

Investment Agreement between the Republic of Uruguay and UPM

in a nutshell

Introduction

UPM and the Republic of Uruguay (ROU) have signed an agreement which outlines the local prerequisites and infrastructure development for a possible pulp mill investment in central Uruguay. The site of the mill would be close to the city of Paso de los Toros, in the department of Durazno. The planned capacity of the mill would be about 2 million tonnes of eucalyptus market pulp. This agreement reflects the mutual understanding of stable and predictable environment for long-term industrial development.

The discussions between UPM and ROU covered a number of topics, including infrastructure development, fiscal and regulatory topics, rural and educational development initiatives, environment, forestry and land planning as well as labour and energy conditions.

The Investment Agreement details the roles, commitments and time-line of both parties. Further it outlines the roadmap for a possible investment decision, which will be based on UPM's own judgment. From now on, UPM and ROU will work together to implement the agreed actions.

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This document includes complementary background information related to each chapter of the Investment Agreement and a summary explaining the main content of the agreement.

1. Regional planning

Background

The focus of regional planning is to support local development for forestry operations, mill construction and mill operations while improving well-being in the Uruguayan inland.

Regional planning will cover the central and north-eastern parts of the country. Topics like community planning, housing, connectivity, education and health services will be implemented in a planned manner.

The pulp mill project will create new employment throughout the whole value chain from forests to export markets.

The central and north-eastern region is the relatively least developed area of the country when looking at the share of households below the poverty line, as well as capability to regional competitiveness. There are differences also in socioeconomic dimensions and operating conditions, like roads. All these are restricting development of economic activities by private sector, opportunities for employment and possibility for community development.

Summary

UPM and ROU agree to co-operate for improving regional development and living conditions.

ROU will provide for workers access to housing and public services (health, public education, day care) as well as transportation and internet connectivity.

UPM will support ROU in their efforts by providing precise information on the needs of human resources.

During the construction phase UPM's contractors will provide temporary accommodation for their employees. After the construction phase UPM will transfer some sixty permanent houses to ROU. These houses are targeted at the local people.

2. Development, research and innovation

Background

Promotion of human and business interests is essential for a sustainable forest-wood-cellulose chain and it adds value and benefits at national and regional level. Strengthening capabilities in the areas of technology, innovation and environmental protection will maximize the positive impact of the potential pulp mill in the country.

Summary

Both parties agree to establish a forest sector innovation fund. The fund will finance:

- Centers for Forest Wood Technology, Bio Economy and Business Development creating research and development projects
- Development program for national providers
- Professional training and labour counselling for construction phase and operation
- A scholarship program for masters and doctorates
- Río Negro Initiative

These initiatives will generate new skills, products and services, develop local economy and suppliers and contribute to the improvement of the water quality of Río Negro.

UPM will make an annual contribution of USD 1.5 million to the fund for a period of twenty three years after the start-up of the mill.

3. Forestry

Background

Predictable rules for forest regulations and long-term consistency are crucial for sustainable forest plantations.

Summary

ROU will be looking for stability of land use rules related to forest priority soils at departmental level by promoting consistency with no generic restrictions to forestry activities in plantation areas.

In addition, stability declarations from the relevant local governments would be welcomed in order to maintain their current regulations on land use.

ROU has agreed to validate at least three rotations at a time for the new and existing plantation projects under normal conditions.

4. Environment and water

Background

The parties share the interest in responsible and safe operations and are committed to mitigate the environmental impact.

A well planned process for environmental authorizations is beneficial for both parties, the regulator and the operator. This is especially important in case of large-scale projects. The Ministry of Housing, Territorial Planning, and Environment (MVOTMA) and the Uruguayan Environmental Directorate (DINAMA) will prepare and communicate the general guidelines which will be complied by the operator.

Río Negro is the main river in the interior of Uruguay. The plan will be to implement a wide stakeholder initiative to improve the water quality of Río Negro.

Summary

The emission levels to be required by ROU would be within the ranges of the Best Available Techniques (BAT) of the European Union, within the national legal framework, and in line with the Environmental Impact Assessment (EIA) technical results.

UPM will select the technology for the emission control and the mill processes using the BAT criteria in order to secure a minimum environmental impact. The final effluent of the pulp mill shall comply with the existing discharge standards. In addition, the parties recognize that additional daily, monthly and annual limits for phosphorous are needed considering the characteristics of Río Negro.

