

## Investigation of the effects of International Sanctions on Iran Insurance Company in Marine and Reinsurance Fields

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### ABSTRACT

The fact that Iran is an oil-rich country, relies on petroleum income for different types of economic investments, has access to free waters and conducts more than 90% of its export and import via marine transportation, necessitates presence of insurance industry and foreign insurers for investing in internal projects. As a result of international sanctions, big risks were accumulated inside the country. Insurance industry plays an important and vital role in today's modern economy but this industry was also harmed by sanctions. The present research investigates the impacts of economic sanctions on marine insurance and reinsurance treaties in Iran Insurance Company. This company is the only state company which has 5 active branches in UAE (Dubai Emirates, Abu Dhabi Emirate, Al-Ein Emirate, Sharjah Emirate and Ajman Emirate) and two branches in Oman (Muscat and Salalah) and one branch in Bahrain. One sample t test was used for analysis of research hypotheses. The results showed that all research hypotheses were supported.

**KEYWORDS:** Sanction, Marine insurance, Reinsurance, Risk accumulation, Credit Rate.

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### INTRODUCTION

International sanction is an instrument for obliging a country to change its political behaviors. Comprehensive economic sanctions and targeted sanctions are the most common types of sanctions. Economic sanctions are used for disrupting economic activities inside a country and making its people to protest against their government and make it to change its political behavior. In targeted sanctions, only governments or key man are aimed by sanctions and establishment of different restrictions changes political behaviors of a country (Etel Solingen, 2012). Economic sanctions can be imposed in three manners: trading, investment and investment removal. Therefore, there are four major ways for imposing sanction on a single-product country (oil) like Iran:

- A. imposing sanction on petroleum purchase as the main resource of income,
- B. sanction on product sales, commercial services and industrial services to mother industries and important infrastructural and strategic fields.
- C. sanction on navigation lines and oil tankers and transport airplanes.
- D. sanction on banking system, insurance industry and financial and credit institutes.

Iran was first put into black list by USA just after Islamic Revolution came to fruition. More sanctions were imposed on Iran after development of Iranian peaceful nuclear programs by UN, EU, USA and many other countries. In the aforementioned comprehensive sanctions imposed by UN and EU, all people and companies related to navigation industry, insurance industry, banking system, petroleum, gas and petrochemical industries and other industries regarding energy were aimed by sanctions. These sanctions which were accompanied by insurance and banking system sanctions, caused a lot of heavy costs on Iran, especially in insurance field. All European and American insurance & reinsurance companies and brokers like Munich Re, Allianz Insurance Company Lloyds syndicate, and stop their services to Iran Insurance market. These insurance companies refrained from presenting insurance coverage services like hull and machinery insurance of ships and tankers, insurance coverage on ships liability like P&I Club for shipping lines and reinsurance coverage for industries which were under sanctions. This research investigates the impacts of comprehensive economic sanctions on marine transport insurance and reinsurance in foreign branches of Iran Insurance Company.

### RESEARCH LITERATURE

#### Internal and external investment

Internal and external investment in industrial and service fields play important roles in development of any economy. It is obvious that absorption of foreign investment requires economic and political stability, successful diplomacy and good relationship with other countries (Taghvayee and Deh Namaki, 2012). In today's world, no country can live on without international trading. Countries become members in commercial, political and

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economic treaties & union like ECO, EU, W.T.O in order to establish regional and global relationships with other countries. In fact, having a successful relationship and diplomacy is the main factor for economic, commercial and industrial success. If powerful countries want to isolate a country which moves against their tastes and interests (like development of nuclear activities), they send out the country from their global village and remove it from their political and commercial circle and harm its economic and commercial infrastructure by imposing different types of sanctions. These sanctions affect other sectors like viruses and affect their performance adversely. Insurance industry is a sector which is badly affected by sanctions, because it is related to economic boom in other sectors. Insurance industry plays an important role in economy and no economic activity can become operational without insurance. International sanctions have had adverse impacts on Iran insurance industry. Insurance company serves as the provider of security for investors, importers and exporters of industrial, commercial and financial services and products and plays an important role in absorption of investments and maintenance of economic growth. Insurance industry has lost a considerable part of favorable and profitable portfolio and this has caused dissatisfaction in its internal and external partners and customers and loss of old and loyal customers (Ettel Solingon, 2012). Adverse impacts on insurance industry can be investigated from two dimensions as follows:

