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SNAPSHOT INVESTMENT GUIDE TO IRAN

by Nasim Gheidi, Otabek Suleimanov & Assel Nassimoldina

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I. Overview

Iran is the eighteenth-largest global economy, with an estimated Gross Domestic Product (GDP) of $387.6 billion in 2015 and the second-largest population in the region with 78.8 million people. Nonetheless, Iran is considered to be an upper middle income country.

Iran holds the world's fourth-largest proven crude oil reserves and the world's second-largest natural gas reserves. Its proven oil reserves exceed 158 billion barrels and gas reserves stand at 33.5 trillion cubic metres.

According to the World Bank, Iran's economy is characterised by a large hydrocarbon sector, small-scale agricultural and services sectors, and a significant state presence in the manufacturing and financial services industries.

II. Legal system

Iran has quite a well-established legal system that has developed and evolved over the last hundred years or so. However, due to the fact that there has not been much foreign investment in Iran in recent decades, its legal system is not well designed for cross-border business transactions and is not yet ready for sophisticated instruments.

Iran's legal system is influenced by the models of the French and German legal systems. It currently consists of both civil and Sharia laws, and although the majority of transactions are governed by civil law, the principles of Sharia law may still be applicable in certain cases as it stems from several very important articles of the country's constitution.

Nevertheless, the application of Sharia principles is rather limited and serves to prevent the adoption of laws that contradict Islamic doctrines rather than being directly applied to commercial transactions.

As an indication of the gradual change in the country's foreign policy, Iran has adopted a major law on the attraction and protection of foreign investments, called the Foreign Investment Promotion and Protection Act of 10 March 2002 (FIPPA). FIPPA provides considerable privileges and incentives to those who want to invest within its framework.

The economy's strategic sectors include energy, oil & gas, the financial sector, and media and telecoms, all of which are very closely regulated by the government and require a long list of approvals and clearances.

III. Foreign investments

The activities of foreign investors are mainly regulated by FIPPA. Although FIPPA entails many of the internationally accepted standards on the protection of foreign investment, it is not well tested and there is no extensive court practice interpreting its application. Therefore, shrewd investors must make well-informed decisions before investing in Iran.

FIPPA is a framework legislation regulating foreign investors' entry into Iran and their subsequent activities within the country, whilst also providing for a number of privileges and protections for foreign investors. In order to benefit from such incentives a foreign investor must obtain an investment licence. However, a foreign investor may choose not to apply for the investment licence, and rather invest in Iran without it.

IV. Types of investment

A foreign investor may invest in Iran:

- by purchasing shares or securities; or
- within contractual arrangements, including Iran petroleum contracts (IPC is considered as a newly developed and special format of buy-back contracts), buy-back, or BOT (PPP) type contracts, or other forms of partnerships where profits are generated through the economic performance of the project.

Both options may provide privileges and incentives under FIPPA. However, foreign investors must demonstrate that such investments create added value (i.e., the enhancement of management, increase of exports or improvements in the technology level of the existing entity, etc.)

V. Investment license

The Organization for Investment, Economic and Technical Assistance of Iran is the investment licence issuance governmental body and the main state authority in charge of foreign investments in the country.

In order to apply for an investment licence a foreign investor must submit the application to the Organization, whose official website can be found at: http://www.investiniran.ir/en/home. The Organization specifies the list of documents required for the issuance of the investment licence. We note that this list of documents is not clear and gives the Organization ample discretion to require any type of document. The law states that the issuance process of investment licences takes 45 days. However, in practice it may take up to six months.

The issuance process is not transparent or well regulated. For example, FIPPA does not specify on what grounds an application may be refused. However, we must note that in view of the general governmental policy to attract foreign investments, there must be a very serious reason for the refusal to issue an investment licence.

VI. Foreign capital regulation

Iran remains subject to primary US sanctions and currently no payments in US dollars, Euros or other major currencies can be made into bank accounts located in Iran.

Dubai and Turkey are the most popular intermediary hubs for foreign currency exchange. Long-term contracts are linked to the foreign exchange rate and hedged by the banks. Also, there is a possibility that a newly opened bank in Kish Island may be able to process payments in major foreign currencies. However, this has not been tested yet.

