WILHELM

RECHTSANWÄLTE

Sanctions clause does not replace guidance and advice

With the regulation (EU) 961/2010, the EU issued a prohibition to grant insurance cover for Iranian risks. Many insurers consequently added a so-called sanctions clause into their contracts. A declaratory clause on its own does though not provide transparency.

As a reaction to the extension of the Iranian nuclear program, the European Council decided on 26th July 2010 on stricter sanctions against the Islamic Republic. The EU regulation 961/2010, which came into force on 27th October 2010 (and is currently about to be tightened), extended the existing embargo significantly.

The regulation announced for the first time a direct insurance prohibition (Art. 26 EU-regulation 961/2010): insurers are not allowed to provide insurance cover for Iranian persons, organizations or institutions. The prohibition is comprehensive. It applies independent of the goods to be insured. A similar insurance prohibition exists since January 2012 also for Syria (EU regulation 36/2012). It relates to the Syrian state and its representatives as well as for persons and companies acting by order of the state.

This new regulation applies for direct insurers, re-insurers, captives and brokers. Policy holders are affected directly as well. They, for example, cannot co-insure affiliates located in Iran or Iranian contract partners anymore. A violation of the sanction does not only have consequences for the underlying insurance contract but may also have consequences with regard to criminal law.

Increased legal certainty through sanction clause?

The insurance industry reacted on the Iran embargo with the insertion of an exclusion clause into new and partly also into existing direct and re-insurance contracts. It shall exclude the risk of a violation of the sanction by the insurer. The sanction clause recommended by the German Insurance Federation (Gesamtverband der Deutschen Versicherungswirtschaft "GDV") says in the first paragraph:

"Notwithstanding other provisions of the insurance contract, cover shall be granted only insofar as and as long as not in contradiction to economic, trade or financial sanctions or embargoes enacted by the European Union or the Federal Republic of Germany that are directly applicable to the contracting parties."

This first paragraph of the sanctions clause is a declaratory wording. At first it only confirms that the insurance contract is subject to applicable law. Solely the wording “insofar as and as long” may in so far be attributed an own regulatory content as it makes clear that a violation of the sanction does not necessarily infect the entire contract.

At first this does not change much for the policy holder regarding the consequences of the insurance prohibition which apply anyway. Already according to sec. 134 German Civil Code (BGB) policy holders do not receive cover for risks that are clearly forbidden to be insured according to the EU regulation – no matter if there is a sanctions clause in the insurance contract or not. An exemption applies for existing contracts which were concluded before 27th October 2010: the regulation does not prohibit compliance with agreements concluded before that date (exemptions apply for contracts in favor of persons and organizations listed in the Annexes VII and VIII to the regulation 961/2010). But as soon as these contracts are changed, extended or renewed, they become subject to the sanctions of the regulation.

It is understandable that policy holders examine any new clause critically and ask whether an exclusion is necessary and useful or if it cuts cover – without any compensation. Insurers should ask themselves, whether serious changes of risk have occurred or must be expected which justify to burden customers with further exclusions.

Sanctions clause does not prevent cover disputes

The insertion of the sanctions clause is often justified with the aim of increased transparency and legal certainty for the policy holder. Given the general wording, no increase in transparency can though be reached. The sanctions clause does not support the policy holder in his examination of own risks regarding possible violations of embargo. The policy holder still has the responsibility to identify possible cover gaps in his insurance program.

A clause which only refers to sanctions cannot create additional legal certainty beyond the wording of the EU regulation. If the insurer refuses cover in case of an insured event by referring to the insurance prohibition, it must, in case of dispute, be decided - independent of the clause - in how far the damage causing risk underlies the provisions of the regulation. It seems unlikely that the sanctions clause can avoid cover disputes.

US sanctions cause uncertainties

On the contrary, the sanction clause causes legally unclear situations in many cases. This is because the model terms and conditions of the GDV provide for a second paragraph which includes US sanctions:

"*This shall also apply to economic, trade or financial sanctions or embargoes enacted by the United States of America with regard of the Islamic Republic of Iran, insofar as those are not in contradiction to European or German legislative provisions.*"

As a consequence there is no insurance cover if the insurance contract violates sanctions issued by the United States with respect to Iran. The sanctions clause thus takes reference to the Iran Sanctions Act of 1996 and the Comprehensive Iran Sanctions, Accountability and Divestment Act (CISADA) of 1st July 2010 with universal validity claim. It is though not limited thereto, but does also apply for additional – future – US sanctions against Iran. The second paragraph of the sanctions clause thereby limits the insurance cover in the disadvantage of policy holders, more than required by law.

The relationship between European law and US sanctions is problematic. The inclusion of this sanction is, according to the wording of the clause, subject to its compatibility with European law. Whether the application of foreign embargoes in the EU will though persist at German courts, is unclear (also against the background of the anti-boycott-regulation of the EU (2271/96 of 22nd November 1996). The second paragraph of the sanctions clause thus creates uncertainties for all contract parties. For this reason, many insurers have decided not to make use of this part of the clause.

Transparency only through comprehensive guidance and advice

The inclusion of the sanction clause into insurance contracts is, from the insurer's point of view, an attempt of prevention of own sanction violations. Re-insurers are said to have made the inclusion of the sanction clause into direct insurance contracts a requirement for cover. Some auditors and rating agencies demand the inclusion of the clause as well. This does though not change its declaratory character. Against the background of the legal regulation (by the EU), the sanctions clause is primarily a burden for insurance contracts.

Further, insurers do not advice legal certainty about the scope of insurance cover in the contractual relationship with their policy holders. The multitude of and regular extensions of EU sanctions should rather give reason for an intensified exchange between insurers and policy holders about the insurability of individual risks and possible cover gaps before conclusion of contract. Only comprehensive guidance and advice creates transparency and legal certainty for all parties.

Albrecht Birke and Dr. Friedrich Isenbart, lawyers, Wilhelm Rechtsanwälte, Düsseldorf

Partnerschaft von Rechtsanwälten
Reichsstraße 43
40217 Düsseldorf

Telephone: + 49 (0)211 687746 - 0
Telefax: + 49 (0)211 687746 - 20

www.wilhelm-rae.de
albrecht.birke@wilhelm-rae.de
friedrich.isenbart@wilhelm-rae.de

Registered office: Düsseldorf - AG Essen: PR 1597