

Overview of Budget Bill 1382 (2003-2004)

The Iranian government spends and develops annual policy on the basis of an annual budget that is presented by the executive and ratified by the Parliament. The 1382 (March 2003-March 2004) Budget Bill ("the Bill") obtained final approval from the Expediency Council after disputes between Parliament and the Guardian Council on certain aspects of the bill and was published in March 2003. The following provides an overview of the Bill relating to foreign investments and foreign undertakings of the country.

Tender Requirement for Foreign Transactions

Under Note 1-F of the Bill, all government organizations and companies are required to conclude their foreign transactions with value of more than one million US Dollars only through limited or open tenders. The tender requirement can be waived only by a decree of the Council of Ministers, which must

be issued on an ad hoc basis.

Moreover, the Central Bank of Iran may not undertake to provide the foreign currency needed for government transactions unless the head of the relevant organization confirms that the tender requirement is complied with or duly waived.

Privatization in Electricity Sector

The process of privatization of power plants, which had been initiated by last year's fiscal budget bill, has been extended to the 1382 Budget Bill. Under Note 12-F of the Bill, Tavanir - the state power/utility company - is authorized to privatize its existing and installed power plants up to 10% of the established capacity of the country. For privatization of such power plants the approval of the Ministry of Energy must be obtained in advance. The price of the power plants must be paid

by installments in a five-year period.

Marketing Activities of Foreign Companies

Along with the government's recent campaign against illegal importation of goods, the Bill has provided certain measures to stop smuggling of goods into the country. Note 19-L of the Bill requires the government to eliminate all discriminations, exemptions and monopolies in import-export activities and adjust the tariffs in order to encourage and promote legal importation activities. Conversely, the storage, transportation, distribution and sale of goods for commercial purposes are deemed as smuggling if such goods are not imported through legal channels.

Moreover, in order to regulate the importation activities and prevent illegal importations, all

foreign manufacturers of goods and service providers are required to establish their official representatives in Iran before providing their goods or services in Iranian markets. Foreign companies shall provide appropriate after sale services for their goods and services through such representative offices. Supplying of the products of the foreign companies in Iranian markets without having an official representation in Iran in the form of a branch or representative office would be deemed as smuggling.

Furthermore, in order to support domestic industries vis-à-vis importation, the government is required to encourage domestic productions under license or in partnership with foreign reputable companies in the fields of home appliances, video-audio equipments, mobile phones and computer CKDs as a replacement for importation of consumer goods.

Oil and Gas

Under Note 21-D of the Bill, NIOC is required to develop South Pars field in order to achieve an additional ceiling of

100,000,000 cubic meters per day of natural gas. NIOC shall develop liquefaction establishments as well as gas refineries in order to supply liquid gas in domestic and foreign markets.

The reimbursement of the contractors in the mentioned projects shall be made either through the products of the same projects (i.e. under buy-back schemes) or through the income of NIOC or NIGC accrued through the exportation of other oil products, gas or gas condensates.

Further, NIOC is required to expand the shared oil fields in order to achieve the ceiling of 6,000,000 barrels per day of additional crude oil production. The reimbursement of the projects shall be made exclusively through the products of the same projects i.e. under buy-back schemes.

NIOC is also authorized to run exploration operations through its contractors and at the risk of contractors. A contractor would be reimbursed only if a commercial field is discovered. In this case, NIOC would enter into an agreement with the same contractor for performing of the expansion and exploitation

operations under the buy-back scheme up to the ceiling of US \$1,000,000,000. The buyback contract shall recover both exploration and expansion expenses.

It should be noted that the mentioned authorizations are in addition to those granted under the previous years' budgets and extended by the Bill.

Foreign Undertakings

Under Note 20-G of the Bill, the government is authorized to accrue US\$ 6.8 billion of foreign undertakings by obtaining and guaranteeing of foreign financial facilities during 1382. This includes up to US\$ 3.9 billion for execution of national infrastructure projects whose repayments are made through their own incomes (i.e. through buy-back scheme) and US\$2.9 billion for other projects which shall be recognized by the High Council of Economy Council as having priority and economic-technical feasibility.

Furthermore the Bill has re-authorized the government to utilize outstanding amounts of facilities permitted under the previous years' budget bills but not used thus far. This includes several project finance and

buy-back projects.

All project finance operations, as well as financial agreements to be entered into by executive organizations must be approved by the Central Bank in advance. The Central Bank must also approve the repayment schemes under such agreements.

