

Practice area	Country	Firm	Title	Summary	Contact person
Capital Markets/ Corporate Finance	Uruguay	Hughes & Hughes	The New Uruguayan Securities Act	Uruguay has approved a new Securities Act (N° 18.627; the "Act"), substantially improving the legal framework for capital markets and corporate finance activity in the country. The Act regulates the stock market, tender offers, brokers' activities, corporate governance issues, and the role of the Uruguayan Central Bank in this area.	Andrés Durán Hareau aduran@hughes.com.uy

### (i) Introduction

The new Uruguayan Securities Act, N° 18.627 ("Act"), was published in the Uruguayan Gazette on December 16, 2009 and expressly struck down the former Securities Act (16.749) of 1996 which, when was passed, had improved the Uruguayan securities market as a complement of the General Corporation Act (16.060), mainly in terms of issuance of bonds by openly-held corporations and book-entry securities. After more than a decade in force and having been incorporated to the Uruguayan System, among others, the Trust Act and the Act regarding Closely Investment Fund of Credits, which enhanced asset securitization, it became blatant that our system needed an updated securities Act.

The Act relaunched the Uruguayan Securities market, as a trigger to obtain economic development, something that was originally projected by lawmakers when passed the General Corporation Act of 1989, and in order to achieve corporate financing in a way different from the banking system getting access to private investors.

The New act, more complex than the 1996 act, regulates not only tender offers and the stock market but also it pays special attention to securities brokers which regulation was not comprehensive in the former act. Also, the Act reassures the Uruguayan Central Bank (UCB) as the government agency that has to assure transparency, competitiveness and a correct operation of the securities market, by offering complete and accurate information to the investors, reducing the systemic risk. The UCB will be also in charge of administrative intervention and liquidation of market exchange entities (*bolsas de valores*), similar entities and securities brokers as well, in a role similar to the one it undertook regarding Banks and other financial institutions.

In Section 2 of the Act a tender offer is defined as a communication targeted to either general public or specific groups of investors, in order to acquire, sell or exchange securities. Even though the Act excluded private issuances (as the former act did) it does include the invitation to buy securities made to clients of a specific institution in a generic way even when no publicity is conducted.

Likewise, the Act renewed the relevance of the Financial Services Agency of the UCB ("Agency") stressing the fact that a tender offer can be made only if the corresponding securities and the corporation offering them are registered with the Agency. The Agency is only in charge of controlling securities brokers.

A commission for securities market promotion ("Commission") was created by the Act in order to assist the Executive Power in promotion and development of securities market.

The idea of "security" that is used by the Act, as well as the former act, includes those assets (tangible and intangible) and rights easy transmissible such as stock, bonds, commercial papers, shares of investment funds, etc.

## **(ii) Book-entry and paper-based Securities**

The Act recognizes two types of securities, book-entry and paper-based, distinction that has existed in the Uruguayan Law since the General Corporate Act. However, in this case the Act extensively regulated book-entry securities; paper-based ones were only mentioned and regulated, by reference, in the same terms of book-entry securities.

A specific analysis of the types of securities is beyond the scope of this introductory report. Nevertheless, it is interesting to point out that by regulating, as the rule, book-entry books instead of paper-based, Uruguay is adopting new tendencies regarding securities. Likewise, the Act, following the principles enacted with the recent act 18.600, about digital signature, authorizes electronic document authentication of book-entry securities, either private or public.

In terms of evidence of standing, in connection with book-entry securities, it is possible to prove standing to exercise the rights derived from entry-book securities through certificates issued by the company that listed the offer and by the intervening securities broker.

The referred certificates do not grant other rights than standing and are not negotiable.

## **(iii) Bonds**

The new Act does not substantially modify the former legal regime of Bonds. It is still possible to issue bonds convertible into shares of the company, which can be issued by corporations in the terms of the bond, contract and law. The owner of a bond, which exercises the option of conversion, will become a shareholder of the corporation and the corresponding shares must be issued by the corporation.

If the corporation is intervening in a tender offer, it must sign a contract with a financial institution, securities broker or other authorized specialists, in order to regulate the offer and its compliance.

Provided the contract has not set a different majority, a special majority of bondholders (75%) can ask for a substitution of the institution that is representing them or modify the conditions of the issuance of bonds.

Banks and financial institutions can buy securities in a tender offer. The Agency will be in charge of controlling those investments.

#### **(iv) Securities Brokers**

According to the Act a securities broker is a natural person or a legal entity which professionally and habitually deals with securities exchanged in public and private tender offers.

The Act appoints natural persons as eligible for a broker position. However, when detailing the features a broker has to comply with to be registered with the Agency, one of them is to be a Company regulated by the General Corporate Act (16.060) - any of the types available. It seems that the Act kept the definition of the former act in order to regulate natural persons that were brokers before the Act. Likewise, as we will explain, natural-person brokers need to become a business association (company) within **one year** (during 2010).

The Act regulates two types of securities brokers, which are the same the former system foresaw, and needs to be registered with the UCB:

(a) Market Exchange Broker: They are the brokers that work as a member of a market exchange entity (*Bolsa de Valores*) or similar institutions where securities are bought and sold.

(b) Market Exchange Agents: They are the brokers that work outside the forums referred in a).

