

## Insurance Law Flash

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## Sanctions Against Iran The Impact on Insurers and Reinsurers

Insurers and reinsurers could face serious, even criminal, charges if they breach draconian new rules on trade with Iran. Following UN Security Council Resolution 1929 on 9 June 2010, both the EU and the US have beefed up their sanctions regimes. We consider the recent changes and their potential effect on the insurance industry.

### The EU Position

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#### The EU Council Decision

In a Council decision on 26 July 2010, the EU imposed its harshest sanctions yet on Iran, targeting the energy, transport, finance and insurance sectors. The EU Council's decision is binding on all EU member states, which must "*ensure that their national policies conform to the Union positions*".

Some sanctions have immediate effect; others—including those concerning insurance and reinsurance contracts—require further EU and member state legislation, which is expected later this year.

**Penalties for breach are likely to be severe against both individuals and companies, and could carry criminal charges.**

#### Sanction Targets

The sanctions target a number of sectors: *nuclear* (Articles 1-3); *energy* refining, including exploration and production (Article 4), though there is no ban on the export of crude oil or LNG; *financing of trade/the financial sector* (Articles 5-12; Article 12 expressly deals with *insurance and reinsurance*); *transport* (Articles 15-18), including supplying services to Iranian vessels reasonably suspected of carrying embargoed goods; and *named individuals* and companies/assets controlled by them (Annexes 1 and 2).

In all relevant cases, there is a ban on providing financial assistance to any of the prohibited entities and this is almost certainly wide enough to embrace insurance contracts, even apart from the provisions of Article 12.

#### The Insurance Industry

Article 12 prohibits the "*provision of insurance and re-insurance to the Government of Iran, or to entities incorporated in Iran or subject to Iran's jurisdiction, or to any individuals or entities acting on their behalf or at their direction, or to entities owned or controlled by them, including through illicit means, shall be prohibited.*" Health and travel insurance to individuals is exempt.

Neither can one "*participate, knowingly or intentionally, in activities the*



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*object or effect of which is to circumvent the [main] prohibition". Unlike the US position (see below), the question of knowledge is simply one of fact; there is no issue as to whether one ought reasonably to have had such knowledge.*

The precise operation of Article 12 in the UK will only be clear after the next round of implementing legislation, expected this Autumn, but we see three situations which might be in play:

*(a) Contracts ending before 26 July 2010*

The Council decision is not retroactive, so payments under such contracts do not fall foul of the new regime, though insurers should note the specific rules for the transfer of funds to and from Iran, requiring notifications to and/or authorisations from the Treasury (Article 10(3)):

- (i) below €10,000 -- no special action is necessary
- (ii) below €40,000 -- payments can be made without prior authorisation but amounts above €10,000 must be *notified*
- (iii) above €40,000 -- all payments must have prior authorisation.

*(b) Contracts spanning 26 July 2010*

Where a policy period spans the decision date, the position is less clear. At present, the matter appears to lie with the Treasury, as per the notification/authorisation regime above.

*(c) Contracts incepting after 26 July 2010*

Prohibited. Although, pending national legislation, there is no criminal offence involved, **insurers would be extremely unwise to enter into any contracts involving sanctioned activities.**

## The US Position

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### The Comprehensive Iran Sanctions, Accountability and Divestment Act 2010

On 1 July 2010, the US enacted the Comprehensive Iran Sanctions, Accountability and Divestment Act 2010 (the **2010 Act**), which expands upon the Iran Sanctions Act of 1996 (the **1996 Act**).

In particular, the 2010 Act provides for sanctions on anyone—*not just US persons and companies*—who assists Iran in buying or importing refined petroleum products, or facilitating the maintenance or expansion of Iran's own domestic production of such products. This thrust, against Iran's petroleum sector alone, is narrower than the wider and arguably much tougher EU regime.

#### Sanctions Under the 2010 Act

The 2010 Act increases the potential sanctions for violators. The new sanctions include:

- Prohibiting relevant *transactions in foreign exchange* subject to US jurisdiction
- Prohibiting relevant *transfers of credit or payments through financial institutions* if such transfers or payments are subject to US jurisdiction; and
- Prohibiting the sanctioned person from acquiring, holding, withholding, using, transferring, withdrawing, transporting, importing, or exporting of any *property* subject to US jurisdiction.

#### Knowledge and Enforcement

Critically, the **2010 Act reduces the level of knowledge required to fall foul of the regime**. The 1996 Act required actual knowledge; under the 2010 Act, "knowingly" means that "a person has actual knowledge, or *should have known*, of the conduct, the circumstance, or the result" (emphasis added). Further, this new standard applies to corporate parents, subsidiaries, or other affiliates of the offending company. Thus, a parent company may face penalties arising from a subsidiary's conduct if the parent company "should have known" that its subsidiary was engaged in prohibited conduct.

Further, the 2010 Act provides for more rigorous monitoring of breaches and enforcement of the sanctions. The 1996 Act required merely that the US president "should" launch an investigation upon receipt of credible evidence of offending conduct; the 2010 Act provides that the president "shall" do so.

### **Impact on Insurers and Reinsurers**

The Office of Foreign Assets Control (OFAC) has confirmed that providing insurance or reinsurance cover to prohibited arrangements is, in itself, prohibited. However, the 2010 Act introduces a welcome safety mechanism for carriers: if they can show that they have "*exercised due diligence in establishing and enforcing official policies, procedures, and controls to ensure that the person does not underwrite or enter into a contract to provide insurance or reinsurance for the sale, lease, or provision of goods, services, technology, information, or support*" that is prohibited, then they should be able to escape sanction.

On August 16, 2010, the Iranian Financial Sanctions Regulations came into force, to implement certain provisions of the 2010 Act. Under these regulations US financial institutions, including insurance and reinsurance companies, are prohibited from maintaining correspondent accounts or "payable-through" accounts for foreign financial institutions that engage in certain proscribed activities (for example, helping Iran obtain weapons of mass destruction or providing support to known terrorists), or providing "*significant financial services*" (including insurance and reinsurance) for financial institutions whose assets are blocked.

Further OFAC regulations and guidance can be expected. Accordingly, insurers and reinsurers engaged in international business would be well-advised to seek advice and find out whether and how far they may be subject to this new and developing sanctions regime. In particular, given the new standard of "knowledge" (i.e. not only actual but imputed) they need to assess their existing procedures and controls and, as appropriate, take the necessary measures to ensure that they are neither maintaining prohibited accounts, nor covering or otherwise providing significant financial services to prohibited entities.

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