

## The New Law on Foreign Investment in Tehran Stock Exchange

For nearly 45 years, no specific legislation existed in Iran concerning corporate merger and acquisition as well as foreign investment in the Tehran Stock Exchange ("TSE"). Rather, these issues had been governed based on the general provisions of the Commercial Code of 1932 and its amendment of 1969, banking laws such as Law on Usury Free Banking Operation of 1983 and Monetary and Banking Law of 1972, and finally the Law on Establishment of the Stock Exchange dated 1966. Neither of the mentioned laws and regulations specifically provided for corporate merger and authorized direct foreign investment in the TSE. Most recently, with ratification of the Fourth Five Year Economic, Social and Cultural Plan ("Fourth Plan") in 2005, new regulations have been formulated to cover these issues.

With approval of the Fourth Plan and particularly its Article 15, which requires the Central Bank of Iran and the Ministry of Economic Affairs and Finance to facilitate foreign investment in TSE, and subsequently with ratification of the executive bylaw of this article on 1 June 2005, the TSE stepped into a new stage of its existence. Implementation of this semi-modernized regulation, despite the still existing restrictive conditions for foreign investment in the capital market, could lead to greater participation of foreign companies in Iran's stock market which until now had been prohibited.

These regulations now permit, subject to certain conditions, direct foreign participation in the TSE. The main provisions of the new regulation are:

- Foreign investment in the TSE is dependent on obtaining a permit from the Organization for Investment,

Economic and Technical Assistance of Iran (OIETAI) an organization dealing with foreign investment in Iran and adjunct to the Ministry of Economic Affairs and Finance;

- Within one year after obtaining the permit, foreign investors shall import into Iran all of the cash funds, either as lump sum or in installments, and initiate their investment in the TSE. Otherwise, the foreign investor shall obtain a new permit for further investments;
- All of the foreign investor's financial activities related to its investment in the TSE, shall be done through Iranian banks and banking system;
- Foreign investment is authorized in:
  - The stock of the companies listed in

- TSE;
  - Other securities accepted in TSE; and,
  - Any kind of Participation Bond accepted by TSE.
- Importation, repatriation and balancing of the principal of the foreign capital and profits thereof, is subject to and permitted under the law and regulations of the Foreign Investment Promotion and Protection Act (FIPPA) and foreign exchange laws;
  - The maximum foreign investment shall not exceed 10% of the listed company's total issued stock. Investments shall occur based on either of the following methods:
    - Purchasing the listed company's stock pursuant to obtaining a permit as mentioned above;
    - Purchasing the GDR of the company's stock;
    - Purchasing the shares of a listed company through international stock exchange markets.
  - The maximum authorized

foreign investment in Participation Bonds shall at no time exceed 10% of the foreign investor's imported capital. Same restrictions apply to other securities mentioned in this regulation.

- Repatriation of the principal foreign investment and capital gains is subject to a 3-year commitment, but dividends can be repatriated on an annual basis. In other words, foreign investors shall maintain their invested capital or re-invest their capital gains in the stock exchange market for at least three years while dividends can be repatriated on an annual basis.
- Should the foreign investor be unable to maintain the above-mentioned commitment, it shall be authorized to repatriate its non-investable capital pursuant to OIETAI's approval, provided that two thirds of the stocks quoted for foreign investment has already been purchased by foreign investors.

### **Recent Changes on Legislation Controlling Corporate Merger**

Prior to ratification of the Fourth Plan, corporate merger and

amalgamation of companies were governed not through specific legislation but based on general provisions of the Iranian Commercial Code. Based on Article 40 of the Fourth Plan, corporate merger is now permitted as long as it does not result in monopolization and is approved by four fifth of the shareholders of the merging companies. Upon merger, the new company will become the successor-in-interest to the former companies. This means, all of the assets and debts of the merged companies will be automatically transferred to the new company and the employees of the former companies will become employees of the new company. However, surplus workforce can be terminated with the agreement of the employees unions or with the approval of a special committee consisting of the representatives of the government, employers and employees. The capital of the new company, up to a ceiling totaling the capital of the merging companies, is exempt from corporate taxation.

While appreciating that this is very limited legislation which should be fully developed and provided for in the new Commercial Code which is currently under consideration, the

Fourth Plan obligates the government to implement anti-trust laws and regulations, in order to prevent monopolization and promote competition.