Securities brokers are regulated and controlled by the Agency which authorizes them to work in the Uruguayan market.

The Act set the group of requisites the broker has to comply with to be admitted by the Agency, being the most important that the broker has to be a business

association (one of the types of the General Corporate Act). Also, partners need to be natural people and shares of a corporation have to be nominatives (bearer shares are not allowed in this case). Shareholders of a corporation need to be natural people or the corporation have to be able to submit documents evidencing who is the person, ultimately, in control. As we have already pointed out, natural people who are securities brokers have one year to adjust themselves to the requirements of the new Act.

Companies must have a minimum capital and offer guaranties, in order to operate as a securities broker, in the terms the Agency will eventually set. Even though the Agency has not set the minimum capital yet, it should be notice that Uruguayan law returned to the idea of "minimum capital" which was stoke down after the Act 18.083 (Tax Act) regarding corporations and limited liability companies.

Companies acting as securities brokers (whose corporate purpose must be, **exclusively**, "securities broker") must have a minimum capital and offer guaranties in the terms set by the Agency.

Likewise, stock purchase of these companies must be approved by the Agency.

#### **(v) Other players in the Securities Market**

The Act did not follow the former securities act, because it extensively regulates other players of the securities market.

a) Entities dealing with Safe keep, Setting off and Liquidation of Securities: These entities, whose purpose is to safe keep, set off and liquidate securities, must obtain an authorization granted by the Agency to work in Uruguay. They will be controlled by the UCB that will also set the corresponding requisites to be admitted.

b) Market Exchange Entities and similar entities where securities are bought and sold: Different from the former act, the new Act not only regulates market exchange entities (*bolsas de valores*) but also "other institutions" where securities are bought and sold. Both market exchange entities and the other entities must be authorized by the UCB to operate in Uruguay. One important difference with the former system is that, now, Market Exchange Entities must be corporations with nominative shares and they cannot be civil associations like in the past. Existing entities are not affected by the new Act.

c) External Auditors: They purpose will be to audit, under international standards, corporations making tender offers. The Agency will be in charge of regulating and controlling them. External Auditors must be registered with the Agency to be eligible.

d) Credit Risk: The credit bureaus, to work for a corporation involved in a tender offer (it is not compulsory), has to be registered with the Agency.

e) Investment Advisors and other players of the securities market: The Act defines an "investment advisor" as a natural person or legal entity that professionally and habitually advises clients in connection with investments, securities that are about to be bought or sold in the context of a tender offer or sends clients' orders to a local or foreign securities broker. They are not, so far, under the Agency's control. However, the Act provides that, in the future, if the Agency deems necessary, they can be embraced by the Act. If the investment advisor also custodies securities on behalf of a third person the same requirements of a securities broker (market exchange agent) are applicable.

#### **(vi) Corporate Governance**

The Act provides that market exchange entities, as well as, other institutions where securities are bought and sold and corporations involved in tender offers must follow corporate governance principles in order to assure correct supervision, control of the direction and fair and egalitarian treatment to shareholders if applicable.

Among other obligations, it will be necessary to inform in an accurate and complete way about their financial statements and further relevant information. Also, they need to use international standards regarding accountability and audit.

#### **(vii) Professional-client Privilege**

Entities that list book-entry securities and securities brokers are bound by the professional-client privilege in the same terms banks and other financial institutions are according to the Act 15.322. This privilege cannot be opposed to the UCB that can ask for privilege information without justifications.

The privilege is also applicable to any person that works in the direction, operation or audit of an entity that lists securities or any securities broker, as well as any employee with information about the issuance of securities. The exception we referred to, regarding the UCB, is also applicable in case of employees.

#### **(viii) Insider Trading**

The players of the securities market must refrain from revealing privileged information before the referred information is spread. They cannot assist or make recommendations about securities' operations regarding which he has privileged information (or misused it) in its own benefit or the benefit of a third person. Those that act in contravention of the Act will be sanctioned by the UCB in the legal terms and can be criminally and civilly prosecuted.

The Act defines "privileged information" as the information, regarding securities, the market player obtained due to his position, even the information received from a client in the context of own pending orders, that, if spread, can materially affect securities market.

It is important to point out that the Act, when dealing with insider trading, does not include just securities brokers, but all market players e.g. investment advisors.

### **(ix) Tax regulation to enhance Securities Market**

The Act devotes an extensive chapter to regulate tax exonerations which aim to enhance securities market. For instance, the Act authorizes the Executive Power to totally or partially exonerate Capital Tax in case of openly-held corporations. This exoneration can be applicable up to 5 financial years.

In terms of Personal Income Tax or Non-Resident Income Tax, it is provided that income derived from certificates issued by financial trusts, through the market exchange system, with more than 3-year term, will pay a rate of 3% instead of 12% (general rate).

Abatement, for openly-held corporations, is set forth regarding Capital Tax in the same terms of the Corporate Income Tax and similar taxes, with a 50% tops for the corresponding financial year.

The Act is intending to foster the use of warrants, authorizing the Executive Power to apply the same tax system available for bonds. This authorization can be used if the issuance is made in within the securities market system.

*For further information on this topic please contact Andrés Durán Hareau at [aduran@hughes.com.uy](mailto:aduran@hughes.com.uy) .*