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# **Trading with Iraq**

by

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## Trading with Iraq

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Since the imposition of sanctions against Iraq pursuant to the U.N. Resolution no. 661/1990, all types of trading with Iraq are restricted and are subject to the U.N. procedures and the approval of the Sanction Committee, which was set up by the said Resolution. However, the business generated by the large oil revenues of Iraq and the U.N. Oil for Food Programme is very substantial, and has raised considerable business interests as well as legal questions.

In general, foreign companies may use or establish any of the following business entities to trade with Iraq, and would be advised to invest some time and money in order to identify the appropriate market structure suitable for their business with Iraq.

With this purpose in mind, I shall attempt to present in this article an outline of the U.N. Oil for Food Programme first, and shall highlight the main aspects of the following types of business entities which a foreign company may consider to use when trading with Iraq:

- Supply and Export to Iraq
- Commercial agencies
- Branch Office
- Representative Office
- Foundation of a company or a joint venture

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## **I) U.N. Oil For Food Programme**

After the imposition of the comprehensive economic sanctions against Iraq, many international organisations as well as UN personnel reported that Iraq was facing a human catastrophe, and in view of those reports the Security Council adopted in April 1995 the Resolution no. 986, establishing the so called "Oil for Food Programme". Under this and subsequent UN resolutions Iraq was allowed to sell a limited amount of oil in every 180 days period. The ceiling on the oil sales was gradually eased until it was completely lifted by the Security Council Resolution no. 1284 of 1999. The proceeds of the sales of oil are deposited in a UN escrow account strictly controlled by the UN, and are used to cover the costs of humanitarian goods and certain spare parts exported to Iraq subject to detailed and complicated procedures set out by the UN.

In fact, only 72 % of the oil revenues is used for the Oil for Food Programme after deducting 25 % of the revenues to pay the UN Compensation Commission, which was set up by the UN Resolution no. 692/1991 to process claims resulting from the Gulf War. Also, another 3 % is deducted from the oil revenues to cover the United Nations costs for administering the programme and for the UN Monitoring Verification and Inspection Commission (UNMOVIC).

In October 1997 the Office of the Iraq Programme "OIP" was established at the headquarters of the UN to implement the Oil for Food Programme, and to process applications for export to Iraq of food and humanitarian goods. The procedures for exporting goods to Iraq may be summarised as follows:

The Government of Iraq periodically prepares lists of humanitarian goods classified according to sectors, such as food, medicines, and agriculture, which Iraq requires to import. These lists are submitted to the UN Secretary General for approval subject to the various resolutions of the Security Council. Contracts for export to Iraq may be approved only if the goods contracted are included in the said approved lists.

The Iraqi governments ministries and companies conclude contracts directly with foreign suppliers and contractors. The state of the exporting company must submit an application for approval to the OIP together with copies of the relevant contract.

The applications are checked by the OIP either under the “fast track procedures” and approved or examined by experts in OIP and send to the UN Sanction Committee, which was established under the UN Resolution number 661/1990 for consideration. Experts in the OIP examine each contract and may request further information and decide whether the item to be exported are on the pre-approved lists or not, and accordingly inform the OIP. The Sanction Committee may approve or reject or put on hold the applications, and will inform the government of Iraq accordingly, and the UN Mission of the exporting state, as well as the UN Secretary General.

If the contract is approved, the Central Bank of Iraq will request the bank holding the Iraq UN escrow account to open an irrevocable, non-transferable, non-assignable letter of credit in favour of the supplier. The L/C is subject to the ICC uniform Custom and Practice for Documentary Credit.

The arrival of the goods supplied has to be confirmed by inspection agents appointed by the Secretary General before any payment is made out of the relevant L/C.

The chart attached to this article shows the steps followed under the Oil for Food Programme:

## **Fast Track Procedures**

In 1999 procedures called “fast track” were established by the UN Security Council Resolution no. 1284. According to this Resolution, the Sanction Committee was authorised to issue a predetermined list of approved food and humanitarian materials. Under the said Resolution 1284 the Sanction Committee has approved several lists covering different basic needs of Iraq. This list was subsequently extended several times to cover additional items.

