Disputes Resolution Procedure in Financing Contracts

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Abstract
Providing financial sources for trade affairs, purchase or investment is called financing. Finance contract using international resources is also called finance. Establishment method of these contracts with rule ruling them and dispute resolution place for these contracts is highly important because parties in such contracts live in different countries. Finance agreements are important international contracts, parties of these contracts are usually banks or financial institutions that are called loan provider or supplier (lender), the other party is a governmental (public) or private commercial company called loan receiver (borrower). Resolution of disputes raised from a foreign investment in another country is implemented as compromise or arbitration. Arbitration condition is not contained in finance agreements and ruling law is the law of a country with more loans anticipated to protect and advocate rights of lender bank.

Key words- Disputes resolution procedure, financing contracts,

Introduction
Current world requirements has made the law to create new legal frames and institutes compatible with daily evolutions in order to achieve their major goal that is organizing relationships between community people. This tendency has been serious and open in international trade scope considering its specific properties and nature; hence, emergence of new trade contracts is one of aspects of this tendency. In many of these contracts, two real individuals from two countries make a legal relationship with each other but now active presence of government and governmental organizations can be seen in this field. In majority of cases, some governments should implement infrastructural and construction projects, while have not enough expertise for implementation; such governments tend to attract foreign investments and use technical knowledge and capital of foreigners to exploit from required projects in exchange of protecting their right of supervising activity of foreign private sector and being owner of project after a while. In such countries, a Build-Operate-Transfer (BOT) contract is the most suitable legal framework. Importance and role of these contracts in modern trade stimulated the author to study different aspects of this legal-economic phenomenon in frame of two chapters describing position of Iran law toward this phenomenon.

Background
Historical foreign investment in Iran indicates that this scope has been based on oil and petrochemical industries. Post-revolution period in Iran can be divided into two distinguished periods in terms of foreign investment inflow. Iran government implemented policy of self-reliance and self-sufficiency at first decade of revolution (1979-1988). At that time, some problems occurred in economic and political relations of the government with capital exporters and transnational companies. The situation created by revolution, war, economic sanction, and seizure of properties of joint Iranian-foreign companies led to inappropriate situation for investment and activity of transnational companies in Iran. Iran did not experience any considerable foreign investment at that time.

In post-war period, some factors such as economic losses, renovation and reconstruction necessity for damaged areas as well as identification of defects and weaknesses of single-product economy and dependence on oil export led to implementation of structural reforms and economic adjustment policy in order to eliminate foreign currency bind. One of important factors of this policy is privatization, liberalization of exchange rate, liberalization of foreign trade and enforce of policies of Article 44 of Constitution. Foreign investment attraction through signing buyback contracts, obtaining project loans and attracting foreign direct investment (FDI) were emphasized during that period. However, Iran could not develop due to some legal, judicial, political, and economic problems such as economic blockade in field of foreign investment attraction.

A. Types contracts financing from international resources

Border of ministers approved an Article in May 2006 based of the joint recommendation of Ministry of Economic Affairs and Finance and Management and Planning Organization of Iran considering Article 6 of law of amending some articles to regulation law of financial regulations of government approved in 2005. According to this Article, Iranian governmental companies were allowed to sign contract with foreign and Iranian investors in framework of FDI methods considering Iranian investment priority in order to finance. Accordingly, Ministry of Economic Affairs and Finance considers a condition about the guarantee payment for contractual obligations of Iranian governmental company that is the party of contract in subject of Article 6 of mentioned Act. When the plan is accepted by the Board, the most important condition for receiving foreign currency loan is allocation to projects with economic justification and logical rate of return on capital. Finance contracts, which are signed between different international loan provider resources and loans users after negotiations and agreements, generally consist of some regulations that determine rights, liabilities, and commitments of parties precisely. Since parties of these contracts live in two or more countries with different judicial scopes, legal regulations, governing rules and dispute settlement place are highly important. Therefore, these contracts are written and organized by legal experts and consultants in many of cases. Causes contained in these contracts encompass definitions, loan fees, use of loan granted, repayment time (and its method), dispute resolution method, governing rules, prosecution authorities for disputes, guarantee method, insurance and other specific options that are discussed in detail at this study.

