[WHITE PAPER]

A North Korean Sanctions Evasion Typology

Use of Complex Ownership Structures

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Contents

Abstract

1.0

The international campaign to disrupt North Korea's nuclear weapons program includes sanctions imposed by the United Nations Security Council, the European Union, the United States, and the United Kingdom, among other jurisdictions and authorities.

According to U.N. Panel of Expert reports, under pressure from the international community, the North Korean government relies on illicit activity to evade sanctions and generate revenue for its weapons programs, including cybercrime and stealing and laundering cryptocurrency. North Korea also makes use of networks consisting of front or shell companies to gain access to the international financial system.

Financial institutions and multinational corporations, in turn, must ensure they conduct enhanced due diligence to accurately detect North Korean support and facilitation networks. This white paper will highlight examples of how North Korea-related actors use opaque ownership structures to evade sanctions.

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Indicators of a North Korea-Related Front Company

2.0

According to the U.N., North Korea accesses the international financial system through networks of front companies, financial representatives, and corporate service providers, which often share similar characteristics. Leading guidance cautions that the presence of certain features in the corporate structures of shell companies may be seen as red flags for potential North Korean exposure. Awareness of these common indicators can help financial institutions and other businesses identify potential risk and ensure that they are not processing transactions for or otherwise engaging with sanctioned North Korean actors.

According to U.N. reports and U.S. advisories, **many front or shell companies, banking and financial representatives, and corporate service providers used by the North Korean government are based in China, especially in Chinese provinces that border North Korea.** These provinces, including Liaoning and Jilin province, are significant locations for North Korea-related actors seeking to access the international financial system through China. Other jurisdictions where such front and shell companies are registered include Hong Kong, Panama, Russia, the United Kingdom, Singapore, Vietnam, and other countries in Southeast Asia.

Another indicator of North Korea-related front and shell companies is that **they are often set up to operate in non-financial industries**, including shipping, import/export, textile, garment, fishery, and seafood. However, these companies often **lack a stated business purpose**, or the **payments they receive for products and services do not correlate with their specified business lines**. They also typically **do not maintain a website** or other online presence despite their significant transactions.

In addition, the **names of North Korea-related front and shell companies are often overly generic and non-descriptive**. Sometimes they can be easily mistaken with that of another, better-known corporate entity. Company names may also be **intentionally misspelled** in different ways. These indicators may be treated like red flags and integrated into enhanced due diligence and Know Your Customer (KYC) controls.

North Korea-related financial facilitators often establish and use multiple companies that **share the same owners and managers**, and at times, **the same address, telephone number, and employees**. Such companies also may **transact with similar business partners**. The use of multiple companies provides financial facilitators with alternatives in the event that one company is sanctioned or shut down. Consequently, in order to prevent North Korea-related actors from using shell companies to conceal their illicit activities, it is critical to identify the beneficial owners of and individuals with control over an account or entity.

According to a September 2020 United Nations Office on Drugs and Crime (UNODC) report on beneficial ownership regulations and company registries in Southeast Asia, "countries in Southeast Asia are considered to be very secretive when it comes to the transparency of ownership of legal entities and other forms of wealth." Due to a lack of comprehensive, accurate, and current information on beneficial and legal ownership, law enforcement agencies in the region often encounter significant challenges in detecting and investigating suspicious cases, and financial institutions are sometimes unable to conduct reliable due diligence on their customers.

North Korea and its facilitators have established numerous joint ventures and front companies in jurisdictions with **limited access to or regulations on beneficial ownership information**, such as Cambodia, Malaysia, and Thailand. The UNODC report highlights the need for further work in Southeast Asia to address information gaps on beneficial ownership, including through the collection and verification of such data in central registries.

Case Studies

3.0

3.1 MCM INTERNATIONAL TRADING COMPANY LIMITED

This case study demonstrates how North Korea can use complex ownership structures to evade sanctions.

According to the March 2021 U.N. Panel of Experts report on North Korea, MCM International Trading Company Limited was a North Korean joint venture or cooperative entity operating in Thailand. The company was exposed during the course of a U.N. Panel of Experts investigation into possible sanctions evasion activities.

According to corporate records accessed in April 2021, North Korean national Chol Min Myong was a director of

MCM International Trading. Corporate records also show that **49% of MCM International Trading was owned by two North Korean nationals**, and the remaining 51% of the company was owned by three Thai nationals. Thailand does not have a mechanism to record or report on beneficial ownership information, as laws and regulations in the country do not cover beneficial ownership.

According to corporate records, the reported business line of MCM International Trading was "management consultancy," but MCM International Trading also appears to have manufactured and distributed tobacco products, according to a business-to-business portal for the tobacco industry. **Tobacco joint ventures have historically been a lucrative source of revenue for North Korea**; its illicit international cigarette trade, for example, was reportedly worth billions of dollars per year as of 2018.

