
16. The legal point of view

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Estudio Garrido Abogados

16.1. Introduction

Biofuel projects in Argentina can be export or domestic consumption oriented.

As concerns export projects, the government regulation basically requires the registration of the plant and encourages the production and exports of biodiesel by imposing higher taxes on the export of the commodities than on the export of the biodiesel. Two provinces: Santa Fe first and Buenos Aires later, have established tax benefits for plants locating in the respective province. As to other aspects of an investment, the biodiesel export projects are subject to general corporate and tax rules. We provide below an explanation of the tax benefits available in Santa Fe, the province which has already attracted several investments, in the Province of Buenos Aires, and a brief description of the taxes applicable to a project funded with debt, as has been the case on several of the exiting projects.

As concerns domestic oriented projects, the government regulation is intromissive, provides tax benefits and access to a "quota" to satisfy domestic demand and compliance with an incremental mix with fossil fuels to a restrictive list of beneficiaries.

16.2. Export Projects

a. Registration of the Plant

Every individual or entity interested in producing, mixing and commercializing biofuels, whether promoted or not, under the terms of the National Law No.26,093 shall be registered with the Secretariat of Energy of the Federal Government (the "Secretariat"), fulfilling all the requirements established by the Secretariat.

b. Reduced export tax

The export of seeds of soja is subject to a 27.5% withholding rate (its derivatives, as oils and flour, are subject to a 24% withholding rate). Otherwise, the exports of Biofuels are subject to a 5% withholding rate.

c. Tax Benefits in the Province of Buenos Aires

The matter is governed by Law No. 13,719 and its supplementary Decree No. 2189/2007, which regulate and promote the sustainable production, mixture, commercialization, distribution, consumption and use of Biofuels in the Province of Buenos Aires whether for domestic consumption or export:

c.1. Duration of Benefits

The tax benefits of this regime shall be applicable for:

- 15 years as from their effectiveness if the applicant: (i) produces biofuels for self-consumption; or (ii) is subject to the benefits of the National Law 26,093, described under Domestic Projects below.
- 10 years as from their effectiveness if the applicant produces Biofuels for selling in the domestic or international market.

c.2. Beneficiaries

The applicants must a) be settled in Argentina, and b) have a Plant in the Province of Buenos Aires, duly authorized by the Secretariat.

c.3. Tax Benefits

Within the 15 or 10 year tax stability period the company's global tax burden in the Province of Buenos Aires cannot be increased, for example, by (i) the creation of new taxes, (ii) the increase in tax rates, (iii) the repeal of exemptions or deductions, or (iv) broadening of the tax base.

Beneficiaries will be exempt from Turnover Tax (the average rate is 3%), Stamp Tax (the average rate is 1%) and Tax on Real Estate (the average rate ranges from 0.517% to 1.965%).

d. Tax benefits in the Province of Santa Fe

Through Law No. 12,692 and Decree No.158/2007, the Province of Santa Fe has established a Promotional Regime for the research, development, generation, production and use of products related to non conventional renewable energies (energies that are produced naturally, inexhaustible and without causing any damage to the environmental; Biogas and Biofuel).

d.1. Eligibility Requirements

Beneficiaries must comply with the following conditions:

- Settle or be settled in the territory of the province of Santa Fe. Companies already settled in Santa Fe at the time in which the law was enacted may be granted with the promotional benefits if (i) they increase their production capacity significantly, as the result of investments in fixed assets of the industrial plant, or (ii) they increase their staff significantly.

The promotional benefits will be granted proportionally (a) to the increased production capacity or (b) to the increase of their occupied labor force.

- Be approved by the Secretariat.
- Integrate in the same process all or some of the industrial stages for the obtaining of renewable raw material.
- Produce air generators, solar panels, solar collectors, solar ovens, biodigestors, biogas, biofuels, petrochemical derivatives, energy converters or any other non-previously described products that are originated in a process derived from non conventional renewable energies.
- Obtain approval of the investment project by the Ministry of Production of the Province.
- Comply with all other requisites established by the Ministry.