### **Direct Impact of Sanctions on Insurance Industry**

After imposing different sanction like insurance, on Iran by USA, the insurance industry was providing its insurance and reinsurance needs from European insurance market. However, provision of financial and credit services to Iran by European countries has been forbidden as a result of resolutions No. 1803.2008 and 1929.2010 (Garshasebi, Alireza, 2014). These sanctions caused many problems in different insurance fields as follows:

- Binding different types of reinsurance treaties with valid insurers which have high international credit rates were stopped.
- Restriction on reinsurance outward, ceding reinsurance treaties and complex risks beyond insurance industry capacity & retention to international reinsurers and finally unwise accumulation of risks inside the country.
- Evaluation, assessment and management of special and complex risks.
- Calculation and determination of actual loss of petroleum, energy, marine and aviation risks that before sanctions was done by international loss adjusters
- Settlement of claim with foreign insured of Iran Insurance company (direct risks and inward risks)
- Payment of reinsurance premiums to reinsurers & brokers.
- Payment of international surveyor's fees.
- Providing P & I club covers for Iranian ships and tankers.
- Providing international guarantees for general average claims.
- Providing of required coverage for airlines and ships.
- Providing of insurance services of travel policies to passengers who travel to Iran or outside Iran.
- Cooperation with London Lloyds Syndicate was disconnected.
- Inalienability of Intentional credit rating services institutes like Fitch Credit Rating, Moody's credit rating, S&P credit rating and ... to Iranian insurance companies.
- Unacceptance of Iranian issued policies by international organizations like international transport companies, banks, customs of foreign countries (Afkhani, 2013).
- Absence of training services

### **Indirect Impacts of Sanctions on Insurance Industry**

- Petroleum purchase sanction
- Product and service import and export sanction
- Non availability of classification of ships and tankers of IRISL and other Iranian shipping lines
- Sanction on international investments in infrastructural, petroleum, energy, gas, petrochemical and sectors
- Sanctions on banking system and Central Bank of Iran through disconnection of SWIFT cooperation with Iranian banks.

### **Definition of Sanction**

In Persian language, Tahrim (=sanction) literally means forbidding something. Sanction refers to aggressive actions which are imposed by one or several countries against a country which has violated international laws or has violated unacceptable ethical criteria (Karimi, 2006). That is to say, sanction is an action which is taken by one or several countries (sanction imposer) against one or several countries (sanction targets) in order to punish them so that they cannot transact with other countries and have to accept especial norms (from sanction imposers' viewpoint) (Karimi, 2014).

### **Economic Sanctions**

Economic sanction refers to actions which are taken by one or several countries against another country which has violated international laws or disobeyed ethical criteria (Hoseini, 2012). Sanction imposers aim to force the target country to leave its aims or at least come to negotiation table. Generally, economic sanctions are imposed against governments. However, after 11<sup>th</sup> of September 2001, economic sanctions were developed and included individuals and non-government organizations. Moreover, since 2001, another aspect of sanction which is smart & targeted sanction was developed (Karimi, 2012).

### **Success or Defeat of Sanctions**

Although there are basic challenges regarding successfulness of economic sanctions due to globalization of economy and removal of borders, researchers believe that sanctions have not been that much successful. However, economic sanctions are imposed to draw economic space of a country into chaos. Sanctions perform well only when economies are in mutual commerce space or when an economy is the center of global commerce (like USA). There are 6 important pillars for investigation after imposition of economic sanctions (Goudarzi, 2013).

