SUSEP Circular Letter on Embargoes and Sanctions, of August 7, 2019

santos bevilaqua ADVOGADOS

santos bevilaqua ADVOGADOS

Private Insurance Superintendence - SUSEP Circular Letter on Clauses on Embargoes and Sanctions

On 8/7/2019, SUSEP issued SUSEP/DIR2/CGCOM Circular Letter no. 6 that explains the clauses of insurance contracts providing for violation of laws or rules on embargoes or economic or commercial sanctions and their consequences.

The extraterritoriality of the rules on embargoes and sanctions is a problem and has been discussed in many jurisdictions. In Brazil, however, this issue acquires specific contours that call for even more care on the part of insurers and reinsurers.

SUSEP, considering (i) that many insurers are including, among the contractual conditions of their products, a clause on loss of rights, coverage limitations and/or exclusions from coverage deriving from violation of laws or rules on embargoes or economic and commercial sanctions, (ii) that the language of the clauses is, many times, comprehensive and addresses several different situations, and (iii) the number of inquiries of insureds and insurers about the legality and lawfulness of the Clause, explained:

> "The prevention measures taken by the insurers as to aspects of their activities that may have a connection with the elements of prevention and fight against terrorism, money laundering, and other types of wrongs in Brazil and abroad are legitimate.
>
> On the occasion of the risk underwriting, the insurer is expected to analyze if there are or not limitations for the coverage to be granted. If there are limitations, the proposal must be refused.

The situations of loss of rights or exclusion from coverage, whichever they may be, must be clearly and objectively described, without generic references.

The situations of loss of rights or exclusion from coverage arising from a violation of the laws or rules on embargoes or economic or commercial sanctions may be provided only in case of an intentional act of the insured or the insured's representative, with a causal relation with the event that generated the loss.

The situations of loss of rights or exclusion from the coverage cannot be based on international laws or rules, except for international agreements ratified by the Brazilian Parliament.

An event occurred subsequently to the issuance of the policy and that contravenes a Brazilian law or rule, or a law or rule incorporated into the Brazilian legislation, does not automatically entail exclusion from the coverage or the insured's loss of rights, and the insurer must comply with the law or rule and/or wait for the court decision.

In the case of sanction of freezing of assets, under Law no. 13810, of 2019, the insurer must suspend all types of payments arising from the insurance contract to the insured or the sanctioned beneficiary, according to said law. The suspension of payment is not characterized as loss of rights or exclusion from the coverage.

The insurer's possible exposure to sanctions, prohibitions or restrictions due to violation of laws or rules on embargoes or economic or commercial sanctions is not a justification for structuring the clause in disagreement with this Circular Letter.

The use of a certain clause in reinsurance and/or retrocession contracts is not a justification for the insurers to structure said clause, in disagreement with this Circular Letter, in the respective insurance contracts.

The use of a certain clause in insurance contracts does not exempt the insurer from evaluating the need to provide information as established in Law no. 13810/2019 and SUSEP Circular, which regulates Law no. 9613/1998."

Some aspects of the Circular Letter must be highlighted.

Note that SUSEP determined that the insurers that have a product containing a clause not in conformity with the understandings described above, must, within

a maximum period of 30 days as from the date of publication of the Circular Letter, change them to adjust the Clause in question to the terms of the Circular Letter.

Therefore, understanding the content and determination of the Circular Letter is a matter of urgency to mitigate the risk of imposition of penalties and even suspension (prohibition to sell) of those products.

To this end, initially, it is necessary to understand the background of the actions and responses of SUSEP concerning this issue.

In 2010, after an insurer's inquiry about a case involving the payment of an indemnity to a Cuban insured, SUSEP stated that: (i) a country's adoption of economic embargoes does not necessarily imply its adoption by other countries; (ii) there were at that time rules for the fight against terrorism financing; (iii) the non-coverage in that case would be a discriminatory act, without legal grounds; and (iv) SUSEP/DECON/GAB Circular Letter no. 03/07 listed the persons and entities connected to terrorism.

