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EFFECT OF CHANGING SANCTIONS REGIME ON SANCTIONS EXCLUSION CLAUSES

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In a significant decision for parties engaged in global trade grappling with increasingly complex international sanctions regimes, the English High Court has considered the meaning and effect of a sanctions exclusion clause in a marine cargo insurance policy.

The decision gives helpful guidance on the protection offered by such clauses. However, it also highlights the significant potential for conflict between EU and US sanctions regimes following the US withdrawal from the so-called "Iran deal", the Joint Comprehensive Plan of Action ("JCPOA"), whereby sanctions relief was given in exchange for nuclear non-proliferation commitments from Iran.

The case is a salutary reminder of the issues likely to arise from this conflict (as highlighted in our previous briefing note on the topic).

BACKGROUND

The claimant, Mamancochet Mining Limited, was the assignee of the rights of Metalloyd Limited ("Metalloyd"), the insured under a marine cargo insurance policy (the "Policy") over two cargoes of steel billets shipped from Russia to Iran in August 2012. The defendants were some of the insurers under the Policy.

The cargo was delivered to the port of Badar-e-Anzali in Iran, where it was put into

bonded storage pending delivery. However, before delivery, the cargo was stolen. Following discovery of the theft in March 2013, Metalloyd claimed under the Policy. Although insurers accepted the claim was covered, they refused to pay because to do so would breach US sanctions. According to the insurers, their liability to pay was excluded by a Sanctions Limitation and Exclusion Clause in the Policy (the "Sanctions Clause") which provided:

"… no (re)insurer shall be liable to pay any claim… to the extent that… payment of such claim… would expose that (re)insurer to any sanction, prohibition or restriction under… the trade or economic sanctions, laws, or regulations of the European Union, United Kingdom or the United States of America."

THE APPLICATION OF THE US SANCTIONS REGIME

The insurers were UK entities ultimately owned or controlled by US persons and therefore, as "US owned or controlled foreign entities" under US law, were potentially subject to the US sanctions regime.

The US sanctions regime for Iran evolved significantly over the six-year period between the Policy being entered into and the claim being heard:

- It was common ground that the US sanctions regime2 did not apply to the parties, the transaction, or the Policy at the time the Policy was entered into in 2012;
- However, as of 8 March 2013, the sanctions regime changed3 and became applicable to the parties and the Policy. It was common ground that the claim was submitted after this date, so the Sanctions Clause was engaged and insurers were not liable to pay it;
- The position changed again when the US, EU and Iran (among others) entered into the JCPOA and, as of 16 January 2016, a number of the sanctions against Iran were It was agreed by the parties that as a result of these changes the payment of the claim under the Policy was no longer prohibited, provided it was not made in US dollars;
- The parties disagreed, however, whether the approval of the US and UK authorities responsible for the enforcement of the sanctions regimes was required before the claim could be The insurers insisted approval was required from at least the UK authorities and eventually, in January 2018, the parties submitted a joint referral;
- However, on 8 May 2018, before any final response to the referral was received, President Trump announced that the US would be withdrawing from the Accordingly, the US re-implemented its sanctions against Iran from 27 June 2018, subject to a "wind-down" period until 4 November 2018 in which existing transactions which were previously permitted under the US sanctions regime could be closed out without breaching the re-implemented regime; and
- The insurers contended that the Sanctions Clause was therefore re-engaged, and they were no longer liable to pay.

THE ISSUES BEFORE THE HIGH COURT

The claimant brought proceedings for payment under the Policy, seeking an expedited determination of the matter before the end of the "wind-down" period on 4 November 2018.

THE INTERPRETATION OF THE SANCTIONS CLAUSE

The key issue between the parties was whether the wording "expose that (re)insurer to any sanction" meant the Sanctions Clause applied in the event there was any risk that making a payment under the Policy might engage the sanctions regime.