1. Goal: in fact, whether the imposed country is self-sufficient in sanction area or not? On the other hand, what is the position of sanction target in economic transactions of the imposed country with international economy? In case of self-sufficiency, sanction will be defeated and sanction imposers have to change sanction target or the sanction will be defeated. If the position of sanction target is decisive for the country, it can harm its economy seriously.
2. Partners of the sanctioned country: if the sanctioned country is not self-sufficient in sanction target, it is necessary for sanction imposers to determine main political and commercial partners of the target country and therefore block possible escape routes. At the beginning, sanction imposers specify partners which are required for elimination of the uncertainty.
3. Executive costs: sanction execution costs should not be high both for sanction imposers and the imposed country. A high cost will fail because partners will not be adherent to sanctions. Sanction imposition costs should not be so high that economic activities reduction loss weakens imposer and its partners.
4. Communications: in sanction literature, former relationships between the imposer and imposed are very important. If the relationship is friendly, we can expect that sanctions are not executed and if there is no aggressive relations between them, sanctions will be implemented more probably.
5. Sanction imposers behavior: diplomacy should be at the top of sanction agenda. In other words, the imposed country should always try to show its goodwill regarding disagreements and eliminate misunderstandings. This has fewer costs compared with sanctions implementation and sanction imposer behaviors (Irvani, 2014).

### **Economic Sanctions Targets**

Virtually all sanction experts unanimously agree on difficulty of determination of sanction imposer targets. It is right that imposer targets are first obvious for internal and international addressees. Furthermore, a sanction imposer is usually a country or institute which wants to reach several targets. Consequently, investigation of latent goals of sanctions is required. A review of former economic sanctions and studies regarding them reveals that goals of economic sanctions can be classified in four categories punishment (deterrence), compliance (coercion), destabilization (subversion) and symbolism (obvious impact). We discuss them in the following sentences.

#### **A. punishment**

Economic sanctions have been mainly used for punishing an offender both historically and conceptually. The goal is not necessarily to change offender's behavior but it is used for punishing offender and indication of the end of such a behavior to others. Economic sanctions are also used for achieving punishment targets so that unacceptable behaviors are become logically acceptable. If a target country is affected seriously enough, it is less possible for it to repeat the action (Arnove, 2013).

#### **B. compliance**

a sanction imposer may impose sanctions in order to make target country comply with international requirements and change its policies and behavior. this facilitates rebuilding unfavorable situation or acceptance of international standards. In contrast, sanctions imposed by an imposer are aimed at making the imposed country to do trustable actions. This is very difficult (Paul, 2012).

#### **C. Destabilization**

G. sanction imposer may impose sanctions for destabilization of target government or collapse of total political regime.

### **Classification of Different Types of Sanctions**

Different classifications have been mentioned for sanctions in different texts and papers. All classifications have more or less the same meaning. Concept and application:

### **Private Sanctions (national)**

Sometimes, sanction may be imposed by individuals, groups or non-state institutes in order to make a country or its citizens or even their own governments do a particular course of action and behavior. Private sanctions have limited applications. The first private sanction (territorial) took place by Chinese people during 1905-1931. In this period of time, 11 sanctions were imposed by Chinese commercial groups and 9 of them were imposed against import from Japan. During 1931-1933, after occupation of Manchuri by Japan, Chinese Government also joined semi-formally to sanctions and supported them (Bailey, 1994). Other examples of private sanctions include: Indian people sanctions against England. After nationalization of petroleum industry in Iran during 1951-1953, foreign tankers which transported Iranian petroleum imposed sanctions on Iran and refrained from serving.

### **Government's Sanctions against Each other or Multilateral Sanctions**

One of the effective techniques in implementation of foreign policy for implementation of targets and reaching national benefits is use of economic, financial, commercial and technological instruments. A government which makes use of such tools tries to convince other government change their foreign polices so that these changes can provide the benefits of the country which has used the instruments. These sanctions can be one-sided (one government against another government) or multilateral (several governments against one government).