VII. Privileges and protections

Investments made under the FIPPA regime get certain privileges and incentives, including:

(i) Exemption from expropriation or nationalisation, unless necessitated by public interests, when appropriate compensation must be made. The concept of compensation is a grey area in Iranian legislation, and it is not clear whether the foreign investor may claim for damages and lost profit.

(ii) Guaranteed repatriation of unused foreign capital in Iran within the framework of the investment licence is exempt from all foreign exchange, export and import laws and regulations.

(iii) Due state support for the issuance of entry visas, residence permits, work and employment permits, and other government approvals.

(iv) No limitation in terms of ownership percentage within the areas where foreign investments are allowed.

VIII. Restrictions for foreigners

Generally, there are no restrictions for foreigners in Iran and they receive the same treatment as Iranians. However, there is a limited list of restrictions that apply to foreign investors:

- Iranian laws prohibit foreigners from owning immovable property. However, a foreigner may own immovable property indirectly by holding shares in an Iranian company under FIPPA or under the ordinary rules of law for residence, business and industry after obtaining the necessary permits and complying with the formalities;
- Ownership of oil and gas deposits are generally not allowed by foreign companies, either directly or indirectly;
- Ownership in the financial sector is limited to 40% and is subject to the approval of the Banki Markazi (Central Bank);
- Ownership in the telecoms sector is limited to 49% and is subject to the approval of the telecoms regulator.

IX. Corporate vehicles

Limited liability companies are for long-term partnerships, which are generally regulated by only 22 articles in the Iranian Commercial Code. Therefore, this formation is usually used by very close partners that base their businesses primarily on trust. In comparison, joint stock companies are generally regulated by 300 articles of law. In Iran, joint stock companies and limited liability companies are the most commonly used forms by foreign investors, which choose the exact form depending on their business model and scale.

Joint Stock Companies

Charter capital of joint stock companies (JSC) is divided into shares. The liability of shareholders in a JSC is limited by par value of the shares. There are two types of JSCs: public, whose shares are publicly listed at the stock exchange, and private, which is fully owned by its shareholders. A minimum of three shareholders must form a JSC and foreigners willing to own 100% of a JSC usually introduce their affiliated companies. Charter capital is nominal and the regulation of JSCs is very detailed and stipulates lots of procedures.

Limited Liability Companies

In limited liability companies (LLC) the participants are liable for the obligations of the LLC to the extent of their contributions. The section regulating LLCs was only introduced recently and is not well regulated. A minimum of two participants must form an LLC. As a matter of practice, the Company Registration Authority, a state authority maintaining the companies' registry, applies certain procedures stipulated for JSCs to LLCs. Any sale of interest in LLCs is subject to the prior approval of at least 75% of the capital representing the majority of participants. In addition, an increase in shares can only be made through a unanimous vote.

Representative offices and branches

Representative offices, defined as branches of foreign companies, are becoming increasingly common in Iran. The procedure for opening them is fairly straightforward: they are usually registered when foreign companies require merely representative functions with minor commercial activity. For more active participation, for example, for the purposes of owning real estate and investing in industrials and other sectors of the real economy, foreign companies usually incorporate subsidiaries in the form of LLCs or JSCs.

In addition, representative offices and branches need to file annual audit reports with the Iranian authorities. However, this is rather a formal requirement and does not require much work.

There are other forms of corporate vehicles, including general, limited and proportional partnerships, but these are not commonly used.

X. Consent for the acquisition of shares

The acquisition of shares in an existing Iranian company does not generally require the consent of government authorities, unless the Iranian target company is engaged in one of the economy's strategic sectors, which include mass media, telecoms, energy, oil and gas, and finance. Such consent from other existing shareholders will be mandatory, however, due to their pre-emptive rights.

XI. Antimonopoly regulation

There is no separate statute on competition law; however, antimonopoly regulations were enacted in several laws relatively recently in 2008.

The acquisition of shares and participating interest does not generally require clearance from an antitrust perspective. However, as the Iranian market will get more sophisticated and fragmented, and because Iran expects a significant boost in foreign investment, we expect that the government may reinforce the antimonopoly regime.

XII. Currency control regulations

Generally, there is no requirement to register transactions in a foreign currency and there are no restrictions on currency convertibility. What's more, because conversion rates are based on the market rate, which may change quite often, investors must be aware of all potential foreign exchange losses.

