5 Uruguay

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I. Introduction

Uruguay -- República Oriental del Uruguay -- is the second smallest country in South America. It is organized as a Democratic Republic with a presidential system. After being disputed by Portugal and Spain for almost two centuries, Uruguay became an Independent Republic in 1825 and established its first Constitution in 1830.

It borders with Argentina on the west and Brazil on the north. On its east coast it is surrounded by the Atlantic Ocean and on its south the river Río de la Plata separates it from the Argentina. With 3.3 million people making up its population 1.3 million live in Montevideo, its capital. Montevideo also has the most important port, followed by Paysandú and Salto over the Río Uruguay river coast. Colonia del Sacramento, another important city, is one of the oldest European settlements of the country and was declared a World Heritage Site by UNESCO for its historic quarter. Other important cities are Ciudad de la Costa, Las Piedras, Maldonado, Punta del Este (the most international and famous tourism point), Artigas and Rivera.

Uruguay is the safest country in South America. The criminality rate is low in comparison with the rest of the countries form the region and there are no ethnic or religious conflicts.

Circulation of transport is fluid, even in urban centers. The time used to move from one place to another is much reduced; Montevideo can be crossed from one side to the other in a little more than half an hour in any given time during the day. The cities have vast green spaces and due to the flowing winds and lack of contamination industries there is no smog. The same can be said of rivers and seas on the coasts.

The national sport is football, which brings together vast amounts of population from all social echelons. There is also a very important cultural activity that provides a wide mirage of theater spectacles, musicals and cinematography. In general shops are open from 9 am to 7 pm from Monday to Friday and from 9 am to 1 pm on Saturdays. There are various commercial centers that open from 10 am to 10 pm including weekends. The shops offer a variety of electro domestic supplies, drinks, food, automobiles and other consumable goods of any origin and level of quality. The local coin is the Uruguayan Peso; $ being the official symbol of it. Weights and measures are based on the metric system.

Geography, Climate and Resources

With a territorial size of 175,215 square kilometers -175,016 square kilometers of land and 1,199 square kilometers of the Río Negro artificial lakes'- it also exerts sovereignty over 105 square kilometers of islands situated over the Río de la Plata river. Its jurisdictional waters amount to 16,799 square kilometers -include the Río Uruguay river, Río de la Plata river, the Laguna Merín lake- and 125,057 square kilometers of territorial sea. Uruguay's complete area would be of 318,413 square kilometers with two longstanding diplomatic border disputes with Brazil about the Isla Brasilera and Rincón de Artigas that cover 237 square kilometers. Uruguayan landscape is made up of mostly green plains and a few low hills in some areas known as 'cuchillas', the highest elevation being the Cerro Catedral with 514 meters.

The country side provides lots of green spaces from low trees and pastures and small lakes and rivers that run throughout the country which favor agriculture. The three main rivers are the Río Negro, which crosses the country from east to west, the Río Uruguay that borders part of the country on the west and the Río de la Plata, that is born were the Río Uruguay and Paraná river flows join and then spreads until it meets the Atlantic Ocean. Along the Atlantic coast there are also several lagoons.

The climate in Uruguay is template and humid with warm summers and more or less even rains through out the year. There is a double rain season, the first on during autumn and the second one during spring due to the continental and maritime influence. The temperatures during summer vary between 24º C to 30ºC and during winter between 6ºC and 14ºC.

The geography of the country is ideal for livestock due to the great amount of grass extensions and for agriculture since the regions are fertile and propitious. It is also famous for its wine production. The main resources of Uruguay are based on its livestock, agriculture and service. Livestock and many livestock related products of high quality are exported, like meat, leather and wool and agriculture products in general. Much of the economy is based on services and tourism.

Demographics and Language

According to the last census, in 2004, the population amounts to 3.3 million people. The population is basically of European origin with a 88 percent, with an almost nonexistent indigenous population. The consecutive immigration waves created a population made up mostly of Spaniards, followed by Italians and with an important number of French, German, Portuguese, British, Swiss, Russian and Polish immigrants among others.

It is known for being the country with the highest longevity rate in the region, with a life expectancy of about 76 years of age (72,4 males and 79,7 females). The growth rate is the lowest in Latin America, 13.9 crude child births per 1,000 habitants. The urbanization rate is very high and reaches the 96,1% of the population.

The blandness of the weather, the absence of contamination, the wide coverage of sanitation and drinkable water, and the reach of medical attention combine together so that the population has a high degree of salubrity and epidemics of any kind are practically nonexistent.

The official and most used language is Spanish. There is a historical tradition of teaching both English and French; being English the second most used language after Spanish in the business community. Lately the study of Portuguese has risen due to integration process in the MERCOSUR and closer ties to Brazil.

The basic principles of education in Uruguay are that it has no religion ties, it is free of cost and it is mandatory. Population has access to education from kindergarten to University. The largest university in the country is the Public University and covers most of the faculties. The alphabetization index reached 97.7 percent in 2006 making Uruguay one of the most alphabetized countries in Latin America. Uruguay in 2009 became the first country to reach full educational coverage of the primary students and teachers by the One Laptop Per Child through the Ceibal Plan. Through it students all over the country are able to access internet due to the telecommunication infrastructure with no cost.

Uruguay has no official religion. Church and state are separate entities, guaranteeing religious freedom. Although the main religion is Catholicism, and most of the population baptize and marry in churches although most are not devoted practitioners, there is a presence of Protestants and a very small percentage of Jewish. There is also a high percentage of people that professes no religion. Uruguay is considered the most secular country in the Americas.

Government and Administrative Divisions

Uruguay is a presidential representative democratic republic. The State is organized in three independent branches: Executive, Legislative and Judiciary. The President is both head of state and head of government exercising Executive Power with the cabinet. According to the Constitution, the members of the government are chosen every five years by a universal suffrage system by proportional representation. The Legislative Branch is constituted by the General Assembly or Parliament composed by two Chambers. The Senators Chamber is composed by 30 members and presided by the Vice-president of the Republic and elected at a national level. The Chamber of Deputies has 99 members and is elected at departmental level. The Judiciary Branch is lead by the Supreme Court of Justice, its members are chosen by the General Assembly and last 10 years or until they are 70 years of old. The Supreme Court of Justice is the last appeal instance and is in charge of judging the constitutionality of the laws.

Uruguay has a consolidated system of political parties. Nowadays 4 of them have parliament representation: ‘Frente Amplio’, ‘Partido Nacional’, ‘Partido Colorado’ and ‘Partido Independiente’. Both the Partido Colorado, a right wing coalition, and the Partido Nacional, a center-right wing coalition, are considered the traditional political parties. The Frente Amplio, a left wing coalition, is considerably new and was created after dictatorship of 1973. The last two presidential elections have been won by the Frente Amplio - Encuentro Progresista, as is the new denomination.

Uruguay is composed by 19 Departments. They are organized similarly to the country with two principal organs: The ‘Intendente Municipal’ (Executive Branch) and the Departmental Assembly (Legislative Branch). The ‘Intendente’ is elected every 5 years directly by the citizens of each department. The Departmental Assembly is composed by 31 members, called ‘Ediles’. The political party that gets the majority of votes has 16 of the sits and the rest is divided between the rest of the political parties according to the votes each got. The oldest departments date back to 1816 but the youngest, Flores, was formed in 1885.

Commerce Policies

Uruguay has had strong political relationships both with the neighboring countries and with Europe. With globalization and regional economical problems its bond with North America has grown. Now a day's with the turmoil caused by the global financial crisis of 2008 several new trade partners have increased in participation like China and Russia.

Historically the international relationships have been defined by the principles of no intervention, multilateralism, respect to national sovereignty and trust in the law to solve controversies.

Uruguay was one of the first economies in Latin America that evolved towards an open and unrestricted international commerce. In 1991, Uruguay signed a treaty with Argentina, Brazil and Paraguay that established the Mercado Común del Sur, roughly translated as Southern Common Market, MERCOSUR. It accelerated the aperture of the Uruguayan economy and established a process of progressive integration.

In 1991 MERCOSUR and the US signed a treaty, that even though it was not in effect until 2001, it opened the way to the creation of 4 groups of work in industrial commerce, electronic commerce, agriculture and investment. The US wanted to sign a FTA but the government did not approve it, so instead a TIFA was agreed upon.

Between 1991 and 1994, MERCOSUR member countries established a free trade zone with progressive tariff reductions that eventually reached 0 percent on 31 December 1994 (certain products were delayed a few years and the sugar and automotive industries were excluded from the elimination). On 1995, the MERCOSUR became a definitive customs union with the enactment of a common external tariff with rates varying from 0 percent to 20 percent.

In recent years the MERCOSUR has signed several free trade agreements that have been ratified by Uruguay. The objective is to establish a free trade zone through a trade liberalization program with progressive tariff reductions.

II. Overview of Macroeconomic Activity and Fiscal Position

The last years of most world economies have been characterized for severe shocks leading toward downturns but also periods of high growth in developing economies. World markets have suffered from several financial crises and in 2008 the global financial crisis of which most developed economies are still trying to get out. The sluggish recovery of the advanced economies and the heavy impact absorbed by them created a favorable ground for developing economies but also many risks. In this scenery Uruguay is well positioned to benefit from the global recovery as shown by an 8.9 percent economic growth and a total GDP of 31,178 million US dollars in 2008. By 2009 the effects of the financial crisis caused a slowdown of the economic growth to 2.9 percent affecting largely the manufacturing, agribusiness and commerce sectors, but 2010 preliminary indicators already show a recovery.

In the period between 1996 and 1998 Uruguay's economy shows a 5 percent average annual growth, but the following period from 1999 to 2002 is marked by the economic problems of Argentina and Brazil whose effects on the region lead Uruguay to a major downturn. The massive withdrawals of U.S. dollars deposited in Uruguay by Argentine citizens once Argentina froze the bank deposits led to a plunge in the Uruguayan peso, a banking crisis and an economic contraction. Real GDP fell almost 20 percent, worsening towards 2002. In this situation unemployment rose, inflation surged and external debt burden doubled. The worst scenario and recession was averted by utilizing IMF financial assistance and a restructuring of the external debt in 2003. Economic growth resumed in 2004, and averaged 8 percent annually in the period 2004 to 2008. With activity running significantly above potential in this period private investment rose and unemployment fell to pre 1999 values.

Uruguay entered the 2008 global financial crisis with a strong and well regulated banking system, a solid external position and a flexible exchange rate regime, all results of the policy changes derived from the severe banking crisis suffered in 2002. These conditions together with the government policies focused on consolidate macroeconomic stability, lower debt to GDP ratio and reduce poverty, allowed to take advantage of the external situation and contributed to dampening the impact of the global crisis.

FDI in tradable sectors, principally agriculture and agribusiness, has grown considerably in recent years contributing to important productivity improvements. Nevertheless, the short term growth is still subject to the risks of an economy considerably dependant on the developments in the region.

During the first quarter of 2010, the Uruguayan economy shows a strong recovery from the global crisis. GDP expanded 1.7 percent compared to the previous quarter in seasonally adjusted terms. The international context, in particular the high commodities demand that allowed an increase in agricultural exports, and the price increase of some Uruguayan export products that improved the terms of trade, contributed to an overall economic growth.

From the point of view of supply, the GDP growth can be linked to an overall expansion of all sectors with the exception of construction, the main contributors were electric generation and transport and communication due to the sustained growth in cellular telephony and data transmission. The major commercial expansion was registered in car sales and imported goods, as well as hotel activity. For their part, the agricultural sector and manufacturing industry grew at a reduced rate than GDP.

From a spending point of view, the growth was sustained by domestic demand with external demand only contributing to a lesser extent. Private spending was the most dynamic with consumption and investment growing at the same rate as GDP, while the government spending remained constant.

II.1 Macroeconomic Activity

II.1.1 International Environment

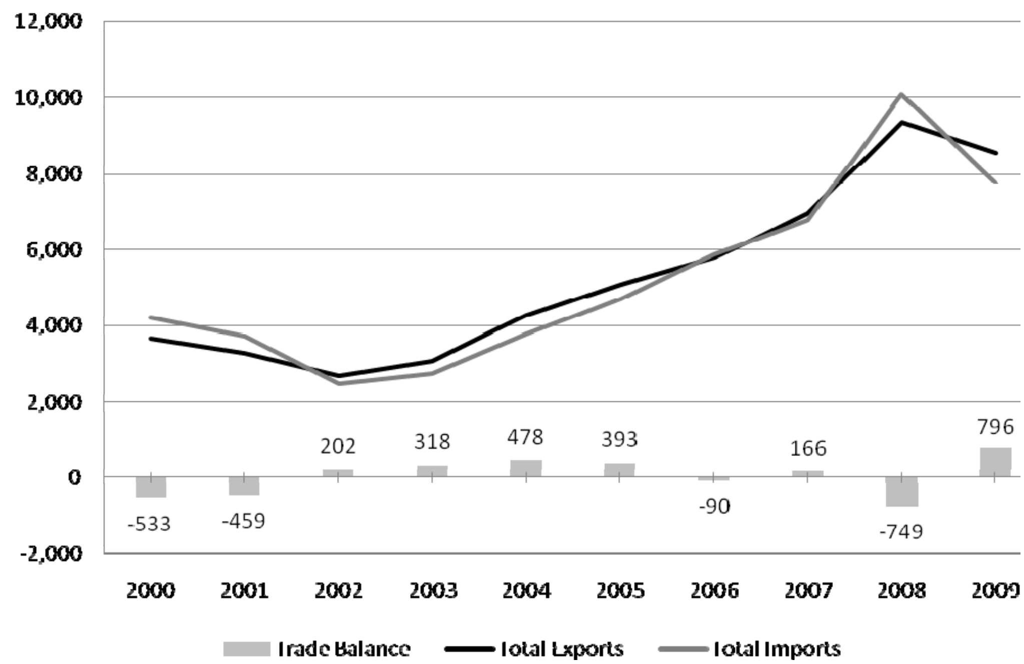
Trade balance

Uruguayan economy registered in 2009 a sharp reduction in trade balance deficit with a net positive balance for the year. This was mainly the result of a contraction in imports of goods and services derived by the reduction in growth rate and a framework of uncertainty after the worsening of the international crisis in late 2008. In the last quarter of 2009 the imports continued to decline but at a much slower peace that in previous quarters, in line with the recovery of economic activity in the second half of the year. Data of the first quarter of 2010 exports reached 1,408 million U.S. dollars, representing an increase of 26 percent over the same period last year.

In the period between 2003 and 2008 there was a moderate increase in exports of goods and services, being the main drive the agricultural and agribusiness sector, while exports of services declined due to the effect of the crisis on external demand with the exception of the tourist services exported within the region. Imports of goods and services increased, which together with the increase of GDP, expanded the final bid. The largest foreign purchases should be associated with the acceleration of economic growth and a change in the behavior of private spending. In effect, imports of intermediate inputs were the most increased, while those for consumer goods and investment also grew. 2008 trade balance deficit reverted to a surplus of almost 800 million US dollars in 2009.

Figure 1: Uruguay Balance of Trade

(in million US dollars)



Source: *World Bank and Uruguay XXI (Uruguayan office for trade promotion).*

In particular highlights from imports, as can be seen on Table 1, the peak in oil imports during 2008 that was caused by a long period of drought which reduced Uruguay's hydroelectric generation capacity increasing the need of oil as a substitute for electric generation. Toward 2009 the effects of the global crisis shown in reduced purchases of machinery and equipment are consistent with the reduction in private investment in the year.

Table 1: Uruguay Imports by Category

(10 main imports in million US dollars)

Description	2005	2006	2007	2008	2009
Crude oil and derivatives	865	1,107	1,148	2,367	1,350
Machinery and mechanical appliances	346	388	536	869	791
Motor vehicles, tractors and parts	265	346	454	712	592
Plastics and articles thereof	255	284	349	426	340
Chemicals and pharmaceuticals	209	235	282	388	297
Miscellaneous chemical industry	114	130	176	274	198
Fertilizers	96	98	216	305	157
Paper and paperboard	89	98	112	136	122
Articles of iron and steel	47	61	66	114	119
Optical and precision instruments	58	63	71	92	109
Others	1,409	2,088	2,238	2,984	2,589
Total Imports of goods	3,753	4,898	5,648	8,667	6,664
TOTAL Imports	*4,693*	*5,877*	*6,771*	*10,083*	*7,755*

Source: Central Bank of Uruguay and Uruguay National Institute of Statistics.

Volumes of exports have increased between 2003 and 2008 with Uruguay's export market share rising, especially in 2008, lead by the export growth of meat and agricultural products, despite the appreciation of the real effective exchange rate. During the period there is an increase in export earnings strengthened by the benefit from booming commodity prices, specially meat, leather and goods, three of the main traditional export products of Uruguay.

However, this trend declined in 2009 and did not pick up until the preliminary data of the second quarter of 2010, with the first quarter export growth being lead by wood and oils.

Table 2: Uruguay Exports by Category

(10 main exported goods in million US dollars)

Description	2005	2006	2007	2008	2009
Beef	807	1,010	891	1,334	1,103
Cereals	213	231	365	590	775
Oil seeds and oleaginous fruits	136	158	221	360	462
Milk and dairy products	255	272	360	448	386
Wood and wood products	142	194	253	416	355
Plastics and articles thereof	134	150	189	224	190
Skins, fur skins and leather	278	339	336	287	188
Milling products	79	85	96	190	187
Wool and animal hair	181	207	232	207	175
Fish and mollusks	135	160	175	198	170
Others	1,414	1,594	1,982	2,858	2,398
Total Exports of goods	3,774	4,400	5,100	7,112	6,389
TOTAL Exports	*5,085*	*5,787*	*6,937*	*9,334*	*8,551*

Source: Central Bank of Uruguay and Uruguay National Institute of Statistics.

With over 50 percent of exports of goods comprised by commodity exports in the 2005 - 2009 period and oil playing a major role on imports, disentangling the impact of the simultaneous increase on oil and food commodities' prices is difficult. According to IMF economic estimates, even as a net commodity importer, the effect on Uruguay growth was positive.

Changes in the terms of trade do not directly affect the level of real output, but influence real purchasing power, both through nominal incomes and through their effect on domestic prices. The indirect effects of changes in the terms of trade on real output in turn depend on the impact of these changes on spending. Moreover, domestic activity and income receives an additional boost from the indirect impact of commodity prices shocks on neighboring country's GDP, Argentina and Brazil in the case of Uruguay, particularly when economic links between the countries are strong.[1]

[1] IMF Country Report No. 10/43, Uruguay: Selected Issues.

Table 3: Evolution of Import Origins

(9 principal import origins in percentage of total imports)

Origin	2005	2006	2007	2008	2009
Argentina	12.2	12.4	11.3	10.7	11.4
Brazil	13.1	12.5	11.9	10.9	11.1
China	4.1	5	6.1	7	7.6
USA	4.3	4.6	4.8	4.1	4.9
Germany	1.5	1.4	1.3	1.1	1.6
Italy	1.3	1.2	1.1	0.9	1.1
Mexico	0.9	0.9	0.9	0.9	0.9
Chile	1.2	1	0.9	0.8	0.9
Spain	0.8	0.8	0.8	0.7	0.8
Others	60.6	60.2	60.9	62.9	59.7
TOTAL	*100*	*100*	*100*	*100*	*100*

Source: Central Bank of Uruguay and Uruguay National Institute of Statistics.

In terms of imports, their origin has remained stable over the last 5 years, with a slight increase in the participation of China. Brazil was the main supplier of Uruguay in the first quarter of 2010, with 307 million US dollars, followed in importance by Argentina with 298 million and China with 231 million.