The Brazilian market began to discuss this issue with SUSEP more thoroughly after SUSEP has determined the elimination of the clauses on embargoes and sanctions from the insurance products. During those discussions, the relevance of the clause for global groups and even purely Brazilian companies was pointed out.

Notwithstanding the market efforts, the Circular Letter still reveals a sheer lack of knowledge of the issue and the consequences of the non-adoption of and/or disrespect for the clause.

In the Circular Letter, SUSEP recognizes that the measures adopted by insurers to prevent and fight terrorism, money laundering, and other types of wrongs in Brazil or abroad are legitimate.

SUSEP also affirms that the responsibility for the analysis to determine, on the occasion of the risk underwriting, if there are or there not limitations for the coverage to be granted rests with the insurer, and should it find that there are limitations, the proposal must be refused.

However, not always is it possible for the insurer to determine, on the occasion of the risk underwriting, if there are such limitations because some may emerge during the validity of the policy or may be identified only if a loss occurs. As an example, we may cite mass insurance whose characteristic is underwriting processes that are simple and, often, associated with the insured group and not with each individual.

Added to this, SUSEP affirms that the situations of loss of rights or exclusion from the coverage,

whichever they may be, must be clearly and objectively described, without generic references, and that the situations of loss of rights or exclusion from the coverage arising from a violation of the laws or rules on embargoes or economic or commercial sanctions may be provided only in case of intentional wrong committed by the insured or the insured's representative evidencing a causal relation with the event that generated the loss.

Indeed, the rules must be clear and objective. The violation of laws or rules on embargoes or economic or commercial sanctions may be not only a "passive" classification (caused by a new sanction or the characteristics of the loss) but also, and in general, does not depend on an intentional wrong because it is identified based on objective criteria.

Added to this is the fact that, contrary to SUSEP's understanding that situations of loss of rights or exclusion from coverage cannot be based on international laws or rules, except for international agreements ratified by the Brazilian Parliament, in our globalized world, foreign companies operate in several countries and, even if the laws of their countries of origin are not internalized by the other countries, this does authorize them not to obey such laws. Quite the opposite, if it is not possible to operate according to the requirements of their countries of origin, those companies may opt to leave the country and stop doing business there, a risk that is particularly relevant for non-central markets, such as the Brazilian market.

Concerning this aspect, SUSEP's understanding of the nature of the clause on embargoes and sanction is mistaken.

The clause is not a new contractual rule that is changed or revealed along the life of the contract. Rather, it is a contractual rule that, if well and clearly established, refers to a set of embargoes and sanctions that is in update process permanently and naturally.

It would not make sense, and there is no need to deepen the discussion about this aspect, to consider that embargoes and sanctions apply to contracts entered into after their enactment. And it would not make sense that Brazil should take a position different from that of the rest of the world and/or require that the companies that operate here follow costly and exotic practices and understandings that have no legal basis, are conceptually erroneously and are divorced from the logic and practices that govern the global markets. This, in addition to the evident mismatch between the insurance and reinsurance coverages, may make insurance and reinsurance contracts inviable.

As a matter of fact, the purpose of Law no. 13810, published on March 8, 2019, that provides for the

compliance with sanctions imposed by Resolutions of United Nations Security Council and specially designated nationals under investigation or charged with terrorism, terrorism financing, or terrorism acts, is to expedite asset freezing and the identification of individuals and legal entities associated with the terrorism and the distribution of weapons of mass destruction, in relation to the law previously in effect (Law no. 13170/15).

Upon the enactment of this Law, the regulatory and inspection bodies, among them, SUSEP, will be responsible for setting rules for the compliance with this Law; they will also supervise and enforce the measures to freeze assets of individuals and legal entities, as provided in art. 9 of Law no. 9613, of March 3, 1998, and will apply the applicable administrative penalties.