Government Guarantees of Foreign Investments

The Foreign Investment Promotion and Protection Act (2002) has authorized foreign investors to invest in all economic fields through buy-back, BOT and civil partnership schemes. In many cases, the exclusive customer for the products and services of the foreign investors is a government organization or company – such as Tavanir in case of power plants -- so the foreign investors frequently require the government to guarantee the payments by such organizations or companies. The Bill has attempted to respond to the increasing demands of foreign investors. Under Note 21-L of the Bill, the government has been authorized to provide payment guarantees in favor of government organizations and companies with respect to their

undertakings vis-à-vis foreign investors. Such guarantees may be granted to foreign investors only in cases where their products or services are to be purchased exclusively by the government or a government company or organization. Note that under Iranian law, all government guarantees must have legislative authority. Such payment guarantees are authorized to be given in the following projects and fields:

- Establishment of power plants up to the aggregate capacity of 12,000 MW;
- Establishment of Refineries up to the capacity of 300,000 barrels per day;
- Tehran's Sewage System;
- Construction of 3,400 km of railways;
- Construction of 1,300 km of freeways;
- Expansion and exploitation of Imam Khomeini International Airport and seven other international airports;
- Expansion and equipping of large commercial ports;
- Providing rail vehicles; and
- Communication projects.

The Ministry of Economic Affairs and Finance can use the resources, bank accounts and credits of the respective organizations for repayment of

their undertakings. However, the government is not authorized to use its own other resources for repayment of such undertakings in case such organizations lack the credits and resources. In other words, the government can provide a guarantee that in case of default by a state organization, the government will dip into the resources of that organization itself and cannot provide additional resources. Therefore, such guarantees may not necessarily be deemed as a government guarantee whereby payment will be made by the government if one of the state entities defaults. As such, it remains to be seen whether such undertaking by the government would satisfy foreign investors as there seems to be no additional guarantee other than the relevant state organizations own resources. Moreover, in the case of existing power plants slated for privatization, the government cannot refer to this authority for providing supplemental guarantees.

The by-laws of Note 21-L shall be drafted by the Ministry of Economic Affairs and Finance in cooperation with the Management and Planning Organization and shall finally be

approved by Council of Ministers. The by-laws will provide for the extent of undertakings and payment methods and also shall determine the projects in which the guarantees are to be granted.

New Circular Letter Requires the Registration of a Branch or Representative Office for Providing Foreign Goods and Services in Iran

Pursuant to the requirements of the 1382 Budget law, a directive has been issued by the Ministry of Commerce in April 2003. Under Article 1 of this directive, all natural and legal persons, as well as official representatives of foreign companies intending to provide foreign goods and services in Iran, their activity being in the form of company or trade sector, are required to register their branch or representative office for supplying products. Also, all foreign companies and official representatives subject to this circular are required to provide after-sale services and authorized repairs centers in accordance with the quantity and scope of the distribution of their products and provide the

Ministry of Commerce with a list containing details of such centers.

In addition, companies and representatives subject to this requirement shall register by the "General Bureau for Trade Sectors and Traders", and foreign companies and authorized registered companies shall observe the Law on Trade Sector's Order.

Importantly, in case of failure to observe the regulations of the directive, the goods brought into the country will be deemed as contraband and smuggled goods. Companies and representatives involved in such activities will be penalized in accordance with commercial and penal laws of Iran.

As such, it is imperative for foreign companies providing such goods and services to ensure compliance with this new requirement.

It should be noted that the registration of the branch and representative office will be done within the Ministry of Commerce and not the Companies Registration Office.

New Law on Unification of Duties

The Law on Amendment of

Some Articles of the Law on Third Economic, Social and Cultural Development Plan and Method of Establishment and Collection of Duties and Other Charges from Manufacturers, Service Providers and Imported Goods, ("the Law"), generally known as law on unification of duties, was ratified by Parliament on January 12, 2003.

The main intent of the Law is to unify under specific fixed titles all kinds of duties used to be collected from manufacturers, importers and service providers and thus simplify the payment and collection of duties. This would release business ventures from payment of various confusing local and national duties, which were imposed on them from time to time. The following is a summary of the main provisions of this Law.

Abrogation of Duties

Under Article 1 of the Law, all kinds of taxes and duties paid by manufacturers of goods, service providers and imported goods as provided for or permitted under different laws and regulations are abrogated save as the following:

- Taxes and duties provided for under Direct Taxation Act;
- Taxes and duties under the

Law on Administration of Free Trade Zones;

- Duties under the Law on Passage of Foreign Vehicles;
- Freeways Tolls;
- Duties under the Law on Transport and Transit of Foreign Goods from the Territory of Islamic Republic of Iran;
- Balance Charges imposed on certain imported goods;
- Civil Aviation Duties (2% of the price of tickets of internal flights; and
- Roads duties.

