

Iran

Chamber of commerce:

Iran Chamber of Commerce, Industries and Mines
254 Forsat Street
Taleghani Avenue
15814 Tehran
Iran
Tel: +98 21 884 6031
Fax: +98 21 882 5111
Email: info@iccim.org
Web: www.iccim.org

Professional body:

Iranian Central Bar Association
3 Zagros St.
Argentin Square
Tehran
Iran
Tel: +98 21 888 7167
Fax: +98 21 877 1340
Web: www.centralbar.ir

Taxation of loans granted to Iranian entities by foreign banks

Cyrus Shafizadeh
Tavakoli & Shahabi
Tehran

The taxation of income arising from the grant of foreign loan facilities has for some years been a contentious issue, the established position being that income earned therefrom was not subject to tax. A recent circular issued by the director-general of the Taxation Affairs Organisation, however, changed the position in that it provided, among other things:

“... given that the income earned by foreign entities in the form of interest and commission charges must be regarded as to include their activity in Iran and an instance of exploitation of capital in Iran, therefore, the grant of loan and credit facilities by foreign investors and banks who carry out their activity by means *other than* a permanent establishment, branch, representative office, agency and the like, shall be subject to taxation on income as the case may be in accordance with the provisions of the Direct Taxation Act.”

The language of the circular is clear and confirms that the income of foreign lending banks, being earned in Iran, will be made subject to tax. This could have significant repercussions on agreements entered into by foreign banks and Iranian borrowers.

Reasoning

The legality of the imposition of this tax is arguable. Given that Principal 51 of the Iranian Constitution unequivocally provides that “no tax shall be imposed unless by law”, the legality of any tax imposed on such income must be specifically provided for in a law enacted by Parliament. The Direct Taxation Act 1988, as amended (the DTA) is the only item of parliamentary legislation dealing with taxation. The only provision of the DTA imposing an obliga-

tion on foreign entities to pay tax is Article 107. The wording of the circular clearly relates to paragraph (c) of the Article, which provides:

“The taxable income of foreign legal entities and organisations domiciled outside of Iran shall be assessed in the following manner...

...(c) In the case of exploitation of capital and other activities that the legal entities and the said organisations perform in Iran *through* representation such as a branch, representative, agency and the like in accordance with Article 106 of this Law1.”

It would seem that the reasoning behind the circular is fundamentally flawed. Whereas the DTA provides for income derived *through* representation, etc, the circular seems to take a diametrically opposite view and speaks of income derived by means *other than* representation, etc.

A question of origin

Further, a previous decision made by the High Council of Taxation confirmed that:

“... pursuant to... Article 107(b) of the [DTA]... any non-Iranian person (whether real or legal) shall be subject to taxation in Iran on their income in Iran... but in the case of income earned from Iran, on the basis of the said authorities, the intention of the legislator was that this related solely to income derived from the transfer of licenses and other rights and/or the provision of training and technical assistance and/or film rights and apart from these, other income derived from Iran shall not form part of the matters mentioned, including profits related to credits and facilities granted by foreign credit institutions domiciled abroad who, having no operational activities in Iran, shall not be liable to pay tax to the government of the Islamic Republic of Iran.”

The decision confirms that income derived from the grant of loans and facilities by foreign banks, being income derived “from Iran” (as distinct from income earned “in Iran”), is not sub-

ject to tax, given the absence of specific provision for this in the DTA.

The decision is a confirmed interpretation of the DTA, and as the DTA is a higher form of law than a circular, it would seem likely that the contents of the circular may be found to be contrary to the DTA.

On the basis of the circular however, from the date of its issuance, the practice would be such that the income of foreign lending banks will be made subject to tax (deducted at source). This practice will continue until the circular is set aside as a result of judicial review.

It is the experience of the author that in all cases where financial facilities are granted by foreign banks to Iranian entities (which are almost invariably government companies in any case), the relevant facility agreement contains provisions whereby any payment made to the foreign bank shall be grossed up by the amount of tax attributable to it. Given this, it would seem that it will ultimately be the Iranian borrower who will suffer the consequences of the director-general's circular.

Financial and corporate

Recommended firms

Tier 1

Atieh Associates
Tavakoli & Shahabi
Torossian Avanesian & Associates

Tier 2

Dr Akhlaghi & Associates
Dr Jamal Seifi & Associates

Tier 3

AA Atai & Associates
Adib Law Firm
Hossein Lotfi
IRCLS (Hendizadeh & Associates)

Political pressure on Iran has intensified, and this year saw further international sanctions imposed on the country. This appears to have reshaped the financial and corporate market: according to one lawyer, the percentage of inbound investors is swaying from a Western majority to a higher percentage coming from Middle Eastern and Arab countries.

"90% of our clientele were western, that has changed," says the lawyer. "Lots of western companies haven't come to market waiting to see the market unravel." Though this implies a slowdown in foreign direct investments, other commentators report investments pouring in from alternative jurisdictions like Turkey and emerging Asian economies, following encouragement from the Iranian government's. In a recent statement, the government also said it will repeal or amend laws in an effort to gain investors' confidence.