In summary, in finance contracts, a bank or foreign trade institution gives a loan to another country or firm for determined operations without controlling the spending way; therefore, the lender bank does not guarantee the project and receives the loan and its interest at determined due dates from contract party or guarantor bank.

B. Buyout Finance

In this method, buyout finance method of a firm is done by employees of that firm or an investor group out of the firm at high Debt Leverage. Finance is divided into three categories including short-term, medium-term, and long-term in terms of time classification. If foreign financial resources are granted based on the guarantee by government, central bank, and other financial institutions, these sources are borrowed and other forms of finance are included in non-borrowed resources. Accordingly, Finance, Refinance and Usance are classified as borrowed financial sources and BOO, BOT, and Buy Back are classified as non-borrowed group.

C. Finance (long-term letter of credit)

When a seller does not accept long-term letter of credit and purchaser and purchaser is not able to open letter of credit, purchaser asks a financial institution to enter to the transaction and pay the fee to seller in cash; these loans are usually long-term. Foreign bank or financial institution allocates 85% of proforma fee to demander in order to pay LC opening fee. From the view of seller, this type is payment at sight LC.

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3 Akhlaghi, B. Discussion on investment in Iran, brief overview of causes the barriers to progress, P. 10; Akhlaghi, B. (2004). “challenges of the Islamic countries entrance to international economic law with an emphasis on Iran”, Journal of Law, No. 5, Pp. 11-28
4 Islami, P., Ismaili, Sh. (2009). A review of the practices and methods of projects financing, the International Conference on the development of the financial system in Iran, Pp. 6-7
5 Islami, P., Ismaili, Sh. (2009). A review of the practices and methods of projects financing, the International Conference on the development of the financial system in Iran, Pp. 6-7
D. Refinance (short-term LC)
Refinance is defined as use of short-term interbank loans. Seller receives letters’ fee (in cash) from broker bank at the time of letters transaction and purchaser pays the fee at the due time of contract.

E. Direct investment method of Finance
Financing from international sources is done in two general forms:
1. Corporate Finance
2. Project Finance
In first form, finance consists of full obligation and all corporate assets are used for repayment of project financial obligations. The second form of finance consists of limited obligation or is without obligation and revenue obtained from sold product and capitals related to project is considered as the source of project obligations repayment. The latter is more accepted by executive authorities. However, finance is a short-term method for capital transfer to the country, because the initial capita plus its interest is returned after loan repayment deadline. Therefore, the most important condition for foreign currency loan is its allocation to project with economic justification and reasonable rate of return on investment\(^8\).

Dispute resolution rules
According to literature of law and jurisprudence (Feghh) principles, rule is a general issue that is matched for all individuals\(^9\). Whereas, principle is an issue anticipated by lawgiver (legislature) to determine the situation of responsible person in case of doubt\(^10\). However, this rule is used as a concept of law and principle and some researcher assume that rule “is a general law that is the origin of more limited laws understanding or base of other laws”\(^11\).

-legal rules are applied in different types of dispute resolution in relation with foreign investment but these applicable rules are distinguished based on the mentioned methods.

Foreign Investment Disputes Resolution Procedures

1- Court (judicial) prosecution
In this procedure, domestic court (investee country) would finish the dispute between parties based on the domestic procedural rules issuing the verdict (binding issue or verdict). According to Article 19 of Iran’s Foreign Investment Promotion and Protection Act, “Disputes arising between the Government and Foreign Investors with regard to their respective mutual obligations within the context of investments under this Act, if not settled through negotiations, shall be referred to domestic courts…”. This dispute resolution method has some problems despite its advantages. The major advantage of this method is binding procedural regulations of prosecutor authority in compliance with procedural mandatory regulations and the other advantage of this method is that defendant should implement the issued judgment through governmental authorities. There are 17 methods entitled “Alternative dispute resolutions”\(^12\). These methods are as follows: conflict prevention, negotiation, mediation, investigation mission for dispute, reconciliation, prosecuting with evaluation, short private prosecution, short judicial proceeding, counsel before the hearing, a preliminary assessment impartially, administrative proceedings, summary proceedings by jury, judicial assessment, specialized assessment, judge renting, combined judgment and arbitration with approach to friendly decision-making. Although some of these methods are similar, there are differences between them. It is necessary to separate binding (arbitration) and non-binding methods in out of court proceedings.