The export of any such listed materials no longer requires the submission to the Sanction Committee for approval. Applications by the exporting state are made in the above mentioned manner to the Office of the Iraq Programme. This Office will determine whether the required goods fall within the approved lists without referring the matter to the Committee. But, the remaining procedures will remain applicable.

## **Resolution 1409**

Recently, on 14<sup>th</sup> May 2002, the Security Council approved a new Resolution no. 1409, extending the Oil for Food Programme for another 180 days, starting from 30<sup>th</sup> May 2002. The Resolution has laid down strict time limits during which each of OIP and the Sanction Committee as well as the applicant states must respond. On the other hand, the Resolution adopted 419 pages of lists of items called “Revised Goods Review List”, which the Security Council considers of dual military and civilian use. Although, the imposition of time limits is a positive step aimed at accelerating the process of approvals, the extensive lists of so called dual use items have tightened the economic embargo on Iraq, first because of the extensive nature of the lists and secondly there are many basic items which are essential for the humanitarian needs of Iraq, which in theory may have a dual use, such as optical and medical laser equipment and educational and agricultural items.

Under the said Resolution no. 409/2002, applications are submitted as usual to OIP for examination by the experts. After the registration of the applications, the contracts for export of goods are checked by the International Atomic Energy

Agency (IAEA), and the UN Monitoring Verification and Inspection Commission. If the goods are not listed in the aforesaid dual use lists, then OIP will issue an approval letter. But if the UN Monitoring and Verification Commission “UNMOVIC” or the International Atomic Energy Agency identifies any item of dual use, then the contract is forwarded to the Sanction Committee for a decision. Contracts containing any item of military use will be rejected.

## **Evaluation**

The UN procedures remain slow and subject to the political will of the states, members of the Security Council, and the Sanction Committee. As it was stated in the report of the OIP Executive Director, the Oil for Food Programme was never meant to meet all the humanitarian needs of the Iraqi people, nor can it restore Iraq’s economic and social infrastructure to a normal standard.<sup>1</sup> It is mainly a programme to feed 23 million people and provide partly spare parts and maintenance to certain oil and sanitary installations. In protest to the UN policy on Iraq, two UN appointed Humanitarian Coordinators for Iraq have resigned.

The Sanction Committee consists of the representatives of the states members of the Security Council. It is neither a judicial nor an independent body.

Each member of the Sanction Committee has a veto right to reject an application or place it on hold. Since December 1996 up to August 2002 the OIP received \$ 45 billion worth of contracts, of which \$ 36,7 billion were approved. At that date and even after the adoption of the Security Council Resolution 1409 in May 2002, there were more than 1664 contracts totalling \$ 4.3 billion delayed and put on hold mainly due to the objections of the representative of one state in the UN Sanction Committee. The Executive Director of OIP has several times expressed his concern and appealed in his reports to the Security Council to reconsider the contracts on hold.<sup>2</sup>

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<sup>1</sup> See the Executive Director of OIP Report to the Security Council dated 21.05.1999

<sup>2</sup> See the Executive Director of OIP Reports to the Security Council dated 26.02.2002 and 20.04.2000

## **II) Supply and Export To Iraq**

As stated before, foreign suppliers may conclude directly contracts for supply of goods and materials with Iraqi government departments.

Iraqi law does not require a foreign supplier to appoint an Iraqi agent or have a business presence in Iraq for the purpose of exporting goods or materials to Iraq. In this respect it is worthwhile to mention that supply contracts are not subject to Iraqi income tax unless the contract includes maintenance or installation works. In such cases where a contract consists of works to be carried out in Iraq, foreign contractors are advised to divide the contractual works into two contracts, one for supply of materials and a second contract for maintenance and installation works. In this case only the work contract would be subject to taxation excluding the value of the supply contract.

