Uruguay

Negotiated M&A Guide 2022

Corporate and M&A Law Committee

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1 INTRODUCTION

This guide provides an overview of the law and practice dealing with private M&A transactions in Uruguay. This guide does not constitute legal advice. Anyone involved in private M&A transactions should seek specialist advice.

2 THE LEGAL FRAMEWORK IN URUGUAY

2.1 Company law

Uruguay has a company law enacted as of 4 September 1989 (Law No. 16.060, which has been in force since 1 January 1990). This law regulates the incorporation of mercantile companies, including personal companies or joint ventures (*sociedades colectivas*), limited liability partnerships and companies with share capital (*sociedades anónimas*).

All matters regarding the existence of said entities all are dealt with in this law, including:

- their incorporation;
- the status (rights and obligations) of their partners and shareholders;
- the running of said entities;
- the board and general shareholders meeting;
- the auditor;
- the disregard of the company as a legal entity;
- judicial intervention;
- the paid-in capital and reserves allowed; and
- the winding up events and the liquidation.

There are several decrees that clarify certain expressions or concepts of the law. Decree 335/990 in particular refers to the feasibility of having a company with only one shareholder or a board of only one member (which may also be an individual or a legal entity, resident or non-resident Uruguayan citizen or non-citizen).

Additionally, the recent Entrepreneurship Law (Law No. 19.820, enacted as of 27 September 2019) created a new type of company called denominated simplified share companies (*sociedad por acciones simplificada*). These entities have similarities with share companies, but certain incorporation requirements and formalities have been eliminated to achieve a faster and less costly incorporation process. Likewise, shareholders are allowed to regulate the rules that will govern the company through the bylaws, except for some mandatory provisions that must be complied with.

2.2 Agricultural company law

The law relating to agricultural companies was enacted in Law No. 17.777 on 21 May 2004 and has been in force since 12 June 2004. It provides for a legal structure applicable to companies that do not have a mercantile scope of activity, but an agricultural or cattle-raising objective. These companies are also legal entities and may have their capital divided in shares. The shares must be issued on a registered form.

2.3 Cooperatives

The legal framework for cooperatives is provided by Law No. 18.407, enacted as of 24 October 2008. This law provides a uniform regulation to all types of cooperatives: finance or cooperative banks, business cooperatives, working cooperatives, consumer cooperatives and even artistic or artisan cooperatives. These are also considered to be legal entities.

2.4 Bankruptcy law

Although this law does not deal with the legal structures of companies, it is important since it refers to all alternatives which companies (whether mercantile or not) have when they need to request for reorganisation or they are declared bankrupt. Enacted as Law No. 18.387 on 23 October 2008 and in force since November 2008, the law provides for:

- all matters dealing with insolvency (events of insolvency, and who is to declare such insolvency or who may be declared the same);
- agreements under performance before or during such insolvency procedure (it should be noted that agreements that are governed under Uruguayan law may not have the request to reorganisation or bankruptcy as a termination event);
- graduation and preference of creditors (note that secured credits have a privilege to collect by enforcing their credits and auctioning the mortgage or pledged assets);
- a receiver to deal with the insolvency or bankruptcy procedure; and
- the reorganisation proposal, among many other matters.

3 TRANSACTION STRUCTURES IN URUGUAY

3.1 Documents required for Uruguayan M&A transactions

Generally speaking, when a M&A transaction in Uruguay is considered, the following alternatives are explored:

a) to enter into a share purchase agreement concerning the shares of the target company;
b) to enter into a sale of assets agreement by which all or a substantial part of the assets and liabilities of the target company are transferred; and
c) a merger or spin off with the target company (which is not tax efficient in certain cases).[1]

Stock purchase agreements are the most commonly used structure, mainly for tax reasons. Indeed, the sale of shares is generally subject to 2.4 per cent tax of the price of the sale of shares (except if the seller is located in a tax haven, where the rate is 7.5 per cent), while the sale of an ongoing concern or a business unit is subject to income tax at the rate of 25 per cent and to VAT at the rate of 22 per cent.

Although less efficient from a tax perspective, there are benefits to a sale of a business unit. Indeed, if the purchaser follows certain formal steps described in the law, the scope of the purchaser's liabilities *vis-a-vis* third parties and the tax authorities can be restricted. This alternative may be preferred in situations where the target's contingencies are very significant and/or cannot be avoided, and the purchaser is not willing to rely on the seller's ability to indemnify it for any loss.