2- Non-binding methods
In out of court dispute settlements, except for arbitration, majority of issues are not bound to the result of prosecution that the most important of them, which are common in foreign investment dispute resolution, are discussed here.

In these methods, applicable regulations are applied with regard to two properties:

\(^8\) Finance of international Trade by Alasdair-Watson Edition 1988
\(^9\) Rule (En) Regle (fr)
\(^12\) Alternative dispute resolutions (En) Resolutions alternatives de con fli (fr)
A: deciding tribunal should pay attention to autonomy of parties in proceeding and it can be stated that dispute resolution regulations are usually more effective than willpower of dispute parties in these methods. B: result of proceeding and opinion of authority (court or tribunal) is not indeed binding unless parties agree on opposition state. Therefore, if third party (mediator) suggests a solution in non-binding methods considering justice regulation, it will be acceptable based on legal logic because the case will be cancelled if the recommendation is not accepted due to non-binding recommendation. Whereas, some lawyers assume that in binding method, arbitrators can settle disputes based on the justice regulation and if such authority is delegated to them. Dispute parties choose mediator and ask him to help them finding a solution during a private, secret and flexible process. Mediation is a voluntary and impartial non-binding method for foreign investment dispute resolution or other international dispute with or without presence of lawyers. This method is used if the negotiation is not possible or is inclusive. Mediation in international and foreign investment disputes in used in cases in which, parties tend to continue collaboration with each other. Some scholars consider mediation as synonym of compromise. In some of legal systems such as Iran compromise reaches to issuance of judgment or amendment report through specific formalities, while in mediation, parties are encouraged to settle dispute without formalities at presence of mediator. Accordingly, the difference between compromise and mediation is not deniable. A type of mediation called administrative mediation is applied for foreign investment dispute resolution in China to encourage and attract foreign investment. In this method, some centers are established for foreign investment dispute mediation and they try to settle such disputes as soon as possible.

Procedural rules of investment dispute resolution

Some rules and principles are applied during dispute resolution proceeding that a part of it is procedural followed to determine a competent authority for applicable law without considering nature of issue and to achieve fair proceeding. First, arbitrator or arbitrators were chosen and arbitration establishment was established to have applicable jurisdiction and this issue caused prolongation of case and high costs. However, arbitration authority has jurisdiction to appeal jurisdiction of authority in accordance with current international arbitration procedure and this is called “jurisdiction to jurisdiction”.

1. Effect of respective law of court (appealing authority) to determine competent authority

Appellate court performs usually based on the law of their respective government at least at the beginning of the appealing and enforcement of financial conflict settlement rules and competency qualification, which is called “jurisdiction to jurisdiction rule” among scholars. Parties in an international dispute are sometime two governments or sometimes a government against a non-governmental real or legal individual that it is assumed that they agree on dispute resolution in order to determine an appellate authority (such as Washington Treaty or bilateral Contracts of Foreign Investment) or some agreement may not exist. However, an appealing authority that prosecutes a case would refer to law of its respective government to recognize agreement between parties about competent authority whether this agreement is valid or not. In assumption that foreign investment dispute resolution is done using out of court methods, on the one hand, the subject of dispute resolution rules of appealing court is ignored because the court shall refer to this law, due to its legitimacy dependence on national law, in order to find applicable law, while an arbitrator obtains his legitimacy from parties and refers to explicit or implicit tendency of parties in order to find enforceable law. On the other hand, there is no relation between dispute and arbitration location rule in many of cases. For instance, the Hague is the arbitration location for disputes between Iran’ Government and USA, but enforcing dispute resolution rules of the country, which is arbitration location, is not justifiable. Moreover, disputes between two parties, in particular in a foreign investment contract, might be settled based on the