### Synopsis of Iran's Budget Law for Fiscal Year 1384 (2005 – 2006)

Despite various criticisms and notwithstanding the continuing modifications, the budget plan for year 1384 (2005-2006) was ratified and published in March 2005. This year's fixed budget of 1,589,989,770,000,000 Rials (approximately \$176.54 billion) stipulate the following revenues and expenditures:

#### 1. Foreign Exchange and Monetary Affairs

According to the Fourth Plan all ministries, government institutes and companies, and other companies which more than 50% of their capital and stocks, individually or jointly, belong to ministries, government institutes and companies, with the exception of banks, credit institutes and legal insurance companies, are bound to comply with the

following regulations:

- (a) To conduct all of their foreign currency transactions through banks and foreign currency accounts that have been approved by the Central Bank of Iran ("CBI"). New foreign currency accounts outside of the country can only be maintained upon approval of the CBI.
- (b) The government is also required to schedule repayment of all short and long term foreign debts and obligations in such manner that during the last year of the Fourth Plan the annual installment of such debts and obligations (without considering buy back obligations) does not exceed more than 30% of the foreign currency earnings of the government. Furthermore, the amount of foreign obligations and debts of the government shall not exceed more than US \$30 Billion at the last year of the Fourth Plan.
- (c) Commercial and specialized banks shall be authorized to procure the financial resources for investment projects of non-government

sectors from international sources without guarantee to be made in respect of such facilities by the government.

In those cases where the government utilizes foreign financing for its investment projects, the observance of the following guidelines is necessary:

- The minister or highest organ of the entity must take responsibility for the plan and obtain the approval of the Economy Council. Such investments must have financial, technical and economic justification and must comply with local content requirements;
- Prior to execution of the agreement, the permission of the Management and Planning Organization must be obtained;
- All transactions and contracts in excess of US \$1,000,000 must comply with local content law requirements, as well as being conducted through limited and/or international tenders.

Now with the new budget plan the government entities and the CBI

are allowed to create foreign exchange obligations provided that the above provisions of the Fourth Plan are observed. In implementation of the provisions of the Fourth Plan, and within limitations of financial facilities set forth in the Fourth Plan, the government in 1384 is allowed to procure and guarantee repayment of the funds obtained from foreign capital markets for the purpose of investment, by virtue of entering into project financing agreements and/or joint venture agreements.

Investments subject to the said financial facilities are convertible into buy back arrangements, provided that such projects are anticipated for in the budget plan.

In order to regulate the country's foreign payments balance, the organizations being in charge of the buy back projects shall make the necessary coordination with the CBI regarding their foreign exchange commitments and time scheduling for the repayment of these commitments, and present the information required in this field to the CBI, Management and Planning Organization ("MPO") and the Ministry of Economy and Finance, at least every six months.

## 2. Allocation of Funds of the Foreign Exchange Reserve Account

- The Cabinet may, for the purpose of expediting completion of the projects reaching completion in 1384 and 1385, pay and guarantee repayment of 42,289,050,000,000 rls out of the Foreign Exchange Reserve Account or through sale of participation bonds in 1384. Priority shall be given to chapters on agriculture, natural resources, water resources, industries, mines, environment, transportation, urban development, power generation, sports, tourism, sewage and facilities providing water supplies to rural areas. Projects related to undeveloped areas have even further priority for facilities available based on this article.
- The government is authorized to allocation \$8 billion of the funds available in the Foreign Exchange Reserve Account (provided that this amount is not more than 50% of the total available funds) to investment and provision of parts of the credits required for the private sector's projects which have appropriate technical and economical feasibility have been approved by the relevant ministry. Allocation of

this sum shall be in form of guaranteed facilities provided by internal banking system and Iranian banks abroad.

- In order to reduce the costs of financial facilities provided to exporters and for the purpose of encouraging the exportation of non-oil products, the government is allowed to allocate up to \$500 million of the above-mentioned funds (\$8 billion) to agent banks. The agent banks are obligated to provide this sum to exporter of non-oil product, in form of financial facilities and based on conditions to be approved by the Cabinet. At least 20% of such facilities shall be allocated to projects in undeveloped areas.
- The government is allowed to use \$500 million from the Foreign Exchange Reserve Account for refurbishment of transportation vessels. Of this amount \$150 million is stipulated for refurbishment of governmental aircrafts and an equal amount in form of credit is given to the government for the purpose of its investment in industries related to refurbishment of railroad vessels. The remainder \$200 million shall be allocated to agent banks

for provision of loans and facilities to the four branches of the transportation sector (aerial, marine, railroad, and roadway) for the purpose of refurbishment of their crafts.