In order to be eligible for the granting of promotional benefits, all the projects must prove feasibility, profitability and reasonable production costs. The companies must present a production plan which must be complied in at least 80%. Also, an Environmental Study Impact must be filed.

d.2 Beneficiaries obligations

Beneficiaries must:

- Present periodic reports and respond information requests
- Register in the National Industrial Registry.
- Comply with the plan of production and sales fixed in the promoted project.
- Maintain the assets of the project.
- Comply with the schedule of works and stages of the project.
- Maintain the installed capacity and the staff.
- Comply with environmental regulations.

d.3. Tax Benefits

Those who comply with the requirements set forth above will be granted with the promotional benefits of exemption and/or reduction and/or deference of the following provincial taxes:

- Turn over tax: on the promoted activity (as opposed to other activities of the applicant). The exemption is not available for the commercialization of resale products.
- Stamp tax: on the incorporation, capital increase, modification of the by-laws, transformation, merger and, generally, all the acts, agreements and transactions related with the promoted activity. A provisional certificate can be requested so as to not pay the stamp tax until the definite tax exemption is granted. The tax exemption will also apply to third parties granting guarantees in favor of the applicant.
- Tax on real estate: on the real estate owned by company used for the exploitation of the exempted industry, including those destined to management, deposit and/or staff residence.

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- Tax on vehicles: on the annual tax set forth in Article 259 of the Fiscal Code for cars or trailers owned by the company, registered in the province of Santa Fe and affected to the promoted activity.

e. Financing a biodiesel project with debt

e.1. Exchange Control Regulations

According to Argentine exchange controls regulations, Argentine borrowers are required to bring the principal of the loans granted by non-Argentine lenders, and convert it into Argentine pesos, within 365 days from the date funds are disbursed. Additionally, under Decree No. 616/2005 (the "Decree"), the repayment of the principal of cross-border indebtedness of Argentine residents, and any refinancing of existing debt, should be agreed for a term of at least 365 days.

The Decree also sets forth that Argentine borrowers are required to set up a mandatory reserve in US Dollars equal to 30% of the principal amount of the cross-border loan in a local financial institution for a 365-day period. The mandatory reserve is non-transferable, does not accrue interest, and cannot be used as collateral of any credit transaction.

Failure to comply with foreign exchange regulations is punished under the Exchange Criminal Law with both monetary sanctions and/or imprisonment, including fines arising up to 10 times the amount of the transaction. Prison may also be applicable after the first recidivism.

Based on these rules, the Individual should (i) bring the principal of the Loan to Argentina, and (ii) set up the one-year 30% mandatory reserve, unless:

- The loan has a duration of not less than two years, taking principal and interest payments into account, and
- The funds are used to invest in non-financial assets (e.g., fixed assets). Such use should be stated by the client in an affidavit detailing investment so as to enable the institution involved to determine univocally how those funds will be used.

This exception shall automatically expire when uses differ from those stated. In that case, the mandatory reserve shall be made within the following 10 business days of such expiration.

e.2. Tax Implications

Interest on the Loan would be subject to a 15.05% withholding tax (17.72% if grossed up) when it is paid to foreign financial institutions (i) supervised by a Central Bank or equivalent agency, and (ii) residing in countries not deemed tax havens or with exchange of information mechanisms with Argentina with no resort to bank secrecy or other types of privacy laws.

Otherwise, the applicable withholding tax rate would be 35% (53.85% if grossed up). These withholding tax rates could be reduced up to 12% if an income tax treaty were to apply. (The 12% withholding tax applies to interest payments made to beneficial owners of such income that reside in Belgium, Denmark, the Netherlands, Spain, Switzerland, the United Kingdom, among others; interest paid to a German bank is subject to a 10% withholding tax.)

Interest payments will be subject to VAT if the Argentine borrower is a VAT taxpayer. The applicable rate will be: (i) 10.5% if interest is paid to a bank located in a non-tax heaven jurisdiction; or (ii) 21% in all other cases.

The Argentine borrower will be able to use the VAT paid on the interest as a credit against his VAT liabilities.

e.3. Guarantees

The Argentine Law sets forth several kinds of guarantees in order to assure the repayment of the Loan, such as pledges, floating pledges, and mortgages and trusts (the "Guarantees").

Pledges are the security interest usually required. The Argentine Commercial Code establishes the procedure to be followed in order to pledge shares and quotas of a company. The only difference is that the Pledge of Quotas must be registered before the Office of Corporations -Registry of Commerce- and the Pledge of Shares must only be registered on the Stock Ledger Book of the Company.

Additional security interest could be a mortgage on debtor's or third party's real estate property, but since its perfection is quite expensive (about 4% of the amount of the loan) they are not usually required.

