CHAPTER VII

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The international flow of capital has facilitated development of the world's natural resources and has been instrumental in transmitting the direct effect of the industrial revolution from one region to another. A number of presently more advanced countries owe a good deal of their earlier industrial development to the influx of foreign capital. In fact, nearly every developed country had to rely on external sources to supplement its own meager savings during the early stages of its development.

Foreign capital combined with skill and enterprise is essential for the development of economic potentialities in under-developed or developing regions where the opportunities for the accumulation of capital are unequally distributed.

"Attraction of foreign capital inflow can contribute for generating a self-sustaining rate of economic development, by boosting the rate of capital formation and increase in the productivity of labour".1

The external assistance by bringing-in technical experts and technical know-how, can bridge the gap between the need for, and supply of, technical knowledge as well as trained personnel to carry through the programmes of industrialization. "External assistance has a vital role in supplying to under-
developed countries the fruits of years of scientific and industrial research, accomplished by the older industrialized countries"².

Moreover foreign aid makes it possible to run a deficit in the balance of payments, caused due to the import of capital goods and other equipment required for strengthening the industrial structure and enables to plan for quicker development without the inherent inflationary pressures of the developmental outlay.

Different countries are at different stages of economic developments; some are more profusely equipped with savings available for investment while others have large and more urgent opportunity for the profitable investment of savings.

The factors which have shaken the confidence of foreign capital in Iran was the formation of the centre for the attraction and protection of foreign investment in Iran (CAPFI) during the year 1962. The organization for the attraction and protection of foreign capital investments in Iran is comprised of the following organs;³

1. The centre for the attraction and protection of foreign capital investment in Iran, acts as an investigative, coordinative, and executive body. All applications or inquiries for capital investment must be submitted to this centre and the centre will, on request, furnish needed information on capital investments in Iran.
2. The permanent committee, the main function of which is to make initial studies on investment projects and to carry out the required formalities in the ministries and in Governmental organizations. The members of this committee are from the:

   a - ministry of foreign affairs,
   b - ministry of Economic affairs and finance,
   c - ministry of Labour and social services.
   d - The plan & budget organization.

3. The foreign investments board (also termed the supervisory board), in which was vested the final decision on the import of capital and authorization for the use of the facilities of the law concerning the attraction and protection of foreign capital investments in Iran. The members of the board are:

   a - Governor of Bank Markazi Iran (Central Bank of Iran), as Chairman of the Committee (Board).
   b - Deputy Chairman of Economic Affairs and Finance.
   c - Deputy Chairman of Foreign Affairs.
   d - The General Manager of Plan and Budget Organization or one of his assistants.
   e - President, Tehran Chamber of Commerce or one of his Vice-Presidents,
   f - Head of the Exchange Control Department.
During the years 1955-1961, there was some streamlining of the procedures relating to foreign investments in Iran. In order to minimize the delay in processing and deciding on applications for foreign collaboration the CAPFI is empowered to deal with all matters relating to private foreign investments and collaboration." The centre has set up the ownership of the foreign equity investments to the maximum minority ownership of 49 per cent. However, exceptions were made for the firms established earlier, or those with unusual product lines. Moreover, foreign firms with exceptionally favorable export prospects have received special treatment in terms of their equity ownership".

Among these, the contributors to agricultural activities, or firms with very specialized technologies received special treatment in terms of majority ownership; among such firms, those in pharmaceuticals, agriculture and petrochemicals are most notable. In addition, the market condition for certain industries has also been another criterion for rising the relevant share of foreign firms, in order to limit the monopolistic market position of the particular firm, and meet the ever increasing demand of the society.

In 1975, "the maximum foreign ownership share was lowered to 20-25 percent for the light manufacturing industries and to 35 percent for heavy industries, but exceptions were maintained for the needed and basic industries such as petrochemicals"."
The Government's main concern was now changed. It aimed to increase in the number of technical agreements for the transfer of technology in the form of adoption of training programmes at both the technical and managerial levels that has become as an important aspect of foreign participation in the Iran's economy.