### **Non-Economic Sanctions**

Different types of non-economic sanctions

These sanctions are usually started before economic sanctions and are aimed to convince target country to change a course of action and include the followings:

1. Refraining from issuing visa
2. Reduction in the level of political representatives
3. Prevention from membership of target country in international organizations
4. Disagreement with target country hosting for international meetings
5. Refraining from financial contributions and formal aids

### **Economic Sanctions**

War and coercion are usually substituted with economic sanction. By economic transactions, we mean all types of economic relations including commercial and financial (Valizadeh, 2011).

a. Economic sanction for strategic targets:

It usually takes place of war and its economic costs are less than war and it is considerable for imposing countries.

b. Economic sanctions for non-strategic targets/other economic benefits

### **Sanctions Dimensions**

- Commercial and economic sanctions
- Financial-logistic sanctions (bank, insurance, investment sanction)
- Scientific sanction
- Human sanction
- Human right sanction
- Nuclear sanction
- Terrorism support sanction (terrorists financing)(Abolhasani, 1996)

### **Research hypotheses**

#### ***Main hypothesis***

International sanctions have influenced marine-cargo portfolio of Iran Insurance Company (Overseas branches).

#### ***Subsidiary hypotheses***

1. International sanctions have affected marine-cargo portfolio of Iran Insurance Company (Overseas branches).
2. Absence of collaboration of well-known European and American reinsurance companies have affected marine-cargo portfolio of Iran insurance company (Overseas branches)
3. International sanctions have affected collaboration of international credit rating institutes with Iran Insurance Company.
4. International sanctions have affected increase in risk retention and accumulation of risk in Iran Insurance Company.
5. International sanctions have affected acquisition of technical knowledge required for insurance operations of Iran insurance company.