According to this Law, the assets will be frozen in compliance with the Resolutions of the United States Security Council or through designations of its sanctions committees or at the request of the foreign central authority, provided that in accordance with the applicable legal principles and based on objective grounds to meet exclusively the designation criteria set in the Resolutions of the United Nations Security Council or resolutions of its sanctions committees.

It should be noted that this is a rule that requires that the companies follow certain procedures, but whose nature and modification dynamics are similar to those of embargoes and sanctions, however, it does not even contemplate the possibility that the immediate application of the freezing is a violation of any contract. And, in Brazil, this is a constitutional matter since the Constitution protects the perfect juridical act against the effects of supervening laws. That is, the Brazilian legal system recognizes that an international decision may cause an immediate impact on contracts, but SUSEP does not recognize this possibility.

In conclusion, likewise Law no. 13810 and the efforts of the United Nations Security Council and its sanctions committees, the international sanctions are actions aimed at a social, political or commercial purpose at the international level, and the countries and organizations may impose fines on their members if they fail to obey the international sanctions.

The text of Law no. 13810 makes it clear that a law, as it is the case in question, or a clause on sanctions may incorporate elements contained in the International Law rules, even if they change along the life of the contract and/or are not easily identifiable in exhaustive contractual rules.

According to SUSEP/DIR2/CGCOM Electronic Circular Letter no. 6, Law no. 13810, but not the contractual rules, must be observed, which, given the constitutional nature of the protection of contracts, does

not make sense, not to mention the major disturbances and exoticism that this ensues.

Another example that may be cited and that perfectly reflects the application of the sanction in the Brazilian territory is the decision of Brazil's Prosecutor General Raquel Elias Ferreira Dodge suspending the act ordering Petrobrás to fuel Iranian ships because Iran is on SDN list – *Specially Designated Nationals and Blocked Persons List* – of OFAC – *Office of Foreign Assets Control* - of the US.

The decision highlights the statement of the Foreign Relations Secretary-General that "*although the unilateral US sanctions against Iran are not applicable within the Brazilian territory, the inclusion of the Brazilian economic agents in the scope of the US legislation on this matter, with possible practical effects produced in the US territory, may have political and commercial repercussions that cannot be disregarded.*"

Finally, for SUSEP, the insurer's possible exposure to sanctions, prohibitions or restrictions due to violation of laws or rules on embargoes or economic or commercial sanctions is not a justification for structuring the clause in disagreement with this Circular Letter. Moreover, the use of a certain clause in reinsurance and/or retrocession contracts is not a justification for the insurers to structure said clause in disagreement with the Circular Letter, in the respective insurance contracts.

In fact, the mere possibility of sanctions and use of a certain clause in the reinsurance and/or retrocession contracts does not justify the inclusion of the clause in the insurance contracts. However, treating this fact as a premise for the prohibition against the inclusion of the clause on embargoes and sanctions in the insurance contracts reveals, in addition to an inadequate understanding of the clause and the Brazilian legal system, an alarming detachment from reality.

It is clearly a mistake to understand that the clauses on sanctions that refer to sanctions imposed by countries on other countries are contrary to the Brazilian law.

It remains for the insurers to set procedures to deal with specific cases and, in an extreme case, it may be necessary not to perform the insurance contract and waited for a court order for its enforcement, which will reduce the risk of the insurer being held liable for noncompliance with embargoes and sanctions. All in all, this is another "jabuticaba"[1].

[1] Fruit similar to grape that exists in Brazil only, the reason why it is often compared to our ruling exoticism.

João Marcelo dos Santos
Insurance and Reinsurance
(55 11) 5643-1066
jsantos@santosbevilaqua.com.br

Ana Paula Costa
Insurance and Reinsurance
(55 11) 5643-1067
apcosta@santosbevilaqua.com.br

**** This Circular is for informational purposes only and does not contain any recommendation or legal advice from Santos Bevilaqua Advogados on the subject under discussion.*