2. Mosleh, A. H., Sadeghi, M. (1) take a look at alternative methods of dispute settlement, a magazine shelf, the tenth year, 1383, No. 46, p. 136.
5. Articles 178-192 of Civil Procedural Code
arbitration regulations of International Commerce Chamber not based on ICSID or UNCITRAL rules in 
order to anticipate legal analysis for dispute resolution. Solutions provided by International Arbitration 
Authorities for dispute resolution are matched with specific conditions of each case. 

A- Procedural criterion 
Jurisdictional dispute resolution sometime is done using procedural criteria that is discussed here. 

1- Domestic authorities’ jurisdiction principle 
According to legal analysis, contrary to disputes raised from contracts in compensation (non-contractual 
liability), relation with law of location where the offense occurs is acceptable and domestic authorities can 
implement this law more better that any authority; hence, jurisdiction of domestic authorities is accepted. 

2- Validity of Finalized issue (non bis in idem) (not twice in the same thing) 
In this method, any authority that has legal justification for jurisdiction, either domestic or international, 
judicial or arbitration, based on bilateral investment contract or arbitration court of ICSID and or an 
authority agreed by parties that has appealed the case or issue the judgment, its judgment is finalized and 
other authorities has no jurisdiction to appeal the case. 

B- Substantive criterion 
Sometimes, judicial dispute resolution is considered using substantive criteria. According to this clause, 
“all individuals, who are qualified for lawsuit, can refer to arbitration for their international trade disputes 
either it is submitted to judicial authorities or not and make and compromise based on rules and regulations”. 
Therefore, the rule of reference of issue to international trade arbitration (such as reference of dispute related 
to foreign investment) or to arbitration is the same rule of “jurisdiction of lawsuit in judicial tribunals”. 
Appealing court or tribunal can determine the jurisdiction and qualification. 

1- Appealing application 
According to Clause 4 of Law on International Trade Arbitration, “… except for cases with agreement 
between parties, the arbitration demand should encompass following points: 
1-application of dispute reference to arbitration, 2- name and address of parties, 3- expressing and 
demanding claim, 4-arbitration condition or arbitration agreement…”. 

2- Written Arbitration agreement 
According to Article 7 of Law on International Trade Arbitration about the form of arbitration agreement, 
“arbitration agreement should be signed by parties through a document and electronic data interchange, 
Telex, Telegram, or similar means should imply on the existence of this agreement. It is contained in an 
exchange of statements of claim and defense in which the existence of an agreement is alleged by one party 
and not denied by the other. The reference in a contract to any document containing an arbitration clause 
constitutes an arbitration agreement separately”. According to UNCITRAL rules, the agreement on 
reference to arbitration should be in writing20. Article 1: whenever, parties have agreed, in writing, on 
referring to arbitration for disputes araised from a contract considering rules of UNCITRAL arbitration, 
these disputes shall be settled based on these rules and any amendment in these rules considering written 
agreement between parties. 

3- Appealing process 
According to examination of applicable rule and appealing authority respecting procedure rules, appealing 
is done based on following options: 
- Rule Of Distinguishing Claimant From Defendant 
- Rule Of Claim Substantiation 
- The Burden Of Proof 
- Providing Reason For Claim Proof 

A- Rule of distinguishing claimant (plaintiff) from defendant (respondent) 
The burden of claim proof is shouldered by claimant that is one of dispute parties and the other party is 
called defendant. From the viewpoint of lawyers, claimant is a party that the dispute is ended if he/she ends 

20 www.uncitral.org/pdf/english/texts/arb-rules/arbrales
the disputes. It means that the dispute starts if claimant demands\textsuperscript{21}. Other lawyers consider signs of claimant opposed to the principle. It means that claimant is a person whose claim is opposed to the rule or principle of valid evidences\textsuperscript{22}.

