

Iran sanctions and rule change Frequently asked questions

1. What are the rule changes, what is their practical effect and why are they necessary?

A new sub-rule 17.2(5) has been inserted (applying to P&I and Standard Offshore rules):

[17.2 A member shall cease to be insured by the club in respect of any ship entered by him if:]

...17.2 (5) *“the ship is employed by the member in a carriage, trade or on a voyage which will thereby in any way howsoever expose the club to the risk of being or becoming subject to any sanction, prohibition or adverse action in any form whatsoever by any state or international organisation, unless the managers shall otherwise determine”.*

A new rule 6.22 with a side heading “Sanctions” is also inserted as follows:-

“The member shall in no circumstances be entitled to recover from the club that part of any liabilities, costs and expenses which is not recovered by the club under any reinsurance(s) arranged by the club because of a shortfall in recovery from reinsurers thereunder by reason of any sanction, prohibition or adverse action against them by a state or international organisation or the risk thereof if payment were to be made by such reinsurers. For the purposes of this rule 6.22 “shortfall” includes any failure or delay in recovery by the club by reason of the reinsurers making payment into a designated account in compliance with the requirements of any state or international organisation”.

An equivalent new rule 6.16 is inserted into the Standard Offshore rules (obviously cross-referencing 6.16 rather than 6.22). The rule change takes effect from noon GMT on Monday 12 July 2010.

If a member is in breach of sanctions by the operation of an entered ship which would then put the club in breach, then that member's entry for that ship will automatically cease. The member's cover remains in place for incidents predating the cessation. The member remains liable for premium up to and including the date of cessation and overspill calls; he is not liable for premium after the date of cessation. The club can meet a member's liabilities up to the date of cessation in the usual way but the club will not respond to incidents thereafter.

It was necessary to make this rule change because if it had not been made and the club was insuring a member whose ship was operating in breach of sanctions, then the club itself might be in breach of the sanctions by providing insurance. The club might then be subject to penalties such as prohibition of the use of US banking facilities.

2. Do the rule changes affect owners and charterers?

Yes. The rule change will apply to all members' coverages and will therefore apply equally to owners' and charterers' entries.

3. Do these rule changes affect Standard Offshore Rules too?

Yes albeit the "Sanctions clause" (rule 6.22 in the P&I rules) is merely renumbered to be SOR 6.16.

4. Are these changes applicable to entries in all of the Standard Clubs?

Yes.

5. Does the club's rule change only bite in respect of sanctions aimed at Iran?
No. The rule change relates to "sanctions busting" conduct by a member that puts the club in breach of those sanctions. It is purposely not limited to sanctions relating to Iran, nor relating to sanctions emanating from the USA.

6. Do members need to seek permission from the club for each voyage to Iran?
No. Members need to satisfy themselves that they will not breach any applicable sanctions legislation.

7. Will the club prohibit owners entering into charterparties with Iranian entities?
No. Members must satisfy themselves that they are not in breach of sanctions and should seek appropriate legal advice. If members do not believe that CISADA 2010 will be applicable, care should still be taken to ensure that their contractual partners do not appear, for example on the OFAC SDN list and that they comply with their domestic law.

8. What is CISADA 2010, why is it important and when did it come into force?
This is the Comprehensive Iran Sanctions, Accountability, and Divestment Act 2010. It was signed by President Obama on 1 July 2010 and became effective that day. It introduces and builds upon significant and wide ranging sanctions against Iran, the Iranian government, and the Iranian Republican Guard. The Act impacts shipowners, charterers, insurers, brokers, banks and financiers, and in practice has extra-territorial effect.

9. Does it apply to charterparties and contracts of carriage that were signed before 1 July 2010?
Yes. It is of direct application now

10. Is CISADA 2010 a stand-alone Act or are there other US sanctions?
CISADA 2010 is one aspect of the US sanctions regime. It amends and adds to existing legislation, particularly the Iran Sanctions Act 1996, and presidential orders that bar nearly all US trade with Iran. It imposes new sanctions and is of wider impact than the ISA 1996.

