

## **New York Financial Regulator Probes Sanctions Compliance Efforts of Non-US Reinsurers**

Following a year-long investigation, the New York Department of Financial Services (“DFS”) has directed twenty international reinsurers to provide information on their efforts to comply with stricter US sanctions on trade with Iran. In a letter sent last week, the DFS directed each recipient to produce information on sanctions compliance, including information on any lines of business potentially subject to sanctions and its policies and procedures for ensuring compliance. The DFS inquiry illustrates the increased emphasis of US regulators on extraterritorial sanctions compliance, and is a wake-up call for non-US insurers and reinsurers to assess their sanctions due diligence and compliance needs and to put programs in place to meet those needs.

US sanctions are designed to prevent certain targeted countries such as Iran from accessing the US financial system and to isolate them from the global financial system. The sanctions are enforced by the US Office of Foreign Assets Control (“OFAC”) and thus are commonly known as “OFAC sanctions.” They include civil and criminal penalties for violations of the restrictions. Historically, OFAC sanctions enforcement focused on transactions with a sanctioned country in which US corporations or individuals were involved, or which touched the US through some means, such as a wire transfer clearing through a US bank.

In the past few years, however, US policymakers have sought to increase economic pressure on sanctioned countries by broadening the extraterritorial reach of US sanctions regulations and imposing penalties on non-US entities that assist those countries in evading the sanctions. These developments make it imperative for non-US insurers and reinsurers to take stock of their policies and procedures for sanctions compliance. Recent changes in US law have tightened restrictions in an effort to disable Iran’s petroleum industry and to make other sanctions targeting Iran more effective. Last year, for example, President Obama issued Executive Order 13622 to bring within the scope of US sanctions any financial institution that knowingly conducts or facilitates any significant financial transaction: (1) with the National Iranian Oil Company or the Naftiran Intertrade Company; (2) for the acquisition of petroleum or petrochemical products from Iran; or (3) with the Central Bank of Iran relating to the purchase of US bank notes. The involvement of a US entity in the transaction is *not* required for a penalty to be imposed, and the penalty on the violating financial institution could be as severe as cutting it off from the US financial system by penalizing any US bank that engages in business with the non-compliant company. Other recent OFAC sanctions extend enforcement to foreign entities owned or controlled by US companies, and require the disclosure of Iranian transactions in US securities filings.

On 1<sup>st</sup> July, the Iran Freedom and Counter-Proliferation Act of 2012 (“IFCPA”) went into effect. It specifically provides for penalties against any entity providing insurance or reinsurance for (1) prohibited economic activity with Iran; (2) any person engaged in prohibited transactions; or (3) any “specially designated nationals.” An insurer or reinsurer found in violation of the IFCPA could potentially be barred from conducting business in the US.

The new IFCPA penalties applicable to the insurance industry were the stated reason for last week’s DFS inquiry to reinsurers. The DFS said it had learned that “several insurers had issued insurance coverage that applied to trades made with Iran,” that a claim had been made on a shipment of Iranian metal products under a policy “issued by a group of European domiciled insurance companies,” and that “the policy and the resulting claim payment would likely violate the IFCPA.” Although these are matters primarily for federal rather than state enforcement, the DFS expressed concern for New York cedants, stating that “similar transactions could jeopardize the ability of any involved insurer to conduct business in the United States. As a reinsurer certified under [the New York insurance regulations], the scope of your global operations and compliance with the IFCPA presents a new challenge to your ability to meet any future obligation to New York domiciled cedants.” The DFS noted the possibility that “insuring a sanctionable transaction, whether or not a claim is ever made, may be found to violate the IFCPA.”

The DFS admonished the reinsurers that “a robust due diligence regime is required to ensure that an insurance company is fully advised of the risks it is taking. Because an insurer may violate the IFCPA by engaging in conduct it should have known was improper, incautious due diligence could expose an insurer to the imposition of sanctions.” Accordingly, the DFS asked the reinsurers to identify and describe, by 15<sup>th</sup> July, their “plans to implement compliance and due diligence programs designed to avoid any potential violations of the IFCPA.”

The DFS inquiry, the continuing trend of extraterritorial enforcement of sanctions restrictions, and recent laws creating greater exposure for the insurance industry all indicate that non-US insurers and reinsurers should expect increasing scrutiny from US regulators – both federal and state – on sanctions issues. If they have not already, non-US insurers and reinsurers would be well advised to confirm the efficacy of their due diligence process and, if they do not have one, to begin the crucial process of identifying their compliance needs, and devising and implementing a program to ensure full compliance with sanctions restrictions.

We can help. Lewis Baach lawyers include former prosecutors and counsel to financial institutions who have extensive experience investigating alleged sanctions violations, helping clients develop and implement due diligence and compliance programs, and representing clients before government agencies on sanctions compliance issues. Of course, we also understand the

specific business needs of international insurers and reinsurers through our longstanding relationships in the London insurance market. With our unique blend of expertise in sanctions compliance and insurance, we can help to develop an effective program at a reasonable cost.

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