



Impact of President Obama's April 13, 2010 Executive Order on Somalia and Piracy on US and non-US Insurance Companies

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I. Introduction

On April 13, 2010, President Barack Obama issued an Executive Order "Blocking Property of Certain Persons Contributing to the Conflict in Somalia" (the "Executive Order")¹ stating that:

...[T]he deterioration of the security situation and the persistence of violence in Somalia, and acts of piracy and armed robbery at sea off the coast of Somalia...constitute an unusual and extraordinary threat to the national security and foreign policy of the United States, and I hereby declare a national emergency to deal with that threat.

The Executive Order goes on to specifically state that:

I hereby determine that, among other threats to the peace, security, or stability of Somalia, acts of piracy or armed robbery at sea off the coast of Somalia threaten the peace, security, or stability of Somalia. Sec. 1(b).

The president additionally issued a "Message to Congress" which summarizes and provides some background to the Executive Order. It clarifies that the Secretary of the Treasury, in consultation with the Secretary of State, has the authority to take action to carry out the purposes of the Executive Order.

That same day, the Office of Foreign Assets Control ("OFAC") published the Executive Order and issued a Bulletin listing various individuals and entities that have been added to its list of Specially Designated Nationals ("SDNs"). This list comprises the Annex of the Executive Order and contains the names of individuals and a group that the U.S. considers to be particular threats. It has been reported that, among other reasons, the Executive Order was issued as a result of recent American intelligence linking the Somali insurgence group Al-Shabaab to the terrorist group Al Qaeda, and the concern that any payments made to this entity, or the individuals identified in connection with the Executive Order, would contribute to the growing threat of terrorist activity in Somalia and elsewhere.

The Executive Order thus seeks to block the payment, transfer or dealings in any property or property interests (including the "provision of funds") to the specifically designated persons. It also prohibits any similar transactions made for the benefit of any person whose property is blocked pursuant to the Executive Order.

This memorandum discusses the effect and impact of Executive Order and specifically addresses the impact, if any, it will have on an insurer's ability to pay ransom to pirates operating off the coast of Somalia.

¹The Executive Order was issued pursuant to the International Emergency Economic Powers Act (50 U.S.C. 1701 et seq.) (IEEPA), the National Emergencies Act (50 U.S.C. 1601 et seq.) (NEA), section 5 of the United Nations Participation Act, as amended (22 U.S.C. 287c) (UNPA), and section 301 of title 3, United States Code.

II. To Whom the Order Applies

Section 1 (a) of the Order states:

All property and interests in property that are in the United States, that hereafter come within the possession or control of any United States person, including any overseas branch, of the following persons are blocked and may not be transferred, paid, exported, withdrawn or otherwise dealt in.

Section 1 identifies two distinct categories of blocked persons or entities:

1. The individuals and entities listed in the Annex to the Executive Order (Sec.1(a)(i)); and
2. Any person determined by the Secretary of the Treasury, in consultation with the Secretary of State, who has:
 - [A] engaged in acts that directly or indirectly threaten the peace, security, or stability of Somalia; or...
 - [E] which is owned or controlled by, or have acted or purported to act for or on behalf of, directly or indirectly, any person whose property and interests in property are blocked pursuant to this order. (Sec.1(a)(ii))

The Executive Order also applies to:

The making of any contribution or provision of funds, goods or services by, to, or for the benefit of any person whose property and interests in property are blocked pursuant to this order. Sec. 1 (d)(i)

Finally, the Executive Order defines "Person" as "an individual or entity." "Entity" is in turn defined as "a partnership, association, trust, joint venture, corporation, group, subgroup, or other organization." Sec. 2 (a),(b).

III. What Payments or Transactions are Blocked?

A. It Appears that the Executive Order Applies to Specifically Identified

Individuals and Groups Section 1(a)(i) is straightforward and only applies to specific persons identified and listed in the Annex attached to the Executive Order. Section 1 (a)(ii), however, includes persons to be designated or identified by the Secretary of the Treasury, pursuant to the criteria then described. Although Section 1(a)(ii) lists classes of persons who could be identified, it still requires that individual **persons** (which as noted above, includes "entities," and which in turn includes "groups," "subgroups" and "organizations") must be specifically identified. Thus, the Executive Order does not now generally ban payments to "pirates," nor would it appear that "pirates" could be designated as a "group, subgroup or other organization." Section (1)(b) which "determines" that acts of piracy threaten the peace and security of Somalia has led some commentators to conclude that any person operating as a pirate off the coast of Somalia is a designated person, and that paying ransom to a Somali pirate would be in violation of the Executive Order. This appears to be too broad a reading of the Executive Order.

Instead, and as noted above, it appears that the Secretary of the Treasury must first designate specific blocked persons; just because an individual is a "pirate," or is engaged in the act of piracy, does not make that individual automatically a designated blocked person. The above has in fact be confirmed by a representative from OFAC who characterized the Executive Order as "list based" and stated that blocked persons had to be designated specifically by the Secretary of the Treasury. It is also consistent with the White House message to Congress, which discusses the "designation criteria" and the First Amendment requirements which must also be considered in connection with any designation pursuant to the Executive Order.

Importantly, however, the above described Section 1(d) provides that the “prohibitions” referred to in section 1(a) shall include but not be limited to “the making of any contribution or provision of funds, goods or services to or **for the benefit** of a person whose property is blocked...” Thus, a ransom payment to a group of pirates that could benefit an individual or group that is designated would be prohibited. This obviously complicates matters, as further discussed below.