Table 4: Evolution of Export Destinations

(9 principal export destinations in percentage of total exports)

Destination	2005	2006	2007	2008	2009
Brazil	13.6	14.5	16.5	16.4	20.3
EPZ*	2.9	4.5	6.5	9.4	16
Argentina	7.5	7.5	8.5	8.5	7.8
China	3.5	4.2	3.6	2.9	4.3
Russia	1.1	5.6	2.6	5.6	4.1
Venezuela	1	1.9	2.2	4	3.4
USA	22.4	13	10.9	3.6	3.3
Germany	4.3	4.2	4.6	3.5	2.9
Spain	3.9	3	3.4	4	2.7
Others	39.9	41.4	41.3	42.1	35.2
TOTAL	*100*	*100*	*100*	*100*	*100*

* Export Processing Zones are called Zonas Francas in Uruguay.

Source: Central Bank of Uruguay and Uruguay National Institute of Statistics.

The region remained the main destination of exports with sales to Brazil reaching 20.3 percent of the total, and exports to Argentina accounted for 7.8 percent, in line with the expansion of economic activity verified by both economies. The exports to the Export Processing Zones are increasing more rapidly than any other trade partner, taking since 2008 the second place as exports destination.

Both in exports and imports the main trade partners are Brazil and Argentina with an increasing trend in the last 5 years. There are some new markets like Russia, Venezuela and in less degree Japan that are the target of the trade previously done with USA.

Figure 2: Uruguay Import Trade Partners
(year 2009 principal import origins in percentage of total imports CIF)

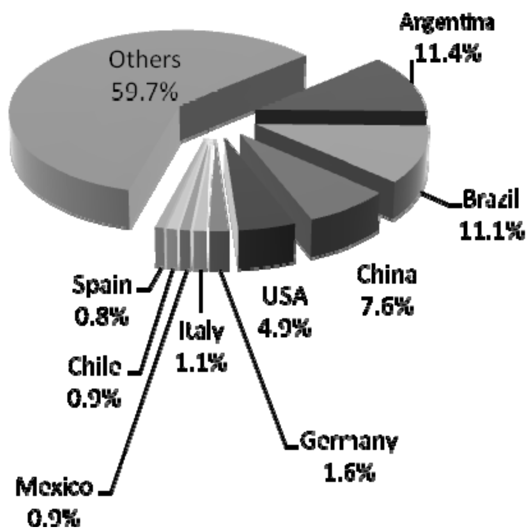
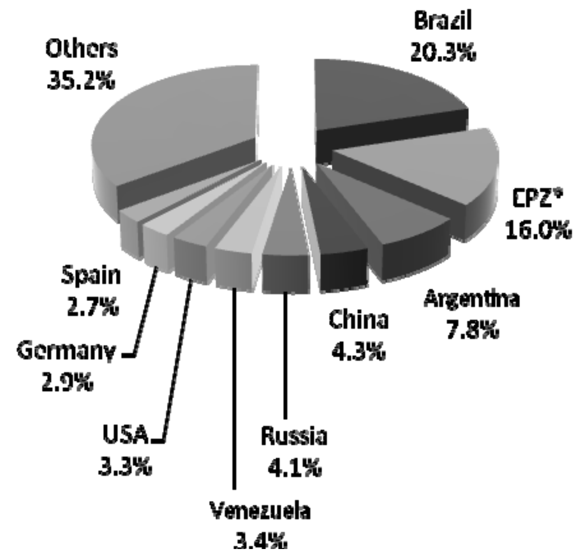


Figure 3: Uruguay Export Trade Partners
(year 2009 principal export destinations in percentage of total exports FOB)



* Export Processing Zones are called Zonas Francas in Uruguay.
Source: Central Bank of Uruguay and Uruguay National Institute of Statistics.

Current account balance

Uruguay's Balance of Payment registered during the first quarter of 2010 a surplus of 108 million US dollars derived from the current account surplus and the net capital inflows into the country in unregistered movements according to the Central Bank of Uruguay data. This positive balance is inferior to the 577 million US dollars surplus registered on the same period of 2009, year that closed with a surplus of 1,588 million US dollars on the Balance of Payment. This reflects the continuation of the deceleration in net capital inflows through financial movements that began with 2008 crisis. The most important remarks from the preliminary data of the first half of 2010 are a significant loss of reserve assets from of 579 million US dollars and a net outflow of funds through financial movements. While during 2009's first half Uruguay received more than 600 million US dollars, during the same period of 2010 there was a loss of 974 million on the preliminary estimation, mainly due to the public sector operations.

In terms of the Current Account, the deficit widened from 0.9 percent to 4.7 percent of GDP in 2008, reaching the biggest imbalance in Uruguayan history. The main cause of increased deficit was the deterioration in the trade balance. This trend started to revert in 2009 and continued at a slower pace in 2010.

Central Bank of Uruguay data for 2010's first quarter, registered a surplus of 253 million US dollars, slightly lower to the 270 million registered in the same period during the previous year. Preliminary data of the 2010 second quarter shows the surplus reaching 322 million as a result of the private sector behavior, which increased its income-expense gap to 405 million.

The Financial and Capital Account shows in 2010 second quarter an accelerated outflow of funds that had already been present in the first quarter, exceeding 800 million UD dollars. In the public sector, the net outflow of foreign exchange in the first half of the year was due a 76 percent increase in foreign assets and 24 percent decrease in liabilities. For their part, the private banking system increased their net position with non-residents in substantial reduction of assets against the Central Bank.

International Reserves

According to the measurement of balance of payments, during 2009 the Central Bank of Uruguay international reserves increased by 1,625 billion US dollars in the first nine months of the year, USD 577 million in the first quarter, 450 million in the second and 597 million in the third quarter, in line with the debt contraction by the Central Government and the allocation of SDRs by the IMF.

In 2010’s first quarter BCU international reserves increased by 108 million US dollars due mainly to purchases of foreign exchange, while foreign currency deposits of financial institutions fell steadily throughout the quarter, given the gradual reduction of reserve requirements. Notably, the increase in reserves is well below the same period of 2009, mainly because uncertainty in the international scene had receded eliminating the need to contract additional debt with multilateral lenders as done in 2009 for precautionary reasons.

Table 5: Central Bank International Reserves

(in million US dollars)

	Reserve assets	Other short term foreign assets	Foreign currency obligations with the public sector	Foreign currency obligations with the private sector	Net reserve assets	BCU foreign exchange position
2002	772	n/d	n/d	n/d	n/d	n/d
2003	2,087	0	538	1,384	165	n/d
2004	2,512	0	799	1,998	-285	143
2005	3,078	328	1,069	2,180	157	789
2006	3,091	0	630	2,192	269	1,600
2007	4,121	896	1,023	2,274	1,721	2,939
2008	6,360	299	1,027	3,745	1,887	3,233
2009	7,987	173	1,771	3,105	3,284	4,293
Q1-2010	8,061	171	1,640	2,725	3,867	4,920
May-10	7,648	176	1,368	2,227	4,230	5,302

Source: Central Bank of Uruguay

Exchange System

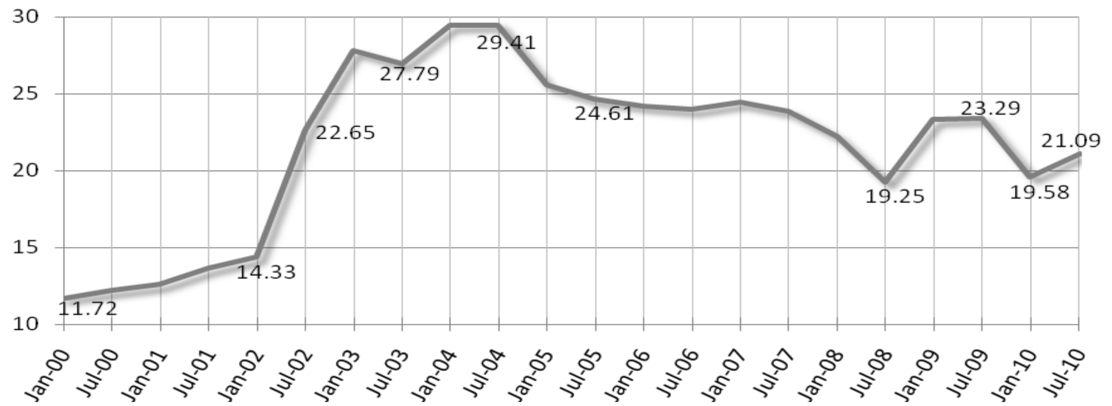
Among other important monetary and financial reforms taken since the 2002 banking crisis, Uruguay switched the exchange rate policy to a managed float. The initial effect of this policy change was a depreciation of the Uruguayan peso of almost 50 percent in a couple of weeks, having a heavy impact on companies and individuals who held debts denominated in US dollars. Due to this, Uruguay has implemented several other policies tending to de-dollarize the economy but still many expenditures and debts are being traded in U.S. dollars (e.g. real estate, construction, vehicles and electronic devices).

Previous to the actual exchange rate system, Uruguay applied a currency band with the form of a sliding range with top and bottom margins at which the government would intervene that was enacted in the 1990s. Before that system, the Uruguayan peso was pegged to the U.S. dollar, period from which came the dollarization of the economy.

The actual managed float is controlled by the Central Bank of Uruguay who makes direct interventions in the exchange market and indirect interventions through instruments of public debt denominated instruments of monetary regulation. This allows the evolution of the peso to accompany the international trends but without suffering abrupt changes, which results in less volatility with respect to other emergent economies. The flexibility of the regime has allowed a smooth adjustment in the relative prices without damaging the competitiveness of the economy, but also without undue pressure on domestic inflation.

Figure 4: Exchange Rate Evolution

(Uruguayan pesos per 1 US dollar)



Source: Central Bank of Uruguay and Uruguay National Institute of Statistics.

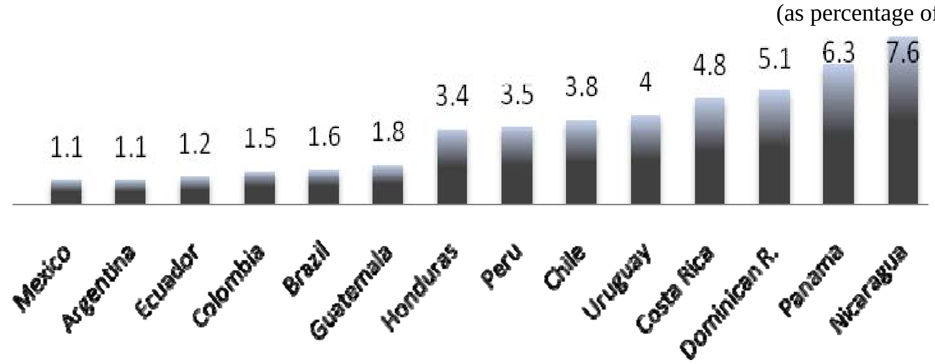
The IMF asserted in their 2009 REER report that Uruguay shows no signs of competitiveness problems despite the appreciation of the peso that followed the 2002 depreciation. The appreciation on the real effective exchange rate has been partly a result of inflationary pressures in Uruguay relative to the ones in trading partners, in particular the US and Brazil. The report concludes that the real exchange rate is broadly in equilibrium.[2]

Foreign Direct Investment

The annual FDI inflow to developing countries in the last decades has increased manifold. The effects of the financial crisis hit Latin America & Caribbean mostly during 2009, already showing in 2010 an important recovery. In the year 2008 the region received 126.26 billion US dollars on FDI which is 6.8 percent of the aggregate inflows of the world and 25 percent of the aggregate FDI inflows of the developing world. The same figure for 2009 is reduced to 76.68 billion, from which South America received 54.45 billion. In that year Uruguay managed to attract FDI amounting to 4 percent of its GDP.

Figure 5: 2009 FDI inflows in Latin America

(as percentage of GDP)



Source: Economic Commission for Latin America and the Caribbean (ECLAC)

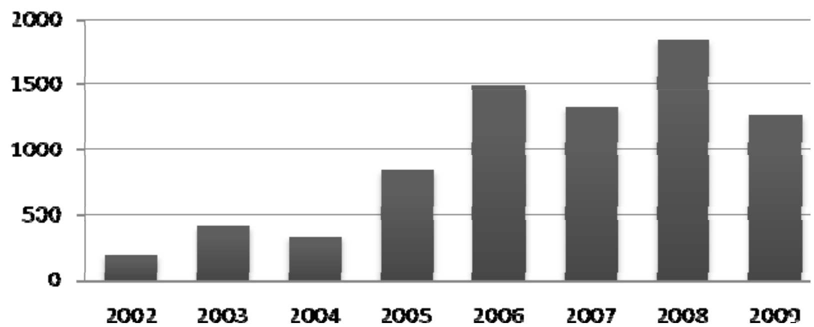
In this context we find that FDI inflow in Uruguay was very low in the 1990s, increasing steadily after the 1998 Investment Promotion and Protection Law declared that promotion and protection of national and foreign investment was of national interest.

[2] See IMF Country Report No. 10/43, Uruguay: Selected Issues.

ECLAC analysis in Latin Americas shows, that although inflows have been substantial, most of them continue to target natural resources, manufacturing sectors with low and medium technology intensity, and services. Uruguay in particular has been target of FDI mainly in tree differentiated areas. The first one is the forestry and agricultural sector, with high levels of investment in land acquisition and change of ownership to Brazilian investors of most meat processing plants. The second is the market seeking FDI; Trans National Companies (TNC) like Carrefour Group have acquired all the supermarkets chains. The last one is on services operated from within EPZs like trading companies, call centers and information technologies services. In the field of information technologies, is important to mention the establishment of the regional headquarters of Tata Consultancy Services and Trintech in Zonamerica EPZ.

Figure 6: Uruguay's FDI Flows

(in million US dollars)



Source: Economic Commission for Latin America and the Caribbean (ECLAC)

The last important identifiable FDI in Uruguay was the construction of a paper pulp processing plant by the Finland firm Botnia in a EPZ, which amounted to almost all 2006 FDI.

Foreign Aid and External Debt Outstanding

In 2009 the Uruguayan external debt reached 12,900 million US dollars approximately 37 percent of GDP.

ODA received rose sharply in the 2003-2004 period, as can be seen on Table 6, as an indispensable tool to get out of the 2002 banking crisis. Financial aid from the International Monetary Fund aided to stem the damage.

Table 6: Net ODA Received

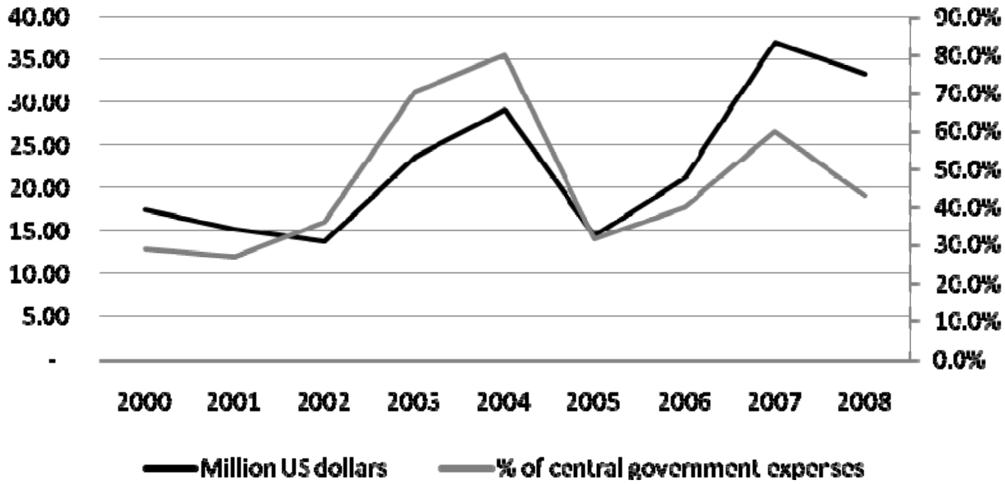
	2000	2001	2002	2003	2004	2005	2006	2007	2008
Million US dollars	17.40	15.19	13.72	23.58	29.05	14.44	21.07	37.01	33.29
% of central government expenses	28.7%	26.7%	36.2%	70.1%	79.8%	31.3%	40.1%	59.7%	42.8%
% of GNI	7.6%	7.3%	10.0%	20.4%	22.2%	8.6%	10.9%	15.8%	10.9%

Source: World Bank databank, OECD.

But even after the crisis was over ODA remained at higher levels than before. However, it shrinks toward 2008 as an effect of world ODA contraction due to the international crisis.

Figure 7: Net ODA Received

(in million US dollars and percentage of government expenses)



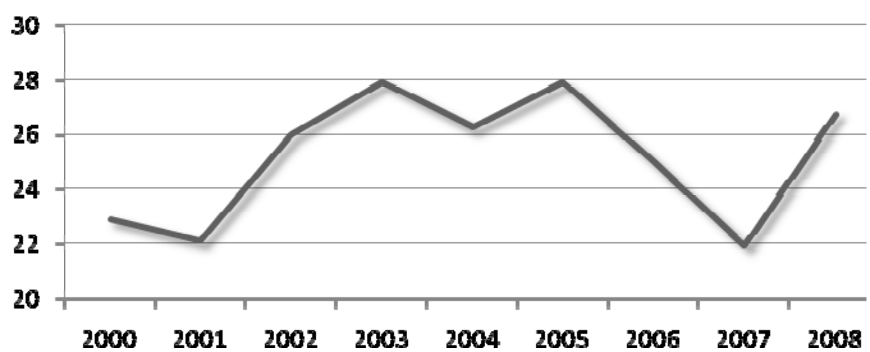
Source: World Bank databank, OECD.

In 2003 Uruguay restructured its external public state debt without asking creditors to accept a reduction on the chief. Short term debt decreased from 29 percent in 2001 to 7.5 percent in 2008.

The impact of 2002 crisis on Uruguay's debt rating can be clearly appreciated in the figure below as private owned debt diminishes and conditional debt increases. By 2009 the investment rate has recovered the trend of diminishing multilateral debt; it was reversed by the private contraction due to the international crisis.

Figure 8: Multilateral Debt

(as percentage of total external debt)



Source: World Bank databank, Central Bank of Uruguay.

Continuing with the policy to reduce dependency on multilateral assistance or credit, in November 2006 the Government carried out some liability management operations aimed to extend the average maturity of the outstanding debt. The operations were, in one hand, the advanced redemption for the full amount of the outstanding debt with the IMF for 1.090 million US dollars, and in the other hand the time reprofilement of the sovereign external debt.

As a result, both the asset stock and the amount of debt service for the period 2008-2015 have fall considerably. Debt service amounted in 2004 to 27 percent of the Central Government expenditure and was reduced to 11 percent in 2009.

There are other factors together with the public policies that made this scenario possible, and all should be considered, like the appreciation of the peso which results in a decrease of the weight of US dollars debt servicing, and the international environment that allowed for very high growth economic rates.