11. Are sanctions against Iran limited to the US?
No. CISADA 2010 should not be read in isolation. Members should be aware of other sanctions regime in the UK, Bermuda, EU and elsewhere. Care should be taken to comply with such laws (with the assistance of local lawyers) as they may conflict. CISADA 2010 will have extra-territorial effect.

12. What is CISADA 2010 aimed at sanctioning?
CISADA 2010 substantively imposes sanctions in three circumstances, i.e. where a party (whether a US or non-US entity) is involved in:
(A) investing in the development of petroleum resources of Iran
(B) facilitating the domestic production of RPP in Iran
(C) supporting the export of RPP to Iran

CISADA also aims to cut off access to the US financial sector to non-US banks that maintain correspondent accounts with Iran, and writes into law the broad prohibitions (applicable to US citizens and firms) on virtually all dealings with Iran.

13. When are the sanctions triggered?

The trigger for the imposition of the sanctions depends on the circumstances and the sanctionable activity:

(A) investing in the development of petroleum resources of Iran

Sanctions are triggered when the President determines that a person knowingly makes an investment of \$20m or more (or at least US\$5m per year and which exceeds US\$20m in the aggregate).

(B) facilitating the domestic production of RPP in Iran

Sanctions are triggered when the President determines that a person knowingly sells, leases or provides to Iran goods, services, technology, information or support, with a "fair market value" of US\$1m or more (or US\$5m or more in a year) that directly and significantly facilitates the maintenance or expansion of Iran's domestic production of RPP, including any direct and significant assistance with respect to the construction, modernization or repair of petroleum refineries.

This could include the provision of pipes, pumps, generators, valves, building materials etc. used in the construction and maintenance of refineries.

(C) supporting the export of RPP to Iran

Sanctions are triggered when the President determines that a person knowingly sells or provides to Iran RPP (or sells, leases, or provides to Iran goods, services, technology, information or support that could directly and significantly contribute to Iran's ability to import RPP) with a "fair market value" of US\$1m or more (or US\$5m or more in a year) including underwriting (either directly or via reinsurance) financing or broking such sale lease or provision, OR providing ships or shipping services to deliver RPP to Iran.

14. Does the Act affect charterers as well as owners?

Yes. The Act prohibits the provision of ships or shipping services to deliver RPP to Iran. This is wide enough to encompass owners and charterers.

15. What are refined petroleum products ("RPP")?

Refined petroleum products are defined by the Act to include "...diesel, gasoline, jet fuel (including naphtha-type and kerosene-type jet fuel), and aviation gasoline."

16. Does this definition include refined petroleum products carried in containers?

Yes, it does not matter how it is transported.

17. Does the definition include petrochemicals or gas based petroleum products?

The list provided by the Act is unlikely to be exhaustive and as such there is need to exercise caution. Further advice should be sought by members from their preferred US attorney.

18. What does "directly and significantly" mean?

These are not defined terms in the Act and therefore will be open to interpretation by the US Authorities and courts. It is likely to be a factual determination and will vary between cases and industries.

19. What does "knowingly" mean?

Under the Act the term "knowingly" with respect to conduct, a circumstance, or a result means that a person has actual knowledge, or should have known of the conduct, the circumstance or the result. Therefore "knowingly" will be treated as actual or imputed knowledge.

20. Does CISADA 2010 affect the export of Iranian goods worldwide?

Yes. Of course CISADA 2010 cannot ban the export from Iran of their goods but, in addition to other US legislation, it does codify the existing prohibition on the import of Iranian goods to the US (and eliminate narrow exceptions, such as foodstuffs and carpets) effective 1 October 2010. The Act states that no goods or services of Iranian origin may be imported directly or indirectly into the United States. Passage of such Iranian goods through a third party country will not "cleanse" them of their origin.