When the shares are in bearer form, the sale of shares only requires the delivery of the actual share certificate and the communication to the Central Bank of Uruguay of the new owner and

[1] Since February 2021, there has been the ability to ignore goodwill for tax purposes, if certain requisites are met (eg for two years following the merger, the ultimate beneficial owners shall maintain at least 95 per cent of its original participations and the core business shall remain the same, and the full chain of ownership be communicated before the Central Bank).

ultimate beneficial owner. If the shares are in registered form, the endorsement and registration within the corporate books is required, together with the communication to the Central Bank of Uruguay of the new owner and ultimate beneficial owner. The following formal steps need to be strictly complied with in connection with a sale of assets to protect the purchaser.

3.1.1 Promise of sale

A promise of sale must be executed by the buyer and seller. This may be done in a private or public document (that is, a document prepared by a notary public) and filed before the National Registry of Commerce. The buyer then takes possession of the business and continues it in its own name.

3.1.2 Publications

Once the promise of sale is executed, publications must be made for 20 days in two newspapers, calling all of the company's creditors to denounce their credits within 30 days as of the first publication.

The purpose of these publications, as stated by law, is to limit the liability of the purchaser regarding the target's debts. If the publications are made, the purchaser may be held liable only for the credits denounced and for the credits resulting from the books of the company. If publications are not made, the liability of the purchaser will be extended to all the present and future debts of target without any limit whatsoever.

3.1.3 Certificates

As part of the formal steps to be performed to complete the sale of an ongoing concern, the following certificates must be obtained:

a) A certificate issued by the tax authorities (Dirección General Impositiva) setting forth that no taxes are due. The Dirección General Impositiva has 150 days to issue said certificate. If it is not issued within the abovementioned term, the law establishes a procedure to deposit the estimated sum due with the tax authority in order to execute the definitive sale and purchase agreement.
b) A certificate issued by the Social Security Authority (Banco de Previsión Social) setting forth that no amounts are due (section 664 of Law No. 16.170). Obtaining this certificate generally takes about 34 weeks.
c) Certificates issued by the State Insurance Bank (Banco de Seguros del Estado) regarding the obligation to obtain insurance for labour-related accidents (Law No. 16.074). Obtaining this certificate generally takes about one week.

In case these certificates are not requested or obtained (except when the estimation procedure applies), the buyer will be liable for the entire amount of any past tax debt.

3.1.4 Definite purchase and sale agreement

After the end of the term when the creditors may come forward, and all necessary certificates are obtained, the definitive purchase and sale agreement must be executed before a notary public in a public deed (*escritura pública*). The agreement must be registered before the National Registry of Commerce within 30 days of its execution as per Law No. 11.924.

There are situations where certain significant assets of a target company are transferred but without performing the previously described formal steps required for the sale of a business unit. In those cases, there is a risk that the transfer may be deemed a 'partial sale of an ongoing concern', and thus hold the purchaser liable for the target's liabilities. Uruguayan courts have considered and applied 'whenever the transaction implies that the seller will not be able to continue running the business in the same way that used to be run before the sale' as a basic test to confirm whether the sale of a business unit took place.

4 PRE-AGREEMENT DOCUMENTATION

4.1 Letter of intent

Letters of intent or memorandum of understanding are customarily used in Uruguay to set out the major terms and conditions of the transaction. Uruguayan courts have ruled that, if such letters of intent reflect in their contents all the major terms of the transaction (for example, if it is purchase and sale of shares – the description of the shares to be sold, the price and payment, full indication of the parties, time of performance of such payment), then such letter of intent is to be regarded as a final and conclusive contract and hence binding as such. Otherwise, such letters of intent are regarded as pre-agreements where parties express their intention and willingness to enter into a future agreement on the grounds of the terms and conditions set out in such letters of intent, plus any other terms that they may agree while negotiating the final agreement.

In such a scenario, Uruguayan courts have ruled that, when any party fails to perform the final deal without a proper and sound reason (hence causing damages to the other party), the execution of such letters of intent may give legal grounds to a pre-agreement liability, and therefore force the non-complying party to indemnify the other party for the damages caused which are duly evidenced.

4.2 Lock-up or voting agreements with major shareholders

Lock-up or voting agreements (known in general as shareholders' agreements) are expressly regarded as valid, binding and enforceable among the parties who have entered into such agreements. Uruguayan Company Law (Law No. 16.060) in Section 331 expressly grants validity to these voting agreements or lock-up agreements. Moreover, Uruguayan law stresses that said shareholders' agreements may have any content (voting agreements, lock-up agreements, or any other restriction or agreement among shareholders) that is in accordance with Uruguayan law. Therefore, the content of such agreements is very broad in Uruguay.

Whenever a shareholders' agreement is in place, it is customary practice to amend the bylaws of the target company so that they mirror the relevant provisions of the shareholders' agreement.

5 KEY CLAUSES IN URUGUAYAN ACQUISITION AGREEMENTS

5.1 Holdback and escrows

These two issues are treated differently under Uruguayan law.

