Member Circular No. 4/2016

May 2016

Iran trading – fixed premium P&I cover update

Dear Sirs,

Introduction

Members are referred to our Circulars 1/2016, 2/2016 and 3/2016 concerning Iran sanctions. This Circular is intended to update Members on the latest developments in relation to the interim and longer-term solutions to the reinsurance recovery shortfall risk under *Gard's Fixed Premium P&I Excess Loss reinsurance programme*.

1. Discussions with the US Administration

To recap, formal implementation of the Joint Comprehensive Plan of Action (JCPOA) was agreed on 16 January 2016 between the P5+1 countries and Iran, and Gard through the International Group has been continuing its engagement with the relevant departments within the US government (the State Department and the Treasury Department's Office of Foreign Assets Control (OFAC)) to discuss the P&I insurance ramifications of the implementation of the JCPOA.

However, to date, the US administration has not undertaken under the JCPOA to lift the primary US sanctions which prohibit the provision of insurance/reinsurance cover by US-domiciled reinsurers.

2. **Insurance cover solutions**

The Rules of all of IG clubs:

(a) contain provisions, under which the Member has no P&I cover in respect of activities or liabilities which breach applicable sanctions, or otherwise expose the club to sanctions or to the risk of sanctions,[1] and

(b) prohibit or limit (reduce) a Member's right of recovery from its club if there is a shortfall in the club's reinsurance, because of the application of sanctions (which includes any shortfall under the Excess Loss programs or any other reinsurance arrangement).[2]

Gard's Fixed Premium P&I Excess Loss reinsurance programme consists of two contracts providing limits;

Layer 1 USD 230 million excess USD 20 million; and Layer 2 USD 500 million excess USD 250 million; and in the event of losses both contracts have unlimited reinstatement of cover.

US-domiciled reinsurers have shares amounting to 37.5% under Layer 1 and, for reasons outlined above, would prohibit or limit (reduce) a Member's right of recovery from the club because of the application of sanctions.

[1] Relevant Gard Rules are: Rules 24.3 and 25.4 in the Rules for Ships; Rules 15.3 and 16.4 in the Rules for Mobile Offshore Units; and sections 13.2 and 14.4 in Additional Covers –Terms and Conditions 2016.
[2]Relevant Gard Rules are: Rule 77.3 in the Rules for Ships; Rule 30.5 in the Rules for Mobile Offshore Units; and section 26.4 in Additional Covers –Terms and Conditions 2016.

In an effort to find an interim solution to facilitate a resumption of lawful trading with Iran, Gard has been investigating the possibility of placing a "fall-back" reinsurance cover for its fixed premium P&I business. This cover is designed to respond to reinsurance recovery shortfalls resulting from the inability of US-domiciled reinsurers on the Fixed Premium Excess Loss reinsurance programme to make payments due to the continuing application of US primary sanctions.

3. "Fall-back" cover

The cover is an annual cover in respect of P&I liabilities and provides indemnity in respect of claims which would otherwise have been recoverable under Gard's Fixed Premium Excess Loss reinsurance programme but for an inability to pay by US domiciled reinsurers by virtue of continuing US primary sanctions.

The cover limit is for an amount of €75.5 million in respect of any one event, and in the annual aggregate, with one full reinstatement of cover. This limit would at current exchange rates accommodate a single loss scenario based on a combined single event liability of USD 250 million within Gard's Fixed Premium Excess Loss reinsurance programme. In the absence of exhaustion through a single loss scenario, the cover would be available to respond to a series of smaller loss events up to the €75.5 million aggregate limit.

However, because of the cover limit, and the single reinstatement terms (in contrast to the Excess Loss programme which has unlimited reinstatements), there is a risk that the cover could be exhausted by several very significant Iran-related liability claims, or an aggregation of smaller claims up to the overall current policy limit of €151 million (2 x €75.5 million).

Consequently, the cover is not a "like for like" replacement of the cover currently available under Gard's Excess Loss programme. Thus, if and to the extent the special Gard "fall-back" cover for fixed premium P&I business should become exhausted, the Member's right of recovery will be reduced accordingly pursuant to standard terms of cover.[3]

The "fall-back" cover itself contains a sanctions clause, which could be engaged in the event of future sanctions or prohibitions constraining the subscribing reinsurers. This "fall-back" solution is, however, only a temporary one, due principally to the cover and reinstatement limits. Efforts and engagement will continue with US Reinsurers and the US administration with a view to ensuring that a permanent long-term solution is in place for 2017 at the latest.

Any questions with regard to the above may be addressed to Kjetil Eivindstad or Malin Petre Gustavi, Gard, Arendal.

Yours faithfully,
GARD AS

Rolf Thore Roppestad

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Chief Executive Officer

[3] Rule 77.3 in the Rules for Ships; Rule 30.5 in the Rules for mobile offshore units; and section 26.4 in Additional Covers – Terms and Conditions 2016.