Government invitation for suppliers are normally announced through international tenders, and in few cases direct invitations by government departments are made to foreign suppliers for specific products. Therefore, it is advisable to contact government agencies and register directly and make representation in advance with the hope to be invited in the future. Tendering, evaluation of tenders, and award of contracts are subject to special regulations issued in 1988 by the Ministry of Planning. Iraq has not enacted a Tendering Law as in some Arab countries, but the said Regulations of the Ministry of Planning are intended to cover the same issues and more.

## **III) Commercial Agency and Distributorship**

Commercial agencies and distributorship are governed by the Iraqi Civil Code as well as by the provisions of the new Iraqi Commercial Agencies Law no. 51 (the Agency Law) which was enacted in the year 2000. The Agency Law is applicable to all types of commercial agencies and distributorships. Therefore, references to agents and agencies shall include distributors and distributorship. The Agency Law is not comprehensive and has left a number of issues such as

termination and exclusivity to the agreement of the parties and to the relevant provisions of the Iraqi Civil Code, which are supplementary to the Agency Law.

### **Role of the Agent**

The role played by the agent in Iraq is less significant if compared with the role of the agent in many Arab countries, for Iraqi law does not require the appointment of an agent as a precondition for participating in government tenders or registering a branch office as required by the laws of most Arab Gulf States<sup>3</sup>. On the contrary, the Iraqi law prohibits or restricts using agents or sponsors for government contracts and projects.

However, the selection of an agent or a distributor demands a careful consideration and caution, because there are many in the Middle Eastern market who may pretend that they have the highest contacts in the country and will guarantee you big contracts, without actually having the right qualities and influence in the market.

The choice of an agent is more important in Arab countries where an agency or distributorship agreement is treated as a “catholic marriage”. Unlike Iraq, termination of an agency agreement in the Gulf States, whether for a limited or unlimited period, entitles the agent to claim compensation. Also, the agency laws in most Gulf States stipulate that no new agency or distributorship agreement may be registered and recognised unless the existing agency agreement is terminated with the approval of the agent<sup>4</sup>. **In Iraq it is not so.**

Notwithstanding the limited role played by the agent in Iraq as compared to the role of the agent in the Arab Gulf States, the appointment of an agent in Iraq is a very useful tool to contact clients, to promote and introduce foreign companies to the market and to follow up projects and tender invitations issued by government agencies.

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<sup>3</sup> See for instance UAE Company Law no. 8/1984, article 314

<sup>4</sup> See for instance UAE Commercial Agency Law no. 18/1981, articles 8 and 9

## **Iraqi Civil Code no. 40 of 1951**

The Civil Code articles, 927 to 949, have laid down general principles on agencies, while the Agency Law lays down specific conditions for the appointment and registration of an agency or a distributorship.

Therefore, a short outline of the general principles of the agency under the Civil Code is necessary, because the said provisions are supplementary to the Agency Law.

The following are selected basic rules derived from the provisions of the Iraq Civil Code, which parties to any agency agreement should keep in mind:

### Limits of the Agency

As a general rule the authority of the agent is limited by the terms of the agency agreement, which he may not exceed. If the agent exceeds his authority, the principal is not liable unless he gives his consent<sup>5</sup>. The agent must regularly report to the principal<sup>6</sup>. He cannot appoint another agent unless expressly authorised to do so, as stated in article 939 of the Civil Code.

### Relationship between the Agent and the Principal

When the agent concludes a contract with a client or a third party, he acts either in the name of the principal or in his own name, and in each case a separate rule applies:

- a) If the agent concludes a contract with a third party in the name of the principal and within the scope of his authority, all the rights and obligations of the contract will revert to the third party<sup>7</sup>. Thus, the third party may claim directly from the principal.
- b) But, if the agent concludes a contract in his own name without disclosing the name of the principal, the third party has no direct recourse to the principal<sup>8</sup>.