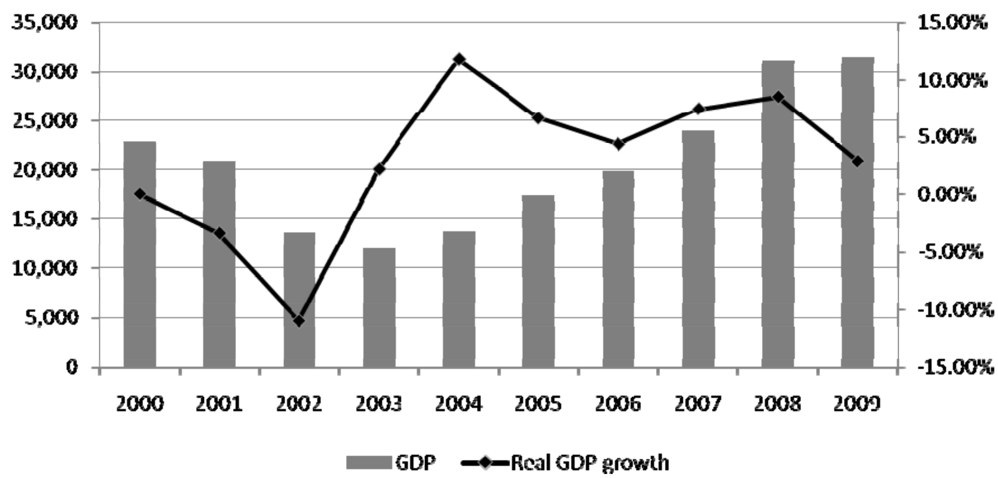
II.1.2 Domestic Environment

Economic growth rate

National Accounts data indicate that in 2009 Uruguay's economy experienced a slowdown in growth compared to the observed record in previous years with the GDP reaching 36,093 million US dollars and a real growth averaging 2.9 percent over 2008. This confirms early diagnosis of a reduced impact from the international crisis on Uruguay’s level of activity and that the country is far from recession. The closing numbers of 2009 put Uruguay among the few economies in the region and the world that showed economic growth during the year.

Figure 9: Uruguay GDP and Real GDP Growth

(in current million US dollars and percentage)



Source: World Bank databank and IMF WEO 2010.

From the Figure 9 can be easily appreciated the economic downturn caused by the crisis in Brazil during 1999-2000 and the financial crisis in Argentina during the 2001-2002 period, which ultimately lead to the banking crisis in Uruguay that worsened toward the end of 2002. After the crisis an economic rebound as well as the circumstances in the region fueled an important period of growth slowed at the end of 2008 by the global financial crisis and a severe drought that affected the main export sector, agriculture, but regaining momentum as shown on the indicators for 2010.

Central Bank data show that GDP grew during 2010 second quarter by 10.4 percent over the same period of 2009. The seasonally adjusted growth in the quarter was 1.8 percent, equivalent to 7.2 percent in annualized terms. This confirms that by July 2010 the level of activity took up a clear path of expansion, with growth records similar to those seen prior to the global crisis of late 2008 and early 2009.

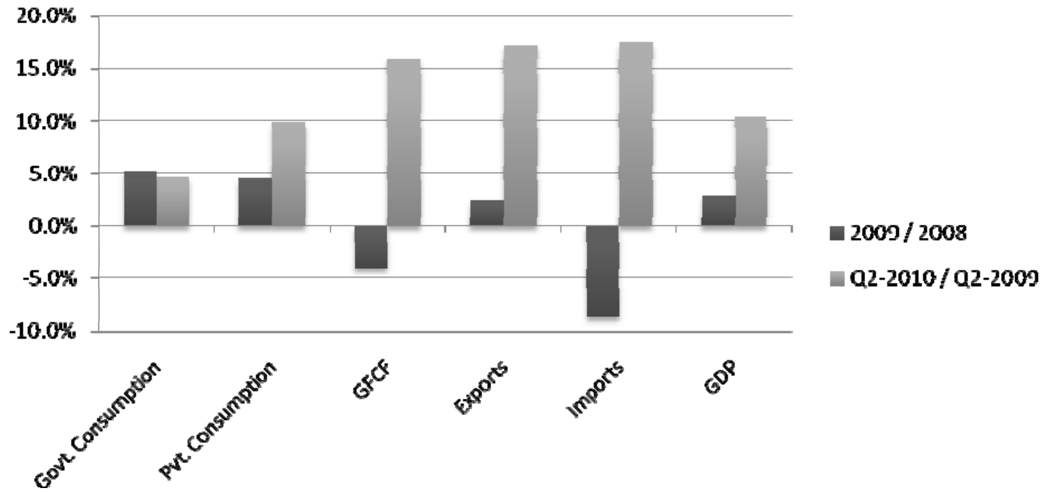
From the aggregate expenditure side the sources of growth for the second quarter of 2010 can be identified as the increase in domestic demand of 9.8 percent and gross fixed capital formation of 15.9 percent relative to the same period in 2009. The relative lesser growth of exports compared to imports also contributed by increasing the positive net balance on foreign trade.

Growth decomposition by components of aggregate expenditure for the year 2009 illustrates how the economy processed the international shock. It can be observed in Figure10 that the fiscal stimulus by the public sector and exchange rate flexibility were instrumental to cushion the effects of the crisis. Growth was uneven in the different components, with government consumption increasing 5.2 percent, which accounts for the dampening effect played by public expenditure, while private consumption grew only 1.5

percent. Gross fixed capital formation decreased by 4 percent reflecting the inventory adjustment. The public sector expansive policy can be appreciated in the 20.1 percent increase on public gross fixed capital formation which offset part of the private sector contraction of 10.7 percent. But much of the net growth observed was a result of the external sector of the economy. While exports showed an average growth of 2.5 percent, imports contracted 8.6 percent, result largely accounted on the exchange rate flexibility.

Figure 10: Uruguay GDP and GDP Components

(in percentage change)

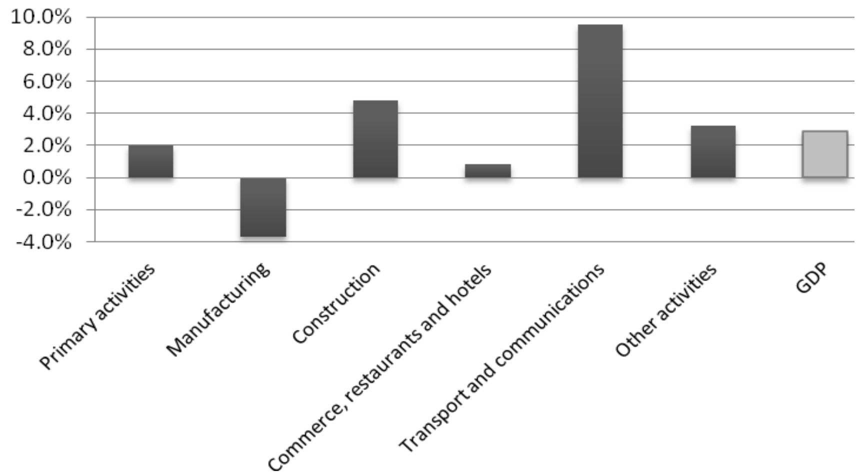


Source: Central Bank of Uruguay

In terms of growth by sector, 2009 was characterized for a generalized increase in goods production and services with the exception of manufacturing which registered a decrease of 3.7 percent. This can be explained due to the contraction on foreign demand and the maintenance that shut down the only oil refinery in the country (owned by the state enterprise ANCAP) during the last quarter of 2009 considering the weight ANCAP has on this activity sector. The sectors that had the greatest impact on growth were Transport and Communications with a 9.5 percent and Electricity, Gas and Water supply with 41.9 percent. This last number can be explained mainly by the end of the drought that allowed the reestablishment of the hydroelectric generation. The expansion on Transport and Communications was primarily the effect of cellular telephony growth of 9.5 percent, even if lower that the remarkably high 34.6 percent showed on 2008. Construction on its part grew at a rate of 4.8 percent recovering from the decrease suffered in 2008. The agricultural sector had a mixed behavior with an important growth of 12.9 percent in agriculture, while the livestock sector showed a decrease of 1.3 percent, accounting for a 2.9 percent growth of the whole sector for 2009.

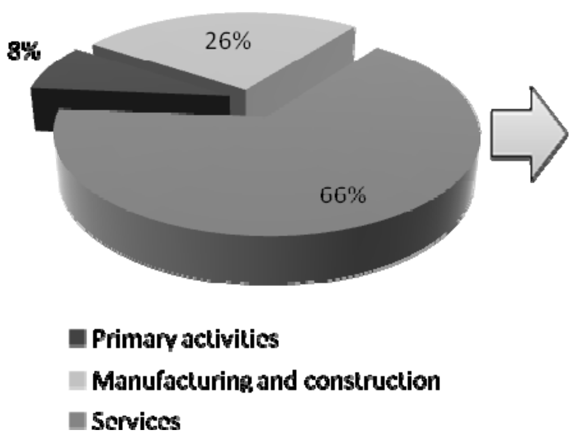
Figure 11: GDP growth by Economic Sector

(in percentage change 2009/2008)



Source: Central Bank of Uruguay

Figure 12: Total 2009 GDP Participation by Economic Sector



Services		
Commerce, restaurants and hotels	15%	23%
Transport and communications	14%	21%
Financial intermediation	6%	9%
Real estate and renting business	13%	20%
Public administration and defense	5%	7%
Other activities	13%	20%
	66%	100%

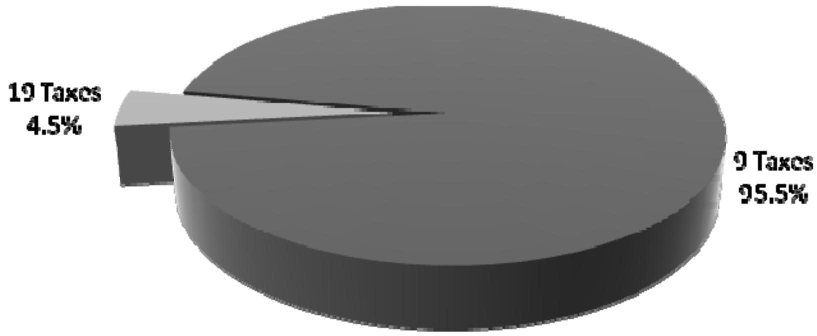
Source: Central Bank of Uruguay

Inflation

During 2009 inflation measured by consumer price index (CPI) rose 5.9 percent, but inflation was kept within the target range established by the Macroeconomic Coordination Committee (Comite de Coordinación Macroeconómica) which is an important achievement after two years of non compliance. Still, it brought Uruguay to the forth place regarding inflation among Latin American countries. The reduced inflation in 2009 weigh against the 9.2 percent of 2008 is attributable to the fall in commodity prices, specially food and energy which in 2008 had reached record highs and the reduction on regional demand as a result of the global crisis.

Figure 13: Uruguay CPI Evolution

(annual change in percentage)



Source: Uruguay National Institute of Statistics.

Considering the inflation by category, we find in Table 5 that the best performing items in 2009, with growth at or below the average were: recreation and culture -2.7 percent, transport and communications 0.5 percent, furniture and household accessories 2.0 percent, clothing and footwear 3.3 percent and food and beverages 4.5 percent. On the other hand, those that recorded an above average growth were: healthcare 8.7 percent, housing 11.6 percent, education 12.3 percent and other goods and services 16.6 percent. In 2008, the government used various tools to try to contain price rise and inflation from reaching double digits, because in that case, it would have triggered a wage increase clause agreed with public employees that would have increased the inflationary spiral. Combined monetary and commercial policies allowed keeping inflation below double digits throughout the year, although slightly above the guidelines provided. In 2009 it was not necessary to resort to similar measures.

Table 7: CPI by Expenditure Category

(annual change in percentage)

Categories	2004	2005	2006	2007	2008	2009
Food and beverages	7.86	3.03	9.07	18.13	10.62	4.51
Cloth and footwear	7.81	3.45	1.37	3.16	3.45	3.26
Housing	7.97	6.87	7.88	8.66	13.77	11.59
Furniture and household accessories	5.35	17.02	7.50	5.05	10.17	1.98
Health and healthcare services	8.35	3.17	8.41	3.03	6.25	8.66
Transport and communication	9.02	3.79	0.26	0.75	5.54	0.53
Culture, leisure and recreation	2.87	-0.79	5.51	1.97	12.56	-2.66
Education	7.45	8.01	7.98	8.78	10.40	12.29
Other expenditures	6.43	8.12	4.76	8.48	6.07	16.58

Source: Uruguay National Institute of Statistics.

The CPI data recorded in the period from January to May marks a 2.8 percent cumulative inflation for the first five months of 2010. Recorded inflation shows an upward trend in 2010 and economists estimate it will surpass the target range set between 4 and 6 percent. The main contributors in the CPI between January and May 2010 were food and beverages followed by healthcare. Regarding the former much of it is explained by a notable increase in meat and dairy.

In particular, the rental price has been one of the most persistent in the evolution of the CPI since 2005, accompanying Real Wage Index evolution, with an increase of 27 percent in real terms between January 2005 and March 2010.

Consumption

Domestic demand in annual terms significantly grew in the second quarter of 2010 driven by increases in both consumption and investment, having the first a higher incidence due to their greater participation in domestic demand with a 9.8 percent growth and 8.1 percentage points of impact. In this sense, there was an acceleration in consumption growth in both quarters of the year after. In this respect it is necessary to differentiate public and private behavior.

In 2009, government consumption had increased significantly, offsetting the less dynamic private sectors, but in 2010 this behavior was reversed, registering a higher growth in private consumption in relation to public. The behavior of private consumption was positively affected by the good performance of the labor market. Business spending has increased this year, driven both by investment in machinery and equipment and by the construction.

Investment

Although the greatest effect on increasing domestic demand accounted for consumption, its most dynamic component in the second quarter of 2010 was the gross capital. Private sector regained momentum after a contraction in 2009 and increased almost 13 percent, both in machinery and equipment and construction, as public sector investment fell for the second consecutive quarter.

Analyzing the behavior of the seasonally adjusted gross fixed capital formation, there is a return to the upward trend from the first quarter of 2010, which coincides with the recovery of business expectations. Thus in the first half of 2010 private investment exceeded 18.4 percent year on year, while public investment fell 8.9 percent in same comparison. The public contraction is mainly a result of the completion of some important infrastructure projects like the maintenance and overhaul of the Port of Punta del Este, the new route access to the Carrasco International Airport and others.

Table 8: Consumption, Savings and Investment

(in percentage of GDP)

	2006	2007	2008	2009
Gross national income	97.38	97.09	96.47	99.22
Final consumption expenditure	82.22	80.99	80.43	80.34
Gross savings	15.79	16.67	16.51	19.31
Total gross capital formation	19.17	18.94	21.73	19.98
Total gross fixed capital formation	18.06	18.79	20.49	19.27

Source: Uruguay National Institute of Statistics.

Table 9: Investment by Activities

(in percentage of GDP)

	2006	2007	2008	2009
Total gross fixed capital formation	18.06	18.79	20.49	19.27
Construction	9.70	10.00	9.68	10.14
Plantations and perennial crops	0.65	0.58	0.56	0.35
Machinery and equipment	7.70	8.21	10.24	8.78
Gross fixed capital formation of Public sector	3.40	4.12	4.45	5.23
Construction	2.60	3.34	3.59	4.31
Machinery and equipment	0.80	0.79	0.86	0.92
Gross fixed capital formation of Private sector	14.65	14.67	16.04	14.04
Construction	7.10	6.67	6.10	5.83
Plantations and perennial crops	0.65	0.58	0.56	0.35
Machinery and equipment	6.90	7.42	9.38	7.86

Source: Uruguay National Institute of Statistics.

Stock Market

Uruguayan stock market is of much reduced size, with only three domestic companies listed traded in 2009 and a few with bonds and commercial papers issued. However, there exists an adequate institutional investor base, mostly pension funds. The main focus has remained on transactions of public papers and investment on foreign securities.

The stock exchange consist of the Bolsa deValores de Montevideo and Bolsa Electrónica de Valores SA, the latter one exclusive for banks and other financial institutions. It provides markets for government debt papers and private ones, although the markets for the latter ones are of lesser magnitude. At March, 2010 there were registered in the Securities Market Registry 108 stock brokers, 72 brokers and 36 brokerages.

Table 10: Overview of Uruguay's Capital Market

	(December 2009)
Brokers and dealers	108
Stock exchanges	2
Mutual Fund Administrators	17
Pension Fund Administrators	4
Pension Fund Assets, % GDP	10.4
Securities, % GDP	44.6
Public securities traded , % GDP	42.8
Private securities traded, % GDP	1.8

Source: Central Bank of Uruguay

The 2002 financial crisis affected the capital markets and showed deficiencies in the legislation. The collapse of two major private banks, both issuers of Eurobonds, reinforced the negative sentiment of investors. The amounts traded since 2003 are below those observed in 2001 and the composition of instruments has shifted to shorter terms. As March of 2009 the market capitalization reached only 0.5 percent of GDP.

Table 11: Stock Exchanges Activities

(in million US dollars)

	2006	2007	2008	2009	Q2 2010
Stock exchanges	**7,597**	**12,067**	**14,999**	**12,315**	**7,728**
Primary market	**6,587**	**11,115**	**13,840**	**10,829**	**6,977**
Public sector	75	2,128	6,094	4,787	3,113
Private sector	6,512	8,987	7,746	6,042	3,864
Secondary market	**1,010**	**952**	**1,159**	**1,486**	**751**
Public sector	942	858	1,116	1,470	741
Private sector	19	53	30	11	8
Foreign sovereign securities	49	41	13	5	2

Source: Central Bank of Uruguay

For the first quarter of 2010, total stock market operative reached 6.106 million US dollars, an increase of 14 percent over the previous quarter. The total amounted operated on the stock exchanges was 4.513 million, representing a 10 percent increase in the amount traded over the fourth quarter of 2009, and almost twice as operated in the first quarter of the same year. The primary market transactions rose 14 percent over the previous quarter amounting to 5.678 million US dollars, while the secondary market volume of operations increased by 7 percent, to 428 million. The trading of government securities accounted for 98 percent of secondary market with private papers amounting 6.29 million US dollars.

In recent years, the government has begun a series of reforms to capitalize on the benefits from development of capital markets. In 2008 a new Bankruptcy Law was approved in to address adequately the deficiencies of the previous legislation in the matter. Also, a new Securities Market Law (Ley del Mercado de Valores 18627) was approved in December 2009 establishing a regulatory framework for issuers, stock exchanges and agents participating in the market.

Among the most important changes brought by the new Act is the creation of a security registry, controlled by the Central Bank, in which all Uruguayan issuers and securities will be recorded. To this end it reorganizes a superintendence of the Central Bank of Uruguay to address the problems of capital market and facilitate the implementation of the new Act. Several measures to increase investor's confidence in capital markets, such as corporate governance requirements, increased monitoring, control of market abuse, and strong disciplinary sanctions are included.

The Act establishes a Public commission (Comisión de Promoción del Mercado de Valores) whose task is the development of this market, which will have functions such as advising the Executive on the matter, the promotion and realization of market studies and the proposal of public policies and actions within its jurisdiction. And also several tax benefits aimed to promote and foster market dynamism.

Money Supply

During the first half of 2010, lending in national currency expanded at increasing rates driven by the recovery of economic growth and increased levels of activity. This is an important change of trend since the credit contraction caused by the effects of the international crisis. The credit demand stimulus was transformed into lending primarily due to the higher availability of funds resulting from the Central Bank policy that reduced the reserve ratio on deposits in national currency. The main contributor to this expansion was the public banking sector.

The stock of foreign currency loans also grew, albeit at a slower rate than the national currency. However, given the real appreciation of the peso during the first six months of the year, this evolution implies a reduction in terms of purchasing power. In the case of credit in foreign currency, the private banks have been the more proactive.

Deposits maintained a growing trend in the second quarter of 2010, both in national and foreign currency denominated. However, there was continuity in the process of de-dollarization, which was temporarily reversed during the financial crisis in late 2008. By the end of 2010 second quarter, the deposits dollarization level stood close to 72 percent.