21. Does the prohibition of insurance only relate to the importation of RPP into Iran?

It could be argued that the provisions making the supply of underwriting services sanctionable only relate to the import of RPP to Iran. It could be argued that the provision of insurance services relating to the maintenance or expansion of Iran's domestic production of RPP is not sanctionable. We believe the better view is that the intention is to prohibit the provision of property and liability insurance in both circumstances.

It could also be argued that under CISADA 2010 the prohibition against the provision of shipping also only relates to the importation of RPP into Iran and would not apply to the importation by a shipowner into Iran of goods that would facilitate the expansion of Iran's domestic refining capability. However, US authorities appear likely to take the view that the provision of services (in the context of seeking to sanction Iran's domestic refining capability) should be construed to include the provision of shipping and insurance services. Therefore care must be taken in all shipping sectors beyond the tanker sector.

22. What are the penalties that can be imposed for breach of CISADA 2010?

The President is obliged to impose 3 or more sanctions from a list of 9 (formerly there were only 6 possible sanctions under the ISA 1996) when the President determines that a person triggers the sanctions (see below). The sanctions that may be imposed on parties worldwide include the prohibition of US imports, banking, foreign exchange or property transactions. US persons violating the Iran embargo also face significant fines and/or imprisonment.

23. Will the sanctions be enforced?

Members should assume that CISADA 2010 and other sanctions regimes will be enforced rigorously by the authorities. In the US significant budgetary funds have been allocated to increased enforcement efforts, eg approx \$320m in the 2011 fiscal year.

24. I think my commercial activities may be subject to CISADA 2010 or other sanctions regime. What should I do?

Our comments can only be general guidance and should not be relied upon in relation to specific voyages, charters, contracts of carriage, joint ventures, COAs or otherwise. Members are strongly advised to contact their preferred lawyer for specific advice relating to the interpretation of legislation such as CISADA 2010.

25. Are there protective charterparty clauses available?

Yes, for example, as prepared by Intertanko. BIMCO is also developing a clause. It should be published shortly. Of course such clauses should be carefully considered and agreed between owners and charterers before being incorporated into charterparty contracts. Care should be taken interpreting such clauses and members should carefully consider the appropriate law and jurisdiction clause of their charterparties.

26. Can the club confirm which cargoes can and can not be carried?

No. We cannot provide members with a list of what is permissible and what is not. Some commentators have focussed on references to the prohibition of exporting to Iran refined petroleum products (as defined). The sanctions are wider and in our view also prohibit knowingly exporting to Iran goods or services that “could directly and significantly facilitate the maintenance or expansion of Iran’s domestic production of refined petroleum products”. This could be pipes, pumps, generators, valves, building materials and potentially even books on how to crack oil or build a refinery. It is not clear whether the US authorities will adopt a “dual use” test in respect of cargo. For example a pump may be destined for use as a water pump in a hydroelectric facility. However, it could have another (dual) use as part of an oil refinery. The US authorities may argue that the export to Iran of such a pump would be sanctionable. Similarly unclear are US authorities’ plans for applying certain subjective tests in the law, such as the “knowing” standard (defined to encompass matters parties know or “should have known”) and the “direct and significant” test for evaluating whether goods facilitate Iranian refining.

27. Can the club confirm whether a member factually is in breach of sanctions?

No. This is a function of interpretation of local law and advice must be sought from a suitably qualified local lawyer. The club can provide contact details of lawyers in many jurisdictions worldwide. It is for members to determine whether they are or may be in breach of US sanctions and we strongly recommend that members seek advice from suitable US attorneys. It is a question of fact as to whether any member in breach of US sanctions and following the recent rule change (w.e.f 12 July 2010) if they are in breach then club cover will have ceased at the moment the member is in breach.