Mr Justice Teare held that for the Sanctions Clause to be engaged it was necessary for him to find that, on the balance of probabilities, the US sanctions regime would be breached if the insurers paid the claim before 4 November 2018. He observed:

"…one would expect an assured would only be willing to agree that the insurer was not obliged to pay an otherwise valid claim where the insurer was prohibited in law from paying – rather than where there was merely a risk that the relevant authority would (perhaps wrongfully) impose a sanction… these considerations suggest that clear words would be required to establish a common intention that the insurer need not pay an otherwise valid claim where there was merely a risk that payment would incur a sanction."

The insurers also argued that the effect of the Sanctions Clause was to permanently extinguish any claim brought while it was engaged. Mr Justice Teare rejected this, concluding that the correct interpretation of the clause was that it merely suspended the insurers' liability to pay a claim for such period as the Sanctions Clause was engaged.

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WOULD PAYMENT "EXPOSE" THE INSURERS TO US SANCTIONS?

The question whether payment of the claim would be a breach of the US sanctions regime turned on whether the "wind-down" period, which permitted otherwise prohibited transactions to be carried out until 4 November 2018 to close out existing arrangements, applied to the close out of arrangements entered into before the relaxation of US sanctions under the JCPOA in 2016.

The insurers argued that as the "wind-down" period was put in place to allow for the transition from the sanctions position after 16 January 2016, the correct interpretation was that it should apply only to arrangements entered into between 16 January 2016 and the withdrawal from the JCPOA on 27 June 2018. The claimant, on the other hand, argued there was nothing to this effect in the US legislation or guidance, and that it should be interpreted as applying to the winding down of any arrangements entered into before 27 June 2018.

Mr Justice Teare again agreed with the claimant's submissions. Accordingly, he concluded that on the balance of probabilities the payment of the claim by the insurers before 4 November 2018 would not breach the US sanctions regime. Given his conclusion on the construction issues he therefore held the Sanctions Clause was not engaged, and the insurers were liable to pay the claim.

THE EU BLOCKING REGULATION

As noted above, on 8 May 2018, United States President Donald Trump announced that the US would withdraw from the JCPOA and as a result, almost all of the US sanctions waived or lifted in 2016 were reinstated. In an attempt to protect EU business from the re-imposition of US secondary sanctions, the European Commission re-activated the "blocking statute" (Council Regulation (EC) No 2271/96 or the "EU Blocking Regulation"). This prohibits EU companies from complying with US secondary sanctions on Iran, and entitles them to recover damages arising from such sanctions from the person causing them. See our earlier e-briefing for more information.

The court did not specifically decide whether the claimant could use the EU Blocking Regulation as it concluded the defendants were not entitled to rely on the Sanctions Clause.

Nevertheless, Mr Justice Teare commented *obiter* that he recognised "considerable force" in the defendant's arguments on this issue, i.e. the EU Blocking Regulation is not engaged where the insurer's liability to pay a claim is suspended under a sanctions clause such as the one in the Policy. This is because the insurer is not complying with a third country's prohibition but is simply relying upon the terms of the policy to resist payment

CONCLUSION

The decision in *Mamancochet v Aegis* gives helpful guidance on the interpretation of a widely-used standard form clause. It will also assist in the interpretation of similar provisions in other contracts.

It makes clear that for sanctions clauses of this kind to be engaged the beneficiary must demonstrate not merely that there is a *risk* that an action might be treated as a breach of a relevant sanctions regime, but that on the balance of probabilities it *would* be a breach of that sanctions regime. It further emphasises that such clauses merely suspend liability, rather than extinguishing it completely.

Mr Justice Teare's obiter remarks on EU Blocking Regulation may appear helpful for insurers with a US nexus but they are not binding and any analysis in other cases will be fact-dependent, particularly the exact wording of a sanctions clause and the timing of its inclusion. It also remains to be seen whether the other European authorities responsible for the enforcement of the EU Blocking Regulation will interpret it similarly.

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