**B-Rule of Claim Substantiation**

Claim substantiation of dispute parties is an important point in prosecution of a dispute out of a court or a judicial procedure for judging a dispute.

**C-Substitutive rules of foreign investment dispute resolution**

There are some substantive rules and principles in foreign investment dispute resolution rules in addition to procedural rules respected by dispute resolution authority. The mentioned procedural rules shall be followed by appealing authorities and parties based on the written or unwritten rules.

1.-Enforchble rules without parties’ agreement

According to substantive theory, suitable law is a legal system that contracts are signed subjected to such system or there is a close and real relation between contract and this system\textsuperscript{23}. In case of silence of parties to determine the governing rule, paying attention to communication factors is effective in finding the governing rule. Regulations have determined this assumption. For instance, Article 42 of Washington Treaty states that in case of silence of parties, the arbitrator refers to law of government, a contract party, such as conflict resolution rules of that government or international law principles\textsuperscript{24}.

2.-Law of National country of individuals

This rule is used when the case consists of parties with a nationality that is different with nationality of appealing authority. For instance, when one party is Iran government and the other party is a foreign legal or real individual. In such case, appealing authority for foreign investment dispute to qualify legal establishment of a French Investor Company shall refer to the law of this country.

3.-Residence Act

This assumption is considered when residential place of a party or parties of dispute regardless of their nationalities determines the subject. According to Article 5 of Civil Code, “all inhabitants of Iran, whether of Iranian or of foreign nationality, shall be subject to the laws of Iran except in cases which the law has considered exception”.

**Jurisprudential Analysis of Finance Contracts**

In context of Islamic finance, the common tools such as specific future contracts, equal future contracts, Swap, and bonds have not been completely accepted because social benefit, which is used as a justification for such contracts, is not as important as sever Quran conviction of some subjects such as Gharar, Zarar, Reba, Qomar, and Miser. Swap contracts can be replaced with Islamic Foreign Currency contracts and bonds can be replaced with Islamic bounds considering objections of Islam in this field. Islamic rules have a potential capacity to design new financial tools to facilitate transactions and risk management. However, this point should be mentioned that Islamic Financial System is an asset-backed financial system that connects each financial debt to a real asset related to it. In Islamic financial system, each financial debt is considered as a conditional debt that its return or performance is related to return on an obliged real asset leading to stability of Islamic banking\textsuperscript{25}. Nowadays, development of financial institutions and expansion of trade domain has led to importance of risk management in economic studies. Various approaches and tools have been created for risk management and reducing different types of risks. One of the most applied tools in field of risk management is swap in which, a set of fixed cash flows are transacted with a set of floating cash flows. Swap contracts of interest rate as a type of swap contracts have an important role in interest rate risk management or coverage. Every economic activity faces a risk and risk is not completely removable. Risk management has become an important factor in economic studies due to developed financial institutions and expanded trade domain. Various approaches and tools have been created for risk


\textsuperscript{23} Akhlaghi, B. (2003-2004). International trade law, pamphlets of private PhD Tehran University, P. 38

