

BRANCHES AND REPRESENTATIVE OFFICES IN THE LAW OF IRAN

Executive summary

Since 1931 when Article 4 of the Corporate Registry Act of Iran recognized two distinct legal forms for activities of foreign companies in Iran, namely establishing a branch office or appointing a representative, all of the Iranian laws and regulations have remained loyal to this dichotomy as if no other option exists. Even the new Commercial Code of Iran (2014) could not succeed in creating a modern business law for regulating the activities of foreign companies in Iran.

If a foreign company intends to establish a legal presence for itself in Iran, it needs to consider the following issues:

1. Which legal structure is the most appropriate form of representation in Iran: establishing a branch office or appointing a representative?
2. What are the legal consequences of establishing a branch office in comparison with entering into a representation contract with an Iranian natural or legal person?
3. What controlling measures will be adopted and applied by the Iranian authorities on the activities of a branch office or a representative?
4. How can a foreign company put an end on the activities of its branch office or representative?
5. Under what conditions the Iranian authorities terminate the activities of a branch office or a representative of a foreign company?

This News & Analysis has a brief and rapid look at the available responses to these five crucial questions.

Which one to choose: a branch office or a representative?

A foreign company that intends to start a commercial activity in Iran needs to choose the legal form of its presence in Iran. Two main options are available: branch office or representative. Which one is the most appropriate legal form for establishing a commercial presence in Iran? There is no 'one for all' response to this question. Before making a decision, foreign companies need to know about the advantages and disadvantages of establishing a branch office or appointing a representative in Iran. They need to know whether both of them may be used for all of the available business activities or not. If the response is positive, the next question is about the procedure for registration and the mechanisms provided by the laws and regulations of Iran for controlling branch offices and representatives of foreign companies in Iran. Finally, foreign companies would be interested to know about the means and ways of terminating the activities of their branch offices and representatives in Iran. Having a general picture of the process of creating, maintaining and terminating their activities in

Iran would enable the foreign companies to make an informed decision about establishing a legal presence in Iran.

Fields of activity and the resulting responsibility

Article 2 of the Executive Regulations on Permitting Registration of Branches and Representative Offices of Foreign Companies (“the Executive Regulations”) defines ‘branch office of a foreign company’ as the local office of the principal company which directly functions and attends to all the activities of the principal company within the objectives and duties undertaken by the principal company. This means that any business activities by a branch office shall be in the name and under the responsibility of the principal company.

Representative of a foreign company is a *legal or real person*, who, based on the "representation contract", performs a part of the activities of the company. The representative is responsible for activities performed on behalf of the company (Article 4 of the Executive Regulations).

Three main differences between a branch and a representative office are:

- 1) A branch has a vaster scope of functioning in Iran because it can involve itself in every field of activity of the company while a representative can only undertake the activities stated in the representation contract. This means that the legal basis of the authority granted to a branch office is its registration in Iran while a representative acquires its authority for functioning in Iran from the representation contract and its registration.
- 2) A branch is always a legal person while a representative may be a natural or a legal person. A major consequence of this difference is that a natural person may be subject to criminal responsibility but it is impossible to impose a criminal responsibility on a legal person. For example, if a foreign company is involved in a corruption case in Iran through its branch office, the foreign company *per se* shall have nothing to do with the criminal accusation. The high official of the branch office, however, may find themselves in prison at the end of a criminal court procedure.
- 3) A branch has no separate legal personality. Therefore, a company that establishes a branch in Iran is responsible for the contractual obligations and tort liabilities of the branch. Representatives of foreign companies in Iran, on the contrary, accept their own contractual obligations and tort liabilities, and shoulder their own criminal responsibilities. Iranian counterparts of foreign companies must pay close attention to the rights and authorities delegated to representatives of their foreign counterparts before signing an agreement with them. It is evident that where foreign representatives act beyond the authorities delegated to them, they are personally liable for their *ultra vires* actions.

It must also be noted that the overall scope of activities of a branch office and a representative in Iran are the same because under Article 1 of the Executive Regulations, both of them are authorized to carry out the following activities:

1. Providing after-sales services for foreign goods and services sold at the Iranian market;
2. Involvement in execution of contracts concluded between Iranian entities and foreign parties;
3. Considering the available options and paving the way for foreign investment in Iran;
4. Cooperation with Iranian technical/engineering companies for working in third countries;
5. Increasing Iranian exports other than oil;
6. Providing technical and engineering services and transfer of know-how and technology; and
7. Other activities requiring authorization of the (Iranian) government e.g. providing services such as transportation, insurance, inspection, banking, marketing, etc.

Although a branch office or a representative are not permitted to go beyond the above activities but a branch office is in principle authorized to carry out all of the above activities while representatives must always check their 'representation contract' to verify the scope of the authorities delegated to them by the foreign company before conducting any activities.

Whom they represent?

A branch office and a representative are two different legal forms of presence of a foreign company in Iran. What is the meaning of 'foreign company' under the laws of Iran? Definition of this term can be inferred from Article 131 of the New Commercial Code of Iran: A legal person shall be considered non-Iranian if it is not incorporated in Iran. In other words, a foreign company is a company that is incorporated outside Iran. Article 133 of the same Code adds that Iranian legal persons shall not situate their domicile out of Iran but this does not necessarily mean that foreign companies cannot situate their domicile in Iran.

