

Solving national ownership restrictions in Iraq

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Investors wishing to have a local footprint and operate in Iraq are sometimes faced with national ownership requirements and other legal restrictions. The natural solution to such problems is engaging local partners or nominees. In this Article we will assess and compare the two different approaches.

Doing business with local Iraqi partners



Iraqi partners may be engaged through incorporated or unincorporated joint ventures. Incorporated joint ventures can be set up through establishing a company in Iraq or establishing a branch of a foreign entity. Company law No 27 of 1977 ('Company Law') with the amendments applicable in federal Iraq requires 51 per cent Iraqi ownership. Unlike Iraqi companies, branches of foreign companies do not suffer from the same limitations because they are governed by the law of their home jurisdiction. However, branches can only be established in federal Iraq if the parent company is at least two years old.

The semi-autonomous region of Kurdistan in north Iraq has not legislated the same amendments to the Company Law as those applicable in federal Iraq. Therefore, there is no 51 per cent Iraqi ownership requirement in Kurdistan. Companies registered in Kurdistan can only open branches in federal Iraq if they meet the federal requirements. However, companies registered in Kurdistan are still considered Iraqi nationals and are able to fully own subsidiaries in federal Iraq if the federal Registrar of Companies is satisfied that they meet certain conditions.

In both federal Iraq and Kurdistan, the Company Law makes it difficult to separate management rights from ownership stakes. There can only be one class of shares and each share must have one vote. Shareholder agreements are considered amendments to the articles of incorporation and for this reason must be registered. However, the Registrar of Companies in federal Iraq and Kurdistan are not familiar with shareholder agreements and registering them would be difficult. If more control is desired the solution would be an unincorporated joint venture. Iraq does not have detailed rules governing partnerships and there aren't many mandatory restrictive rules applying to unincorporated joint ventures. In addition, non-Iraqi law may be chosen to govern the joint venture/partnership agreement.

The main advantage incorporated joint ventures offer is limitation of liability, often to a set amount of

share capital. The main disadvantage of incorporated joint ventures is that they are costlier to set up and take longer than an unincorporated joint venture would. In comparison, unincorporated joint ventures offer more flexibility than their incorporated counterparts without the added costs. The trade-off is that an unincorporated joint venture agreement can only allocate liability between the partners; it cannot limit liability towards third parties and in some cases cannot avoid joint liability towards third parties.

Appointing nominees or trustees in Iraq

Nominees are more appropriate than partners in situations where full control is desired, or the Iraqi party is to receive a fixed remuneration without sharing in risks and profits. However, trusts and other nominee agreements are often viewed as violations of mandatory legal requirements and are often not drafted in a manner that can be presented to authorities as a recognisable legal concept under Iraqi law. In this context, trusts are also often confidential and contrary to what is declared to the public, thereby adding a further layer of difficulty in proving the arrangement and enforcing the intended results. Fortunately, Iraq does not have an anti-fronting law explicitly invalidating trust or nominee agreements. In addition, Iraqi law contains a legal concept that is functionally similar to a trust, called Waqif.

Waqifs, which some historians link to early common law trusts that were first developed in the crusades, are a Sharia Law concept that separates the beneficial interest in a given asset from the legal title. A Waqif has a manager who has a very similar role to a trustee and also has a beneficiary much like trusts do.

Waqifs in Iraq are traditionally used for charity and estate planning. However, there is no reason preventing their adaptation to commercial purposes in a corporate context. A Waqif under Iraqi law is a right in rem much like other in rem rights short of full title and ownership. Therefore, it would be possible to create a Waqif over a company's shares in the same fashion they would be pledged as a security. Even though it is not a validity requirement, the Waqif instrument may also be filed with the Registrar of Companies much like a pledge of shares would. The Waqif instrument would govern how dividends and voting rights would be applied as they are benefits of the shares put in Waqif. A Waqif can effectively be a nominee arrangement that has some foundation in Iraqi law, and it would not have to be done in secret making it easier to prove and enforce.

Like some common law trusts the owner of the assets to be put in a Waqif cannot amend or revoke the Waqif after it is created, and if no beneficiary can be found in the waqif instrument, then mandatory Cypres rules allocate the waqif property. However, this is where the similarities end. There is no rule against perpetuities in Iraq and some Waqifs have been in existence for hundreds of years. This is an advantage for our purposes because juridical persons are also perpetual and the Waqif would be valid for the lifetime of the beneficiary.

Courts of personal status would have jurisdiction to hear disputes of Waqif matters however they are not particularly adept at solving commercial disputes. Luckily, Iraqi law does not prohibit agreements to arbitrate Waqif disputes and an arbitration clause in a Waqif instrument would be valid. Another important consideration to bear in mind is that Waqifs are a Sharia Law concept and Iraqi law considers the rules of Waqif to be public policy and does not allow derogation from them. Sharia Law is not codified in Iraq and there are not many restrictions in Sharia Law jurisprudence that would cause problems for a Waqif in a commercial corporate context. Therefore, Waqif has the potential to be an enforceable nominee instrument but if drafted badly it would operate in a legal vacuum. The solution is to sufficiently identify an adequate source of Sharia Waqif Law that would be consulted in the case of a dispute and provide for a supplement such as the jurisprudence of modern UK English trust law to ensure a result would be reached if no precedent is found in Sharia Law.

Conclusion

Working with local partners, if possible, is the preferred approach. Incorporated joint ventures offer limitation of liability but are costlier to set up in terms of time and money; in particular if ownership stakes do not reflect management rights. Unincorporated joint ventures such as partnerships offer more flexibility and are easier to set up but they do not offer limitation of liability. If engaging Iraqi partners is not feasible or desirable, Iraqi law offers some tools to set up Waqifs which are similar to trusts. However, they have not been tested in a commercial context.

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