\textsuperscript{24} Hussain Safai, ibid., P. 146

\textsuperscript{25} Vaez Barzani, M., Darafsheh, M., Al Bosalim, M. Islamic financing system engineering, Proceedings of the Second International Conference on development financing system in Iran
management and reduction. Future contract was the first method to control risk and uncertainty but limitations and problems of this contract caused emergence of future contract transactions, while the latter could not remove all of risks and uncertainties. Despite the existence of these tools, risk management issue was not finished, risk hazard existed, and scholars were looking for additional solutions for risk management. At this time, swap market emerged and could considerably expand in financial markets. Increasing expansion of swap contract, from introduction to application, was more considerable than other methods and this is because of ease of use and efficiency of these contracts in risk covering or cost reducing and or finding conditions with more opportunities. In addition to mentioned options, interest rate swap is beneficial to cover interest rate in loans with floating rate or fixed rate as well as to cover risk of finance institutions or lenders. It is not meaningful to define this contract as a new contract with new legal nature. Adjustment possibility of this contract with other common Islamic contracts is debatable. Among the Islamic agreements similar to contracts (debt to debt buy, Kali to Kali buy, and debt-to-debt compromise), it is possible to put this contract I form of debt-to-debt compromise. Accuracy of general conditions of contracts on interest rate swap is discussed and among existed doubts, uncertainty (Gharar) or Reba in interest rate swap contract are approved; therefore, it is concluded that interest rate swap common in West is not matched with principles of Islamic contracts and Shia Fighh\textsuperscript{26}. Sokuk (Islamic bounds) is a new idea has emerged recently and consists of bank deposits and asset-backed governmental bounds that is a practical and interesting issue in the world\textsuperscript{27}. Undoubtedly, Sokuk is one the most suitable and attractive innovations of economic and financial thinker over the three recent decades. This new financial tool has created a practical and commercial approach for Islamic economic and financial issues that had only theoretical aspect before. This tool has been considerably welcomed by Muslim and non-Muslim investors\textsuperscript{28}. Sokuk is Islamic Securities that encompass of a physical asset and some contracts such as Leases and partnership (Mudaraba) and is based on the Usur-less (without Reba) banking rule. According to the rules of Islamic Republic of Iran, “Sokuk” is a bond issued based on the legitimate contracts and indicate joint ownership of its holders in asset that these securities are published based on this point. Sokuk in particular leasing Sokuk can be a suitable tool for finance and changing assets to securities in all of countries especially Islamic countries. Some of Islamic countries such as Iran, Bahrain, Malaysia, Qatar, UAE and Saudi Arabia and some non-Islamic countries such as Germany and England have been using Sokuk in their financial markets\textsuperscript{29}.

Conclusion

Finance and its suitable methods has been one of major concerns of policy makers in different economic scope; hence, it is necessary to recognize and study new financing tools. Increased number of economic firms in world market indicates growth and profitability opportunities in these markets. Presence of these firms not only requires knowledge, specialized human force, new technologies, reduced cost, reduced price, increased product quality, customer orientation and strategic management, but also needs to determine optimal structure of capital to decrease finance costs in order to increase operational activities and create value for firms. There has not yet any solution presented to access to a favorable composition of capital structure. Financial tool of Sokuk, asset-backed securities, and mortgage bonds are the most important finance tools in Iran. Considering all aspects such as current economic situation of Iran, Sokuk can be used as one of the best financing options. This method is one the most comprehensive finance methods that its field has not developed yet in capital market of Iran. In this regard, some recommendations are presented in order to prepare infrastructures required for development of modern finance tool market:

- Study on foreign currency rules and regulations of Central Bank, vital licenses and ratifications, legal contradictions, complicated and time-consuming process of use of these facilities and common methods indicates that executive

\textsuperscript{26} Mohaghegh NIA, MJ., Tamaloki, H., Khajehzadeh Dezfooli, H. (2014). Study of the interest rate swap contracts from the perspective of Jurisprudence, Journal of Islamic Economics

\textsuperscript{27} Ahmadpour, A., Khakpoor, H. (2007). Assessment of new financial instruments in the capital market, stock Magazine, No. 65


process should be shortened, contradictory and restrict rules and regulations should be eliminated and some applicable rules should be created. It is also required to use simpler finance methods such as foreign loans, sell of foreign currency bonds.

- Complex and time-consuming process of using finance facilities is not the natural part of finance method and it is due to inappropriate existing conditions to attract foreign currency attraction. A part of failures is related to low quality of project documents and another part of it is related to strict rules and regulations in field of these facilities, political and economic conditions of Iran.
- The existed rules and regulations for use of foreign currency facilities are highly strict and sometime in conflict with each other and some of these rules play a role of barrier to provided loans and facilities by foreign financers. It is required to review and reform some of these rules, regulations and acts in order to shorten process of use of such loans and facilities and attract more foreign investors.

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