5.1.1 Holdback

Holdbacks may be subject to being declared null and void since Uruguayan law (ie, the Civil Code) prohibits a party from entering, for example, into a sale and purchase where the title to the property is held by the seller until full price has been paid by the buyer. An alternative is to deposit the asset in custody of a third party until full price has been paid. Such a deposit is valid.

To deal with the prior prohibition, within acquisition agreements it is customary to provide for security interests created by the buyer in favour of the seller (mortgage, pledge, trust by way of security, etc).

5.1.2 Escrow agreements

Escrow arrangements are valid and enforceable under Uruguayan law and customarily used, particularly when holdbacks bear such burden of being declared null and void.

5.2 Representation and warranties

Representations and warranties generally included in share purchase agreement do not substantially differ from representations and warranties that would normally be found in similar documents from other jurisdictions.

A typical qualification generally requested by purchasers is that the due diligence of the target company, and actual knowledge by the purchaser of contingencies, will not relieve the seller from the obligation to indemnify the purchaser and/or the target company for any losses resulting from the materialisation of said contingencies.

Since it is customary for conditions precedent to be satisfied after the agreement is executed, most of the deals do not close on the same date that the agreement is executed. Hence, it is customary practice that the seller's representations and warranties should be true and accurate on the date the agreement is executed, and on each day between said date and the closing date. The seller generally agrees to indemnify the purchaser should any of the representations and warranties turn out not true or not accurate. Representations and warranties generally do not cover any situation that takes place after the closing.

Finally, as opposed to other jurisdictions, representations and warranties are generally not qualified by materiality in Uruguayan M&A deals but this trend may be changing in the coming years.

5.3 Covenants

It is a typical buyer's concern to ensure that, from the date the agreement is signed or the financial statements are prepared (as the case may be) until closing, the target does not substantially alter its business structure or the conditions taken into account by the purchaser while entering in the agreement.

Hence, in acquisition agreements that close after signing, it is customary practice to introduce a lengthy clause restricting the seller's ability to make substantial changes to the targets business, activities or corporate structure, terminate or enter into material agreements, increase costs, grant new labour benefits or increase salaries, etc. Strict compliance with this covenant ensures that the target will remain as unchanged as possible during the interim period between signing and closing.

Covenants may be even stricter when the structure is designed as a locked box mechanism. Under this alternative (which is not widely used in Uruguay) the purchaser agrees to purchase the target as of a certain date, and all profits and losses suffered thereafter shall be the purchaser's risk. Under this structure, the agreement needs to protect the purchaser against leakages resulting from activities that are beyond the target's ordinary course of business and generally provides for co-management during the interim period.

Except for non-compete obligations generally assumed by the seller or the seller's controlling shareholder, post-closing covenants are not customarily used in Uruguayan M&A deals.

5.4 Conditions of closing of the buyer and seller

The extent and scope of the conditions to closing depend on a case-by-case basis. For companies in certain highly regulated sectors – like banks, insurance companies, securities brokerage firms and other players of the financial industry – it is mandatory to include provisions dealing with the necessary consent by the Central Bank of Uruguay to the proposed transfer. Hence, the approval by said supervising entity to the share transfer contemplated as part of the M&A deal becomes a requirement and turns out to be the parties' main source of concern and attention after the agreement has been signed.

Another situation that raises some concerns are deals concerning agrarian real estate. Uruguay is an interesting destination for investors in the agriculture business and the price of its agrarian land has multiplied several times in the recent years. Recent laws require that companies (except companies owned by individuals, national or foreigners) must obtain government approval to own and/or exploit agrarian land. This requirement has become a source of concerns and delays, and creative solutions have been contemplated to deal with this obstacle.

In those situations where no regulatory approval is required, conditions precedent generally refer to certain steps to be performed. Conditions whose fulfilment only depends on one party shall be deemed void under Uruguayan law, since they may enable that party to have exorbitant prerogatives towards the counterparty.

Material adverse change clauses included as conditions precedent are generally heavily resisted by sellers. If included, they become the purchaser's nightmare (mainly from an evidence perspective) if non-satisfaction becomes the only available and chosen exit for a purchaser.

Further, antitrust authorisations have become a greater cause for concern since the entry into force of Law No. 19.833 (dated April 2020) and the introduction of a real pre-merger control system in Uruguay (the prior regime only required a less burdensome 'for information' filing 10 days prior to closing). Currently, any 'act of economic concentration' (a term which is defined very broadly as any modification in the structure of control) requires the prior authorisation of the competent authority, provided that the parties exceed certain turnover levels (the joint turnover of the participants of the operation in the Uruguayan territory in any of the last three fiscal years must have exceeded UYU 600m, equivalent to approximately US$70m). When this threshold is met, obtaining the prior authorisation of the competent authority should be made a condition precedent to the closing of the transaction.