It should be pointed out that Guarantees may be subject to Registration fees and Stamp Tax. This tax applies on any written

contract executed or effective in an Argentine province. Tax rates vary depending on the type of activity and the local tax act of each province. In general, the average rate is around 0.6% and 1.5%, respectively. If a contract involves more than one Argentine province, the tax will be normally due in proportion to the effects that such contract has within each jurisdiction.

16.3. Domestic Projects

The matter is governed by Law No. 26,093 and its regulations issued under Decree No. 109/2007, which regulate and promote the sustainable production, mixture, commercialization, distribution, consumption and use of Biodiesel, Bioethanol and Biogas. The regime shall be applicable for 15 years. The Regime is directed mainly to the public sector. The competent authority in charge of supervising and executing the Regime is the Secretariat of Energy, which, among others, has the following powers:

- Create and carry a public registry of plants authorized for the production and mixture of biofuels and of any individuals or entities that produce, mix, store or commercialize biofuels.
- To publish periodically reference prices for biofuels.
- To establish quality standards of biofuels and to control the quality of the product during the different stages of production, mixture and commercialization.
- To inspect without further notice the authorized industrial plants or the plants suspected to be producing biofuels.
- To establish percentages for mixture between biofuels and gasoline or diesel oil.
- To set quotas for distribution of the offer of biofuels.
- To set the supervising and controlling annual tax to be paid by the beneficiaries of the Regime.

a. Beneficiaries

The applicants shall fulfill the following requirements: a) be settled in Argentina; b) have any of the following as controlling stockholder: (i) the Federal Government, the City of Buenos Aires, any Province, local councils or individuals, State owned companies, corporations originally incorporated in Argentina and expressly authorized to carry out the business described in the Regime, being able to carry out all or any of the necessary industrial steps for obtaining biofuels, (ii) persons doing business in Argentina whose main activity is the agricultural production, (iii) in case of cooperatives, its partners shall be involved mainly in the production of agricultural raw materials (it is not required that the cooperative itself is mainly devoted to the agricultural production); c) be registered in a special section of the Oil Companies Register created by the Secretariat, demonstrating technical and economic-financial capacity, d) to prove capacity in production proceedings, which shall be assessed and controlled by the Secretariat pursuant to direct evaluations and technical assessments; e) commercialize its whole production for mixture with fossil fuels within the local market as from the moment in which such mixture is compulsory. The Secretariat may authorize specific volumes for other purposes in case of oversupply of domestic market but such volumes will not be entitled to the tax benefits.

b. Tax Benefits

The promoted entities or projects shall be granted with the following benefits:

(i) (a) obtain the anticipated VAT refund corresponding to the amortizable new assets -except cars- or infrastructure works -except civil works- included in the project or, alternatively, (b) apply the accelerated depreciation on those assets for income tax purposes.

1.1. Anticipated VAT refund: The VAT invoiced for the acquisition, construction, elaboration or final importation of capital assets or for the execution of infrastructure works shall be, within 3 years as from the date in which the respective investments have been made, credited against other taxes collectable by the AFIP (Federal Administration of Public Revenues), or either refunded to the taxpayer, in each case within the term agreed at the time of approval of the project and pursuant to the guaranties and conditions established by the AFIP. Such credit or refund shall be available only if (i) VAT invoiced has not already been recovered from VAT collections originated by the development of the project and, (ii) capital assets are still owned by the beneficiary.

1.2. Accelerated Depreciation of the Income Tax: Beneficiaries shall be able to choose between the normal or the accelerated methods:

(i) Depreciable tangible property acquired, constructed, elaborated or imported within such period: at least in 3, 4 or 5 annual, equal and consecutive installments, depending on if the investments have been made during the first, second or third year immediately after the date of approval of the project, respectively.

(ii) Infrastructure works initiated in such period: at least in the amount of annual, equal and consecutive installments arising from considering their useful life reduced to 50%, 60% or 70% of the estimated useful life, depending on whether the investments have been made during the first, second or third year immediately after the date of approval of the project, respectively.

(ii) Exclusion of the taxable base of the Assets Tax of the assets subject to the promoted activities after the date of its approval. This exclusion shall be admitted until the third financial term closed after the date of initiation of the respective project.

(iii) Biodiesel and bioethanol produced by the beneficiaries will not be subject to the Water Infrastructure Tax, to the Liquid Fuels and Natural Gas Tax, to the Tax on transfers or imports of diesel oil, or to those taxes that in the future may substitute or complete them.