B. Potential Ramifications if Ransom Money is Paid to a Designated Individual

Although section 1(a) requires that blocked persons be identified, there could be many scenarios in which a shipowner or insurer could unknowingly and/or indirectly pay ransom to a designated person. Imagine, for example, the situation in which ransom is sought by a group of pirates whose identity is unknown. The first problem is how to determine whether any of the pirates are on the list, or belong to a group, subgroup or other organization on the list. In most instances, this would be very difficult to determine. Even if the identity of the pirates is known, these particular pirates may be working for, either directly or indirectly, designated individuals or groups. It may thus be impossible to determine whether a ransom payment might ultimately, in whole or in part, end up in the hands of a designated blocked “person,” and thus have been for the benefit of that person and in violation of the Executive Order. Accordingly, while it may not be a complete defense to the charge of a prohibited transaction, it will no doubt be necessary to demonstrate that there was no knowledge on the part of a payee that a designated person benefited from the payment, or was believed to have been the beneficiary of the payment. As described at the end of this circular, notice to OFAC may also lessen any consequences. Of course, whether a designated person in fact benefited from any payment may ultimately prove impossible to determine, since ransoms are paid in cash and are untraceable once paid.

IV. Effect of an Executive Order

A. The Role of OFAC

Often, an Executive Order such as this one that is issued pursuant to the National Emergencies Act and the Emergency Economic Powers Act, designates the Office of the Treasury to promulgate more specific and detailed regulations that provide the framework and the penalties relating to the Executive Order. Such regulations are issued and implemented by OFAC. By way of brief background, OFAC forms part of the US Department of the Treasury and, according to its own website “administers and enforces economic sanctions programs primarily against countries and groups of individuals, such as terrorists and narcotics traffickers. The sanctions can be either comprehensive or selective, using the blocking of assets and trade restrictions to accomplish foreign policy and national security goals.” Although, to date, OFAC has not issued any regulations as a result of this Executive Order, it appears that they may do so based in part on the fact that the Executive Order was made pursuant to the national emergency powers and designates the Secretary of the Treasury to identify designated blocked persons. Moreover, OFAC compiled the list of designated individuals and groups for the Annex and published both the list and the Order on its website the day the Executive Order went into effect.

Should OFAC promulgate specific regulations pursuant to the Executive Order, the regulations will provide further guidance as to what is prohibited trade with Somalis. We should note that the violation of OFAC regulations is a serious matter and can often include criminal charges and/or significant fines and civil penalties.

V. Are Non-U.S. Insurance Companies subject to the Executive Order?

A. What constitutes a U.S. Person?

As set forth above, the Executive Order applies to “all property and interests in property of persons either “within the United States” or within the possession or control of “any United States person,” expressly including “any overseas branch,” as defined in section 3(c).

Specifically, Section 3(c) defines "United States Person" as:

... a United States citizen, permanent resident alien, entity organized under the laws of the United States or any jurisdiction within the United States, or any person within the United States.

Accordingly, the definition of a U.S. Person under the Executive Order is broad and wide-reaching. Foreign insurance companies with U.S. branches organized under the laws of the U.S., or the laws of any state in the U.S., should be aware that they will fall under this definition. Likewise, U.S. citizens working as employees or directors overseas, as well as foreign nationals working in the U.S., also meet the definition of a U.S. Person.

Moreover, because many, if not all, of the payments contributing to a ransom claim will at some point pass through a U.S. bank, prohibited ransom payments (i.e., those payments made to or for the benefit of a blocked entity), even if they are made by non-U.S. insurers, will likely be deemed to be property that is "within the United States" and thus violative of the Order.

B. Ramifications of Paying Reimbursement Claims of Ransom Already Paid by Shipowners

Although the Executive Order does not address insurance or the payment of insurance claims directly, according to the Department of Treasury's publication, Foreign Assets Control Regulations and the Insurance Industry, as a general matter OFAC advises that:

[U.S.] insurance companies should not engage in transactions with respect to an existing policy which has been discovered to cover or facilitate an unlicensed prohibited commercial activity or otherwise constitute an illegal export of a service.... [i]n no case should a U.S. insurance company pay a claim or otherwise service such a violative policy without first contacting OFAC for a specific license.

Thus, all insurance companies subject to the Executive Order would be prohibited from reimbursing prohibited ransom payments. As noted above, in applying the above broad definition of U.S. Person, non-U.S. insurance companies that have U.S. branches organized or incorporated under U.S. law (State or Federal) will be prohibited from reimbursing shipowners for ransom. Again, however, the best course of action when faced with such a scenario would be to contact OFAC for guidance and/or for a specific license allowing the claim to be paid.

VI. One More Thing.....

If and when OFAC promulgates regulations pursuant to the Executive Order, it will be possible to request written and published opinions from OFAC. Additionally, it may be presently possible to apply for a specific license to pay a particular ransom, or more generally, to apply for and obtain a license to write such business without penalty. It should be noted that we are aware that some U.S. insurers have done this already, in order to write business which may inadvertently violate Iranian trade restrictions. However, such general licenses may be of limited help in this case, as even with such a license the insurer must apply separately for permission to then pay the claim on a business covered by the license (i.e. in breach of the prohibitions). In the case of an inadvertent payment of the ransom which breached the Executive Order (i.e. to a pirate group controlled by a designated person, or to an individual who will share the ransom with that designated person or group) the violation of the Executive Order will have occurred before a separate license to pay can have been obtained. Nevertheless, OFAC advises that they should be contacted before a ransom is paid, and there is a hotline set up to contact OFAC for this purpose. We expect that this line may now become extremely busy.

Further information

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