- In order to support job-creating investment of the private and cooperative sectors, the government is obligated to allocate a credit of 15,000,000,000,000 rls to these sectors in form of a 5% subsidy on the interests that these sectors shall pay to the agent banks for their received facilities (loans). The investment contracts that were created prior to ratification of the current budget plan and those contracts that are subject to special treatments are exempt from the privileges set forth here.

The Cabinet is authorized to guarantee the repayment of these facilities as necessary and on a case-by-case basis. In such cases where the government provides an unconditional guarantee, either the government organization or the bank may hold as security the building, equipment and/or other properties of the projects.

- Financing projects indicated in this budget plan are legal only if they are not in form of usury loans.

### 3. Transportation

For the purpose of expediting construction of intra-city railroads (metro system) in cities with population of more than one million, a financing credit of \$1.2 billion is allocated to the Ministry of Interior. Similarly, a financing credit of \$800 million is stipulated for construction of inter-city railroads.

### 4. Interaction with International Markets

- The law on prohibition of importing unnecessary products is not enforceable on importation of tobacco. In order to satisfy the existing shortage, importation of tobacco is allowed in 1384.
- Importation of automobiles is authorized under the following conditions:
  - Imported automobiles shall be new and compatible to international or national standards.
  - Imported automobiles and buses are subject to 100% and 20% tariffs respectively. These tariffs include all applicable taxes and duties.
  - Importers of automobiles (and buses) shall be able to provide after-sale services.
  - Importation of gas-

burning and diesel automobiles are authorized.

- Semi-assembled automobiles shall not be subject to tariff of more than 100% and semi-assembled buses and minibuses shall not be subject to tariff of more than 20%.

### 5. Privatization

- The government is allowed to sell up to 20% of its shares in governmental companies with activities in petrochemical, refinery and distribution of oil products, cement and steel industries.
- Iran Telecommunication Company and companies related to the Ministry of Telecommunication are obligated to grant an amount of 111 billion rls to country's general revenue.
- The Ministry of Telecommunication is allowed to receive license fees, and deposit the received amounts to the public revenue accounts.
- In order to promote the telecommunication and data communication industry and to improve industries related to production of software and IT goods and services,

companies related to the Ministry of Telecommunication are allowed to give loan credits of up to 400 billion rls (upon approval of their general assembly) to the private and cooperative sector for their development projects, job-creating activities and other activities related to exportation of products and services. Provision of such credits shall be pursuant to the proposal of the Ministry of Telecommunication and the MPO and approval of the Cabinet.

## 6. Energy Conservation

- The Ministry of Industries and Mines shall plan production of automobiles in a manner that at least 20% of the total production is specified to production of dual fuel vehicles. To this end and in return for its savings on importation of diesel fuels, the NIOC is obligated to pay to auto producers an amount of \$770 for every (such) automobile produced. This amount shall be paid in form of gratuities aid.
- NIOC is obligated to build 400 new CNG stations by the end of year 1384. In addition, NIOC is allowed to

build another 500 stations with cooperation of the private sector.

- The Ministry of Industries and Mines shall use the cooperation of the private sector for transforming 20% of the existing diesel vehicles into dual fuel vehicles.
- NIOC shall:
  - Improve and refurbish the refineries with the objective of increasing the daily production of oil to 20 million liters in sum of \$2.5 billion.
  - Complete the projects of building and activating three liquid gas refineries with a total daily production capacity of 360 barrels and projected daily production of 32 million liters a day (equal to \$1.275 billion).
- Tavanir is authorized to use financing facilities of up to \$1 million for performance of creation and transportation of electricity.

## Iran's New Commercial Code

With approval of the new Commercial Code by the Cabinet on June 27, 2005, the first step toward modernization of Iran's

70-year old commercial code was taken. Although there might be further changes, the current draft maintains 8% of the old provisions, amending 21% of them and more than 30% of the provisions are new. One of the most important provisions of the new code is providing the possibility of electronic trading. As of the date of this newsletter, there have been no further updates as to the status of ratification of the new commercial code by the Parliament.

## The Law on the Manner of Holding and Conducting Tenders

In February 2005, the law on the Manner of Holding and Conducting Tenders has been approved to define the method and stages of holding tenders. According to the new law, transactions are categorized based on their value limits (contract price):

1. Petty (small) Transactions: Transactions worth Rls.20,000,000 (twenty million rials) or less. In conducting tender in this kind of transactions, the officer in charge of supplies or the purchasing agent shall conclude

the transaction by taking into consideration the interests of the buyer entity, against invoice, at his own risk, with the desired quality and at the lowest possible price.