Notwithstanding the above, even when the threshold is met, there are certain exceptions in which prior authorisation is not required:

a) acquisition of companies in which the buyer already held at least 50 per cent of the shares of such company;
b) acquisition of bonds, debentures, debenture bonds, any other debt security of the company, or shares without voting rights;
c) acquisition of a single company by a single foreign company that does not previously own assets or shares of other companies in Uruguay ('first landing'); and

d) acquisition of companies declared in competition, provided that only one bidder has been presented in the bidding process.

In addition to conditions that are generally satisfied at closing, it is customary practice to include within the acquisition agreement a provision dealing with the steps that need to be completed on the closing date. These issues generally refer to the holding of shareholders' meetings (that must be called by the board of directors, except in cases where 100 per cent of the paid-in capital is present) to remove the directors appointed by the seller and to appoint new directors.

Finally, on closing it is also customary to solve or clear any corporate issue revealed as part of the due diligence process of the target company. Further, it is also the opportunity to resolve the revocation of all relevant powers of attorney granted to the seller's senior personnel and to communicate said revocation to the relevant suppliers, contractors, counterparties and financial institutions.

5.5 **Indemnification provision**s

Indemnification provisions do not substantially differ from similar clauses used in other jurisdictions.

It is customary for the seller to agree to indemnify and hold the purchaser and the target company harmless for losses resulting from the breach by the seller of representations, warranties and covenants. It is also customary practice, albeit depending on the terms and conditions negotiated by the parties, that the seller will indemnify the purchaser for losses suffered by the company originating from causes that are prior to the closing, even if the purchaser was aware of them or were disclosed by the seller. Further, it is also customary practice for the seller to indemnify the purchaser for hidden liabilities (not recorded in the financial statements) or non-existent assets.

A difficult issue normally refers to the maximum liability accepted by the seller, the threshold amount beyond which the seller assumes responsibility and the survival period. All these matters are generally negotiated by the parties.

A key issue for the purchaser is to be aware of is the statute of limitations, which in the case of contractual obligations extends to 10 years (although specific cases afford a much shorter period). Notwithstanding the foregoing, please note that the previous term was reduced from 20 to 10 years by a recently enacted law (Law No. 19.889) and that a transitory regime is foreseen for the current statute of limitations.

Statutes of limitations that came into force after 14 July 2020 are governed by the 10-year term. However, statutes of limitation in progress that, due to the effect of the term reductions established by such law, have been or will be consummated before the term of two years as from 14 July 2020, will be consummated only at the end of this period.

Additionally, tax liabilities may extend up to 10 years, and labour-related liabilities extend up to five years. Although this is determined on a case-by-case basis, the seller's indemnification obligation generally extends between two and five years, except for tax and labour liabilities.

Further, as in acquisition agreements of other jurisdictions, it is typical for the seller to request to have control of the defence in those situations where the seller may be required to indemnify the purchaser or the company.

5.6 Dispute resolution

On 17 March 2021, a new law came into force which partially amends Uruguay's conflict of law rules. As a general rule, international agreements – except for certain exceptions – may be governed by the law freely chosen by the parties under the relevant agreement, provided that, in order for an agreement to be considered an international agreement, the parties must be located in different countries or the agreement must have relevant objective connections with different countries.

Further, the parties are allowed to freely choose the competent jurisdiction. Any judgment against the Uruguayan borrower of a court located in such foreign country will still be capable of being enforced in the courts of Uruguay, provided certain conditions are met as detailed below for the arbitration awards.

Uruguay adheres to the New York Convention of 1958 regarding the enforcement of foreign arbitration awards. Uruguay has also adhered to the Inter-American Convention of 1979 on the same topic. Therefore, arbitration clauses are very often used, particularly in deals were one of the parties is a non-Uruguayan party. Arbitration clauses are strongly recommended when the share purchase agreement is governed by a foreign law, since arbitration improves the chances of a successful enforcement. Uruguayan courts will uphold the foreign award (through the Supreme Court) provided that it has complied with certain rules, such as evidence has been given that the defendant was served with the claim in a timely manner and had 'his day at court'.

Further, in order for the award to be enforced, it must

a) comply with all formalities required for the enforceability thereof under the laws of the country where it was issued;
b) be translated into Spanish and satisfy the authentication requirements of Uruguayan law;
c) have been issued by a competent court after valid service of process upon the parties to the action;
d) have been issued after an opportunity was given to the defendant to present its defence;
e) not be subject to appeal; and
f) not be against Uruguayan public policy *(orden público).*

It should be noted that Uruguayan courts scrutinise the fulfilment of such conditions, but do not revisit the merits of the judgment.