the referred procedure are deducted from the definitive annual tax.

If the amount of the advance payments is higher than the amount of the resulting IRAE annual tax, the taxpayer has a credit to its account. This credit can be granted by the Tax Office through a credit certificate.

- **Minimum Payment**

Notwithstanding the aforementioned provisions related to the IRAE, as from the time when the company begins to generate IRAE taxable revenues, it should begin to pay a minimum tax in a monthly basis, amount which is fixed in Uruguayan Pesos (annually set by the Tax Authority) and deductible from the annual IRAE tax. If the annual IRAE tax amount is lower than the amount of the minimum tax payments made during fiscal year, these minimum tax payments will be considered as the definite tax.

The amount of the minimum tax payment is set by the Tax Authorities in Uruguayan Pesos according to the taxpayer's income level in the previous fiscal year (5 levels are settled). The amount currently in force varies from a monthly floor of \$ 2,550 (approximately USD 140) to a monthly ceiling of \$ 6,400 (approximately USD 350). In the first fiscal year in which taxable revenues are generated, the company starts paying the monthly lowest tax amount.

2.2 Income Tax to Non-Residents (IRNR) on dividends

When Shareholders are Non-residents, dividends are taxed by IRNR at the rate of 7%.

The Corporation is responsible for withholding the IRNR and pay the tax to the Tax Office in the month following the credit or payment of dividends. Therefore, in the following month in which the General Shareholders' Meeting resolves to proceed with the distribution of dividends, IRNR must be withheld and paid to the Tax Office.

IRNR is determined by applying the 7% IRNR rate over the dividends to be distributed, with the ceiling of revenue determined by tax criteria.

2.3 Capital Tax (IP)

The Capital tax is an annual tax which levies company's net worth according to tax criteria at the fiscal year-end, at the rate of 1.5%.

- **Determination of taxable net worth**

The taxable net worth includes the entire Corporations' assets and rights economically located and used within Uruguay, valued according to fiscal criteria.

The deductible liabilities for the purposes of determining the taxable net worth by the IP are limited by tax rules. The deductible liabilities are mostly liabilities with local suppliers of goods and services and financial liabilities with local entities (in this case the liability to deduct comes from considering the average balance within the fiscal year, arisen from the balances at the end of each month).

Among other liabilities, import price balances and general financial liabilities incurred with individuals or other foreign entities are not deductible.

- **Annual and Advance Payment**

Capital Tax (IP) is settled by an annual tax return. This tax return is submitted to the Tax Office (DGI) together with the IRAE affidavit, within the fourth month following the fiscal year closure.

From the second fiscal year on, and when IP taxable net worth would have been obtained in the immediately preceding fiscal year, the company must make IP monthly advance payments on account of the current year's annual tax. The monthly amount of these advance payments is 11% of the annual IP tax which resulted in the previous fiscal year.

At the time of determining and paying the annual IP, advance payments made during the fiscal year are deducted according to the tax system referred to earlier. If the resulting amount of all the advance payments is higher than the amount of annual tax to be paid, the taxpayer will obtain a credit for this balance, which the Tax Office will grant in a credit certificate.

2.4 Corporations Control Tax (ICOSA)

ICOSA is an annual tax that levies Corporations, and is applied at the moment of constituting a company, and at fiscal year-ends.

The taxable base is IU 578.428. To that effect, the IU (indexed unit) price is considered as of December 31st of the year preceding the occurrence of the event (constitution or fiscal year-end).

The applicable rates are: 1,5% for the constitution of the Corporation and 0,75% for each fiscal year closure.

The ICOSA corresponding to the constitution of the corporation is paid only once during the constitution process and is part of the constitution cost.

The ICOSA for fiscal year-ends is cancelled through monthly advance payments equivalent to 1/12 of the annual amount. For advances made during the 2011 fiscal year, the amount to be paid is \$ 773 (about US\$ 40 per month).