UPM commits to support ROU's plans for improving the water quality of Río Negro, which is the main river in the interior of Uruguay. UPM will provide financial support to advance a proper treatment of the community effluent of Paso de los Toros and Centenario. Further, UPM will participate in and contribute to a stakeholder initiative to improve the water quality through best practices within the catchment area of Río Negro. This is estimated to be a total investments of USD 10,5 million

ROU has agreed to a constant minimum flow in Río Negro, downstream of the Rincón del Bonete Reservoir in accordance with the results of the Environmental Impact Assessment for the pulp mill.

5. Labour

Background

Predictable labour relations, clear rules, transparency and good communication between different stakeholders are crucial for proper planning of any successful project. The location, scale and characteristics of this project reinforce the need of a professional plan based on local and international experiences, and developed under a fluent dialogue with the involved parties.

The Labour Framework Agreement signed in September, 2017, between ROU, UPM, unions and business chambers established a roadmap for needed actions. These are necessary for the construction and erection stages and are supporting the potential investment decision for a new pulp mill in the country. Agreed approach to labour protocols and proven mechanisms for conflict prevention and resolution create permanence to all parties.

The labour chapter of the Investment Agreement defines the responsibilities of the ROU and UPM regarding the implementation of the labour plans and actions, as well as the needed tools to address the capabilities for the construction and operational stages.

Uruguay's regulatory framework and the commitment of actors involved create a stable and predictable environment which is beneficial for long-term operations.

Summary

UPM and ROU agree to ensure the implementation of the actions and plans for the construction and erection phases, as well as for forestry and industrial operations.

Parties have agreed that during the construction and erection phases

- to establish working groups for services, training and safety procedures.
- to jointly develop with relevant stakeholders regulations to improve safety, wellbeing and productivity.
- UPM will contribute to the training plan with up to USD 1.5 million.

UPM agrees to maintain a minimum of 75:25 ratio between Uruguayan and foreign workers that enter the Free Trade Zone measured in a jointly agreed cumulative way in respect of the construction, erection and commissioning works.

During the operational phase, ROU will organise and finance the improvement of the technical schools. UPM will finance scholarship programs for local students and will provide to its employees and forestry contractors training courses.

ROU is committed to convene a joint negotiation group between PIT-CNT, UPM and the Ministry of Labour and Social Security, and to invite the Business Chambers to agree on the procedures and regulation for prevention and resolution of conflicts.

The rules resulting from the agreements reached in such negotiation will be incorporated to the Uruguayan Positive Law in the form of a law, decree or collective agreement.

6. Fiscal

Background

The Free Trade Zone (FTZ) is one of the concepts to attract investments and to strengthen the competitiveness of Uruguay.

Main objectives of this regime is to integrate the country into regional and international markets. Furthermore, to increase the skill-base of the national workforce, to generate domestic added value, to develop technology and innovation as well as decentralization of economic activities.

The main part of UPM's value chain from the forests through the mill to the export market is outside of this regime.

Summary

Once the permitting requirements are fulfilled, ROU will grant the mill a FTZ status as of starting from the construction of the new pulp mill and until thirty years after the completion of the construction of it.

The annual FTZ canon to be paid by UPM will be USD 2,100,000 in case the production is lower than 2,000,000 tons/year and USD 3,500,000 if the production is equal to or higher than 2,000,000 tons/year. An additional annual canon of USD 3,500,000 will be paid during the first twenty years after the pulp mill project completion date.

ROU agrees to extend the term of the FTZ authorizations for UPM Fray Bentos S.A so that it will have the same duration as the new UPM pulp mill FTZ authorizations. Such authorization will be granted after the start-up of the new pulp mill and will be subject to additional agreed investments. The annual FTZ canon to be paid by UPM Fray Bentos S.A. will be USD 2,100,000 during the extended term.

In accordance to the Investment Law, ROU undertakes to promote and grant the applicable benefits to those initiatives under the UPM project.

In relation to the mill project UPM and its JV-partners are considering a corporate restructuring of direct and indirect ownership of affiliate companies. ROU undertakes to support this simplification with one-time tax concession if the restructuring takes place prior to start-up of the new mill.

ROU also undertakes to negotiate an advanced price agreement with UPM Forestal Oriental in relation to the transfer of wood to the mills.

7. Energy

Background

Uruguay generates energy based on hydro, wind, biomass and solar power. The biomass energy mainly comes from forest industry. Predictable biomass energy will help the country in supporting its growth strategy with renewable energy. Uruguayan energy demand has been steadily growing.

The expansion and reinforcement of high-voltage lines will improve the energy capacity, improve the use of existing resources and enable new renewable energy projects that are needed to satisfy the demand growth.

Summary

ROU, the National Administration of Power Plants and Electrical Transmissions (UTE) and UPM have entered into a memorandum of understanding with the purpose of negotiating a 20 years' electricity sale and purchase agreement.