Table 12: Monetary Aggregates

(in million Uruguayan pesos)

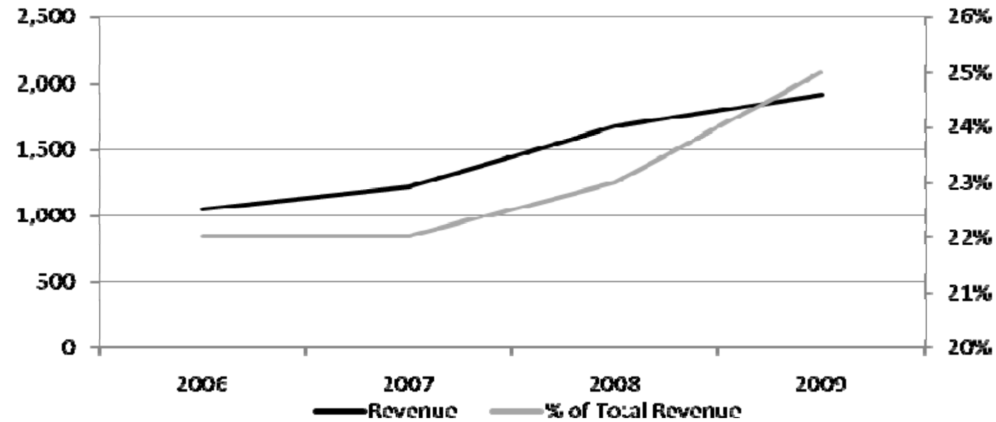
	2005	2006	2007	2008	2009	Q1 2010	Q2 2010
1 - Issued currency	17,285	22,065	24,617	28,263	31,980	32,577	32,041
2 - Currency in the banking system	3,970	5,934	5,725	6,856	7,674	6,203	7,966
3 - Currency not in the BS = (1) - (2)	13,315	16,131	18,893	21,407	24,306	26,375	24,075
4 - Demand deposits in national denom.	16,416	19,561	28,158	33,860	37,538	38,172	40,828
5 - M 1 = (3) + (4)	**29,731**	**35,692**	**47,051**	**55,267**	**61,844**	**64,547**	**64,903**
6 - Saving deposits in national denomination	6,244	8,942	11,853	14,172	18,130	21,978	20,851
7 - M 1' = (5) + (6)	**35,975**	**44,634**	**58,904**	**69,439**	**79,974**	**86,525**	**85,754**
8 - Time deposits in national denomination	8,158	9,232	11,679	13,328	15,124	16,357	18,266
Time deposits	7,003	8,131	10,297	12,227	14,222	15,433	16,679
Certificates of deposit	1,156	1,101	1,382	1,101	902	924	1,587
9 - M 2 = (7) + (8)	**44,133**	**53,867**	**70,582**	**82,767**	**95,098**	**102,882**	**104,021**
10 - Pre savings deposits	1,530	1,697	1,957	2,229	2,603	2,760	2,785
11 - M 2' = (9) + (10)	**45,663**	**55,563**	**72,540**	**84,996**	**97,701**	**105,642**	**106,805**
12 - Seasonally adjusted M1	**27,667**	**33,149**	**43,575**	**51,038**	**56,993**	**62,138**	**64,012**

Source: Central Bank of Uruguay

Measurements taken with the narrow aggregate M1 show a slowdown in money supply growth rate compared to the ones at the end of 2009. This evolution is consistent with a slight slowdown in the real demand for money, and a relatively constant rate of inflation. This is confirmed by analyzing the ratio of M1 / GDP which in the first half of 2010 continued to increase but at decreasing rates.

Figure 14: Central Bank of Uruguay Monetary Base

(in million Uruguayan pesos)



Source: Central Bank of Uruguay

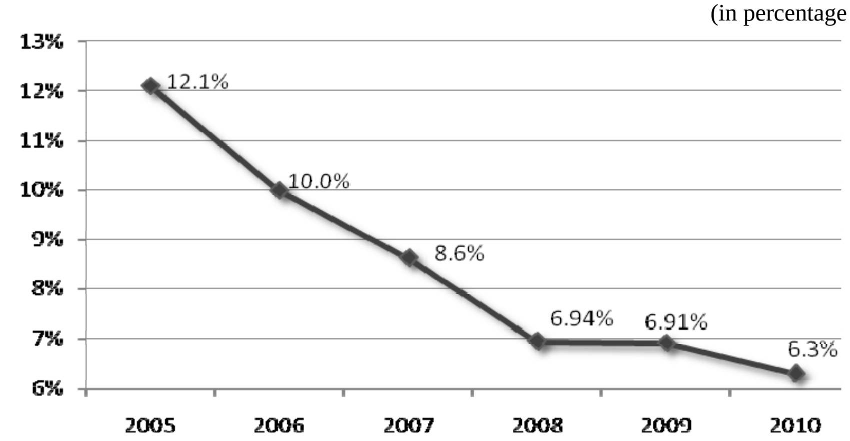
Employment

Employment reached a record high of 65.4 percent at the end of 2010 first quarter. Traditional employment levels in Uruguay have fluctuated between 57 and 60 percent with the tendency growing beyond 60 percent from 2006 onward. Unemployment fell to its lowest level in the last decade, dropping from an average 13.1 percent in 2004 to 6.3 percent in the last 2010 third quarter preliminary data.

The impact of the international crisis toward the end of 2008 and the beginning of 2009 caused a small deterioration on those figures with employment falling to 57.6 percent and unemployment rising to 8.3 percent in mid 2009. Data in the first nine months of 2010 shows the continuation of the trends of reduction of unemployment and employment increase, albeit at a slower pace than in previous years. This slowdown in the pace of expansion of employment is partly explained by the measures adopted by various companies during the crisis, when instead of laying off workers *they* used temporal unemployment insurance and decreased the number of hours worked as mechanisms to reduce production. In the first months of 2010 and after the recovery of economic activity, these measures were reversed, reinstating the workers and increasing hours worked, which does not impact on the rate of employment. The sectors that created more jobs in the period between July 2009 and June 2010 were education, manufacturing, household services and fisheries and agricultural activities.

Figure 15: Uruguay Total Unemployment Evolution

(in percentage at year's end)



*2010 data corresponds to September.
Source: Uruguay National Institute of Statistics.

Although unemployment is at historically low levels, its composition is skewed towards younger women and those individuals with lower levels of skill. The specific rate of unemployment for those under 25 years of age reached 20 percent in 2009 while for individuals of 25 and older was only 4.4 percent. In turn the unemployment rate for women stands at 8.1 percent while that of men is 4.7 percent.

Table 13: Unemployment by Sex

(in percentage at year's end)

	2005	2006	2007	2008	2009	2010*
Male	9.1	7.6	6.1	5.2	5.0	4.7
Female	15.5	12.7	11.6	8.9	9.0	8.1
Total	12.1	10.0	8.6	6.9	6.9	6.3

*2010 data corresponds to September.
Source: Uruguay National Institute of Statistics.

According to the 2009 report by the National Institute of Statistics, the number of work posts amounts to 1,553 million with 109,000 unemployed. Trade and services sector, which typically absorb more labor, occupies 21.6 percent of total employed population. The next most important sector is manufacture with 14.1 percent. It is interesting to distinguish between Montevideo and the rest of the country, since in the latter weight of agriculture and livestock is the second in importance with 19.5 percent and a very low incidence from household or financial services. While in the capital, trade and services occupy 23.5 percent of the total and areas such as financial intermediation and real estate rise to 12.4 percent of the employed population.

Table 14: Employment by Activity Sector

(as percentage of total employment in Montevideo, rest of the country and national total)

	2008			2009			Q2 2010		
	Mont	Rest	**Total**	Mont	Rest	**Total**	Mont	Rest	**Total**
Manufacturing, electricity, gas and water	14.8	13.3	**13.9**	15.2	13.2	**14.1**	14.6	13.7	**14.1**
Construction	5.4	8.6	**7.2**	5.6	7.8	**6.8**	5.4	7.9	**6.8**
Wholesale, retail trade, hotels and restaurants	22.6	20.0	**21.1**	22.2	20.9	**21.4**	23.5	20.2	**21.6**
Transport, storage and communications	7.3	4.6	**5.8**	6.6	4.4	**5.3**	6.8	4.4	**5.4**
Financial Intermediation, real estate and renting business	12.4	5.5	**8.4**	12.7	6.0	**8.9**	12.4	5.0	**8.3**
Public administration and defense	6.5	5.7	**6.1**	6.2	5.7	**5.9**	6.1	6.1	**6.1**
Education	5.3	5.6	**5.5**	6.5	5.0	**5.6**	6.5	5.2	**5.8**
Health and Social Services	10.5	5.5	**7.7**	9.5	4.9	**6.9**	9.0	5.0	**6.8**
Elimination of waste, sewage, sanitation	5.4	4.6	**4.9**	5.6	4.4	**4.9**	5.7	4.3	**4.9**
Private households with household service	7.6	9.3	**8.5**	7.9	9.7	**8.9**	8.3	8.7	**8.5**
Agriculture, livestock, forestry, fishing and mining	2.3	17.3	**10.9**	1.9	18.0	**11.0**	1.8	19.5	**11.7**
	100	100	**100**	100	100	**100**	100	100	**100**

Source: Uruguay National Institute of Statistics.

II.2 Fiscal Position

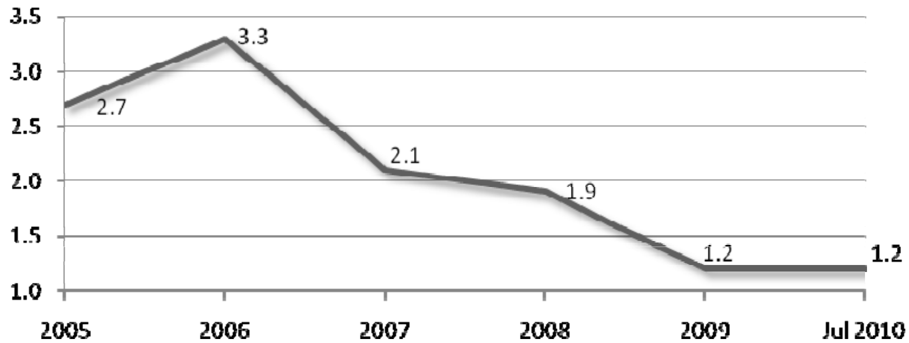
The overall result of the public sector within the twelve months ended in June 2010 was a deficit of 1.1 percent of GDP. Compared to the end of 2009 it improved by 0.6 points and 1.1 points compared to the rolling year ending in June 2009. A primary surplus of 1.7 percent of GDP in the twelve months to June mark an improvement of 0.7 points and one point over December and June 2009 respectively.

The improvement of government accounts is explained by the Public Enterprises results, which increased 0.7 percentage points of GDP compared to the end of last year and 0.9 points on the cumulative to June 2009. Even so, the improved result of the Public Enterprises was due to lower cost of electricity generation. After nearly two years of drought, forcing electricity generation based on fuel oil, a milder climate in 2010 allowed not only to generate all the internally consumed energy by hydropower, but also generated surplus that was exported.

Public Enterprises regulations do not allow this positive result to contribute to financing the rest of the public sector. Wages, pensions, transfers, expenditures, interest payments and investments of the Central Government (CG), are financed by taxes. For this reasons, to have a more precise measurement of public finances performance, CG-BPS data is used. Were GC is the public sector results excluding the Public Enterprises adding the results of the Social Security Bank (BPS).

Figure 16: CG - BPS Primary Balance

(in percentage of GDP)



Source: Ministry of Finance and Central Bank of Uruguay

The overall GC-BPS accumulated result was a deficit during the rolling year ended in June 2010 of 1.3 percent of GDP. A slight improvement of three tenths compared to the year 2009. The primary surplus in June 2010 was 1.2 percent of GDP, the same figure at the end of 2009. Figure 16 shows its evolution.

Table 15: Public Sector Balance

(in million US dollars)

	2005	2006	2007	2008	2009
I. Public Sector non financial revenue (II+III+IV)	4,879	5,568	6,731	8,157	8,823
II. Central Government	3,638	4,246	4,939	6,267	6,456
DGI	2,770	3,294	3,883	5,213	5,390
IRP (1)	135	183	147		
Foreign trade	213	250	304	338	316
Other	520	520	605	717	750
III. BPS	878	1,048	1,216	1,672	1,910
IV. Primary balance of Public Enterprises	362	274	577	218	457
V. Non financial Public Sector primary expenditure (VI+VII)	4,222	4,882	5,972	7,778	8,615
VI. Central government - BPS primary expenditure	3,824	4,373	5,276	6,813	7,525
Wages	797	907	1,804	1,398	1,587
Non wages expenses	695	831	983	1,159	1,158
Pensions	1,597	1,768	1,994	2,528	2,748
Transfers	736	867	1,215	1,729	2,748
VII. Investment	398	509	696	964	1,090
Public Enterprises	172	233	327	431	590
Central Government	226	276	369	534	500
VIII. Municipalities primary balance	29	71	43	42	95
IX. BSE primary balance (State Insurance Bank)	28	-4	52	73	41
X. Non financial public sector primary bal. (IV+VIII+IX)	714	753	855	494	344
XI. BCU primary balance (Uruguay Central Bank)	-9	-31	-31	-41	-29
XII. Public Sector primary balance (V+VI)	705	722	823	453	315
XIII. Interests	773	830	843	891	879
Public Enterprises	734	828	887	877	862
Central Government	28	32	31	29	44
Municipalities	8	8	8	7	6
BCU	18	-20	-60	11	13
BSE	-15	-18	-23	-32	-45
PUBLIC SECTOR OVERALL BALANCE (XII-XIII)	-68	-108	-19	-438	-564
Primary balance (% GDP)	4.0	3.6	3.5	1.3	1.1
Overall balance (% GDP)	-0.4	-0.5	0.0	-1.5	-1.7

(1) IRP stands for the tax on wages removed in 2007.

Source: Ministry of Finance.

Public spending continues its upward trend, and the shrinking of the primary surplus is a sign that expenses are growing at a faster rate than revenues, with only investment spending showing contracting behavior in the first half of 2010.

Government Expenditure

Government expenditure increased 10.95 percent during 2009 year on year, mainly because of transfers to the Social Security Bank, both to help pension payment and investments in the area. Expenditure of the non financial public sector was equivalent to 26.2 percent of GDP in 2009, down 0.1 percentage point compared to the rolling year ended in November. Current spending increased 0.1 percent of GDP as a result of wage and pension rise, while non wage expenses fell during 2009.

For the twelve months ended in June 2010, CG-BPS current spending amounted 20 percent of GPD, showing a slow increase. Although investment grew 0.3 percent of GDP it responds entirely to crude oil stock accumulation by ANCAP.

Table 16: Consolidated Results

(in million of current Uruguayan pesos)

	2005	2006	2007	2008	2009	2010*
Wages	18,361	20,677	24,036	27,565	33,583	18,268
Social Security	33,650	36,354	41,350	49,788	57,196	31,812
Expenses	16,030	18,974	21,752	22,847	24,076	13,618
Transfers	3,898	4,089	7,886	7,695	9,849	4,832
Investment	5,520	6,626	8,507	11,616	11,197	6,115
Public debt interest	17,947	19,881	20,736	18,311	19,441	9,252
Total expenses	95,405	106,600	124,266	137,822	155,342	83,896

* Cumulative data to June 2010

Source: Ministry of Finance

An explanation to the increased public expenditure is the rise to the denominated Social Public Expenditure, which includes expenses on welfare, education and healthcare. One of the main policies of the government expenditure in recent years have been those aimed to diminish poverty and invest in human capital, from 1998 to 2008 this expenditure has doubled its participation on the government expenditure reaching in 2008 21.7 percent of GDP and 75.4 percent of the central government expenditure.

During 2009 CG expenditures real growth was 5.5 percent, led by the social welfare spending increase of 7.4 percent, continuing the trend from 2008. These expenses represented 37 percent of the total. In a similar trend, remuneration spending grew 13.8 percent, the second largest item in the expenses with a share of 22 percent. For its part, non wage expenditure declined 1.4 percent, while public debt interest showed a slight decrease of 0.7 percent, amounting to 13 percent of CG expenditures. Both helped to partially offset the after mentioned rise.

Fiscal Deficit

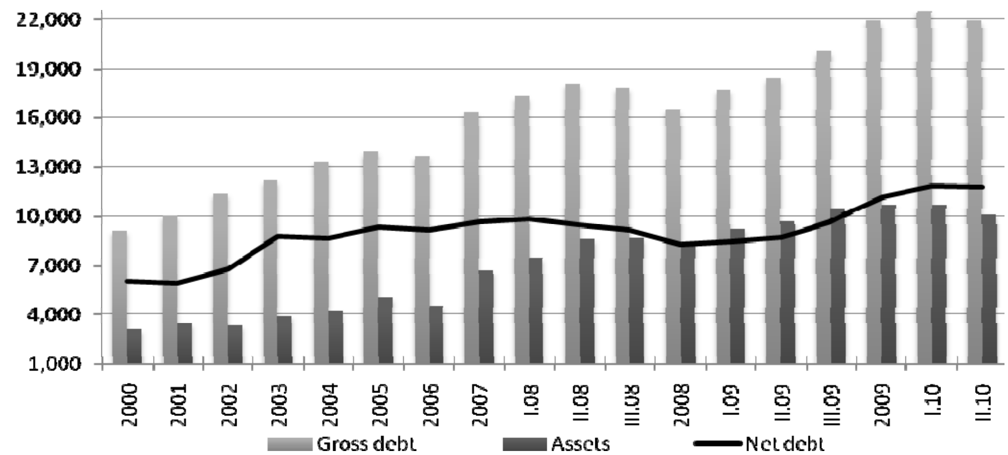
The overall result of the rolling year ended in August 2010 showed a deficit of 361 million US dollars, equivalent to 1 percent of GDP, which represents a significant improvement compared to the result reached in December 2009 of 1.7 percent of GDP. Estimates for the closing of the year expect an improvement in the consolidation of public accounts. The overall fiscal deficit would decline over 2009 and became 1 percent of GDP.

The global gross debt of the public sector rose sharply in 2009 compared to 2008, reaching 5,202 million US dollars, representing an annual increase significantly higher than previous years. Thus, the gross debt also grew in terms of GDP accounting for 68.4 percent, compared to 53 percent in 2008, record at a similar level of 2006. But unlike 2008, the largest fiscal deficit was not explained only by an element largely transient, as was the energy crisis, instead much of it resulted from the continued expansion of expenditures, as well as the slowdown in revenue growth due to the lower economic activity.

Overall net debt of the public sector also grew during 2009, accompanied by an increase in public sector assets of 2,332 billion, reaching 35 percent of GDP, a ratio higher than the 25.6 percent showed in 2008 but significantly lower than those achieved from 2003 onwards. While among the causes of the increase is the fiscal deficit of the period, the variation of the Uruguayan peso during the year also played an important role.

Figure 17: Public Debt

(in million US dollars)



Source: Central Bank of Uruguay

Another element to consider is the policy of reducing reserve requirements implemented by the BCU in 2009, which reduced the amount by about 650 million US dollars, 2 percent of GDP. This represents over 20 percent of the net bet increase in the year.

Table 17: Gross debt by Creditor Type and Residence

(in million US dollars)

	Creditor type				Residence		
		Private creditors					
	Official creditors	Financial sector	Non financial	Others	Non resident	Resident	Total
2000	2,511	6,271	376	-26	6,092	3,040	9,132
2001	2,525	6,620	927	0	5,829	4,244	10,072
2002	4,751	6,056	579	0	8,299	3,087	11,386
2003	5,623	5,753	787	0	9,558	2,606	12,163
2004	5,876	6,660	761	25	10,206	3,116	13,322
2005	5,524	7,390	1,014	21	10,177	3,773	13,949
2006	2,683	9,919	1,097	18	9,311	4,405	13,717
2007	2,689	11,913	1,703	14	11,065	5,254	16,319
2008	3,155	11,622	1,747	11	10,736	5,799	16,534
2009	4,518	15,034	2,261	77	12,770	9,121	21,891
Q2 2010	4,321	15,131	2,351	83	12,376	9,509	21,885

Source: Central Bank of Uruguay

Analyzing gross debt by residence composition, there is a continued trend since 2003 to increase the participation of residents, with domestic owned debt reaching 42 percent from 35 percent at the end of 2008. In the context of credit constraints prevailing in the international financial market crisis scenario, the government opted from the second half of 2008 to resort to credit by international organizations, which implied an increase in their share in the total debt in 2008 and 2009 in parallel to a corresponding drop in public securities.