The aim of Iranian Government in regard to foreign investment was to provide overseas companies with attractive inducements to invest; and once an undertaking has been initiated, to foster its growth and furnish it with the same and complete legal protection which was granted to any domestic company. In the year 1955 the "Law for the attraction and protection of foreign investments in Iran" was passed with the objectives, to encourage foreign participation particularly in the industrial sector and to safeguard the interests of foreign firms.

Article 1 of the regulations implementing the law for the attraction and protection of foreign capital, states that any real or legal person and or any firm, transferring capital to Iran for Development, Productive, Industrial, Mining, Transport or Agricultural purposes and subsequent activities, or for granting credit and financial assistance to Iranian firms engaged in the said enterprises shall enjoy privileges of the above mentioned law, provided that:

a - application to invest is submitted for a field open to local private firms.
b - The investment does not involve any monopoly rights or special privileges.

c - The capital is privately owned without any foreign Government participation.

In addition to the foregoing type of enterprises, foreign banks or their branches in Iran, in accordance with relevant rules and regulations, shall enjoy the protection of the law. If, in the course of operation, a foreign government comes to share in the imported capital in any manner, the said capital should, within a period prescribed by the board, be repatriated from Iran.

The productive and development enterprises must be:

1. - Activities which help to raise the production level and income of Iran.

2. - Directly or indirectly earn foreign exchange.

3. - Effect an economy (savings) as in import substitution cases.

Government Guarantees:

Under article III, IV, V and VI of the law, the Iranian Government commits itself to the full protection of all foreign investments approved under the investment law. The Government guarantees fair compensation in the unlikely events of promulgation of special legislation depriving the owner of the capital from ownership. The owner of the capital is permitted to
export every year the net profit derived from the investment of his capital in Iran in the same currency as originally imported. Transfer abroad of this original capital and accrued profits, or the balance of such capital and profits remaining in Iran, is permitted subject to three months notice to the foreign investment board. The owner must retain in Iran, for six months, at least ten percent of his original capital to meet his contingent obligations. Formally this law, like most in Iran and throughout the world, applies to firms and nationals of such countries where economic activities and reciprocal facilities for Iranian firms and nationals are made possible, i.e., known as reciprocal treatment.

Kinds of Foreign Capital Investments:

The foreign investments law defines the foreign capital as the following denotations:

1. Foreign exchange imported into Iran through authorized banks.

2. Machinery, machine tools, spare parts and raw materials as well as other requirements of this type provided they could be currently used and the supervisory board recognizes their suitability as such. Tools and spare parts shall be related to the factory machinery which is imported as capital; their importation may be simultaneous with that of the main machinery or subsequent thereto and provided that if imported later, they form part of goods specifically imported as capital, and not as current expenditure.
3. Means of transportation; land, sea or air used in the execution of the project for which capital has been imported.

4. Patent rights, provided they are related to and part of productive operation for which the application for the import of foreign capital has been made and that is assessed at the discretion of the supervisory boards.

5. Technical staff salaries in foreign currency, which paid before the commencement of actual exploitation for the purpose of setting up productive enterprises.

6. All or part of net profit accrued in Iran, and added to the original capital, or invested in some other enterprise covered by the provision of the law concerning the attraction and protection of foreign investments.

The importation of capital following approval of a new investment must be undertaken in accordance with the provision detailed in articles 6 through 13 of the regulations implementing the law. The cash capital which is transferred to Iran in a lump sum or in installments and is converted into Iranian rials should be in foreign currencies acceptable to bank Markazi Iran (Central Bank). Upon receipt, it is then registered in the investor's name. The conversion of foreign exchange transferred to Iran into rials shall be at the prevailing commercial buying rates on the date of the filing of the application for conversion.
The foreign investors are not bound to convert all of their capital into rials. According to article 10 of the law, the foreign investors can employ any amount of foreign exchange deposited with the central bank of Iran and not converted into rials for his imports from abroad or for other necessary expenditure incurred for purposes which investments has been approved. Such expenditures obviously, shall be included in the total amount invested.