The annual amount of ICOSA paid by the company can be deducted from the resulting annual Capital Tax (IP). If the ICOSA amount is higher than the IP amount, the payments will be considered as definitive.

2.5 Value Added Tax (IVA)

VAT levies the internal traffic of goods, the rendering of services within national territory, the introduction of goods into the country and the added value arising from construction activities.

The taxable event is considered to occur when a contract or any equivalent event is executed through the delivery or introduction of goods or the provision of services.

Exportations of goods and certain services (exhaustively determined by law)

are not taxed. Exporters can obtain a tax credit certificate for the VAT paid to their suppliers.

Among others, those entities developing activities taxed by IRAE are considered VAT taxpayers.

The basic VAT rate is 22%. There is a minimum 10% rate that applies to goods and services that relate essentially to certain groceries, medicines, pharmaceutical goods, hotel accommodation and real estate first sales made by corporations (construction activity).

○ Liquidation of VAT payment

VAT is a tax of annual liquidation, except for taxpayers included in the CEDE Unit (Contralor Especial de Empresas de la Dirección de Recaudación) which pay this tax under a monthly statement system.

VAT to be paid is calculated by deducting from sales VAT, the purchases VAT directly or indirectly related to the taxed activities. When there are simultaneously taxable and exempt transactions, purchases VAT directly related to taxable supplies is deductible, purchases VAT directly related to exempt transactions is non-deductible, and purchases VAT indirectly related to both activities is deducted proportionally.

In cases where at the end of each month or fiscal year (as appropriate), the VAT charged by suppliers and for import operations is higher than the sales VAT on taxable transactions, the emerging balance will not be refunded. This balance will be deducted together with the amount of tax charged for purchases in the VAT tax return of the following period.

Taxpayers who are not included in CEDE Unit make monthly tax advance payments, and submit its affidavit every six months which includes accrued monthly VAT from the beginning of the fiscal year.

The resulting amount of tax payments from the beginning of the fiscal year until the month before last will be deducted, thereby determining the monthly or annual payment as appropriate.

In those cases in which, the fiscal year's tax return shows that VAT paid for

taxable operations is higher than the accrued annual tax, the balance is returned to the taxpayer through a credit certificate.

Taxpayers included within the CEDE Unit, settle and pay VAT on a monthly basis.

2.6 Excise Tax (IMESI)

The IMESI is levied on first sale of goods determined on an exhaustive list, including inter alia automotive vehicles (except for those usually destined to agricultural activities), fuel and other oil by-products, lubricants and lubricating grease, electric power, alcoholic and non-alcoholic beverages, cosmetics and tobacco.

The IMESI rates vary depending on the taxable product, and are applied on either actual or estimated values determined by the Executive depending on their current selling price to consumers.

The IMESI taxpayers are both, manufacturers and importers of taxable products.

Exports are exempted from this tax.

This tax is settled and paid on a monthly basis, to which end the taxpayer must submit the monthly tax return.

Prior to obtaining customs clearance, any individual who is not an IMESI taxpayer, must pay this tax on imports of any taxable product.

3. OTHER RELEVANT CONCEPTS

Branch office of foreign company

Pursuant to Law No. 16.060, companies duly established abroad are recognized in Uruguay as a matter of law. Such companies are governed, as regards existence, status, operation and dissolution, by the laws of their place of constitution, insofar as they do not violate international public policy in Uruguay.

Foreign companies intending to undertake activities in Uruguay on a regular basis must establish a branch in the country.

For such purposes they must submit their incorporation papers to the Public Registry of Commerce, along with a resolution by the home office establishing the opening of the branch, its domicile, the appointment of an agent, and the allocation of capital in an amount not less than the minimum required for domestic corporations. All documents are to be duly legalized.

Subsequently, a summary of the incorporation minutes are to be published.

Permanent Establishment

The figure of permanent establishment arises when a non resident develops its economical activity partially or totally through a permanent location within the national territory.