If the investments were made under the FIPPA framework, the repatriation of profits, although guaranteed by law, must be approved by the Foreign Investment Board and confirmed by the Ministry of Economic Affairs and Finance. This requirement is aimed at ensuring that all state duties, taxes and other legal deductions are made before the profit is repatriated. Usually, such approvals are not unreasonably withheld.

XIII. Licensing

Businesses in Iran act under a general legal capacity, because businesses are generally allowed to work without licences. However, there is an exhaustive list of licensable activities. In addition, there are no general regulations on the issuance of licences. The related governmental body that issues the licence may specifically regulate the licence through bylaws and directions or sometimes by practice. Each matter must be reviewed on a case-by-case basis.

XIV. State-owned enterprises

When contracting or partnering with state-owned enterprises (SOE), foreign investors must be aware that such SOEs may be subject to certain restrictions and approvals relating to corporate approvals, complicated public tenders, the use of specific contract forms, etc. In addition, SOEs must follow the requirements of prioritised local content, which in certain cases consists of at least 51% of the project cost.

XV. Contracts

Iranian contract laws allow a significant degree of flexibility with regard to the contract term. There are certain limited sectors of the economy where the law prescribes certain formats of contracts. For example, in the oil and gas sector an international petroleum contract has recently been developed, but is still generally negotiable.

With an increasing amount of FDI into the country, typical share purchase agreements and joint venture agreements are no longer a novelty. Loss of profits and consequential damages are not recoverable, but parties may agree on liquidated damages.

XVI. Buy-back contracts and IPCs

Investors in Iran's oil and gas sector have been using buy-back contracts for a long time, whereby the government compensates the investor's costs and also pays specific pre-set remuneration upon the attainment of certain objectives included in the contract. Such contracts mainly cover only the exploration and development stages, and the investor is not supposed to participate at the production stage.

The situation is gradually changing, with the recent introduction of the new Iranian Petroleum Contracts (IPCs). These IPCs cover all stages, i.e. exploration, development and production, and involve setting up a joint venture with national Iranian companies, offering more favourable terms to foreign investors and more elements of a classic production sharing contract. Unlike buy-back contracts, IPCs have no ceiling for cost recovery and remuneration is not attached to oil prices.

XVII. Foreign governing law

The application of foreign law in cross-border transactions is generally allowed under Iranian law. However, contracts between Iranian residents, naturally, must be governed by Iranian law.

Article 968 of the Iranian Civil Code states that contracts are governed by the law of the place where the contract was concluded, unless both parties are foreign nationals and have declared their intention that the contract be governed by the laws of another jurisdiction. However, the Iranian courts do not generally view this article as mandatory, even if one of the parties is an Iranian resident and even if the contract is signed in Iran.

Thus, as a matter of practice, foreign law is generally recognised provided that it does not contradict public policy, and in that sense one cannot completely opt out of Iranian law. On top of that, contracts with land and immovable property in Iran may theoretically also be governed by foreign law, however the Iranian courts will look upon this with much scepticism. Therefore, in most cases, including cross border transactions, contracts with land or immovable property in Iran are subject to Iranian laws.

XVIII. Enforceability of foreign arbitral awards and court judgements

Iran joined the New York Convention in 2001, and arbitral awards are generally enforceable in Iran. In certain cases the Iranian courts may be reluctant to enforce arbitral awards (foreign or local) due to public policy issues and if the dispute involves state-owned enterprises. Thus, any application to the Iranian courts to enforce the arbitral award should be filed with the assumption that it may be denied. There have been cases when the Iranian courts have denied the case on merits and ignored the principles of the New York Convention or Iranian laws.

The Iranian courts have exclusive jurisdiction over certain cases, but these mainly relate to land and immovable property. So, the Iranian courts will not have exclusive jurisdiction over general commercial disputes in petroleum contracts, for example, but if that dispute originates from the issue of deposit, land or oil well ownership, then the Iranian courts' jurisdiction will be exclusive.

The Iranian courts may enforce court judgments of foreign courts provided that a judgment was issued in a country in which, according to its laws, judgments issued by the Iranian courts are also mutually enforceable, or the principle of reciprocity applies to the enforcement of judgments.

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Authors:
Otabek Suleimanov
Nasim Gheidi
Assel Nassimoldina

www.centil.law
Iran@centil.law