Table 18: Gross debt by Currency Composition

(in million US dollars)

	Total	Pesos	Foreign currency	SDR	Others
2000	9,132	640	8,235	253	5
2001	10,072	1,749	7,869	150	305
2002	11,386	456	9,093	1,794	44
2003	12,163	690	9,040	2,416	17
2004	13,322	1,305	9,250	2,683	84
2005	13,949	1,776	9,798	2,311	66
2006	13,717	2,529	11,127	7	54
2007	16,319	4,996	11,278	8	38
2008	16,535	4,993	11,504	7	32
2009	21,891	7,587	13,803	465	36
Q2 2010	21,885	8,099	13,324	441	22

Source: Central Bank of Uruguay

Gross debt denominated in domestic currency increased from 30.2 percent of the total in 2008 to 34.9 percent in 2009, while that nominated in foreign currency fell from 69.6 percent to 62.8 percent. This emphasizes the continuity of de-dollarization of the debt that has been observed since 2003, interrupted only very slightly in 2008, which can be observed in the currency composition of debt of Table 18, resulting in a reduced exchange risk.

Regarding the composition of the debt terms in 2009, it is important to note that although the maturity structure has improved, there are still significant debt repayments for 2011, close to 1,000 million US dollars.

As a last remark, public debt interest remained stable during 2009 at 2.6 percent of GDP, with a slight increase in 2010 to 2.8 percent, but keeping leveled.

Public borrowing

Uruguay has always maintained a track to meet its debt payment obligations, even during the difficult situation of the financial crisis of 2002, year in which Argentina defaulted on its public debt. One of the major macroeconomic achievements of the Administration during the recovery phase of the crisis was the policy of debt management. The good fiscal performance, the appreciation of the peso and increase on international reserves have reduced short-term vulnerabilities and allowed to replace conditional debt for unconditional one.

During 2009 the government managed to continue with the policy of pre-financing of the fiscal needs of next year, getting through increased public debt the necessary resources to meet obligations for 2010. Nevertheless, increases in international reserves were lower than the increase in debt in the year, leading to net debt rose 9 points to GDP ratio from 26 percent to 35 percent, reversing the steady downward trend since 2004.

Table 19: Consolidated Public Sector Founding

(in million US dollars)

	2005	2006	2007	2008	2009
Financing *	98	90	-100	-16	296
Monetary liabilities	17	-32	-11	334	85
Borrowing	438	362	1,774	1,734	1,671
Government securities	573	1,159	1,548	695	85
External loans	-110	-542	226	354	942
Financial sector	-25	-255	-1	686	644

* (+) source, (-) use

Source: Central Bank of Uruguay

Table 19b: Consolidated public sector founding

(in percentage of GDP)

	2005	2006	2007	2008	2009
Financing *	0.6	0.5	0.4	-0.1	0.9
Monetary liabilities	0.1	-0.2	0.0	1.1	0.3
Borrowing	2.5	1.8	7.4	5.6	5.3
Government securities	3.3	5.8	6.4	2.2	0.3
External loans	-0.6	-2.7	0.9	1.1	3.0
Financial sector	-0.1	-1.3	0.0	2.2	2.0

* (+) source, (-) use

Source: Central Bank of Uruguay

Official statements on the next period founding policies disclose that the government intends to attract about 5,000 million US dollars with operations focused in the local market and prioritizing local currency debt, in order to finance a fiscal deficit, projected to reach 0.7 percent in 2015. The policy aim is to forego financing by international organizations substituting it by domestic private participation. The government estimates a gross debt reduction from a level close to 65 percent of gross domestic product to 40 percent by 2015, with an increased participation of bonds in local currency from 30 percent at 2009 end to 45 percent at the end of 2014.

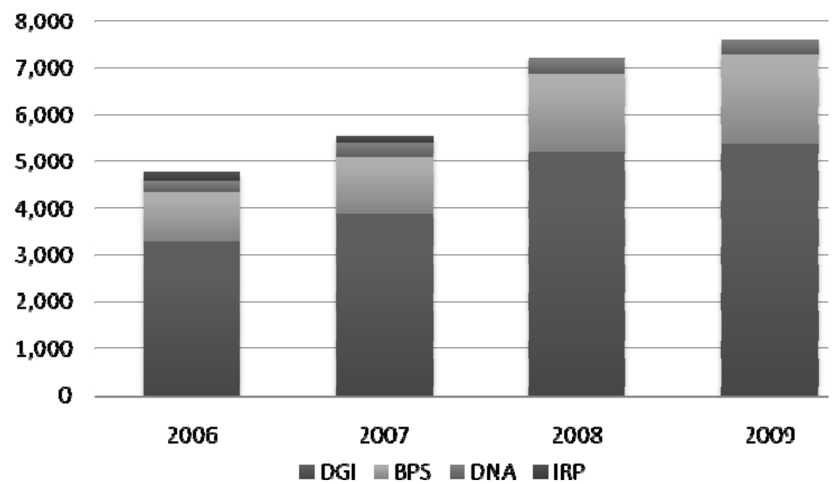
Tax Revenue

When talking about tax revenue in Uruguay is important to make two clarifications, for one part most of total tax revenue is collected by Offices, the General Tax Directorate (DGI) and the Social Security Bank (BPS) with a small amount added by the National Customs Directorate (DNA). Second, BPS is a decentralized service and its revenue is ear tagged and only used in the welfare system, mainly pensions, unemployment insurance and health care programs, and that is why it is not included in the general revenue and expenditure analysis of the Central Government, as the revenue cannot be discretionary used.

Nonetheless BPS revenue is still an important part of the total tax revenue in Uruguay as shown in the figure bellow.

Figure 18: Total Tax Revenue by Agency

(in million US dollars)



Source: Ministry of Finance

Table 20: Total Tax Revenue

(in million US dollars and percentage of total)

	2006		2007		2008		2009	
DGI	3,294	69%	3,883	70%	5,213	72%	5,390	71%
BPS	1,048	22%	1,216	22%	1,672	23%	1,910	25%
DNA	250	5%	304	5%	338	5%	316	4%
IRP [1]	183	4%	147	3%		0%		0%
Total tax revenue	4,775	100%	5,550	100%	7,223	100%	7,616	100%

Source: Ministry of Finance

Note [1]: IRP - Tax on wages, repealed in 2007 tax reform was collected by BPS monthly, together with social security contributions on payrolls, but it was destined to Central Government expenditure instead of the welfare scheme, which is why is presented separately.

Central Government real income experienced an increase of 3.4 percent in 2009 over 2008, mainly by effect of increasing domestic tax revenues, with the General Tax Directorate (DGI) revenues registering a 3.9 percent increase. In the same year BPS revenue increased 12 percent in real terms while its expenses increased 10 percent, thus improving the results of the service.

III. Tax Structure: Institutions and the Reality

III.1 Overview

The current tax system in Uruguay is established in the Tax Code and the Consolidated Tex 1996. The last modifications made to it were done by the law 18341, the Tax Reform Act of December 27 2006, and it entered into force the 1st. of July 2007. This Law restructured most of the national taxes, being its pillars, in the direct taxes, the corporate, natural persons and non residents income tax, and in the indirect taxes the VAT.

One important aspect of the tax reform is that it was complemented by a readjustment of the state through the process of modernization of the Tax Administration, making a restructure on many aspects of the DGI, the BPS and the DNA. Strategic objectives were established as well as management goals, which are actualized yearly in a continuous improvement process. By the beginning of 2010 it is considered that the most critical points of the restructure of the DGI and the BPS have already been covered and the restructure of the DNA is already beginning.

There are several characteristic to mention about the tax system in Uruguay, firstly it is based on the criteria of territoriality or of the source. According to this criterion, the tax burdens fall over the income earned in Uruguayan territory or over the goods located inside the country's borders, regardless of whether the income beneficiary or owner of the property was Uruguayan or was resident of the country. Second it presents a revenue structure inverse to the majority of developed countries, with a high relative weight of indirect taxes and low relative weight of direct taxes. And last, that the system is a self-assessment system that work in base of affidavits submitted by the taxpayers.

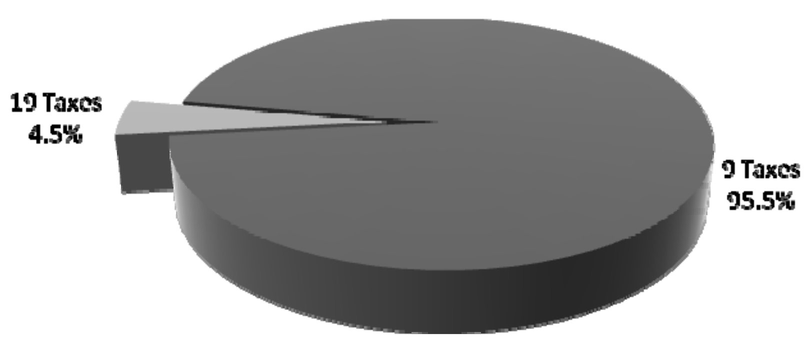
In 1974 there was a strong simplification of the tax system, but since the early 80's until the reform of 2007, there were modifications not over the basis of certain design criteria, but in response to specific contingencies among which are: structural increase of public spending, declines in activity levels and economic crisis and short-term increases in public spending.

To address these issues two resources were mainly employed, the increase in the rates of existing taxes and the creation of new taxes, small from a collection point of view, but that made the tax system increasingly complex and strengthened the incentives for evasion.

The Figure 19 shows how the previous tax system based revenues in a few taxes, while there were a great number of taxes with little relevance in terms of collection.

Figure 19: Consolidated tax composition in 2006

(as percentage of total tax revenue)



Source: Ministry of Finance

The absence of an individual income tax, not a minor thing, caused that the vast majority of taxpayers were businesses and not people. In addition to this, by law the retail prices are shown VAT included, resulting in lack of tax culture and awareness of the tax burdens from most of the Uruguayan population.

Another point made by the reform was to bring the Uruguayan tax system close to modern international taxation, adapting price transfer models and preparing the ground in order to improve the administration in terms of the agreements to avoid double taxation.

One of the most important contributions of the reform in terms of taxes was the simplification reached through the elimination or adjustment of taxes. Mainly, taxes with low revenue capacity and distortive were eliminated since they hampered the management of enforcement agencies and increased the cost of taxpayer compliance. This simplification also decreased administration costs.

Abolished taxes.

1. Wage Tax (IRP)
2. Social Security Contribution Tax (COFIS)
3. Bank Assets Tax (IMABA)
4. Financial System Control Tax (ICOSIFI)
5. Health Services Tax (IMESSA)
6. Small Business Tax (IMPEQUE)
7. Commissions Tax
8. Telecommunications Tax (ITEL)
9. Credit Card Tax
10. Enforced Sales Tax
11. Industry and Commerce Income Tax (IRIC)
12. Agricultural Income Tax (IRA)
13. Tax on the Transfer and Swap of Athletes
14. Public Auctions Tax
15. Draw and Competitions Tax

Implement taxes (the description and characteristics of the main taxes will be developed in section III.4).

1. Corporation Income Tax (IRAE)
2. Individual Income Tax (IRPF)
3. Non-Resident Income Tax (IRNR)

Modified taxes, change description and stated objectives.

4. Wealth Tax (IP) - in the case of individuals, given the inclusion of income tax, the tax was kept as an instrument of control of taxpayers equity changes. In this regard, it maintained its structure but with reduced rates, aiming to a nominal rate of 0.1 percent over 16 years.
5. VAT - basic rate reduced from 23 percent to 22 percent, in order to lower it to 20 percent plans are already under discussion for 2011, and 14 percent to 10 percent for the minimum rate. The aim was to reduce the relative share of indirect taxation in the system and improve the fight against informality and evasion.
6. Excise Tax (IMESI) - was restructured from a fixed price tax base so that most of the tax base now consists of the sale price of the manufacturer or importer, supplemented if necessary.

III.2 Legal Framework

The Uruguayan Constitution establishes than only the Law can create, derogate or modify taxes, compelling all citizens to pay them. Henceforth the Legislative Branch passes national tax laws, which are later implemented by the Executive Branch. The tax administration does not have the legal authority to modify tax legislation.

The Constitution does not expressly prohibit the enactment of laws with retroactive effect. However, the majority doctrine and jurisprudence have understood that the prohibition derives from general principles contained in the Constitution. In practice, there is no enactment of retroactive laws.

Each of the nineteen Local Governments in the country can establish, collect and control only certain taxes through their respective Departmental Councils, by given right in the Constitution.

Case Law

The interpretation of tax laws is based on the regulations established by the Tax Code. They establish that tax regulations shall be interpreted according to the economic reality and not to the legal form. Case Law directs in the sense of how justice can judge in similar cases and on the tax administration's position but it is not binding.

Tax Infringements

Violations to regulations related to accounting and backup documentation of the operations made by the taxpayer, submission of affidavits of taxes and tax payments or withholdings, are enacted according to what the Tax Code establishes.

Binding Consultations

When there are doubts about the application of a regulation to a real situation, the taxpayer may obtain a written position from the tax Administration on the matter. In this case the Administration will be bound to maintain the criterion sustained regarding the consultant. The criterion's modification shall be notified to the taxpayer and it will only be effective for events subsequent to such notification.

Rights of the Administration

The Tax Code establishes that the Administration shall have the broadest powers of investigation and enforcement. Being among the most important:

- Require taxpayers and responsible people the display of books, documents and business correspondence, of themselves and others, and require his appearance before the administrative authority to provide information.
- Seize books and documents when the gravity of the case requires it, starting for a period of time of thirty workable days.
- Carry out inspections in real or personal property held or occupied in any capacity, by taxpayers and responsible people. Private homes may be inspected only with prior search warrant.
- Require information to third parties, even intimating their appearance before the administrative authority.

For its part, the tax authorities and officials affiliated with it are bound to secrecy of the information resulting from its administrative and judicial proceedings. Said information may only be provided to the tax authorities and Courts of Justice in criminal, juvenile or customs when those bodies consider them essential to the performance of their functions and request it by a reasoned decision. The violation of this rule carries responsibility and will be cause for destitution for the unfaithful servant.

Taxpayer Obligations

- Carry the books and special registries and document taxable transactions in the manner prescribed by the law and properly preserve them by the term of limitation for taxes.
- Register in the relevant records, to which will provide the necessary data and communicate modifications in time.
- To facilitate the work of authorized tax officials.

- Present or exhibit at the tax office or before the authorized tax officers the statements, reports, proof of legitimate origin of goods, and all documentation related to events of any tax liabilities and make additions or clarifications that were requested of them.
- Communicate any changes in their circumstances that may lead to alteration of their tax liability.
- Attend the tax office when his presence is required.

A strong criticism of the Uruguayan tax system is that even though it establishes the powers and duties of the Administration, it only establishes the duties of taxpayers leaving their rights defined by the General Law. In an attempt to overcome this problem, the DGI has established a taxpayer bill of rights, but although it compels the officials of said service, it has no legal force.

III.3 Organizations

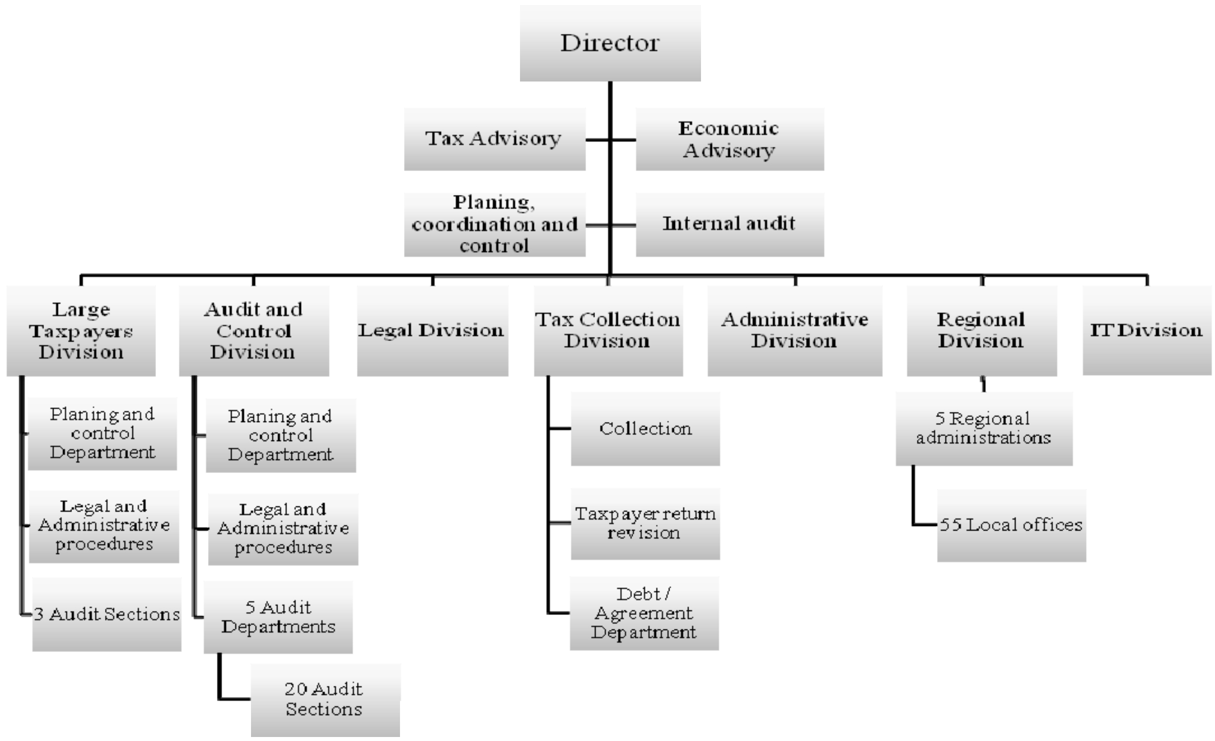
The Administrative structure regarding the national taxes include three separate offices, the General Tax Directorate (Dirección General Impositiva, DGI) and National Customs Directorate (Dirección Nacional de Aduanas, DNA) dependants from the Ministry of Economy and Finance, and the Social Security Bank (Banco de Previsión Social, BPS) as a decentralized service. BPS manages all matters relevant to corporate and individual contributions and taxes regarding the national pension system, unemployment benefits and national health system. DNA administers the borders, imports and exports taxes, and also collects the VAT and Excise tax associated with those operations, meanwhile the administration and management of this is responsibility of DGI which collects, controls and administers all other national taxes.

General Tax Directorate

The established mission for the DGI is to ensure the collection of state resources through the effective application of the rules on internal taxation within its competence, promoting the voluntary compliance of taxpayers in a framework of respect of their rights, acting with integrity, efficiency and professionalism.

While its primary purpose is to raise the necessary revenue for the public treasure it can no longer only focus their strategy in controlling the compliance of tax obligations. Increasing demands from the society require it to seek a balance between control and taxpayer service and also to emphasize voluntary or induce compliance as a strategic performance goal.

Figure 20: DGI Organizational Chart



From the organizational chart can be seen an administration by functions with 3 substantive Divisions, Collection, Audit and Large Taxpayers and 4 support Divisions.