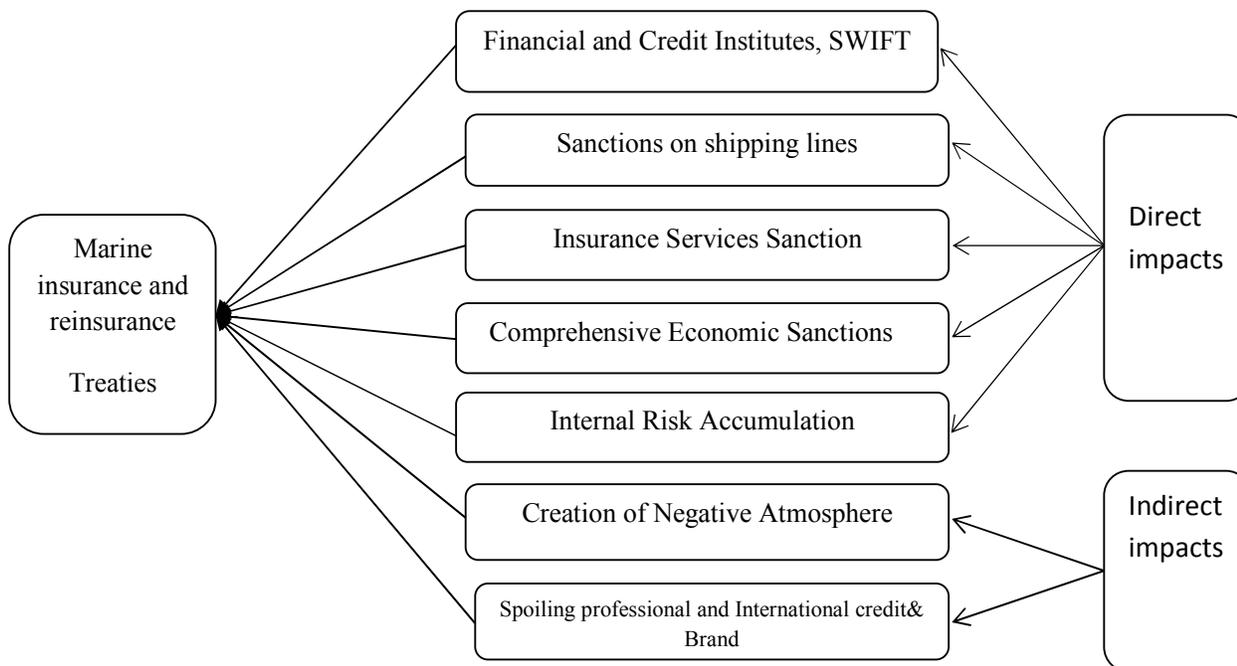


Figure 1. research conceptual model  
Moran and Salisbury, 2013

**RESEARCH METHODOLOGY**

Considering the fact that this research aims to investigate the impacts of international sanctions on Marine Portfolio and reinsurance treaties in Iran Insurance Company from insurance area, experts' viewpoints, this is a descriptive survey. Statistical population of the research included all senior managers and experts of Iran Insurance Company inside Iran and managers and experts of overseas branches. They included 150 people. 110 people were selected according to Krejcie-Morgan Table. In this study, Cronbach's alpha was used for calculation of reliability. 20 questionnaires were distributed among respondents for investigation of reliability. Cronbach's alpha was equal to 0.775 in general questionnaire. The questionnaire has therefore a good reliability value.

**Data Analysis**

We first described data demographic features including gender, age, and education and so on. In inferential statistical analysis, we used Kolmogrov-Smearnov test and one-sample t test using SPSS (version 19).

**Descriptive Analysis of Demographic Features**

Descriptive statistics refer to a collection of criteria which can present general features of data. It should be noticed that descriptive statistics cannot be generalized to other populations and they are used only for presenting an overall view. In the present research, we only present tables and figures for investigation of observations.

Table 1. Descriptive Results of Demographic Features of Respondents

		Statistical Indices	
		Frequency	Percentage
Education	High School and Associate's degree	4	3.6
	Bachelor degree	43	39.1
	Master Degree	52	47.3
	P.H.D	11	10
	Sum	110	100
Work Experience	Below 5 years	4	3.6
	Between 5 to 10	10	9.1
	Between 10 to 15	14	12.7
	Between 15 to 20	27	24.5
	Greater than 20	55	50
	Sum	110	100

### Data Normality Test

Kolmogrov-Smearnov test was used for investigation of normality of data distribution. In all hypotheses, statistical hypothesis is as follows:

H0: data are normal (data come from a normal population)

H1: data are not normal (data do not come from a normal population)

Table 2. Kolmogrov-Smearnov Test for Research Variables

Normality Result	Sig	Z statistic	Data Related to
Normal	0.357	0.927	Hypothesis 1
Normal	0.698	0.708	Hypothesis 2
Normal	0.632	0.747	Hypothesis 3
Normal	0.445	0.863	Hypothesis 4
Normal	0.103	1.217	Hypothesis 5

As it can be seen in table 2, because significance level in all hypotheses is greater than error value (0.02), H0 is not rejected. In other words, research data are all normal and parametric tests should be used.

### Investigation of Research Hypotheses

Table 3. Correlation Coefficient for Subsidiary Hypotheses

Variables	Mean	SD	T Statistic	Sig.	Result
International Sanctions on Insurance Operations	3.712	0.467	15.988	0.000	supported
International Sanctions on Marine Portfolio	3.476	0.392	12.727	0.000	supported
Absence of Collaboration of well-known Reinsurance Companies	3.828	0.756	12.115	0.000	supported
International Sanctions on Collaboration of Credit Rating Institutes	3.677	0.693	10.255	0.149	supported
International Sanctions and Increase of Accumulation of Risk	3.0697	0.503	1.455	0.000	supported
Spoiling professional and International Credit & Brand		313	0.364	0.000	supported

The best solution for the present conditions for Iran is to adopt an economic model which can move Iran forward in war, chaos, revolution, sanction and crisis conditions. These conditions are permanent for Iran and are not transitional like other countries. In this model, sanctions are regarded as opportunities which can be used for correction of weak points of economic system. Economy of a country which has a particular worldview and this worldview contrasts benefits of powerful countries will be a special economy. Therefore, all mechanisms should be designed in a way that protect economy against threats and pave the way for targets.