In contrast to the rationing of petrol in 2007, the oil, gas and petrochemicals industry is still the country's most dynamic sector and a key source of work for Iranian lawyers.

Atieh Associates

Atieh Associates has reeled in many of Iran's biggest deals, keeping the firm in the top tier once again. The firm was unaffected by the departure of two senior associates Parisa Mazaheri and Faraz Naji to work in other cities in the Middle East as it gained replacements in senior associate Maryam Hosseini and associate Mehrnaz Mehrabi.

A relatively large proportion of the firm's mandates come from foreign clients: among its work in the energy sector, the firm advised European lenders in relation to their financing of crude-oil carriers. It also acted for a foreign oil company in connection to a liquefied natural gas (LNG) project. The firm has also been busy in the natural-resources sector, and recently advised a foreign buyer on its acquisition of a gold mine in Iran.

All of the firm's key deals are executed by partner Babak Namazi and his associates. A peer recommended the western-educated partner as one of the top lawyers in the country, since he has strong English skills and provides a "western-style" service to clients. Says another: "He's the most proactive lawyer I've seen in Iran." The firm's excellent client service also means it retains a large number of western clients.

Leading lawyers
Babak Namazi

Tavakoli & Shahabi

"We've been very happy with their service as their response is very prompt," says a client of Tavakoli & Shahabi. "Secondly, they work with international companies and have good exposure. They are in line with international standards: they meet all our requirements so we are very happy because of that."

Although transactions have slightly dwindled in the global market slowdown combined with Iran's political disposition, the firm has yet to see its workload subside. In fact, it received steady work from medium-sized European and Eastern companies, especially from India. According to a partner at the firm, Indian clients "are all coming to Iran as they come to gain some ground before the Europeans come back".

"He did part of his education in London, so he understands what we need," says a client of Cyrus Shafizadeh, an up-and-coming lawyer at the firm. A rival also recommends Shafizadeh as a leading individual who is "very conscientious and hard working." Partner Ahmad Ehtesham is recognised by his peers as a top lawyer in the financial and corporate area.

Clients of the firm come from a variety of industries. For example, the firm represented an overseas electrical appliance manufacturing company in its acquisition of a local company. In the communication sector, the firm performed due diligence on behalf of international financiers on a telecoms operator in Iran.

Other notable deals of the year include acting for an overseas oil company in connection with a buyback agreement with a state-owned Iranian company, and advising an international steel company on its registration in Iran. The firm's work has also included advising clients on securing foreign-investment protection, the acquisition of mines, and the establishment of a steelmaking plant.

Leading lawyers
Ahman Ehtesham
Cyrus Shafizadeh
Mostafa Shahabi

Torossian Avanesian & Associates

Partner Aida Avanesian at Torossian Avanesian & Associates receives recognition from peers and clients as a strong lawyer who offers thorough and accurate support to deals. Meanwhile partner Vrej Torossian is recognised for having particular expertise in the oil-and-gas sector.

The firm specialises in foreign investments. In recent work Torossian advised Al Ghurair Group, an investor from the United

Arab Emirates, in relation to a \$5.2 billion aluminium smelter project.

Avanesian's recent experience includes providing advice to DVB Bank in connection with the arrangement of a \$100 million syndicated ship-financing loan. She has also assisted the National Bank of Dubai on an \$85 million syndicated facility to Iran Petrochemical Commercial Company.

Leading lawyers
Aida Avanesian
Vrej Torossian

Dr Akhlaghi & Associates

For nearly three decades, Dr Akhlaghi & Associates has been advising clients in and around the region on financial and corporate issues. Behrooz Akhlaghi manages the team of lawyers and closely supervises the work being done. Akhlaghi is also an associate professor at Tehran University and is said by competitors to have taught many lawyers in the region.

The firm has represented clients from all over Asia such as the Casio Corporation and the Hyundai Corporation. Other reputable names such as UBS and International Finance Corporation have been clients of the firm. Baytur Construction & Contracting Company is just one of example of the Middle Eastern clients served by the firm. Akhlaghi is well-respected among both clients and peers. Says one: "Partners who know him very well always speak very highly of him."

Leading lawyers
Behrooz Akhlaghi

Dr Jamal Seifi & Associates

The year saw Jamal Seifi and his team relatively unaffected by the slowdown in investment activity as the firm's broad expertise in a variety of practice areas has allowed it to channel resources into other areas.

The firm represented a mixture of European, Iranian and international corporations in the oil, gas and petrochemicals sector. At the end of the first quarter of 2007 the firm was appointed as Iranian counsel in relation to the financing of an LNG project.

Besides the firm's activity in the energy industry, a UK company operating in Iran sought its advice on contractual and distribution matters. Another highlight for the firm was advising a European company investing in the Iranian mining sector.

Seifi heads a team of around 10 lawyers, making the firm one the largest in Iran.

Leading lawyers
Jamal Seifi

Other notable firms

Hossein Lotfi debuts in the rankings with recognition from the market as a laudable firm in the financial sector. With business from big clients, another new entrant in the third tier is **IRCLS (Hendizadeh & Associates)**. Kaveh Hendizadeh has a reputation with rivals as being competent and pleasant to work with across the table.