2. Medium Transactions: The transactions above the value ceiling of petty transactions but not exceeding ten times in value of petty transactions. For these transactions, the officer in charge of supplies or the purchasing agent shall, with due regard to the particular nature of transaction (commodities, services or rights) investigate the matter and shall conclude the transaction by taking into consideration the interests of the buyer entity after obtaining a minimum of three quotations in writing, at the same desired quality and shall have the price approved by the manager in charge of supplies or another officer of similar rank and shall conclude the transaction by concluding a contract or against obtaining invoice. Should obtaining three written quotations prove impossible, the existing number of written quotation(s) shall be sufficient with the confirmation of the manager in charge of supplies or another officer of similar rank.

3. Large Transactions: Transactions having an estimated initial price exceeding

ten times in value of petty transactions. In large transactions, action will be taken in accordance with either holding public tender by publishing a call through newspapers of mass circulation; or holding limited tender.

- Based on the discretion of the tenderer, if a tender requires technical-commercial assessment (called Two-Phased Tenders), the proposal must fully assessed by a technical-commercial committee and only those envelopes containing the prices quoted by bidders who scored the required technical-commercial points, will be opened.
- In case of need to hold international tender or in case of foreign credit facilities, the call shall be made, by obtaining the permissions relating to and in compliance with the criteria under the Local Content Law in Iran approved on March 2, 1997, through publication of notice in one of the newspapers of mass circulation and through, at least, one notice published in English local newspaper and an international periodical or newspaper related to the subject of tender.
- In international tenders,

domestic bidders shall have priority over foreign bidders. The modes of such priority shall be described in tender documents. The tenders for which compliance with the above rule shall not be expedient, must be specified by the Economy Council.

- In the following cases there will be no requirement to hold tender and the executive organizations may proceed with transactions intended to, without undergoing tender formalities (the following is not the complete list):
  - a) Purchase of movable properties, services and rights that, at the discretion and risk of the minister or the highest authority in rank of the executive organization concerned, in the capital or in provinces, or at the discretion of the authorities permitted by them, shall be of exclusive nature without having similar types.
  - c) Purchase of movable and immovable property, goods and services having a fixed price at such fixed prices or less or purchase of rights at prices fixed by competent authorities.

d) Repair of fixed (stationary) and mobile equipment and machineries and supply of equipment and machineries to be purchased solely for the purpose of substitution in order to avoid disruption in the process of production by manufacturing entities in such manner that the above acts may not be construed as expansion, at the discretion and risk of the minister or the highest authority in rank of the executive organizations, in the capital and in provinces, or at the discretion of the authorities permitted by them by duly taking into consideration the interests of the country.

e) Purchase of advisory services including consulting engineering services and technical-commercial advisory services comprising the study, designing, project management, execution of works, supervision and carrying out any type of advisory works and expert tasks.

g) Purchase of spare parts for replacing or completion of supplies, equipment, stationary (fixed) and mobile machineries and equipment as well as measuring and metering equipment and devices and supplies of scientific and technical laboratories and the

like where supplying through tender formalities, at the discretion of the topmost authority of the executive organization concerned, shall not be possible, upon determining the price by, at least, one expert in the related field who will be designated by the minister or the highest person in rank of the executive organization concerned, or the persons authorized on their behalf in the capital and in provinces.

## **Amendment of Article 35 of the Foreign Investment Promotion and Protection Act (FIPPA)**

The amended provision provides that the relevant executive organizations including the Ministry of Foreign Affairs, Ministry of Interior, Ministry of Labor and Social Affairs, and the Law Enforcement Force are required to act for the issuance of visas, residence permits and issuance of work permits for foreign investors, directors, foreign experts and their first degree relatives, Upon the request of Organization confirming their being investors

and in relation to the investments covered by the FIPPA according to the following procedure:

- (a) The Ministry of Foreign Affairs, upon a request by the Organization, shall communicate to the missions of the Islamic Republic of Iran in foreign countries, the authorization for issuance of single entry or multiple entry visas valid for three years and permitting stays of three months on each entry.
- (b) After entering the country, the above persons, who have obtained visas for investments, can refer to the Law Enforcement Forces, provide a confirmation issued by the Organization confirming that their investment are covered by the act, and obtain residence permits of three-year terms. After the issue of residence permits, the Ministry of Labor and Social Affairs shall issue employment permits for the mentioned persons.
- (c) Upon obtaining three-year residence permits as explained above, the investors shall be exempt from exit and entry visa requirement for each case of exit and reentry from/to the country.

## **Recent Treaties Between Iran and Other Countries**

In May 2005, upon approval of the Parliament and the Guardian Counsel the bilateral trade treaty between **Iran and Ghana** was ratified into law.

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