### Recommendations Based on Research Findings

As Iranian Transport Committee chairman says, 90 to 95 percent of foreign trade is done via sea. Marine transport plays an important role in developing countries' economies in today's competitive and free trade world. Therefore, imposition of any kind of sanction and stoppage on marine transport process can eliminate many import and export insiders and they will not be able to maintain an income margin. Research results also showed that after imposition of recent economic sanctions by international assemblies, Iran Insurance Company operations and activities in marine and also reinsurance treaties was adversely affected both internally and externally. Marine portfolio of the company reduced considerably. Furthermore, all reinsurance companies, syndicates, insurance clubs and insurance brokers stopped their cooperation with company and they had to retain a considerable amount of its risks or use Asian reinsurance market capacity as a result of fearing from European Union or USA sanctions. Moreover, sanctions on central bank and banking system contributed to insurance activities reduction because a large part of marine portfolio of overseas branches of Iran Insurance Company is resulted from opening letter of credit and this portfolio dropped considerably as a result of sanctions of banking system and shipping lines.

International sanctions especially sanctions on banking system, shipping lines and insurance service provision did not stop product import to Iran because Iran's geographical and geopolitical position (15 sea and land neighbors with different political approaches) challenges international sanctions. In other words, international sanctions have only increased the cost of services and products. Besides other commercial firms, insurance industry especially foreign branches which are mostly located in Persian Gulf and Oman Sea are economic firms which have incurred costs because marine premium income reduced considerably as a result of

economic sanctions. Marine portfolio is a profitable portfolio in all insurance companies because average loss ratio in this field is less than 40%. Therefore, the following recommendations are presented:

1. Presenting appropriate conditions and rate for marine insurance (Cargo & Hull) of launch which transport Iranian products from UAE to Iranian ports and vice versa. It should be noticed that as launch owner's guild union chairman says, more than 3000 Iranian launch are transporting goods between UAE and Iran.
2. Use of government insurance fund capacity for putting insurance coverage on Iranian and foreign ships which transport goods to Iranian ports. Considering special situation of UAE which has an economy mainly based on re-export activities and geographical distance of two countries, many cargos are transferred to Iran via Launch, which are not classified as ships. Therefore, there is a good opportunity for reforming marine portfolio for branches which are active outside Iran in UAE and Oman via designing appropriate strategies for risk management and absorption of portfolio in this sector.
3. Increasing and strengthen insurance capacity and coverage range of Iranian P & I clubs for provision of coverage for overseas branches insured / clients.
4. Improvement of government fund for providing necessary coverage for insured and then ceding risks to international reinsurers.
5. Cooperation with of Stock Market for turning and securitization of natural/ catastrophe and large industrial risks.
6. Establishment of joint venture Reinsurance Company with friendly countries or purchase stocks of successful international reinsurance companies for using their capacities in submission of risks.
7. Improvement of employees' technical knowledge via participation in training classes, seminars, and international educational workshops.
8. Use of reinsurance capacity of Asian countries and friendly countries for transferring risks and creation of balance in retention and ceding the risks and avoiding accumulation of risk inside Iran.
9. Technical improvement and knowledge promotion of internal insurance funds and consortium in order to understand nature of risks and provision of technical consultancy for insured in order to improve security level of risks and reduce their risk.
10. Employees' technical knowledge level should be promoted in order to accept risks and make decisions regarding way of retaining or transferring the risks via education.
11. Central Insurance of Iran should supervise well on determination of insurance companies, risk share and their rating and acceptance manners depending on their financial and technical capability.
12. <sup>1</sup>Maximum Probable Loss (MPL) and estimated maximum loss (EML) for risk retention share should be considered in companies regarding risks distribution in consortium and internal insurance pool.
13. Necessary reinsurance coverage should be prepared through Asian, African and European countries which are not members in EU, by considering their credit rate and global distribution of risks, in order to commit their insurance obligations and cover natural catastrophes risks in the most compressed insurance spot of country by considering estimated maximum loss.
14. Adequate specialized training should be prepared for employees for familiarizing with different types of risks via inviting international experts or sending employees to professional courses.
15. Globally, it is common to ask reinsurers to hold training courses for employees in return for submission of reinsurance contracts.

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