The foreign investor is entitled to insure the capital which he imports into Iran. The insurer should be a foreign government insurance institution and the said institute, as a result of an accident, replace the investor in accordance with the provisions of the insurance policy. This replacement does not constitute a transfer of capital.

According to article 7, the investor who acquires a license shall, within a maximum of 18 months after the receipt of the said license, start basic operations as regard the importation of an appropriate capital, in case of failure his rights to the license will be forfeited.

Within a period of time fixed with the agreement of the supervisory board the investor holding a license submits a detailed list of the machinery and equipment to be shipped to Iran to the said board, accompanied by a price list. Upon examination and approval of the said lists, the board shall
issue the relevant permission for the importation of capital in question to the foreign investor or his representative. Prior to commencing the project, a license should be obtained from the relevant ministry.

**Foreign Exchange:**

In view of the fact that a foreign investor must adhere to the legislation covering foreign exchange when importing the various materials required in his operation, there are certain conditional sections of the law. According to article 2(b) of the regulations all machinery considered to be part of a foreign investment shall enjoy the relevant protective regulations. There are, however, also certain means and machineries which are not part of the capital and which have to be included in the current expenses of the company.

To import such means and machineries, the foreign investor is subject to the general regulations which allow him to buy foreign exchange for such importable commodities. Foreign exchange regulations do not permit Iranians and foreigners to engage in foreign exchange transactions; however, under certain conditions any person can maintain a foreign exchange account with the authorized banks. Utilizations of such accounts can be made only with the approval of the foreign exchange control department upon application through the centre.
Conversion of rials to foreign currency as payment for imports is permissible. Foreign currency needed for traveling abroad as well as other currency requirements is effected in accordance with the instruction of the foreign exchange control department.

Exporters are legally bound to surrender all foreign exchange accrued from their exports. To guarantee such performance, exporters sign an official foreign exchange undertaking, violation of which renders the exporter liable to pay a penalty up to 50% in addition to the total of his foreign exchange undertaking in rials.

Repatriation of Profit and Capital:

When a foreign investor wishes to send abroad the net profits derived from his investment, he must, according to article 13 (a) of the law, submit an annual balance sheet and profit and loss statement to the center for the attraction and protection of foreign investments. Upon its examination by the center with a view to determining the amount of yearly profits. On approval by the center and foreign exchange control department, a license shall be issued for the transfer of the net profit in its original currency, provided the relevant taxes and duties plus statutory reserves are deducted first.

In case the central bank of Iran experiences foreign exchange shortages and cannot permit any exchange transfers
abroad, the foreign investor can export an equivalent amount of authorized goods without giving any foreign exchange undertaking.

If a foreign investor desires to repatriate abroad all of his investment under article 5 of the law, he must prepare his balance sheet at the conclusion of his activities and submit this to the centre, including notice prescribed in the article. After the centre has studied the matter, it will submit the case to the supervisory board for issuance of license. The board shall approve the transfer of the foreign exchange. The transfer must be effected within a period fixed in the license. This period shall not, in ordinary cases, exceed three months. However, in case where the amount of capital to be transferred is of such magnitude that it could cause a disturbance in the foreign exchange position of the country, a longer period may be fixed. In any event, the annual transfer of capital abroad shall not be less than 30 percent of the total investment.

Contracts conducted by Investors:

Attention must be paid by foreign investors in concluding contracts for the payment of technical services, royalties and patent rights. The centre is authorized to make suggestions concerning the proportion of payment to be made for technical services and royalties, with due consideration to the productive activities to be pursued by the foreign company.
Since the basic responsibility of the CAPFI is to render guidance and supervision; the contracts which were to be concluded with Iranian companies and foreign nationals shall be submitted to the CAPFI for legal examination and to provide facilities in the transference of foreign currency.