UTE would agree to buy all excess energy from UPM pulp mills up to 1TWh/year at a defined price of 72,5 USD/MWh. UPM would be entitled to sell any exceeding amount of electricity at domestic spot market or export markets in Brazil or Argentina.

UTE would reinforce the grid in the center and north of the country to guarantee the electric energy exchanges between the pulp mill and the transmission system and to be able to receive up to 150 MW from the new mill. UPM would contribute to UTE with five annual installments of USD 2 million each after possible investment decision.

UPM would build the connection between the new pulp mill and Bonete hydro plant switch yard.

8. Roads

Background

State agencies are responsible for public road network and maintenance. Quality of the roads and the density of the road network are important factors for rural livelihood and businesses. Their impact on safety, transportation costs, delivery times and competitiveness is fundamental.

The road network in central and north-eastern region, where plantations are located, is neither as good nor as dense as it is in the rest of the country. Such roads will be critical for transportation of wood to the new pulp mill.

Upgrading the infrastructure contributes also to overall development by providing better access to education, jobs and medical services in the rural communities.

Summary

ROU agrees to rehabilitate and maintain agreed network of roads in central area of the country. The road works will primarily consist of pavement works and improvement of bridges. The parties have agreed the scope, technical specifications and timing of the road works.

In addition, ROU has agreed to implement a pilot for high-capacity vehicles (tri-trains) and grant authorisation for the use of 48-ton trucks and tri-train trucks in selected routes.

9. Port

Background

A modern port is highly important to increase Uruguay's competitiveness. The port of Montevideo is currently the only port with railway connection. The capacity of the port is not fully used. To be an efficient outlet for pulp exports, the port needs further improvements.

Today the pulp vessels from Uruguay to export markets need to be top loaded in Brazilian ports because of shallowness of some navigation channels. Development of the port would be beneficial to all Uruguayan exports.

Summary

ROU recognises UPM's need for a connection from the possible pulp mill via rail to a deep sea port. ROU will promote concession for a pulp specialized terminal in the Montevideo port in order to secure reliable and competitive outlet to export markets.

UPM will submit to ROU a private initiative of the port project and ROU will provide a competitive process. The concession area shall be determined by the National Port Administration (ANP) within the Montevideo port and the concessionaire shall be responsible for the construction of the port project and the related infrastructure.

ROU will be responsible for dredging and maintenance works of the connection channel between Río de la Plata and the area of the port project.

10. Rail

Background

Uruguay has 150 years' history with railways. The central Uruguayan railway project brings new business opportunities to the Uruguay inland, such as cost efficient transportation of pulp, grain, wooden products and containers as well as the possibility to develop passenger traffic.

Rail is the safest and most environmentally friendly means of transportation for long-distance heavy logistics. High safety standards and intended improvements in the railway's safety culture are important and necessary elements of the railway project. The railway will be modern, efficient and based on European standards and best practices.

All users will benefit from this competitive alternative for logistics in their long term business development. Railway will reduce transport costs mainly in the departments of Durazno, Tacuarembó, Rivera and Florida.

Summary

Both parties recognize that the central railway project shall be organized and executed in a systematic and well-planned manner in order to ensure the timely execution and implementation of agreed quality specifications.

ROU will execute the engineering and design, procurement, financing, construction and long term maintenance of the rail in accordance with the agreed technical specifications and timeline. The project will be implemented through a construction and long-term maintenance tender. Awarding of the railway contract will be completed by October 2018 and the completion of the central Uruguayan railway project shall occur in February 2022.

ROU will continue its efforts to develop the regulation of the Uruguayan railway system to enhance sustainable long-term operating conditions for public and private operators.

The fees that UPM's railway operator will pay for the use of the railway have been agreed. The estimated amount of daily traffic for UPM operations is seven cargo trains.

ROU will design and execute a fly over at the port area of the Rambla to ensure a smooth entrance of the train cargo to the Montevideo port.

11. Juridical

Background

The agreement between ROU and UPM is based on the law of Promotion and Protection of Investments.

Summary

This agreement is intended to create a legal framework for the actions that have been agreed to be performed by the parties.

UPM and ROU have agreed in the Annex 2 on a gate structure for the coordination and follow-up of the agreed tasks.

Certain complementary topics listed in the Annex 3 need to be further negotiated and a complementary agreement needs to be entered into before final investment decision of UPM.

Either party can terminate the agreement at its discretion at any time prior to final investment decision. If a positive final investment decision is not made by UPM by 15 February 2020, the agreement will terminate. Termination will not cause liability on either party.