The benefits listed in (i) and (ii) above can be claimed for 5 years as from the January 1st of the following year to that in which the term set for the fulfillment of the requirement of the project has elapsed.

c. Mixture of Biofuels with Fossil Fuels

As from January 1, 2010, fossil fuels commercialized in Argentina shall contain a mixture of at least 5% of biofuels over the total amount of the final product. Liquid fuels characterized as "diesel oil" shall be mixed with biodiesel, and the fuel characterized as "gasoline" with bioethanol.

d. Sale of Biofuels

The sale price of Biofuels shall be determined by the Secretariat. Such prices shall cover the reasonable operating costs applicable to the production, taxes, amortizations and a reasonable profitability (for it to be similar to business of comparable risks).

16.4. Doing Business in Argentina

As contemplated in the Argentine Business Law N° 19,550, several kinds of companies – ranging from the simple partnership to the corporation – may be incorporated for conducting businesses on a regular basis in Argentina, e.g. the incorporation of a Sociedad Anónima ("SA") or a Sociedad de Responsabilidad Limitada ("SRL"), or the establishment of a branch of a foreign corporation.

Sociedad Anónima

The SA is the most commonly used as the subsidiary of a foreign corporation in Argentina, because of its shareholders' limited liability. Any company in Argentina must have at least two shareholders (companies cannot be owned 100% by one owner). Both, a corporation (Argentine or foreign) or a physical person may be shareholders of a corporation, being entitled to own any amount of shares (for the second shareholder, ownership of one share would suffice).

a. Corporate Capital

The corporate capital is represented by shares, which must be denominated in pesos and have an equal, fixed par value. The amount of the corporate capital must be expressly stated in the By-laws. Under Argentine Law, the minimum required capital is \$ 12,000 (approximately US\$ 3,750). Upon execution of the By-Laws, the total amount of capital must be subscribed and each shareholder shall pay-in, at least, 25% of the capital stock. If the capital is not contributed in cash, it must be fully paid in. Shareholders responsibility is limited to the capital contributed; however, they must pay-in the shares that were subscribed by them. Notwithstanding that, under special conditions, ex. bankruptcy willfully caused at the subsidiary company level, Argentine courts have go beyond the corporate veil of the subsidiary, declaring also the bankruptcy of the parent company.

Shares may be either common or preferred and issued in registered or book-entry form. Common shares may carry from one to five votes, but for considering certain matters (i.e. liquidation, merger, spin-off, change of the corporate purpose, redemption of stock, etc.) multiple vote is not applicable. Preferred shares may be issued without voting rights; however, when they are in arrears or whenever multiple vote is not applicable, they are also entitled to vote. Common shares are entitled to preemptive rights for subscribing capital increases. The same right may be granted to the preferred stock under the By-laws.

Dividends, which result from earned and liquid profits of a SA as per its annual financial statements duly approved by the Board of Directors and the Shareholders' Meeting, may be declared by the Annual Shareholders' Meeting. Dividends so declared, may be freely distributed to shareholders (either Argentines or foreigners, either persons or corporations).

b. Directors

An SA is ruled by a Board of Directors formed by one or more directors. The majority of the directors must be domiciled in Argentina. Directors are appointed by the Annual Shareholders' Meeting. Directors may be elected for up to three fiscal years and may be reelected. Any or all of the directors may be removed by the Shareholders' Meeting.

Directors have broad powers, except for matters reserved to the Shareholders' Meeting. They are fully responsible for the management of the SA and are subject to the standard of loyalty and diligence of a good businessman. They are jointly and severally liable to the SA, to the shareholders and to third parties for damages caused by breach of their duties, including violations of the law and of the By-laws, or by fraud, abuse of their authority or gross negligence. The statutory duties and liabilities of directors cannot be contracted out by the By-laws or by the Shareholders' Meeting. Under certain circumstances, directors may also be held liable for taxes, social security charges and customs duties, environmental wrongdoings, and in case of bankruptcy, if they willfully and knowingly caused or worsened the insolvency. Save as qualified in the preceding sentence, directors are not personally liable for the obligations of the SA.

Directors must meet at least quarterly, either in Argentina or abroad (if permitted by the By-Laws). They must cast their votes personally, although they may be represented by proxy if the absolute majority of the Board is present at the meeting. It should be pointed out that all Directors (resident in Argentina or not) shall have to be registered as independent workers with the Tax Authority by obtaining a Tax Identification Number ("CUIT"). Said registration implies the inclusion of the Directors in the Argentine Social Security System.