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<sup>5</sup> Iraqi Civil Code no. 40/1951, article 933

<sup>6</sup> Ibid, article 936

<sup>7</sup> Ibid, article 942

<sup>8</sup> Ibid, article 943

In fact, the Civil codes of all Arab States stipulate that the agent must name the principal, so that the principal and the third party have a direct relationship.

### Standard of Care Required by the Agent

Regarding the liability of the agent and the required standard of care, the agent or the attorney must exercise the care of an ordinary person in case of agencies based on fees or commission. If the agency is without remuneration, then the standard of care required from him is legally different, and the agent has the legal duty to exercise the same standard of care as he does in his own affairs<sup>9</sup>.

### Termination

As to termination, article 946 of the Iraqi Civil Code stipulates that an agency terminates when:

- a) the work subject of the agency is completed. For instance, if the agency agreement is for a specific project the agency agreement is deemed terminated upon completion of the project.
- b) when the date of the agency is expired. Therefore, any agency agreement concluded for a certain period is deemed terminated by the end of the period.
- c) when the agent or the principal dies.

Neither the Agency Law nor the Iraqi Civil Code contains any provision which gives the agent a general right to claim compensation in cases of termination of an agency, except that article 947 of the Civil Code grants the agent the right to claim compensation if he suffers damages as a result of termination made in an “improper time” and without justified reason, and provided that the agency is for remuneration<sup>10</sup>.

The expression “improper time” is not defined, but may be understood to mean termination during the validity period of the agency or abrupt termination prior to accomplishing the subject or the purpose of the agency.

In cases where the agency or the distributorship agreement is for a limited period and the principal refuses to extend the agreement after having expired, the agent or the distributor would have no right of compensation under the Iraqi law on the

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<sup>9</sup> Ibid, article 934

<sup>10</sup> Ibid, article 947, paragraph 3

basis of the refusal to extend the agreement. However, a stipulation in the agreement that the agent is not entitled to claim compensation in any case would not, in my opinion, be enforceable.

In this respect, I would suggest to make the agency or the distributorship agreement limited by time and to stipulate in the agreement that the agent or the distributor must achieve a reasonable annual minimum turnover. Failing to achieve that would entitle the principal to terminate the agreement, and the agent would have no right to claim compensation.

## **Agency Law No. 51/2000**

### Scope of the Agency Law

The law applies to commercial agencies concluded between an Iraqi agent and a foreign person or company, excluding agency agreements between two Iraqi parties. The definition of the commercial agent is so widely laid down in article 3 of the law as to include any kind of agencies as well as distributorship agreements.

“Commercial Agency” is defined by the law as “any business activity performed by a person in Iraq in the capacity of an agent for a natural or juristic person outside Iraq whether it is a trade agency or commission agency or any other commercial agencies” which may be referred to in other laws.

Furthermore, article 8 of the Agency Law authorises the Company Registrar to consider “any commercial activity” as an agency, because the law aims to regulate and control all kind of agencies, and sponsorship activities. Consequently, the Registrar has in practice considered distributorship agreements as falling under the Agency Law.

### Qualifications of the Agent:

Article 4 of the Agency Law requires that the agent or the distributor must apply to the Company Registrar for a license to act as an agent or a distributor. In order to obtain the license, the agent or the distributor must satisfy the following conditions:

1. He must be an Iraqi person residing in Iraq, or an Iraqi company owned by Iraqi shareholders.
2. He must have a business office in Iraq,
3. and he must be a member of the Iraqi Chamber of Commerce. It follows that the appointment of persons living outside Iraq without any business presence in Iraq is not deemed to be an agency under Iraqi law.

The application to the Company Registrar must be made by the agent or the distributor himself. But, a foreign company may apply to the Company Registrar for the list of commercial agents who are already licensed by the Registrar<sup>11</sup>.

To undertake agency work without a license is a crime subject to imprisonment<sup>12</sup>.

Exclusivity:

The agency law does not contain any provision regarding commission nor any provision concerning exclusivity or none exclusivity, leaving these issues to the agreement of the parties. Thus, parties may choose to conclude an exclusive agency and determine the amount of the commission.

