Montevideo, Uruguay
August 25, 2016

INTERLEGAL Newsletter – August 2016

Dear INTERLEGAL Friends,

It is a big pleasure to address you once again, this time as a continuation on a hot topic presented in the panel discussion at the Interlegal Specialists Group session of our recent Interlegal meeting, held in New York in May 2016.

May I remind you that on such opportunity, the discussion was focused on various aspects of the U.S.’s Foreign Account Tax Compliance Act (FATCA), using the example of the Intergovernmental Agreement (IGA) between the United States and Brazil, as well as it was provided with different perspectives regarding the OECD’s Common Reporting Standards (CRS) in different jurisdictions, including reactions among financial institutions and individual investors with foreign accounts.

BACKGROUND: The feedback I provided from a Uruguay standpoint, was that it was quite unlikely that Uruguay would bend to signing the OECD’s Convention for the automatic exchange of financial account information and to open it to all countries, involving practices such as tax examinations abroad and assistance in tax collection. The reasons why most of the operators and experts in the tax and financial fields thought so were basically:

- a strong tradition in terms of banking secrecy, which made Uruguay gain a very strong reputation as a financial market;
- the fact that, in compliance of OECD’s previous requirements and some pressure from its neighbour countries, Uruguay has already entered into bilateral treaties, or
is near to through advanced negotiations, with 33 different countries, for the cooperation and exchange of fiscal information, favoring the rights of foreign authorities to fight against tax evasion, but at the same time ensuring the protection of the individuals’ rights, through submitting the requests of information to legal standards and the guarantee of due processes; and

- Last, but not least, the circumstance that Uruguay uses the Territorial Tax System, which -contrary to the Residential Tax Systems most of the countries use- basically taxes income from a source inside the country, and where wealth and assets held abroad are not taxed (1), made reasonably consider that Uruguay would obtain no significant gain in consideration for the provision of information to foreign administrative authorities.

URUGUAY SIGNS THE MULTILATERAL CONVENTION AT THE OECD LEVEL:

Not without surprise by the readers, it was published on the press on 2 June, 2016 that the day before, 1 June, without previous public disclosure, and contrary to most of expectations, Uruguay’s Minister of Economy and Finance had signed in Paris the Multilateral Convention on Mutual Administrative Assistance in Tax Matters (the “Convention”), as amended in 2010, in the presence of the OECD Secretary General, such considered the ideal instrument for swift implementation of the new Standard for Automatic Exchange of Financial Account Information in Tax Matters developed by the OECD and G20 countries. Despite some reservations made in the case as allowed by the text of the Convention, the signature by Uruguay involves automatic exchange of country by country reports, providing all forms of administrative assistance in tax matters such as exchange of information on request, spontaneous exchange and automatic exchange. Different from 54 countries who already committed to implement the automatic exchange of information system for tax purposes as of September 2017, Uruguay’s commitment was to have it implemented as of September 2018.

Not many explanations were further given, but the circumstance that Uruguay must be aligned with international standards against tax avoidance and –basically- with anti money laundry policies, and that the Convention signed constituted a ratification and formalization of the path outlined more than one year ago, as part of several commitments assumed in the past.

Despite the lack of prior publicity and of apparent transcendence given, and leaving aside subjective considerations on whether it was the best decision to make, or if existed or not other lines of action, the fact is that the signature of the Convention shall definitely imply a

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1 The only exception to the Territorial Tax System was incorporated by Act. No. 18.718 in force since 2011, which created a tax just on the earnings derived from the performance of capital abroad, at a rate of 12% without obligation to identify the source.
milestone for Uruguay’s financial regulations and traditional practices, involving the need
to change radically many of its laws and regulations on banking secrecy and practices, as
well as a change in a culture that was firmly rooted among people and financial operators.
On 29 August, 2016, just a couple of days before you will be receiving the present
newsletter, Uruguay’s Parliament approved and ratified the Convention, in order to comply
with the implementation plan as agreed with the OECD.