28. Does CISADA only relate to tankers?

No. The Act is not limited to tankers. It will also apply to, for example, bulkers and container ships. A container of barrelled and palletised RPP may not in of itself contain sufficient volume of RPP to activate the US\$1m “fair market value” trigger. However, repeated shipments over a year may reach the US\$5m annual aggregate trigger. It will be difficult to calculate the “fair market value” of RPP, particularly over a prolonged period of time. Therefore it may be difficult to calculate whether the US\$5m aggregate trigger has been activated. Carriers may wish to refuse to carry any RPP to Iran or indeed other goods that could enhance Iran's refining capability.

29. Is it still possible for a dry cargo ship to still trade to Iran?

Yes but members should be careful that they consider all relevant sanction legislation and in particular they should satisfy themselves that they do not have dealings with parties named upon the US Treasury OFAC list of SDNs or in any other relevant legislation (e.g. under the law of the flag or country of ownership/management). CISADA 2010 prohibits the selling, leasing or providing to Iran of any goods, services, technology, information or support that would allow Iran to maintain or expand its petroleum refineries. The scope of this provision is unclear. However it is likely to include plant and machinery that could be used to enhance or preserve petroleum refineries in Iran.

30. What if a shipper's description of the cargo is wrong?

If the cargo has been misdeclared by the shipper, a carrier could argue that there was insufficient knowledge to make the carriage sanctionable. Carriers should re-examine their bill of lading terms and their relationship with shippers to satisfy themselves that in the event of a misdeclaration, then recourse may be pursued.

31. Does CISADA 2010 affect the export of US goods to Iran?

CISADA 2010 writes into positive law existing presidential orders that no goods, services or technology of US origin may be exported to Iran from the US or by a US person, wherever located. There are limited exceptions to this provision (e.g. permitting the export to Iran of certain agricultural commodities, food, medicine and medical devices).

32. What is the impact on my ship's mortgage?

Members should closely examine their mortgage documentation to see what effect cessation will have. Occasionally the club agrees to give mortgagees 14 days notice of any intention to cancel for non payment of premium. Breach of sanctions will automatically trigger a cessation of cover. There is no need for any notice to be given by the club to the member or his mortgagee.

33. Can I import less than US\$1m worth of RPP into Iran and/or provide less than US\$1m worth of services and avoid these sanctions?

Yes, if the price is indeed a "fair market value" and if in doing so that importation/provision of services does not exceed an annual aggregate limit of US\$5m. However this course is fraught with risk and specific legal advice must be sought.

34. Would the chartering out of drilling rigs be regarded as enhancing the development of Iran's petroleum resources?

It is possible that such charters could be seen as contributing to the enhancement of Iran's ability to develop petroleum resources or to facilitate the maintenance or expansion of Iran's domestic production of RPP. CISADA 2010 provides for sanctions against parties that invest \$20m or more in investments that directly and significantly contribute to the enhancement of Iran's ability to develop petroleum resources.

35. Why was the Act enacted if the UN was dealing with Iranian sanctions in any event?

International disquiet with Iran has been widely publicised in the media. Negotiations at the UN culminated with the passage of UN Resolution No 1929 of 9 June 2010. Nevertheless, over the past year, a nearly unanimous US Congress has backed more aggressive economic measures against Iran, with particular focus on its access to refined petroleum products. Late last year, the US House and Senate each passed similar unilateral measures, but deferred finalizing the new law until the UN negotiations had concluded.

36. Will the International community copy the approach of CISADA 2010?

The UN may enact further resolutions mirroring the US unilateral approach. Equally, the EU and individual States such as the UK may enact similar legislation in the near future. Members are advised to monitor developments closely.

Useful links

UN Security Council Resolution No. 1929 (2010)

www.un.org/sc/committees/1737/resolutions.shtml

UK Sanctions

www.hm-treasury.gov.uk/financialsanctions

US SDN List

www.ustreas.gov/offices/enforcement/ofac/sdn