The expression "Permanent Establishment" includes among other premises, branches, headquarters, office buildings and factories. Income obtained by Permanent Establishments is levied by IRAE at the rate of 25%.

4. TAX INCENTIVES

PROMOTION AND PROTECTION LAW OF INVESTMENTS IN URUGUAY

Law N° 16.906 declares the promotion and protection of investments made by domestic and foreign investors in Uruguay an issue of national interest.

This law and its implementing regulations establish an attractive legal framework for the development of new investments in the industrial, commercial and service areas in Uruguay.

In terms of promoting investments, a legal regime is established in which investors are granted with legal certainty, and equality between foreign and domestic investors is determined. Additionally, it guarantees free foreign transfers of capital, profits and other amounts related to investments. These transfers can be carried out using freely convertible currencies.

Benefits for either specific or general nature investments were established in order to enhance the protection of investors.

3.1 General investment benefits

The beneficiaries of these fiscal stimuli are those companies undertaking industrial or agricultural activities.

The acquisition of the following is considered as investment:

- ✓ Movables directly involved in the production cycle.
- ✓ Equipment for electronic data processing.
- ✓ Fixed improvements for manufacturing and agriculture activities.
- ✓ Intangible goods, such as trademarks and patents.
- ✓ Goods which are considered by the Executive to include technical innovation.

The automatic fiscal benefits offered by this law, are obtained by the mere act of performing the investment; no special process or authorization is required. These benefits are:

- ✓ Exemption from Capital Tax (IP) for moveable goods directly used in production and equipment of electronic data processing.
- ✓ Exemption from Value Added Tax (IVA) and Excise Tax (IMESI) for imported goods, and refund of Value Added Tax (IVA) included in local purchases of moveable goods for production and equipment for electronic data processing.

3.2 Benefits for specific investments

These benefits are included in the regulations of the investment promotion system (decree 455/007) dated November 2007.

Benefits are received by companies whose investments are promoted by the Executive.

The benefits that can be obtained are directly related to the amount of the investment (small, medium, large projects).

In order to evaluate the projects and grant the fiscal benefits, the Executive will take into consideration each project's contribution in the following areas (Objectives):

- ✓ *Employment creation.*
- ✓ *Geographical decentralization of economic activity.*
- ✓ *Increase in exports.*
- ✓ *Increase of Value Added.*
- ✓ *Use of clean technology.*
- ✓ *Increase in Research, Development and Innovation.*
- ✓ *Project's impact on the economy.*

The benefits which are to be granted include:

Capital Tax (IP):

- ✓ Exemption from IP on moveable fixed assets throughout their useful life.
- ✓ Exemption from IP on civil work projects for up to eight and ten years, depending on its location.

Import Taxes and Fees:

- ✓ Exemption from import taxes and fees for moveable fixed assets that are declared non-competitive to national industry.

Value Added Tax (IVA):

- ✓ Refund of VAT (IVA) for local acquisition of materials and services used for civil work projects.

Corporation Income Tax (IRAE):

- ✓ Exemption from IRAE for an amount determined by the Executive according to the project contributions to the mentioned Government's "objectives". According to the size of contributions, the amount of Income tax exemption that may range from 20% to 100% of the amount of the investment.
- ✓ The IRAE exemption is determined by deducting a percentage of the investment from the amount of the tax paid annually.
- ✓ The deduction on the IRAE varies according to the established objectives and may be applied in a range from 3 to 25 years. Such range shall be computed starting in the fiscal year where taxable income is obtained, as long as four periods have not gone through since the promotional declaration.

5. LABOUR REGIME

Availability of labour

In December 2010, the labour force in Uruguay was 49,2% of the population, and the unemployment was 7,4% of the total economically active population.

About 14% of the employed labour force is involved in the industrial sector, 11,5% belongs to the agricultural, cattle, fishing and mining sector, 21,5% to the commercial, hotels and restaurants sector, and the remaining 53% to the private and public sector.