Finally, article 14 of the Agency Law distinguishes the agency law in Iraq from most other Middle East laws by stipulating that Iraqi government departments and companies must contact and negotiate directly with foreign tenderers and contractors and avoid the use of agents and sponsors.

#### **IV Branch Office**

As mentioned before, a foreign company which concludes a supply contract for export of products is not required to have a business presence or an agent in Iraq, but a foreign company which has concluded a construction or work contract with an Iraqi government agency or a public or a mixed sector company must register and open a branch office for the duration of the said contract. A branch office becomes however necessary to implement the contract, supervise local contractors, and local labour etc.

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<sup>11</sup> article 13 of the Agency Law no. 51/2000

<sup>12</sup> Ibid, article 15

The establishment of such branch office is obligatory to foreign contractors as well as sub-contractors<sup>13</sup>.

The Regulations for Branch and Offices of Foreign Companies and Foreign Economic Establishments no. 5 of 1989, hereinafter referred to “Regulations”, have laid down detail provisions for this purpose.

### **Applications to the Company Registrar**

In order to obtain the necessary license, a foreign company wishing to establish a branch office must, in accordance with the provisions of article 4 of the Regulations, submit a number of documents to the Company Registrar in the Ministry of Trade, including the following documents. These documents must be legalised by the Iraqi consulates abroad and translated into Arabic language.

1. A letter from the Iraqi client specifying the nature and main terms of the contract for which the branch office is to be opened.
2. Articles and Memorandum of Association of the mother company together with the Certificate of the company registration.
3. A notarised power of attorney for the Branch Manager, who will have to reside in Iraq<sup>14</sup>.
4. Balance sheet of the mother company.
5. Declaration of Israel Boycott.

Boycott declaration is required in Iraq in several instances including establishing a foreign branch office and in respect of government tenders. Foreign contractors and suppliers have to answer a number of questions as set out in a standard form concerning boycott of Israel. The company may be black listed, and its contract with the government terminated if the answers to the questionnaire are incorrect.

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<sup>13</sup> The Regulation no. 5 of 1989, articles 2 and 3

<sup>14</sup> Ibid, article 6

The Registrar issues a license, which has to be published in the Registrar Gazette and in one daily local news paper.

The branch office acquires a legal personality as of the date of its being licensed<sup>15</sup>, and its domicile will be deemed in Iraq, as provided in article 48 of the Civil Code.

The legal personality granted to the branch office allows the office to conclude contracts with local suppliers and labour, and to sue and be sued in Iraqi courts.

The branch office, subject to the provisions of the Company Law, must keep proper accounting books and submit an audited balance sheet to the Company Registrar. It may carry out any business activity within the scope of the contract for which the branch office was established, but no business activity beyond that is permitted<sup>16</sup>.

Upon completion of the contract, the branch office must be liquidated within 60 days from the date of the completion<sup>17</sup>. Any delay beyond the said period will expose the foreign company to a penalty of ID 1000 a day, as stated in article 213 of the Company Law no. 21 of 1997.

Liquidation of a branch office is a lengthy procedure, similar to the procedures of liquidating a company. An application for liquidation must be submitted to the Company Registrar, together with no objection letters from a number of government departments, including the Iraqi client, the tax office, as well as the labour and pension offices.

A question arises about foreign branch offices which were existing before the imposition of the U.N. sanctions and have never been liquidated. Would they be subject to penalties and liabilities for not observing the provisions of the Iraqi Laws and Regulations?

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<sup>15</sup> Ibid, article 5, paragraph 5

<sup>16</sup> Ibid, article 6, paragraph 3

<sup>17</sup> Ibid, article 15

In reality, the Iraqi government has not taken any action, and it has de facto frozen the application of the relevant provisions of the Company Law and the Regulations, leaving the whole issue for a legal solution after the sanctions are lifted.

In this respect it is worthwhile to mention that existence of a branch office or representative office of foreign companies is not as such prohibited by the national laws, as long as the offices do not conduct any business prohibited by the U.N. resolutions.