Registration of branches and representative offices

Under Article 638 of the New Commercial Code, foreign companies that are legally incorporated in their country of origin may establish a branch office or may appoint a representative in Iran. To establish this fact, foreign companies must submit to the Office of Companies Registrar (the OCR) certified photocopies of their articles of association, notice of incorporation, and the last changes in the company registered with the authorities concerned.

In the next step, the following documents must be submitted to the OCR for registration of a branch office:

1. Registration application in writing to be submitted by the foreign company;
2. The last confirmed financial report of the foreign company;
3. A feasibility study in which the following pieces of information are included:
 - a. Information concerning activities of the foreign company;
 - b. A description of the reasons for registration of the foreign company in Iran;
 - c. A description of the type and the scope of authorities and the place of operation and business of the branch office of the foreign company in Iran;
 - d. An estimate of the required local and expatriate work force; and
 - e. The manner of procurement of the funds in Rials and in foreign currencies required for running the affairs of the branch office.
4. Presentation of a letter of support from a government entity in case the branch has been set up for implementation of an agreement between the foreign company and that entity;
5. The Statement and Certificate of Registration duly filled in and signed by the company;
6. A Letter of Authorization given by the foreign company to its principal representative(s) in Iran; and
7. A Letter of Undertaking whereby the foreign company undertakes to wind up and close down its branch office in Iran if the activity permit given to the branch office by the Iranian authorities is revoked and cancelled.

For registration of a representative, the following documents are required:

1. Documents pertaining to identification of the applicant for representation, namely personal ID card, place of residence, etc. and for legal entities: articles of association, official gazette pertaining to establishment of the foreign company and its latest changes;
2. Presentation of the past record of activities of the representative in respect of the works to be carried out under the representation contract;
3. Report on activities of the foreign company and reasons for its representation and a letter of authorization of the principal representative(s) of the foreign company;
4. The last audited fiscal report of the foreign company;
5. Certified copy of the representation contract;
6. Background information as to activities foreseen in the contract; and
7. A letter of support issued by the Ministry concerned if the contract is concluded with a government entity.

At the end of the registration process, the OCR issues a permit that authorizes the branch office or the representative to start its activities in Iran under the conditions determined by the Iranian authorities.

Control of branches and representative offices

Iranian authorities exert their control over the activities of branch offices through different controlling mechanisms including the reports that must be submitted by branch offices, the inspectors who work inside the branch offices, and the exclusive codes attributed to each legal entity in Iran.

Branch offices must submit the following three reports to the Iranian authorities:

- a) Annual report on the principal company including its annual fiscal report audited by independent auditors in its country of origin;
- b) A report on the branch office activities in Iran together with audited account statements to be submitted within four (4) months starting the end of each fiscal year. It must be noted that standard audit systems like GAAP are accepted and recognized by the tax authorities of Iran; and
- c) A tax audit report prepared by official accountants and audit firms that are members of the Official Accountants Society that must be submitted to the Tax Affairs Office (“the TAO”). The TAO will accept the tax audit report without investigation and will issue the assessment notice according to the regulations. The tax audit report shall be accepted if the taxpayer meets the following conditions:
 - 1) to attach to the tax audit report its financial audit report that is drawn up by the same official accountant or audit firm in accordance with the accountancy standards, and
 - 2) to submit the two documents simultaneously with its tax return, or within a maximum time limit of three months from the expiry of the deadline for filing of tax return, to the respective TAO (Note 1 of Article 272 of the Direct Taxation Act).

Apart from the above mechanism, a branch office or a representative can also be controlled through statutory inspectors to be appointed under the Act on the Use of Iranian Association of Certified Public Accountants from among the auditing firms that are members of the said association.

Finally, according to Article 136 of the New Commercial Code, the OCR shall attribute an exclusive code to each *legal person* registered in Iran. All of the branch offices and some of the representatives registered in Iran are legal persons. Consequently, the OCR can exert its control over the activities of the branch and the representative offices through the information that it gathers about them before, during and after issuing exclusive codes in their name because all the branches and the representative offices must indicate this code on all of their documents, announcements, publicities, writings, etc. In case of failure in respecting this duty, branches and representative offices shall become subject to payment of fine.

Putting an end to activities of branches and representative offices

Winding up and liquidation of branches and representative offices: Activities of branches and representative offices start after their registration by the OCR that is sometimes based on issuance of a permit by the concerned Ministries. Their activities come to an end when the permit is revoked by the same Ministries and the branches or the

representative offices start the process of winding up and liquidation. It is evident that the concerned Ministries revoke the permit where the branches or the representative offices violate the conditions under which a permit is issued. For example, if they start to carry out an activity which is beyond the seven activities stated by Article 1 of the Executive Regulations, then the Iranian authorities can revoke their permit.

Termination of representation contract: A representative office may also apply for winding up and liquidation when the principal company terminates the representation contract. As a result of this termination, the representative can no longer act on behalf of the principal company. In that case, its existence becomes meaningless and it will have to apply for winding up and liquidation, if it is a legal person.

Under Article 135 of the New Commercial Code, winding up and bankruptcy of non-Iranian legal persons shall be subject to their *lex domicilii*.