Specially, in contracts concluded between, Iranian firms or real or legal entities (Govt. or private) with foreign contractors, consulting engineers or specialists involving payments in foreign currency the following points must be observed*

1 - Subject of the contract shall be separately appropriated and dealt with, without mentioning of agreed payable amount in foreign currency.

2 - After deduction of Government taxes and dues, 50 percent of the salaries and fees payable to foreign staff, specialists, and consultants whose employment in Iran has been considered necessary by competent authorities, shall be transferable in foreign currency.

3 - Subsequent to deduction of relevant taxes and dues, fees payable for preparation of plans, projects, studies and services in general, accomplished outside the country according to the contract terms, are wholly transferable in the appropriate currency. In such cases, statements of accounts supporting foreign exchange application shall officially certified by competent authorities in the contractors country and in Iran.
4 - Payments for imports of authorized goods required for execution of a contract which cannot be supplied in Iran at reasonable terms shall exclusively be affected through opening of documentary letters of credit against collection bills received through authorized banks. The central banks does not ordinarily permit such payments to be made in foreign exchange against collection drafts.

5 - Profit accrued by foreign firms under contract with Iranian Government agencies are transferable in foreign currency subject to the certification of the Government agency concerned, after deduction of taxes and dues; provided the said firms are centred abroad and are of foreign nationality.

6 - In general, in all cases where contracts involve payment in foreign exchange, the investor must notify the foreign exchange control committee of the central bank of Iran to obtain their prior concurrence.

From 1960 onwards, Government also followed unobstructed policy that was known as the Laissez-faire ('open-gate policy'). According to this policy, excepting a few strategic goods pertaining to food stuffs (i.e., reserved by Government), all other needful can be imported by any private sectors without any Government control.

In this regard Government approved a bill in March 1961 in which article I of the bill states that; for the
procurement of required necessities of the country, import of foreign goods which has no equivalent in the Iranian market were allowed and unrestricted and need not be conformed by the Government. The only exception was for the goods which were recognized as harmful to hygiene and moral character and are anti-social.

In 1973 the Iranian Government adopted other certain other policies to encourage the foreign investments in Iran for the stimulus improvement of the economy in general and better utilization of foreign productive and technological resources in the development of industrial infrastructure, in particular. "In aiming for these primary goals the specific policies to attain the above objectives were".

A - To eliminate domestic shortages and reduce inflationary pressures, with greater emphasis on imports of consumer, capital and intermediate goods, on the most favourable terms possible. For the implementation of the above, Government was set to revise regularly tariff, commercial benefice, tax and other limitations on the import of goods, so as to lower the price and facilitate imports of goods required. Moreover, government intended to reduce the country's reliance on import of strategic goods from a limited number of markets by establishing links with numerous markets and creating alternate ties with the countries that supply Iran's import requirement.

B - To create national wealth and acquire greater income from foreign investments. In doing so, Govt. approved to
invest in projects for the exploitation of natural resources, including ocean resources, by investing in mining, agriculture and fisheries projects and participate in investments in industrial projects in developing countries by acquiring share holding by means of granting loans on international terms.

C - To make use of the most suitable technology and skilled manpower available abroad for the development of the domestic economy. In this regard government was recommended to encourage direct foreign investment in industries involving monopolistic techniques, and continue economic relations with international finance agencies so as to acquire technical co-operation and skilled manpower. In addition, to overcome the shortage of skilled manpower for specific purposes in limited time periods by obtaining such services from abroad, and train technical and vocational specialists by sending trainees abroad and utilizing services of foreign instructors in Iran on a short-term basis. Government was also to encourage Iranian specialists and experts residing abroad to return to Iran by providing them with guidance and creating favourable conditions for their participation in the domestic economic activities.