Except for the taxes and duties provided for under the above laws or the Law, no duty or statutory payment shall be collected from the following sources:

- Imported goods;
- Domestic manufactured goods;
- The services provided for the Law;
- Taxable incomes;
- Dividends;
- Interest paid to participation bonds;
- Interest paid to bank deposits and other financial operation with banks.

Local duties can be collected from other sources but in any case such duties must be announced to the public not later than February 4th to be effective and collectable for the next

Iranian year (starting 21 March).
Importation Tariffs

All customs duties, importation taxes, order placement charges and all other importation duties (such as port duties, airport duties, municipality duties etc) are combined with a fixed rate of 4%, which shall be applicable to all kinds of imported goods. The aggregate importation tariffs are comprised of the mentioned duty plus the Commercial Interest Taxes, which are determined for different goods on an annual basis.

Previously, the importation activities involved various taxes and duties and the assessment of duties were a very complicated process; in certain cases some 21 kinds of duties were imposed on importations.

The Law has also abrogated most of the customs exemptions.

Final Consumer Goods Duties

The local manufactured goods undergo the following duties:

- Carbonated Drinks: 15% of the factory price (exported products are exempt from duty according to the Law on Third Five Year Development Plan);
- Cigarettes and Cigars 15% of the factory price;
- Gasoline 20% in addition to

the official approved price;

- Fuel oil, 5% of the official price;
- Other final consumer goods, to be listed by a special committee on an annual basis, 3% of the sale prices; (Exported products are exempt from duty according to the Law on the Third Five Year Development Plan).

Duty on Services

The services are subject to the following duties:

- Communication Services: 6% of the service charges;
- Subscription for mobile phones: 20% of the subscription fees;
- Gas and Electricity (except for industrial mining and agricultural uses) and also supplying of water inside the cities: 3% of their final price ;
- Services of hotels, motels, clubs, etc: 2% of the service charges;
- Transport of the passengers outside the cities within the country: 5% of the price of the ticket;
- Annual duty on passenger cars and two cabin trucks: 0.1% of the price (i.e. the factory price for domestic cars or the customs evaluated price plus

customs tariffs for imported cars);

- Registration of passenger cars and two cabin trucks: 3% of the price;
- Transfer of motor vehicles: 1% of their price;
- Also the duties paid for issuance of certain operation licenses and permits such as operation license for kindergartens, hospitals, commercial cards, etc. shall be approved by the Council of Ministers.

Late Payment Penalties

Manufacturers and service providers shall include the amount of duties in their invoices and pay the same to the designated accounts no later than 60 days. Failure to pay the duties within the permitted interval would involve payment of a penalty equal to 2.5% for each month of delay (i.e. 30% per year).

Iran to Join the Multilateral Investment Guarantee Agency

The Iranian Parliament in May 2003, ratified Iran's joining World Banks' Multilateral Investment Guarantee Agency ("MIGA"). The Guardian Council approved the acces-

sion in June. Based on a single article, the Iranian government is authorized to join MIGA with 1659 shares with a maximum payment of US\$17.5 Million. The joining of MIGA illustrates Iran's stepping up of entering into a number of bilateral investment treaties, double tax treaties and the like in order to attract badly needed foreign investment.

Circular Letter Regarding Tax Withholding on Contractors with Foreign Financing

The chairman of the State Taxation Organization has recently issued a new circular letter dated March 26, 2003 on method of deduction of taxes of contractors in Iran. Under this circular, before banks can authorize the payment of letters of credit for benefit of foreign financiers financing the contracting work, proof of payment of the contractors' taxes must be submitted to the Iranian banks issuing the letters of credit.

The taxes should be paid in Rials by the contractor based on the requirements of the Direct Taxation Act. Once the taxes are paid, the proof is submitted to the relevant bank

which can thereafter make the payment. However, until such proof is shown, the banks will not be authorized to make the payments for the benefit of those financing the contracting work in Iran.

Recent Treaties between Iran and Other Countries

Bilateral Investment Treaties

During the last few months, several bilateral investment treaties have been signed and ratified between Iran and the following countries:

- Tunisia
- Tajikistan
- Ukraine
- Italy
- Kyrgyzstan
- Georgia
- Bulgaria
- Croatia

Double Taxation Treaty

In the first quarter of the Iranian year, the agreement on avoiding double taxation has been signed and ratified between Iran and China.

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