DGI employs approximately 2,200 officials with a 40 percent of grade professionals in the payroll. The Audit and Control Division workforce are composed by 250 Tax Officials and 60 administrative personnel.

Social Security Bank

The mission of the Social Security Bank, as a social security institute, is to provide services to ensure coverage of social contingencies to the community as a whole and the collection of the resources in an efficient, effective and equitable manner, promoting policies and initiatives in welfare, applying the same guiding principles in the framework of the tasks assigned to it by the Constitution and laws.

The Bank defined strategic guidelines are:

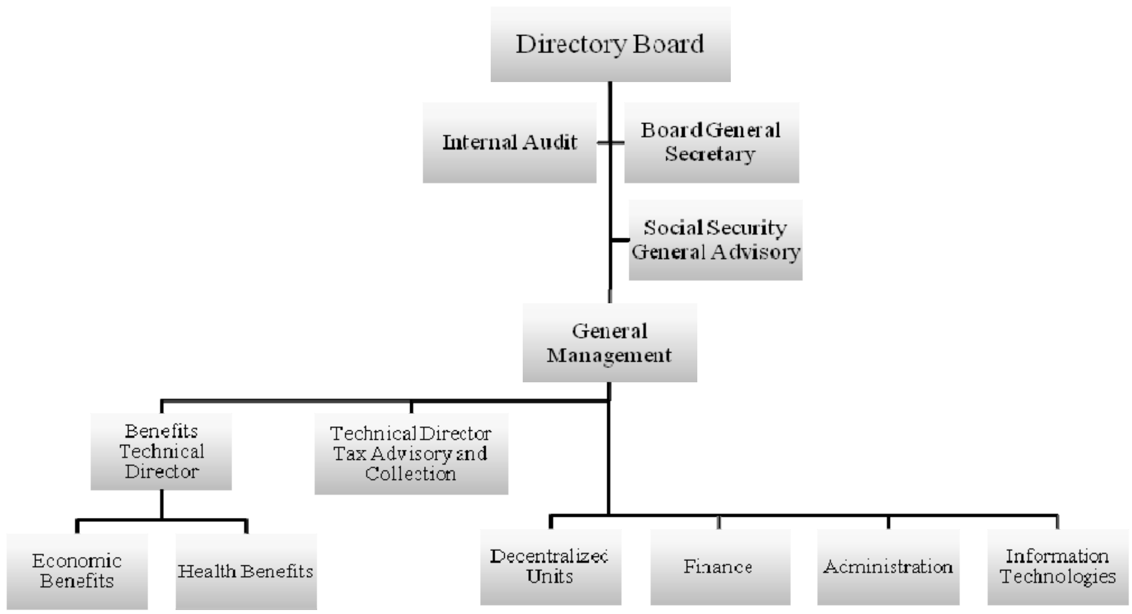
- Strengthening the institutional capacity to manage and promote social policies.
- Improve tax administration, benefits and funding, tending to develop and build confidence in social security.
- Strengthen the Agency's organizational infrastructure, its policy of Personal Information and information technology.
- Strengthen the relationship of BPS with public, private and social at a national and international level.

In its management role of the Social Security, the BPS has the responsibility of administering social security programs that were entrusted to it. In order to fulfill the goals accordingly it shall collect the social security special contributions under its effective and direct responsibility and control.

It is also its responsibility to collaborate with other agencies because of its infrastructure or more consolidated information.

Finally, it shall promote those changes that involve ensuring the principles of tax justice regarding the financing of social security when similar situations are identified in terms of contribution to be made by different economic sectors of the society.

Figure 21: BPS Organizational Chart



National Customs Directorate

The functions of the DNA according to the Customs Code are as follows:

- Check and control the various customs operations, issue compulsory classification criteria for the implementation of the tariff nomenclature for raising taxes, and dismiss, without prejudice to other powers, the respective data for the achievement of foreign trade statistics;
- To enforce the treaty obligations arising from international treaties signed by the country in customs matters.
- To exercise, with the means of surveillance, prevention and repression in their care, control of entry, exit, transit and storage of goods in its territory, in order to prevent and repress the commission of illegal customs.

III.4 National Taxes

This section will cover the Uruguayan tax regime regarding the most important taxes, explaining its taxable bases, rates, calculation and specific situations. Due to the extent and number of taxes and regulations, several minor taxes in revenue and impact on individuals or firms will not be included.

III.4.1 Corporate Income Tax (IRAE)

The IRAE is an annual tax that assesses incomes of Uruguayan source derived from business activities of any nature, at the rate of 25 percent.

Taxable Subjects

Trade companies and permanent establishments of foreign entities pay the IRAE for all their Uruguayan-source incomes. The remaining entities pay the IRAE for their business incomes, this is, those generated in the capital-work combination.

Territoriality

Incomes of Uruguayan source are those obtained from activities developed, assets located or rights exploited economically in Uruguay. Incomes derived from agricultural activities are also assessed by the

IRAE. The taxpayer may choose in certain cases, to pay this tax or the Tax on Disposals of Agricultural Goods - IMEBA (this tax assesses the sale of certain goods produced by such sector).

Permanent Establishment

When a natural or legal person, or any other non-resident entity develops all or part of its activity in Uruguay by means of a settled business establishment, it will be understood that it has a permanent establishment in our country.

The law enumerates a series of situations that configure a hypothesis of permanent establishment with illustrative nature, including also a negative listing

According to what is established in the applicable laws, the permanent establishments of foreign entities shall compute all the incomes obtained in the country in their IRAE settlement.

Foreign entities acting in the country by means of a permanent establishment shall assign a resident natural or legal person to represent them on the Tax Administration. That person will be responsible in solidarity for the tax obligations of the represented entity.

Income and Expenses Valuation

The assessed income is determined considering the incomes and expenses accrued during the accounting year.

Computable Incomes

The gross income is given by the total net sales minus the acquisition or production cost. The following, among others, are also considered gross income:

- The result of fixed assets' disposal.
- The benefit resulting from comparing the tax value and the sale price in the market of the goods awarded or given as payment to partners or shareholders.
- The exchange differences accrued in the accounting year.
- The result of the disposal of establishments or trade houses.
- All other equity increase produced in the accounting year, with exception of those resulting from re-valuations of fixed assets or social capital integrations, reimbursements or redemptions.

Inflation Adjustment

A fiscal inflation adjustment determined by applying the variation percentage of the Index of Prices to the Producer of National Products, between the months of the previous accounting year's closure and the one being settled on the fiscal patrimony, is performed in a partial intent to neutralize inflation's distorting effects.

Valuation of Fixed Assets

The fixed assets' value shall be revaluated as from the following accounting year to the one of their incorporation due to the variation operated during the accounting year on the index of prices to the producer of national products (the revaluation criterion from the accounting point of view may be different). For the purposes of calculating the result of fixed assets' sale, their value is revaluated until the closure of the accounting year in which the sale is carried out. The equity increase produced by the revaluation of fixed assets does not constitute an assessed income; likewise, the fixed assets existent at the accounting year's start is excluded from the base of the fiscal inflation adjustment.

Inventory Valuation

Merchandise inventories may be valued by their acquisition or production cost, or by the reinvestment value at the accounting year's closure, to the taxpayer's choice. Whichever the adopted valuation criterion, the cost of the sold goods is determined by the application of the history costs' convention; thus, when the inventories are valued at market values, the difference between market value and history costs is considered assessed income.

For the purposes of determining cattle sale costs, the initial inventories are valued at market values in force on the date of closure of the accounting year. Cattle is also excluded from the inflation adjustment base.

A sales method, different from the one used in accounting, may be chosen for fiscal purposes (FIFO, LIFO or average).

Previsions for inventories' obsolescence are admitted as long as they correspond to effective losses. Provisions for possible future losses are not admitted.

Securities' Valuation

Securities of any nature are valued at their quotation on the date of the accounting year's closure. If they are not quoted they are valued by their revaluated cost value by the variation operated from the month or accounting year of the asset's entry in the equity (taxpayer's choice) in the Index of Prices to the Producer of National Products.

In the case of shares of companies paying the IRAE, they may choose between the abovementioned valuation system or the value resulting from such companies' account statements adjusted according to the Wealth Tax regulations.

The shares in other taxable subjects of the tax will be valued by the value resulting from such companies' account statement adjusted according to the Wealth Tax regulations.

Capital Gains

Capital gains are considered taxable income, except for fixed assets' revaluations and those derived from the possession of shares or social quotas of other IRAE taxpayers.

Interests

Interests are computed based on the accrued. There are no regulations in relation to indebtedness/equity ratios; therefore, there is no thin capitalization concept according to which the indebtedness may be treated as equity and assessed as such.

Dividends

Dividends paid or accredited to IRAE taxpayers living in Uruguay are considered income not assessed by IRAE, in order to avoid double taxation.

Dividends paid to resident natural persons or non-resident natural or legal persons are assessed by IRPF and IRNR respectively if they correspond to profits assessed by IRAE.

Exchange Differences

The results of the accounting year from exchange differences are computable for the IRAE. They are determined by the revaluation of the asset and liability balances in foreign currency existent at the accounting year's closure.

Exempt Incomes

The following incomes are exempt from the IRAE, among others:

- Those corresponding to maritime or air navigation companies. In the case of foreign companies, the exemption will be valid as long as similar Uruguayan companies enjoy the same exemption in their countries of origin. The government may exonerate the land transport foreign companies on condition of reciprocity.
- Freights for goods' maritime transport abroad are not included in the exemption of the previous item.
- Those derived from the performance of agricultural activities comprised in the IMEBA, provided that they are obtained by someone who chose to pay this tax.
- Those comprised in the Income Tax for Natural Persons.
- Those comprised in the Income Tax for Non Residents.
- Dividends or profits and equity variations derived from the possession of capital shares.

- Incomes of cultural, educational and sports institutions.
- Incomes of official bodies of foreign countries on condition of reciprocity and of international organizations to which Uruguay is associated with.
- Incomes of small companies. Companies whose incomes do not exceed the amount established annually by the Executive Branch are exempt from the tax.

Deductible Expenses

The general principle to determine the net income consists of deducing from the gross income, the expenses necessary to obtain and maintain it, accrued in the accounting year and duly documented, without prejudice of certain limitations or exceptions that could apply.

Additionally, as a general rule, only those expenses constituting the following for the counterpart may be deductible:

- Incomes assessed by the IRAE;
- Incomes assessed by the IRPF or the IRNR;
- Incomes assessed by an effective taxation to incomes abroad (regulations have included a long list of exceptions to this general rule).

For the case of expenses caused by personal services provided in a dependence relationship that generate incomes assessed by the IRPF, the deduction is also conditioned to the payment of retirement contributions if applicable.

When the expenses constitute for the counterpart, incomes assessed by the IRPF in Category I of such tax (Capital Performance and Equity Increases) or incomes assessed by the IRNR, the deduction will be limited to the amount obtained by applying the quotient between the maximum rate applicable to incomes of such category in the corresponding tax (12%) and the IRAE rate (25%) to the expense.

For expenses constituting incomes assessed by a taxation of income abroad for the counterpart, the deduction will be 100 percent if the effective rate abroad is equal or greater than 25 percent. If the effective rate is lower, the corresponding proportion shall be performed, without prejudice to the limit previously mentioned. It will be assumed that the effective rate is equal to the nominal rate, unless the existence of special regimes determining the taxable base, exemptions and similar, which reduce the tax resulting from the application of such nominal rate is verified.

The IRAE regulation decree adds that when the counterpart is assessed by an effective taxation to incomes abroad and also by the IRPF in Category I (Capital Incomes) or by IRNR, the maximum rate of the local tax and the effective rate of the foreign tax will be added to the quotient’s numerator (the deduction may never exceed 100 percent of the expense).

For the purposes of deducing the expenses made abroad, their tax treatment in the counterpart country shall be justified by means of a certificate issued by the tax authorities of such country or by a company of external auditors.

Depreciations

Intangible assets such as trademarks and patents are depreciated linearly in a 5-year period provided that they represent a real investment and that the seller is identified. The registration expenses of limited life intangible assets may be deducted in the accounting year in which the expenses were made or paid off at fixed installments in the validity period, according to the taxpayer’s choice. The depreciation of goodwill is not admitted.

Fixed asset securities are depreciated linearly according to the number of years of their probable useful life. New automobiles are depreciated in a period of 10 years.

The lineal depreciation system shall be used. However, the DGI may authorize another depreciation system if it considers it technically suitable.

The results of fixed asset sales are determined by the difference between the sale price and the cost price of the asset depreciated and revalued up to the date of the accounting year’s closure.

Leasing Contracts

Tax regulations distinguish between the financial leasing and the operative leasing. The financial leasing is basically the one that grants a purchase option at a price lower than 75 percent of the involved good's fiscal value (revaluated and amortized history cost) on the date of the option's accounting year. In other cases it is an operative leasing. If the leasing is financial, the operation is treated as a sale in installments for fiscal purposes. In consequence, economically, the asset's ownership is transferred to the holder who will compute it in his fixed asset and will acknowledge an annual amortization on such good.

Other Deductions

Without prejudice to the rule in matters of expenses deduction, the regulations expressly admit as deducible the following expenses:

- Losses caused by a fortuitous or force-majeure case in the part that is not covered by compensation or insurance.
- Penalties for bad credits.
- The expenses made to train personnel in areas considered as priority and those made to finance research and development projects, which may be computed for once and a half their real amount.

Non-deductible Expenses

The following expenses are non-deductible:

- Losses derived from illicit operations.
- Penalties for fiscal infringements.
- Expenses corresponding to obtaining exempt incomes.
- Personal remunerations for which no retirement contributions are made.
- Income and wealth taxes.

Fiscal Losses

Losses generated in an accounting year may be deducted, adjusted by inflation, from profits generated in the following five accounting years, though such circumstance is conditioned exclusively to losses accrued in fiscal years started as from 1st. July 2007 (for those accrued previously the term is 3 years).

Losses generated in an accounting year may not be deducted from profits generated in previous accounting years.

Settlement

Net Income

For the purposes of determining the net income subject to tax, the following procedure shall be made:

1. The total net income is determined by deducing from the gross income, all the necessary expenses to obtain it and preserve it, as well as losses of previous accounting years.
2. After determining the total net income, the non-assessed part is deducted from it (non-assessed incomes and associated expenses) for the purposes of reaching, in principle, the taxable amount; in case of assuming the benefit of exemption for investments, such amount is deducted, thus reaching the fiscal result on which to apply the tax's rate.

Fiscal Credit

Except for payments on account and compensations with credits generated by other taxes, there are not other credits to compensate with the IRAE.

Since the IRAE only assesses Uruguayan source incomes, no fiscal credit is granted for taxes paid abroad.

For fiscal purposes, the consolidation between subsidiary companies is not admitted. In consequence, it is not possible to compensate one company's losses with the revenues of another.

Transfer Prices

Law 18083 introduces regulations on transfer prices between related companies to the Uruguayan tax system. The same consider the following aspects among others:

Operations made between related parties: Basically, they establish that when operations carried out between related companies are not adjusted to the market's practices between independent entities, which shall be proven reliably by the General Tax Directorate, such operations shall be adjusted according to certain methods established by the legal regulation.

Configuration of the relationship: The relationship will be configured when a subject taxable with IRAE performs operations with a non-resident or with entities operating in customs enclosures and enjoy a null or low tax regime (for example Uruguayan free-tax zones) and both parties are directly or indirectly subject to the direction or control of the same natural or legal persons; or these have the power to conduct or define the activities of the aforementioned taxable subjects, either for their share in the capital, the level of their credit rights, their functional influences or of any nature, contractual or not. The relationship concept considered by the regulation is extremely broad and includes the operations made by the taxable subjects with their foreign subsidiaries, branches, permanent establishments or other type of non-resident entities related to them.

Countries of low or null taxation: It is established that operations carried out with a company located in low or null taxation countries, specifically determined by the IRAE regulation, will be considered as not adjusted to normal market practices or values between independent parties.

Adjustment methods: In case it corresponded to perform adjustments to the accorded prices, the applicable methods are established. The same basically coincide with those recommended by the OECD in its current guidelines on the topic.

Incomes from International Activities

Incomes from activities performed partially in the country are determined, in principle, by the application of regulations that control de concept of Uruguayan source. However, the net incomes of certain international activities are specifically determined by law, these are: Transport companies, Cinematographic and TV industries, International news agencies, and Trading.

III.4.2 Individual Income Tax (IRPF)

The IRPF is a personal and direct tax that assesses the incomes of Uruguayan source obtained by natural persons living in Uruguay. An individual that verifies any of the conditions established under the IRPF law will be considered resident. An individual that stays in Uruguay more than 183 days in a calendar year, have the base of activities or economic interests in the country. Having spouse and under age children living in the country will be taken as presumption of residence.

Foreigners living in Uruguay under specific circumstances will be considered non-residents for the tax under reciprocity conditions.

Taxable Income

The tax is applied under a dual system, assessing two types of incomes: Category I or incomes derived from the capital production factor (securities and real estate) and Category II or incomes derived from the work production factor.

Category I includes capital gains and investment income, among others, interests earned on local loans or deposits and real estate rents that a person collects from real estate leases in Uruguay.

Category II includes work incomes in dependence relationship, as well as work incomes obtained by personal service providers out of the dependence relationship who do not pay the IRAE.

Category I

The taxable amount is calculated by adding each type of income and deduct bad debts that comply with IRAE regulation. The deductions allowed can only be applied to the same type of income they belong. In the case of leases the law establishes a list of the directly associated costs that can be deducted. In the same manner, documented capital losses directly related to investment income can be deduced.

There is no non-taxable minimum in this category and the due amount is calculated by applying to the resulting taxable amount the corresponding rate.

Table 21: Rates for Category I Income

Type of income	Rate
Interest corresponding to deposits in national currency and in indexed units, to more than one year in financial intermediation institutions	3%
Interest of bonds and other securities issued at terms of more than 3 years, by means of public subscription and stock exchange quotation	3%
Interest corresponding to deposits up to a year or less, constituted in national currency without a readjustment clause	3%
Dividends and profits paid or credited by IRAE taxpayers	7%
Remaining income	12%

There are some special Category I income that are exempted by law, such as, interests of Public Debt or capital gains related to them, income from pension saving founds and capital gains from donations by public entities.

Category II

In relation to incomes derived from the work productive factor, they are determined by applying the principle of the accrued. In case of incomes generated with exchange differences and price readjustments are computed in the moment of the collection. Work incomes in dependence relationship are constituted by regular or extraordinary revenues, in money or in kind, generated by taxpayers for concept of payment for their personal activity in dependence relationship. Compensation for dismissals provided that they exceed the corresponding legal minimum and for the quantity exceeding such minimum, are considered included in the aforementioned.

The tax corresponding to work incomes is determined by means of the application of progressive rates linked to an income scale. For such purposes, the addition of the computable incomes is entered in the scale. The rate corresponding to the scale's tranche to which the part of income is comprised in is applied.

Table 22: Income Tranches Scale and the Corresponding Rates

(US dollars values are approximate)

Annual computable income	Rate
Up to the non-taxable minimum of 84 Benefits and Contributions Bases (BPC for their Spanish acronyms) (USD 7,600)	Exempt
More than 84 BPC and up to 120 BPC (USD 7,600 – USD 10,800)	10%
More than 120 BPC and up to 180 BPC (USD 10,800 – USD16,300)	15%
More than 180 BPC and up to 600 BPC (USD 16,300 – USD 54,300)	20%
More than 600 BPC and up to 1,200 BPC (USD 54,300 – USD 108,500)	22%
More than 1,200 BPC (USD 108,500)	25%

Taxpayers may deduct the following concepts:

- Retirement contributions to different social security entities, accordingly.
- Contributions to the public health insurance system and the Labor Reorganization Fund.
- Benefits destined to the Solidarity Fund.
- For medical attention to under age children in the taxpayer's charge: 13 annual BPCs per children. This deduction will be duplicated in case of children, under ager or of age, legally declared disabled, as well as those suffering severe disabilities, according to what the regulation establishes. Identical deductions will be applied in case of persons under a guardianship regime.
- Active affiliates to the Banking Retirement and Pension Fund may deduct the payment.