Another notable adopted policy of the Government was to establish a free foreign exchange market in Iran so as to expand the volume of foreign exchange dealing, to substitute the requirements of the private sector and foreign investors for imported capital by providing loan facilities on normal terms from the governments foreign exchange reserves.
CONCLUSION

The policies of the Iranian Government have been set up to protect and safeguard the foreign capital investment in Iran.

The provisions of the '1955 Law' assured and advanced the foreign contribution, through the Governments guarantee, for repatriation of profit accrued and capital invested. To implement the above, Government has established a "Centre For The Attraction And Protection Of Foreign Investment" to approve the foreigners proposal under the appropriate foreign beneficiaries law in which the foreign investors allowed maximum minority shares of 49% in equal status with the private domestic (Iranian) investors.

However, the empowered centre rolled as an effective element and gradually adjusted the contribution of the industrially advanced countries in the Iranian industrial infrastructure.

Further, the Government demolished the hidden restrictions and limitations of the already existed policy (of 1955) i.e., the import of the specific capital in the form of the machinery and equipments for the assigned activities, under the 'Laissez-faire' of 1961. Adoption of all these foreign favoured assumptions, successfully resulted in soughing the confidence of the foreign investors and consequently the accumulation of foreign private capital investments in the Iranian economy. As
the foreign participation enhanced from 18 firms, with Rls 459.0 millions in 1962 to 162 firms with Rls 21947.0 millions in 1974.

However, the latter policy, i.e., policy of 1973, restrained the foreign ownership to the extent of 20-35 per cent and enacted as a limiting factor to influx the foreign entrepreneurs and investors in the Iranian industrial activities. This has been done due to the fact that, Iran was no more in need of foreign currency on account of its hard currency earner (oil export). Further, in the fitness of things and better competitive efficiency of the foreign based firms as compared to domestic firms, which were lacking in techniques, traditions, organization, by un-unique trained and skilled personnel, Government enacted certain policies (of 1973,c and d) to encourage foreign contribution in the pre-determined fields, due to urgent need to push ahead with the fifth national development plan. In these remedial policies the Government favoured the foreign entrepreneurs that employed in transfer of technology in the form of technical know-how and training of the Iranian personnel.

SUGGESTION

Thus all the above discussion leads one to suggest that, the Government has to take certain steps and provide a clear-cut guidelines for the foreign private enterprises. The Government would have to draw-up a perspective plan and identify as to where foreign investments are necessary; where
the technical collaboration with foreign assistance is needed; where foreign investments and technical assistance/consultancy are considered necessary and the areas for key projects.

Further, as almost all the MNEs in Iran are the producers of the final products and are undertaking the final stage of their production in Iran (mainly in the form of assembly operations with small value-added), therefore, the Government shall put emphasis on the intermediate industries, thereby it can raise the value-added to the Iranian economy and provide the training opportunity also to the employees in Iran.

For the awareness in the marketability and assurance of the standard of MNE's production in Iran, the Governments policy may be framed to insist that, a part (e.g., 25%) of the repatriation of the profit from Iran by the MNEs should involve their own production. Moreover, while entering into an agreement with the foreign enterprises, it is to be consider that, the offered shares to the total individual company in the particular field of industry shall not be implemented to influence the political and economic conditions of the country.

Iranian basic and key industries should not be permitted to have foreign capital, as they may create uncertainty to the economy of the country in the critical situation and conditions of hostilities.
References:


2. Ibid, P.265


5. Ibid, P. 18


7. Central Bank Of Iran, Opcit, P.12

8. Ibid, P. 13

9. Ibid, P. 14

10. Adeli Mohammad, "International Economic and Foreign Trade Policy of Iran", Extracurricular unit of cultural section of Jihad University, Tehran, Iran, 1986, P.150

11. P.B.O., "Iran's Fifth National Development Plan (Revised), PBO Publication, Tehran, Iran, May 1975, PP.23-27