## **V) Representative Office**

Foreign companies which have no contract with an Iraqi government department may, in accordance with article 3 of the Regulations no. 5 of 1989 referred to before, open a representative office in Iraq. Such a representative office may act as a liaison office, collect information, make contacts, purchase tender documents. It is not entitled to carry out any commercial activity<sup>18</sup>. It is a non-profit and non-trading office, unlike the branch office. Though, the said Regulations do not require that a foreign company applying for a representative office must have a contract with government departments or companies, in practice the Registrar has often required the foreign company to submit a copy of a supply contract as precondition for issuing a license. This appears to be an unwritten requirement.

The foreign company must apply to the Company Registrar and submit documents partly similar to those required for establishing a branch office, in order to obtain a license<sup>19</sup>. The representative office is not required to submit the Israel Boycott declaration, while the branch office must do so.

The representative office acquires a legal personality as from the date of the license<sup>20</sup>, similar to the branch office, and is subject to a great extent to the same rules and provisions of the Regulations no. 5 of 1989 as the branch office. It must for instance maintain proper accounts and submit an annual audited account to

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<sup>18</sup> Ibid, article 1, paragraph 2

<sup>19</sup> Ibid, article 4

<sup>20</sup> Ibid, article 5, paragraph 5

the government financial control authority. But, unlike the branch office, the representative office is not subject to taxation.

If the foreign company obtains a work contract with a government entity, then it must transfer its representative office to a branch office, subject to the same provisions as those of branch offices<sup>21</sup>.

It may be added that establishment of a representative office, as a non-trading entity, is in line with the U.N. sanctions resolutions. If a contract for supply or a contract for works is required, then such a contract must be concluded under the U.N. Oil for Food Programme, which would impliedly permit the establishment of a branch or a representative office.

## **VI) Foundation of a Company or Joint Venture**

The Iraq Company Law number 21 / 1997 regulates the types of the companies and conditions of their establishment, management and dissolution.

According to article 12, all the shareholders of the company must be Iraqi nationals. Arab nationals are treated by the said article as Iraqis in this respect and are permitted to become shareholders of Iraqi companies. Foreign companies or persons are not permitted to establish or acquire shares, unlike many other Arab countries, where foreign companies may hold minority shares in national companies.

A new draft for a company law is being considered by the authorities in Iraq, and it is possible that Iraq, after lifting the sanctions, would permit foreign companies to invest directly and take part in establishing companies.

There are four main types of companies<sup>22</sup>:

1. Joint stock, companies consisting of not less than five shareholders, whereby the public is invited to participate.

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<sup>21</sup> Ibid, article 19, paragraph 1

<sup>22</sup> The Company Law no. 21/1997, article 6

2. Limited liability, companies consisting of not less than two shareholders and not more than 25, whereby the liability of each shareholder is limited to the nominal value of his share.

Joint stock companies and limited liability companies may be mixed companies, whereby at least 25 % of the capital is owned by a public sector.

3. Collective companies, consisting of two to ten natural persons, each having unlimited and joint liability for all the obligations of the company<sup>23</sup>.
4. Sole proprietor companies owned by a natural person who has unlimited liability for all the obligations of the company.

### **Joint Venture**

Having stated that foreign companies are not permitted to invest and participate in the share capital of the companies, there is nothing to prevent foreign companies to establish a joint venture for a specific project in Iraq. Such joint ventures may be established by two or more parties by a simple contractual arrangement. However, a foreign joint venture partner who has a government contract in Iraq must apply for a license to open a branch office as explained before.

The joint venture has no juristic personality, and each party maintains its own legal personality whether a company or a natural person. It is not subject to the Company Law, and the parties are free to determine their roles, the management and the distribution of the profits and loss. Towards third parties, the joint venture partners are jointly and severally liable.

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<sup>23</sup> Ibid, article 35

# UN Procedures To Approve Contracts And Open L/C