Responsible Taxable Subjects - Withholding Agents

In use of the capacities granted by Law 18083, the Executive Branch assigned a series of subjects responsible for third parties' obligations in the IRPF regulatory Decree.

Except when there are expressed dispositions on the contrary, the responsible persons shall:

- Issue receipts to the taxpayers for the amounts withheld or collected on each occasion.
- Deposit those amounts in the terms and conditions established by the DGI.
- Submit an affidavit of the performed withholdings in the terms and conditions established by the DGI.

The agents assigned as responsible in matters of the IRPF include:

Withholdings on rents.

The Decree assigned as IRPF withholding agents, a series of subjects for the rents and other return on real estate capital paid to taxpayers of such tax. Among the subjects assigned as withholding agents are the IRAE taxpayers included in the Large Taxpayers Division and the CEDE Group of the DGI. The withholding will be carried out on occasion of the payment or credit, applying the following rates to the addition of the amount collected by or accredited to the rent's holder plus the corresponding withholding:

- 10.5 percent in the case of real estate rents.
- 12 percent in the remaining cases of real estate capital returns.

Responsibility for the payment of dependent work incomes.

Regarding incomes derived from work, the IRPF Regulatory Decree assigned as substitute responsible persons the employers of active affiliates to BPS and other social security institutes. For such purposes, an active affiliate is every dependent or independent worker performing activities under the shelter of such social security institutes.

The withholding will take place monthly, as a monthly IRPF advance, on account of its annual settlement. The amount of the advance will be determined by applying the monthly incomes scale for the determination of rates and deductions to the month's incomes. The value of the Benefits and Contributions Base taken into account for the mentioned determination will be the one established by the Executive Branch, considering the increase expected in the accounting year.

The computable incomes for the determination of the withholdings shall not be less than the assessed amounts for the determination of the Social Security Special Contributions. In principle, the withholding will be constituted by the difference between the amounts resulting from applying the following rates to incomes and deductions of the period:

Table 23: Dependant Worker Withholding Rates

Computable monthly income	Rate
Up to 7 BPC	0%
More than 7 BPC and up to 10 BPC	10%
More than 10 BPC and up to 15 BPC	15%
More than 15 BPC and up to 50 BPC	20%
More than 50 BPC and up to 100 BPC	22%
More than 100 BPC	25%

Table 24: Dependant Worker Withholding Rates

Computable monthly deduction	Rate
Up to 3 BPC	10%
More than 3 BPC and up to 8 BPC	15%
More than 8 BPC and up to 43 BPC	20%
More than 43 BPC and up to 93 BPC	22%
More than 93 BPC	25%

For the purposes of monthly withholdings, the deductions will be computed according to the following procedure:

- Non-proportional deductions (basically the deduction for medical attention to under age or disabled children): a twelfth of the annual amount.
- Proportional deductions (basically social security contributions): applying the percentage corresponding to the amount of the income being computed.

The information available at the moment of such determination will be considered for the application of deductions. For such purpose, the worker shall present the information corresponding to all his personal circumstances related to the deductions to the substitute responsible person through an affidavit. This information will be included in the affidavit that the substitute responsible person will carry out for the Social Security Bank. The mentioned affidavit will establish the corresponding deductions to be made by the employer or entity.

If the taxpayer chooses not to inform the responsible person of the circumstances generating the right for deductions, the responsible taxable subject will calculate the withholdings without considering any deductions (nevertheless, the taxpayers may consider such deductions in their annual tax affidavit).

Dependent workers shall submit the affidavit when the IRPF comes into effect and on occasion of starting the work relationship, as well as any further modification. Otherwise, the corresponding circumstances will be considered as from the following month to that on which they were informed.

Besides the monthly withholdings, the substitute responsible will determine an annual adjustment on December 31st. of each year. The balance will result from the difference between the tax determined according to general regulations and the withholdings made. If a balance payable resulted from such determination, the responsible person will make the corresponding withholding and deposit it on the collection body.

In case it resulted in a balance in favor of the taxpayer, the same will be refunded by the General Tax Directorate in the conditions this body determines. If the taxpayer obtained work incomes exclusively from one substitute responsible person in the accounting year, the withheld tax would have definite nature; therefore, the taxpayer would be released from submitting the corresponding affidavit. If the taxpayer obtained other work incomes assessed by IRPF, the withheld tax would be considered as an advance.

Responsibility for the payment of independent work incomes.

IRAE taxpayers included in the Large Taxpayers Division or the CEDE Unit of the General Tax Directorate are responsible for the IRPF correspondent to incomes generated in services out of the dependence relationship that an IRPF taxpayer provide.

The withholding will be made monthly and will only be applicable in case the monthly total amount invoiced by the taxpayer to the responsible person exceeds 10,000 Indexed Units (UI), excluding the VAT.

The amount of the withholding will be the one resulting from applying the 7 percent rate to the addition of the amount paid or accredited to the income holder plus the corresponding withholding.

The withheld amount will be considered as a payment on account by the taxpayer and will be deducted from the amount of the advances of the same period. If the taxpayer had a credit from the end of the accounting year’s settlement for such concept, the same could be destined to pay liabilities to the DGI or BPS.

IRAE Option

Any IRPF taxpayer have the option to be levied under IRAE regulations for all of their income, only capital income, or only work income, with the exception of income derived of a dependant relationship, dividends and utilities.

To opt for IRAE the taxpayer need to communicate the decision to DGI and it will be valid for the next fiscal year onward. In case of starting operations the option if informed within three months of the start will apply from the running year onward. Once exercised the option it cannot be changed for three years.

IRAE Perceptive

Taxpayers who's income for personal services outside a dependant relationship exceed 4 million UI (approximately 310,000 US dollars) in a year shall pay IRAE compulsory.

III.4.3 Individual Income Tax (IRPF)

IRNR assesses Uruguayan source incomes obtained by non-resident natural or legal persons without a permanent establishment in Uruguay.

Uruguayan source incomes of any nature obtained by these tax's taxpayers, including those of business nature, capital returns, work returns and equity increases are assessed.

The incomes from activities developed, assets located and rights economically used in the country are considered of Uruguayan source for IRNR purposes. Incomes obtained from technical services provided from abroad to IRAE taxable subjects are also considered of Uruguayan source.

The concept of resident established for the purposes of this tax in case of individuals is the same as in IRPF, while legal persons will be considered residents when they have settled according to national laws.

IRAE taxpayers paying or accrediting business incomes, capital incomes or earned incomes to IRNR taxpayers have been assigned as withholding agents of this tax. In case of inexistence of an assigned withholding agent, the IRNR taxpayer shall assign a representative in national territory to be represented on the Tax Administration in relation with his tax liabilities whom will be jointly liable for the referred liabilities.

Table 25: IRNR Rates

Type of income	Rate
Interest corresponding to deposits in national currency and in indexed units, to more than one year in financial intermediation institutions	3%
Interest of bonds and other securities issued at terms of more than 3 years, by means of public subscription and stock exchange quotation	3%
Interest corresponding to deposits up to a year or less, constituted in national currency without a readjustment clause	5%
Dividends and profits paid or credited by IRAE taxpayers	7%
Remaining income	12%

The law has also established exemptions, among which the following are the most relevant:

- Interests of Public Debt or capital gains related to them.
- Interests of loans granted to IRAE taxpayers whose assets influenced by the attainment of incomes not assessed by this tax exceed 90 percent of their assets valuated according to fiscal regulations.
- Incomes generated in the disposal of bearer shares of societies contributing to IRAE.
- Incomes corresponding to maritime or air navigation companies on reciprocity condition. Incomes corresponding to goods' maritime or air transport freights abroad are exempt in all cases.

III.4.4 Value Added Tax

Taxable Subjects

All IRAE taxable subject companies are VAT taxable subjects. VAT is also applied to natural persons and entities delivering personal services.

Assessed Operations

VAT is assessed on imports and sales of goods and services developed within the Uruguayan Customs territory. The tax is configured with the delivery of goods, services or definite introduction of goods to the country.

Exemptions

VAT exemptions are established in the law, among others, the most relevant are the following: raw vegetables' and fruits' disposals, foreign currency, precious metals, credit grants, real estate, agricultural machinery and its accessories, fuels derived from oil except for fuel oil, meat, milk, agricultural inputs, books, newspapers, magazines, educational material and water.

There is also an exemption for the delivery of certain services, including government's securities', bonds' and deposits' interests, real estate rents, banking operations except for interests on consumption loans, personal payments for services related to cultural activities, leases of agricultural machinery, agricultural insurances, and more.

VAT Calculation

The VAT is calculated on the net amounts invoiced for sales and services; the same shall be differentiated in the respective invoice. The VAT included in the acquisition of goods and services which directly or indirectly are part of the cost of goods or services sold or lent by the tax's taxable subject (as long as it is clearly specified in the purchase invoice) may be deducted from the VAT of sales invoiced for disposals of goods or delivery of services.

Invoices shall comply with certain minimal formalities established by the relevant regulations, as the consecutive pre-printed numeration, the identification of the vendor or service provider and the purchaser, the registry number of the vendor or service provider on the General Tax Directorate and the amount of the tax, differentiating the good's or service's value.

Rates

The basic rate is 22 percent, but there is a minimal rate of 10 percent applicable to certain goods as first need food products and medicines, and services provided by hotels regarding lodging.

There is no special rate applicable to luxury products, which, nevertheless, are subject to the Excise Tax.

Zero rate

Exports and sales of agricultural products made by IRAE taxable subjects are assessed by the VAT at zero rate. This implies that the VAT is not included in the invoice, but the VAT of purchases correspondent to goods and services which directly or indirectly integrate the cost of sold agricultural products or exported goods, may be retrieved.

Exempt Services and Goods

In the case of sales of exempt goods and services, the VAT included in the acquisition of goods and services that integrate the cost of the goods sold or services provided, may not be deducted, turning into a cost factor.

III.4.5 Wealth Tax (IP)

IP on Corporations

IP assesses the assets in the country - after deducting certain debts - of industrial and commercial companies and agricultural developments, at the accounting year's closure, with a rate of 1.5 percent. In the case of banks and financial houses the tax assesses the net equity, but with a rate of 2.8 percent.

Companies will lower the IP of the accounting year in the amount generated during the same accounting year by concept of IRAE or IMEBA. The maximum limit of the depreciation will reach 1 percent of the IP taxable base in the accounting year.

Within the industries' assets, the securities influenced by the industrial productive cycle are exempted.

Industrial and commercial companies and agricultural developments may only compute as liabilities the debts from local banks' loans, debts with local suppliers, unless they are Public Entities who do not pay this tax, debts from taxes, as long as they have not expired and bonds or debentures issued by public subscription and listed on the stock exchange.

There are several exempt assets, such as real estate destined to agricultural developments, excluding their improvements, government's securities and securities issued by the Mortgage Bank of Uruguay (BHU) and the Central Bank of Uruguay (BCU), the shares or social quotas of companies paying the IP and bonds listed on the Stock Exchange.

The tax's regulation adopts the territoriality criterion, for which assets located, placed or economically used in Uruguay are computed in order to settle the tax. Nevertheless, when there are assets abroad and exempt assets, only the computable amount of the debts exceeding the value of such assets is deducted from the assessed asset in order to determine the taxable amount.

Some companies' debts, which could constitute assets assessed by the tax for creditors and in consequence, have an impact on interests, constitute exempt assets. Among them are balances of imports' prices, loans and deposits whose holders live abroad and bonds issued by companies that are listed on the Stock Exchange.

IP for Natural Persons

The wealth tax for natural persons, families and undivided successions is applied on the assets in the country after deducting some debts. Only assets located, placed or economically used in Uruguay are assessed.

The tax is applied at progressive rates that vary from 0.7 percent to 2.5 percent with an individual non-taxable minimum of approximately 85,000 US dollars that is doubled for families.

Natural persons living abroad, as well as legal persons abroad are not subject to the payment of this tax regarding exports balances, loans and deposits made to Uruguayan residents. Natural persons are considered as residents for fiscal purposes applying the same criteria as IRPF.

Assets of natural persons, families and undivided successions are valued at market value, with certain exceptions, mainly in the case of real estate and vehicles whose values are periodically determined by the government.

The following assets are exempt:

3. Shares of entities subject to the payment of this tax and of financial entities exclusively dedicated to carrying out offshore operations.
4. Public Debt.
5. Bank deposits of natural persons.
1. Deducible liabilities include only debts with local banks up to the limit in which they exceed the addition of the exempt assets plus assets located abroad.

III.5 Local Taxes

Local governments tax primarily on urban or suburban real estate, vehicles and comptroller or public services fees. The most important tributes are the Real Estate Tax, Vehicle Tax and Bromatological Tax, but its impact on companies is generally not significant.

There is no unity of rates or base valuation among the different Municipalities which in turn generate certain problematic deviations in taxpayers conduct, like registering vehicles in the lowest rate Department.

The revenue from the local taxes is discretionary income of the Department that collected it.

III.6 Special Regimens and Benefits

As in many other countries Uruguay has a history of benefits and tax exemptions as government policies try to attract private investment to areas considered of interest for the country. There is also benefits for activities sector that show growth potential or competitive advantages in an international level.

The main benefits are established in the Investment Promotion Law and in the Consolidated Text 1996 in the automatic benefits. There are also some small or particular benefits for specific investments that due to the immateriality will not be disclosed here.

Investment Promotion Law

The investment promotion scheme is framed in Law 16906, which declares the promotion and protection of investments made by national and foreign investors in the national territory of national interest. This Law classifies tax stimulus in two groups: those of general disposition for investments and those regarding specific investments.

General disposition investment incentives

The beneficiaries of these tax incentives are all IRAE and IMEBA taxpayers who perform industrial or agricultural activities. The Investment Law establishes the conferral of the following automatic benefits:

- Exemption of IP to all personal property directly destined to the productive cycle and to the equipment for electronic data processing.
- Exemption of the VAT and IMESI correspondent to imports and the refund of the IVA included in purchases in the market of personal property destined to the productive cycle and equipment for electronic data processing.

Specific investments benefits

Companies from any sector may present an investment project for consideration. If the project is promoted by the Executive Branch, will have the possibility to obtain additional benefits.

- Exemption of IP in assets not included in the general incentives and in civil works for up to 8 years.
- Exemption of tariffs or taxes to imports of fixed asset
- VAT refund under exporters scheme, for the acquisition in the market of materials and services destined to civil works.
- Exemption of IRAE from 50 percent to a 100 percent of the amount effectively invested in the fixed or intangible assets comprised on the promotional declaration, depending on the qualification of the project according to the indicators established in the regulatory decree.

General and Automatic Incentives

Incentives to research and scientific and technological development.

The expenses directly incurred by the companies or the contributions made by them to public or private institutions to finance research and scientific and technological development projects, may be computed for one and a half its real amount for the IRAE. For such purposes, a request shall be submitted to the Application Commission.

Exemption of profits' reinvestment

The companies investing in certain assets may benefit with an exemption regarding the IRAE, of a percentage of the assets' cost.

Such percentage may be of up to 40 percent in the acquisition of industrial machines and facilities, agricultural machines, fixed improvements in the agricultural sector, utilitarian vehicles, personal property for hotels', motels' and hostels' equipment and re-equipment, capital goods destined to improving services' delivery for tourists in entertainment, recreation, information and transportation, necessary equipment for electronic data processing and for communications, phosphate fertilizers destined to the installation and refertilization of permanent grassland.

The percentage is 20 percent regarding the construction of hotels, motels and hostels and the construction of industrial buildings or their extension.

Incomes exempted for the application of this benefit shall not exceed 40 percent of the net income of the accounting year after deducting other exemptions for special schemes (should there be a surplus it may be dragged up to the two following accounting years) and they shall not be distributed, being compulsory to create a title hold whose final destination is capitalization.

Exemption to plant and industrial equipment investments

Personal property of the industrial equipment directly related to the productive cycle compute for 50 percent of their tax value for IP.

Moreover, capital goods directly used in the productive cycle and equipment used for data processing are exempt from such tax.

Real estate destined to agricultural exploitation, excluding improvements, are assets also exempt from IP.

Incentives to personnel training

Expenses destined to personnel training in areas considered priority may be deducted regarding the IRAE for one and a half its real value.

III.7 Tax Collection

Affidavits

The tax system operates based on affidavits made by the taxpayer, which may be audited by the treasury.

IRAE and IP taxpayers shall submit the affidavits of such taxes in forms supplied by the DGI within the fourth month following the accounting year's closure. The taxpayer shall pay the balance of the settled tax on such date, once the monthly advances made during the accounting year have been deducted.

In case the total tax payable is withheld to IRPF and IRNR taxpayers, they will be exempt from the obligation of submitting affidavits if they choose to give finality to the advances made.

The affidavits may be modified in case of factual error or error of law, notwithstanding the responsibilities for infringement incurred in. The amendments shall not be submitted on occasion of tax authorities' inspections.

Payments

Generally, taxes are settled and paid annually. IRAE, IRPF, IRNR and IP taxpayers shall make payments on account of the tax monthly, and pay the balance of the tax when submitting the annual affidavit. IP withholdings on credits maintained with people abroad up to 31st of December of each year shall be paid to the treasury during the month of May of the following year.

Natural persons taxed by the IP shall present an annual affidavit and payment at year's end, there are also three advancements equal to one fourth of the previous year IP.

For its part, all withheld taxes must be discharged into the public treasury the next month from its collection, and the corresponding affidavit submitted.

VAT Collection

The VAT is collected by the General Tax Directorate. The affidavits shall be submitted monthly, at the expiration of the month following the one in which the assessed event occurred. Should a credit in favor of the taxpayer arise from the affidavit, the same is transferred to the following month or accounting year, without an inflation adjustment until it is absorbed by the VAT of sales.

In the case of exporters and other similar taxpayers, the fiscal authority issues credit certificates for the amount of the VAT of sales, which may be used to cancel other tax or endorsed debts, in their case, in favor of the exporters' suppliers. These certificates may be requested monthly and are generally issued within two or three months from their request.

Tax Audits

The DGI may audit the affidavits submitted by the taxpayers, inquiring the taxpayer to explain some aspects arisen as a result of the performed audit. In case the DGI does not agree with the explanations, it shall formally notify the taxpayer of those observed aspects.

The taxpayer has a term of 10 days to respond formally in relation to the observations made by the DGI. After that period, the DGI makes an appraisal of the observed points that may be appealed by the taxpayer.

The tax authority may perform tax determinations when the affidavits are not submitted or when accounting entries are missing or insufficient.

Administrative actions aimed at the determination of the tax shall be addressed to obtain certain and direct knowledge of the facts mentioned under the law as generator of the obligation. If it was not possible to know in a certain and direct way these facts, the collection agency should infer the existence and amount of the obligation, by one or more of the assumptions based on facts and circumstances that would normally be dully recorder, linked or in connection with the event, and that will only cease to be applicable if proof to the contrary was present relative to the known knowledge and direct to the tax obligation.

It shall be understood that there is impossibility to know with reasonable certainty and in a direct way the facts described by the generator of the tax law as in cases of total or partial absence or non-display of the accounting records or documentation of operations according to the legal provisions or regulations, when the accounting departs from the principles and technical accounting standards and when it shows that the accountability and the documentation does not match the reality. It will be considered nonexistent.