Employee/employer relations

Labour regulations

The Employee/Employer Relations are regulated basically by the law or by the so called "collective agreements".

The law establishes minimum conditions to be carried out regarding labour relationships, so as to mention:

- ✓ *Setting of national minimum salaries: general and specific to each activity area.*
- ✓ *Setting of a maximum of working hours and a minimum of days off.*
- ✓ *Minors working regulations.*
- ✓ *Labour protection for pregnant women.*

In March 2005, the Executive issued a Decree for the installation of a Board to determine salaries as stated per Law 10.449 of 12th. November 1943, which has order its installation and functioning as from May 2005. The aim is to settle an official environment of collective negotiation between employees and employers which provides the necessary salary lines and working conditions.

Trade unions

Membership to trade unions is voluntary and is not legislated by any law.

Trade Unions represent the employees in the negotiations with the employers.

The most important trade union of the country is P.I.T.- C.N.T. ("Plenario Intersindical de Trabajadores - Confederación Nacional de los Trabajadores").

Employee participation

There is no legislation that regulates this matter.

Usually, employees set up representatives that negotiate with employers, and once an agreement is reached, it is submitted to the Employees Assembly for its approval.

Working conditions

Employment contracts

Employment contracts are generally for an indefinite term.

Temporary contracts are permitted under certain circumstances, so as to mention: seasonal occupation, employment contracts to meet temporary production needs.

Wages and salaries

All employees have the right to receive an annual bonus, payable half-yearly.

This bonus is 1/12 of the salaries earned by the employee during the period December 1st. - November 30th of each year.

Fringe benefits

Fringe benefits received by employees such as meals, family medical insurance, clothing supply and working tools are tax exempted for the Social Security purposes.

Employees are not obliged to:

- ✓ *Have representation in the company's management.*
- ✓ *Have participation in profits sharing.*

Hours worked

Working days cannot exceed an eight-hour shift.

The maximum working week is of 44 hours for the commercial sector and 48 hours for the industrial sector.

There are special regulations for certain activities such as supermarkets, banks and textiles.

Paid vacations

Employees have the right to enjoy 20 days of paid vacations per year worked. This number is increased, starting from the fifth year of work at the company, in one day every four-year working period.

In addition to this paid vacations, the employee receives a payment equivalent to 100% of the paid vacation amount called "Salario Vacacional". This amount is not levied by Social Security special contributions.

Termination of employment

Employment contracts can be terminated either by the employee or by the employer.

When the contract is terminated by the employer without just cause, compensation must be paid to the employee.

Such compensation is equivalent to one month of salary for each year or fraction worked, with a ceiling of six salaries.

Pensions

The most important social benefits are:

- ✓ *Unemployment insurance: employees who have been dismissed without just cause can get this insurance for a maximum period of six months.*
- ✓ *Medical insurance: employees who are on sick leave can get this insurance for a maximum of two years.*
- ✓ *Retirement: for men and women older than 60 years, who have effectively worked 35 years.*

Social Security Contributions

The Social Security system is financed by contributions made both by the employer and employee.

	Employee	Employer
Social Security Contributions	15%	7,5%
Medical Insurance	3%, 4,5% or 6% (1)	5%
Individuals Income Tax (IRPF)	variable (2)	-
Reconversion Fund	0,125%	0,125%

- (1) *Depending on very low income (3%), individuals without dependent children (4,5%) or individuals with dependent children (6%).*
- (2) *Individuals Income Tax rate varies from 0% to 25%. The applicable rate is related to the income level, and has a minimum non taxable income (approximately USD 850). Some deductions are also available.*

Residence and work permits

Foreigners are required to obtain a residence permit which will enable them to work in the country. Residency is granted without major requirements: proof of good behaviour in the country of previous residence, a certificate of good health and a certificate of means of subsistence.

Such permit allows foreigners to work in the country subject to the same social security regulations existent for Uruguayan citizens.