WHAT COMES NEXT: The Executive Power already sent to Parliament, for its
consideration (its approval and/or eventually for the introduction of amendments) a draft
law called “Act on International Fiscal Transparency and for the Prevention of Money
Laundry and Finance of Terrorism”.

The text drafted by the Executive Power, in its “Statement of Reasons” declares, among
other points, the belief of the National Government in the commitment with fiscal
transparency and international cooperation as an essential pillar of Uruguay’s international
insertion, and a critic component of its economic and social development, and considers
that institutional quality, one of the key strengths of the national economy, requires an
active participation in the areas of cooperation of the international community.

It is to be noticed that the draft law foresees the implementation of several measures in
compliance with the Convention, but Uruguay government adds to the project a number of
measures and obligations of financial institutions involving the annual provision of
information to the Tax authorities on Uruguay residents, both individuals and entities,
exceeding completely what it was introduced as the motivation of the draft.

With relation to the contents of the he Act, it can be organized in four main chapters:

- First chapter regulates the automatic report to the Tax Administration of the
  balance and income from financial source, establishing the obligation of all resident
  financial institutions and local branches of foreign institutions to provide annually
  to the Tax Department all the information relating to the balances and income of
  the bank accounts, duly identified, held by foreign individuals or entities of any
  kind with tax residence in other countries or jurisdictions; as well as the provision
  of the same kind of information referred to accounts kept by individuals and
  entities residents of Uruguay. It is important to point out that the said information
  would involve the balance and the income of the accounts at the end of every civil
  year, without having to provide any movements in the accounts, unless according to
  the Executive Power’s criterion –to be developed- a certain entity may represent a
  high risk regarding fiscal evasion, in which case it must be informed also the
  beneficiaries. It must be informed the tax residence of the individuals and entities
  holding the accounts, as well as of the final beneficiaries as it may correspond. The
draft foresees that the banking secrecy remains unchanged, and the information can
only be disclosed to the Tax Department, who must handle the information
received for the sole compliance of its purposes and for the exchange of information with foreign authorities according to international treaties and the Convention, always when they ensure reciprocity and confidentiality.

- Second chapter seeks to move forward with deepening the legal advances already made in terms of convergence of technical regulations and related international standards involving the prevention of money laundering and finance of terrorism, as well as of international fiscal transparency, gathering the GAFI’s Recommendations Nos. 24 and 25, of February 2012, as well as of the Global Forum. The draft’s goal is to obtain all the relevant information on the final beneficiaries of legal entities along with the identification of the stockholders. It is foreseen that all such information must be centralized and available at the Registry created within the Central Bank of Uruguay.

- Chapter III – Tax Heavens Entities: this chapter includes new tax regulations applicable to entities belonging to, or residents of, low or no-tax jurisdictions, or that may anyhow benefit from such regimes, adjusting the tax system in a way that it shall be discouraged the use of entities from low tax jurisdictions with the goal of diminishing the tax burden. With the proposed draft it shall be amended certain regulations relating the income tax starting to consider such entities as “residents” and its income as from a Uruguayan source (which has a big impact considering Uruguay’s territorial tax system and certain benefits that non residents -individuals and entities- have according to current regulations), as well as increasing the rate of the Assets Tax payable by these legal entities.

- The final chapter contains new obligations for the Income Tax payers who have special linkages with companies abroad, pursuing to fight against tax planning strategies that exploit gaps and mismatches in tax rules to artificially shift profits to low or no-tax locations with little or no economic activity, following the recommendations of the OECD Base Erosion and Profit Shifting (BEPS), of July 2013.

According to the text it is proposed that the Act, once passed by Parliament, should be in force as of 1 January, 2017. It is currently under study by the Finance Commission of the House of Representatives.

I will keep you informed, my friends, on future developments regarding this and other news.

Sincerely yours,

Ramon Bado