Sanctions

The non total or partial extinction of taxes, withholdings and special social security contributions when appropriate, are penalized with a fine of between 5 percent and 20 percent of the tax's amount and with a monthly surcharge capitalized every four months. Withholdings made and not converted to the treasury is penalized with a fine of 100 percent.

The payment default is penalized with a fine between one and five times the value of the omitted tax and up to 15 times in case of defrauding. The crime of tax defrauding may also be criminally prosecuted.

Statute of Limitation

The right to collect taxes prescribes five years from the end of the accounting year in which the assessed event was produced. The term of the prescriptive period is extended to ten years if the taxpayer incurred in defrauding or did not comply with the obligations of registering and submitting the affidavits.

III.8 Appeal System

By law, all administrative acts including determinations can be disputed by the administered. To protect the judicial system and Courts from being overwhelmed the procedure requires that the first action is made in the administrative.

The taxpayer may resort to the DGI its decisions by a revocation action, simultaneously submitting proceedings to the Executive Branch in a hierarchical appeal. Both proceedings shall be submitted jointly within 10 days from the notification. If both are rejected, the taxpayer may act on the Court of Administrative Litigation in order to declare the administrative act null and void.

It is important to mention that in Uruguay there are not tax specialized courts.

III.9 Tax Revenue

The 3.9 percent increase registered by the General Tax Directorate (DGI) revenues, while important, still represented a significant slowdown in annual real growth of DGI collection compared to previous years, this was due to slowing in the pace of economic growth, although it is important to note that real revenue continued to grow more than GDP.

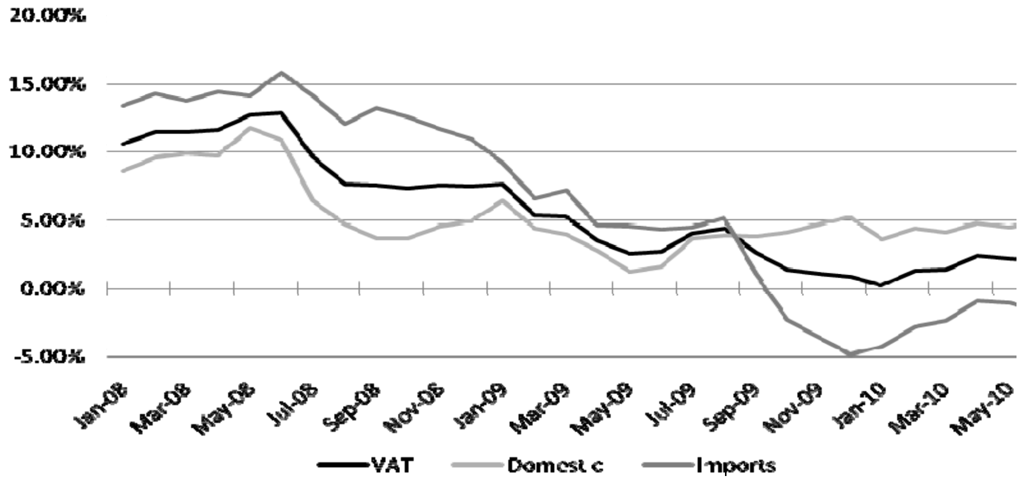
On the other hand, the unfavorable international situation of 2009 resulted in a fall in imports, which affected the collection of external tax revenues, whereas having less impact on CG revenue, showed a real decline of 7.3 percent in the year.

The evolution of domestic tax revenue is largely determined by the behavior of value added tax (VAT), both in its internal and external components. VAT revenue increased in 2009 a 0.9 percent in real terms over the previous year, exhibiting a very significant drop in relation to rates achieved in previous years and showing a declining trend, in particular from the 7.5 percent increase of 2008. This behavior is explained on the one hand, by the slowdown of real growth in domestic VAT, which in any case grew 5.2

percent, and on the other side by a very significant decrease of VAT on imports of 4.9 percent, following the sharp drop in foreign purchases.

Figure 22: VAT Revenue

(rolling year percentage change)



Source: Ministry of Finance

While with less impact on the total revenue, another hit was the slowdown in Corporate Income Tax (IRAE, Impuesto a las Rentas de las Actividades Económicas) and Individual Income Tax (IRPF, Impuesto a la renta de las personas físicas), which grew 5 percent and 5.5 percent respectively. The IRAE increase was driven by the private sector, as public enterprises contributions decreased significantly, according to 2008 poor performance. This increase could have been larger if not for the revenue loss attributable to rate changes from 30 percent to 25 percent that applied for balance closed from 2008 onward, remarking the more than 80 percent of firms close fiscal year in December, thus affecting IRAE payable in 2009.

On other taxes, excise taxes revenue (IMESI, Impuesto Específico Interno) rose 8.2 percent in the year, mainly due to fuel taxes, partially reversing the sharp decline experienced during 2008.

Table 26: DGI Revenue

(in million US dollars and percentage of GDP)

							Rolling year at February			
					real change %				% change	
	2006	2007	2008	2009	2008	2009	2009	2010	US$	real
Indirect taxes										
VAT	1,936	2,410	3,117	3,142	7.5	0.9	3,107	3,282	5.7	1.4
Domestic	1,133	1,396	1,770	1,854	5.0	5.2	1,788	1,953	9.2	4.6
Imports	803	1,015	1,347	1,287	11.0	-4.9	1,319	1,329	0.8	-2.8
COFIS	136	77								
Domestic	45	30								
Imports	90	47								
Excise tax	467	511	530	574	-14.2	8.2	534	606	13.4	8.0
Fuel	223	245	214	243	-28.5	14.4	210	262	24.5	19.5
Tobacco	121	132	142	145	-11.4	2.7	141	152	7.4	2.4
Vehicles	42	56	76	74	11.5	-3.6	75	78	4.7	-0.7
Others	75	91	114	129	4.1	12.3	117	126	7.8	1.9
Imports	6	-13	-15	-17	-15.7	14.6	-9	-12	34.0	35.0
Direct taxes										
Individual income tax		176	601	628	200.5	5.5	611	683	11.9	7.2
Non-resident inc. tax		15	49	80	183.9	61.9	55	81	47.2	38.2
Health services tax	27	18								
CIT	551	492	772	803	29.1	5.0	764	823	7.7	4.5
Wealth tax	199	220	308	372	16.8	21.2	314	389	23.8	19.8
Foreign trade tax	25	22								
Agricultural inc. tax*	54	62	63	53	-16.6	-16.0	60	55	-8.0	-11.3
Capital transfers	41	60	58	46	-20.6	-20.8	55	50	-9.5	-13.3
Commissions tax	19	13								
Bank assets tax	55	34								
Others	108	138	143	154	-15.4	10.2	141	161	14.0	11.9
GROSS TOTAL	3,617	4,249	5,641	5,853	10.1	4.1	5,640	6,129	8.7	4.5
(-) Refunds	293	345	421	457	0.8	9.0	424	468	10.3	6.9
NET TOTAL	**3,324**	**3,904**	**5,220**	**5,395**	**11.0**	**3.7**	**5,216**	**5,661**	**8.5**	**4.3**
NET TOTAL (% GDP)	**16.7**	**16.2**	**16.7**	**17.0**			**16.7**	**16.9**		

*Agricultural Income Tax was repealed in 2007, from there on the numbers shown are the part of CIT that correspond to agricultural business.

Note1:Several taxes were repealed and others created in the Tax Reform of 2007

Note2: Particular taxes are explained in section III

Source: Ministry of Finance

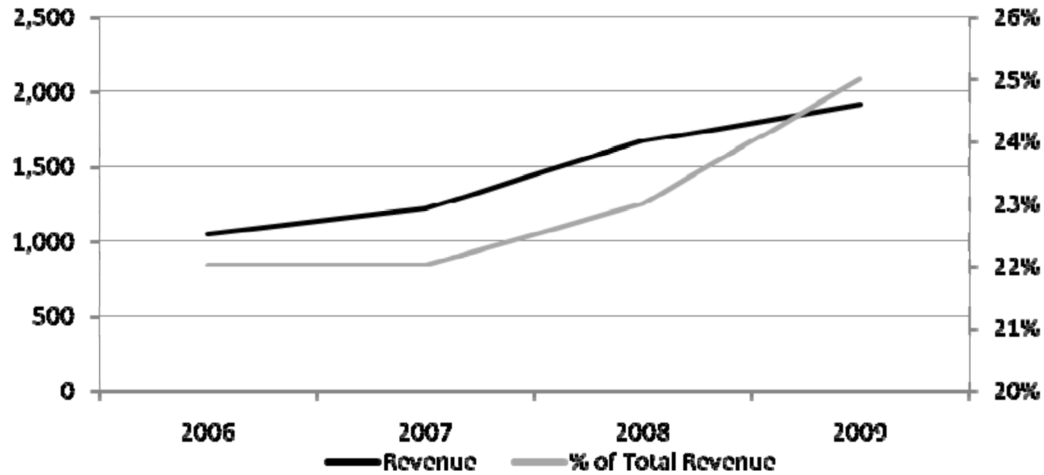
The growth of these taxes allowed the slowdown in domestic tax revenue to be less pronounced than the one of VAT, and then explained the revenue growth.

In real terms, BPS revenues increase 12 percent in 2009 year on year with 2008. Most of the increase is explained by the process of inclusion and formalization in the construction sector which contributions increase fourth fold between 2009 and 2003-2004 period. Declared wages in the sector rose while number of enterprises and workers almost doubled. In general numbers almost 5,000 new business with 17,000 buildings and 55,000 workers, reaching historic highs.

Another important source for the revenue growth is the increase on employment rates and decrease in total unemployment.

Figure 23: BPS Revenue

(in million US dollars and percentage of total tax revenue)



Source: Ministry of Finance

IV. Uruguay Specific Fiscal Issues

Maintaining the Tax Revenue under Decreasing VAT Rates

The Tax Reform Act that came into force on July 2007 introduced many changes that lowered the tax system revenue. VAT basic rate fell 1 percent from 23 to 22 and the minimum rate went from 14 to 10 percent, similarly, Corporate Income Tax rate was lowered from 30 percent to 25. Also, several other taxes were repealed but along with those changes there were many that offset the revenue impact, like the change in CIT regulation that widened considerably its base, and the incorporation of the IRPF.

The net effect after the reform was an increase in tax revenue but it is hard to disentangle all of its components, as the Peso appreciated, economy boomed, commodities prices fluctuated heavily and the DGI was subject to an important administrative reform that greatly improved its performance. All of this happened amid the turmoil generated by the changing external environment of the global financial crisis.

For the year 2011 the government intends to reduce the VAT basic rate an additional 2 percent. This means a fiscal resignation of some 300 million dollars per year that the proposal plans to offset by reducing VAT evasion.

In the 2000-2002 period, the worst moment of the banking crisis, VAT evasion ran rampant to levels as high as 42 percent, representing approximately 600 million US dollars of revenue loss for the Tax Administration. By 2009 VAT evasion was reduced to 16.1 percent according to DGI.

The challenge that the Tax Administration has to face is not minor, with an actual VAT evasion rate among the lowest in Latin America, to lower it further will be to reach levels of developing countries. Beside this, revenue increase already shows a slowdown, and several other variables that escape the DGI control will play a decisive role, the most important being economic growth since without it, voluntary compliance can falter and revert the evasion trend.

Electronic Billing

Among the most ambitious projects for 2011 is the implementation of the electronic billing pilot scheme that will affect a few selected companies. If this initial step is successful it will initiate the gradual transformation from the paper invoice system to the electronic one. This political decision marks a continuation on the strengthening of the tax administration, improving its effectiveness and efficiency.

The system’s basic idea is that whenever a transaction occurs, the seller will send a digital document via the internet to the buyer and also a copy to the tax administration. All taxpayers within the system will not have to issue paper invoices. This will change the way business transactions are recorded in Uruguay.

Taxpayers’ costs to comply with the laws and regulations regarding documentation will be greatly reduced by eliminating physical recordkeeping requirements, especially for large enterprises.

There are also clear advantages for the administration in having this volume of online information, such as determining activity levels and gross margins, and easily cross check VAT invoices. However, there are also difficulties; among the most critical are the training of officials on the new technology and procedures as well as IT developments and infrastructure investments.

To cope with those difficulties the DGI invested 15 million US dollars in technology and human resources training in the 2005-2010 period and it is aiming to keep the same level of investment for the period 2010-2015.

IRPF Voluntary Compliance

As previously stated, the Tax Administration underwent an important restructure to accommodate to the changes in the tax system. Regardless of the improvements in IT, material resources and training of personnel, the number of officials serving the DGI diminished, primarily in the most skilled echelons.

Adding to that, there was no specific plan to control and audit the IRPF previous to its implementation.

As a result, Uruguay is suffering of a common problem that is present in many countries with taxes on personal income, which is that the highest rates of non compliance and underreporting are related to capital gains, investment returns and professional services, due to the difficulty of indentifying and determining them.

In an effort to cope with this situation, several taxpayers in strategic positions were appointed as withholding agents by the DGI in an attempt to seize at source most of this type of income. This decision however, increased heavily the compliance cost for these taxpayers, attracting criticism from the private sector.

Several education and support programs have also been implemented to reach the taxpayers and appeal to the social responsibility.

Nonetheless, the problem still persists and with the DGI undertaking various sized projects for 2011 that will require use of their full-time human resources the IRPF audit will remain far below the needed levels.

A perceived low risk of underreporting threatens to deteriorate the tax base and reduce the incentives to voluntary comply alongside the tax revenue. Since this affects mainly the richest part of the population, being the ones that receive this type of income, the effect can undermine one of the main reasons of the IRPF implementation, which was the progressivity of the tax.

Bank Secrecy

Uruguay has upheld a very strict bank secrecy law since it was enacted in 1982. This regulation both with other particularities of the tax system put the country in the OECD blacklist of uncooperative tax heavens for a short time period. After some tax regulations changed the country was removed from that list but kept on a grey list that brings together those countries that have not sufficiently implemented international standards for cooperation.

This particular assessment from OECD is extremely biased, as there is no such thing as international standards, there is no UN convention or some other multilateral agreement signed by Uruguay, just an OECD convention, of which Uruguay is not a member. This convention is being enforced on non OECD members only by the power held by the member countries and primarily to their own benefit.

In 2010, Uruguay as a small country dependant in many aspect of the international environment, ceded to the international pressures of the OECD and made more flexible the Bank Secrecy Act. The new law allows Uruguay to sign the twelve international agreements on information exchange required by the OECD to be removed from said list, six of which had already being signed.

According to the text of the law, bank secrecy may be lifted by court order, to a request of the DGI, only when objective evidence is provided for suspecting the existence of tax evasion by the individual or legal person in question. The same information may be requested by the tax authority to specific requests by competent authorities of another country if an information exchange agreement has been signed. In this regard, Uruguay proceeded as Swiss, refusing automatic information exchanges and only acting in response to reasoned requests.

Asserting all this brings us to two important issues of this topic. The first one is the implementation and regulation of the agreements that will need to be undertaken by the DGI, the Courts of Law, the Central Bank and the financial sector. And second, the problems that could arise in the financial sector if this change in legislation conveys an important reduction of deposits in a short time period.

V. Conclusions: Where We Stand and Where We Go?

Uruguay has managed to transit the global financial crisis almost unscathed, as a small open economy with important ties to the region in matters of international commerce it was inevitable to suffer some effects from it, but these have been very moderate causing only a slowdown from the high growth rates of past years and a small decline in GDP in the first quarter of 2009.

The government used only moderate countercyclical fiscal policies during the crisis, maintaining in this way a sound fiscal outlook alongside economic growth. Fiscal policy of expansive spending allowed to minimized impact of the lower export and private investment demand.

The situation was even worsened due to the extended drought suffered during 2008 which raised government expenditure much more than anticipated due to the oil imports needed to generate electricity.

By 2010 second quarter the economy already shows signs of recovery and is doing better that estimated in 2009. The many particular reasons mentioned earlier on the review allowed Uruguay to benefit from the external situation, sustaining growth and increasing employment to record levels, lead primarily for the private sector, while the public sector contracted to reduce public deficit and debt levels.

Data of the second quarter of 2010 already shows a reduction on public debt, albeit the results are mostly tied to the effect of hydropower generation that not only eliminated the need for oil to generate electricity but allowed to export some part increasing public enterprises revenue.

Economic growth and investment effect on labor market have been remarkable good, lowering unemployment rate to almost match the structural rate. This had positive impact on alleviating the government spending, mostly on social security, poverty alleviation plans and unemployment insurance programs, that rose during the 2002 crisis and extended well into 2006.

Central Government debt, even if better positioned than in 2009 still remains in deficit and it will be very difficult to revert as most of the expenditure expansion done during the crisis was on permanent expenses, like poverty alleviating programs, wages and the like which cannot be cut in the short term. In this scenario the government has opted to reduce deficit by cutting investment outlays.

Even though debt is still high, the risk has lowered, as the debt denominated in national currency grew to around 37 percent from less than 13 percent in 2005, altogether with longer terms and lower participation of conditional credit.

The high resilience and good policy management showed during the financial crisis have resulted in the continuation of a positive process in terms of investment, especially FDI, which in recent years has contributed to substantial productivity improvements in the tradable sectors, including agriculture and agribusiness.

Even if Uruguay has not been able to attract high quality FDI, but resource and market seeking FDI, the effects on the market labor and the spillovers to the rest of the economy have offset the potential drawbacks.

The government is aware of the issue and by giving special benefits and tax reliefs for research and development is trying to revert this trend, but there is still a very incipient policy.

Another important measure taken to improve investment climate is the revamping of the Stock Market. The new laws on bankruptcy and stock market regulation aim to bring stability and transparency, channeling private savings into private investment. The success will depend on how this new laws are regulated and implemented.

A continuation of growing investment will allow Uruguay to benefit from the recovery of global demand for its exports. Nevertheless, there are still risk regarding the trade balance as Uruguay's external sector remains significantly dependent on developments in the region, particularly Brazil and Argentina.

In terms of inflation Uruguay still compares poorly with many other emerging markets. Even if inflation was kept single digit in the past years the government had to recur to costly measures when it threatened to break the 10 percent barrier. IMF suggested a stronger commitment to the inflation target range and even lowering it.

Achieving lower levels of inflation would allow to further promote the de-dollarization that the government policies are aiming at.

In light of recurrent droughts in recent years and seeing the effects derived by those, the government has created a countercyclical energy found as a mechanism to incorporate this risk into budgeting. The fund will ease the government expenses on energy in times of drought making room for other necessary public spending.

Additionally, the MERCOSUR summit of San Juan authorized to finance part of the electricity interconnection with Brazil using 800 million US dollars from the Fondo de Convergencia Estructural (Structural Convergence Fund) as a key measure to reduce Uruguay's energy vulnerability.

There still remains to resolve in this topic the recent proposal by the ruling party, which is to establish a public-private partnership to increase generation capacity trough a nuclear power plant project.

The establishment of more reliable energy sources will further increase potential growth, and it will allow the government to make future budgets without previsions for changes in energy costs due to externalities arising from climate changes or oil price fluctuation.

As a closing point it is important to mention the continuity in the process of modernizing the Administration, which already shows signs of positive results in the increased performance on revenue agencies like DGI and BPS. Uruguay is transforming its administrative bodies as well as its systems aiming to enhance the level and quality of employment, improve social conditions, and increase social equity. This process and the government disposition are reflected in the new tax system as well as the reform of the national health insurance, but perhaps the most emblematic, even if not directly related to tax matters, has been the Plan Ceibal, whereby one laptop with Internet connection has been provided to every child in public schools.

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