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September 23, 2003

RECONSTRUCTION OF IRAQ COALITION PROVISIONAL AUTHORITY ISSUES ORDER NUMBER 39 ALLOWING FOREIGN INVESTMENTS IN IRAQ

On September 19, 2003 Mr. L. Paul Bremer, the Administrator of the Coalition Provisional Authority ("CPA") signed Order Number 39 ("Order 39") into law. Order 39 not only abolishes the existing Iraqi foreign investment law and replaces it with the provisions of the new Order 39, but also launches a new phase in the process of rebuilding Iraq. The following is a summary of the key provisions of Order 39.

Compared to the initial proposal of this Order 39, first discussed in the August 28, 2003 New York Times article titled "U.S. seeking Foreign Investments for Iraq," which barred foreign investments in certain industries such as railroads, oil, natural resources, electricity, water and sewage, Section 6(1) of Order 39 instead limits these restrictions only to natural resources involving primary extraction and initial processing, without being more specific as to the identity of these "natural resources" and types of "initial processing." Furthermore, Order 39 does not limit the amount of foreign capital to be invested in Iraq as previously proposed by the CPA. Additionally, Section 6(1) of Order 39 expressly states that this Order does not apply to banks and insurance companies.

Similar to Article 16 of Iraq's Interim Constitution, which prohibits foreign ownership of "Immobile Property" except as otherwise provided by law, Section 8 of Order 39 prohibits a foreign investor or a business entity with any level of foreign investor participation to purchase the rights of disposal and usufruct of private real property. However, Section 8(2) of Order 39 allows a foreign investor or a business entity to obtain a license for the use of real property, which license shall not exceed forty (40) years. In addition, Order 39 imposes no limit on the number of times that one may renew these licenses.

Under the old Iraqi law, foreign nationals (other than nationals of Arab countries) were not permitted to directly invest in (i) the establishment of, or to acquire stock in, an Iraqi company, or (ii) in an Iraqi project. Moreover, foreign companies, that were allowed to invest in Iraq, were required to comply with the Arab Boycott of Israel. Section 4 of Order 39, however, and most significantly, now provides foreign investors the same treatment as that given to Iraqi investors. Furthermore, Order 39 no longer limits the percentage ownership of a foreign investor in a newly formed or existing business entity in Iraq or Iraqi project. Such investor may own one hundred percent (100%) in an Iraqi entity or project. Additionally, Section 5 of Order 39 provides that foreign investors establishing trade representation offices or branches in Iraq must register with the Iraqi Registrar of Companies. Order 39, however, has not changed the cumbersome legal requirements of establishing local branch offices, licensing of business activities, record keeping, and maintenance of accounting records in Arabic.

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Section 7 of Order 39 permits foreign investors to establish their presence in Iraq by choosing among a variety of entities: (i) a wholly-owned business entity in Iraq, (ii) a business entity jointly-held with an Iraqi investor, (iii) a branch office or (iv) a direct acquisition of an investment. However, Section 6(2) of the Order 39 prohibits a foreign investor from participating in retail sales in Iraq, until such foreign investor has deposited U.S. \$100,000 in a non-interest-bearing account in a duly-licensed Iraqi bank located in Iraq. Also, Section 7 of Order 39 provides foreign investors full and immediate payment of shares, profits, dividends, proceeds from the sale or other disposition of their foreign investment, interest and royalties.

Section 10 of Order 39 permits contracting parties to elect the arbitration mechanisms outlined in Iraqi law in relation to settlement of disputes. While Iraq has no domestic law requiring the recognition or enforcement of arbitral awards from non-Arab countries, according to the Overview of Commercial Law in Iraq prepared by the U.S. Department of Commerce ("Overview"), Iraq is a member of the Permanent Court of Arbitration at the Peace Palace, The Hague, Netherlands (1899). Iraq also has ratified the Geneva Protocol on Arbitration Clauses (1923, ratified by Iraq in 1926) and entered into several bilateral agreements and Arab League conventions on the enforcement of judicial and arbitral awards, including the Riyadh Convention for Judicial Cooperation (1983) (Riyadh Convention). Article 37 of the Riyadh Convention, with a few exceptions, requires member states to recognize and enforce arbitral awards issued in other member states without looking at the merits of the case. The Overview suggests that companies wishing to enforce a foreign arbitral award in Iraq first may require a judgment from a domestic court and then proceed to enforce that court decision through the Iraqi procedures for the enforcement of domestic judicial awards. This suggestion would prove to be very costly and time-consuming for foreign investors. Further, since Iraq does not officially recognize non-Arab court judgments (other than foreign judicial awards of countries maintaining a bilateral agreement with Iraq, if named by Iraqi government-issued rules, and subject to a condition of reciprocity) and arbitral awards, an U.S. investor or company may be forced to try all of its claims before an Iraqi or other Arab country court or arbiter. Foreign investors, as such, must investigate which Arab country or countries would best provide a just and enforceable judgment of an Iraqi-based dispute so that it is enforceable in Iraq.

CPA ISSUES ORDER NUMBER 38 IMPOSING A RECONSTRUCTION LEVY

While Order 39 opens the Iraq door to foreign investments, and particularly to those from foreign investors that are not nationals of Arab countries, CPA Order Number 38 ("Order 38") issued on September 19, 2003, in an effort to assist the Iraqi people in reconstructing their country, imposes a "Reconstruction Levy" at a rate of 5% of the taxable value of goods. This Reconstruction Levy shall be in effect for two (2) years commencing January 1, 2004. While Section 1(4) of Order 38 imposes the levy on all imported goods, Section 2(1) of Order 38 excludes the following from the Reconstruction Levy: (i) food, (ii) medicine and medical equipment, (iii) clothing, (iv) books, (v) goods for humanitarian assistance, (vi) similar imports which are exempted from the Vienna Convention on Diplomatic Relations of 1961 on the Privileges and Immunities of the United Nations, and (vii) goods imported by the United Nations, other international or not-for-profit organization, or foreign governments which goods are used for the benefit of the public.

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Furthermore, Order 38 exempts from the Reconstruction Levy imports under the Oil for Food contracts and persons and entities affiliated with the CPA (including CPA itself) and the Coalition forces.

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