North Korea also **gains access to international banking channels through joint ventures**. Pursuant to U.N. Security Council Resolution (UNSCR) 2375, the U.N. generally prohibits the creation of joint ventures or cooperative entities and the expansion of existing joint ventures with North Korean entities or individuals. The UNSCR also calls on **U.N. member states to shut down all businesses of North Korea that are operating within their jurisdictions**, unless the joint venture has been pre-approved by the U.N. Security Council Committee. The resolution provides exemptions for joint ventures pre-approved by the U.N. Security Council Committee that are "non-commercial, public utility infrastructure projects not generating profit."

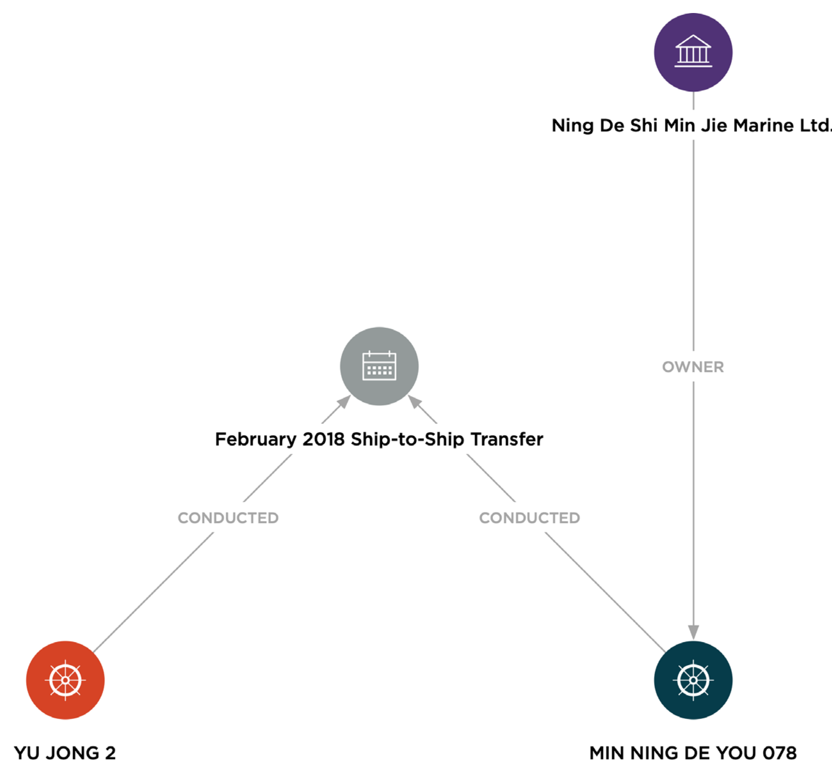
The March 2021 U.N. report stated that the Panel was conducting further investigation into MCM International Trading and had requested additional information from Thailand. MCM International Trading was made defunct on October 28, 2021.

3.2 THE MIN NING DE YOU 078

The Min Ning De You 078 shipping vessel highlights the difficulty of uncovering the ownership structures of entities that may be engaged in activity that violates sanctions on North Korea.

Complex ownership or management is a deceptive practice used by North Korean illicit shipping networks, according to a May 2020 U.S. government advisory. North Korea-related actors attempt to engage in commercial activity with the global shipping sector through the use of opaque business structures, which may involve shell companies and/or multiple levels of ownership and management.

In February 2018, the Japan Maritime Self-Defense Force found that **the North Korean-flagged tanker, Yu Jong 2, was anchored alongside the vessel Min Ning De You 078 in the East China Sea**. Japan strongly suspected that the vessels conducted a ship-to-ship transfer, which is banned by UNSCR 2375, based upon the fact that the two vessels lay alongside each other and connected hoses.



The vessels Min Ning De You 078 and Yu Jong 2 were designated by the U.N. Security Council in March 2018; the Yu Jong 2 is also sanctioned by the U.S. and U.K. The Min Ning De You 078 is subject to de-flagging, and Member States are prohibited from allowing the vessel to enter their ports, unless the Security Council 1718 Sanctions Committee determines in advance that such entry is required. The Min Ning De You 078 does not have an International Maritime Organization (IMO) number and was described by the Japanese government as a small vessel. North Korea has been known to **transport petroleum products and coal through ship-to-ship transfers using smaller vessels**, among other evasion tactics.

The weight of the Min Ning De You 078 was possibly under the tonnage required for an IMO number, which might explain why the owner of the Min Ning De You 078 cannot be identified in maritime databases. However, according to a ship inspection log, China-based Ning De Shi Min Jie Marine Ltd was the owner of the Min Ning De You 078 as of November 2020. Ning De Shi Min Jie Marine Ltd was listed as the owner or operator of more than 30 other vessels at the time.

The majority of these vessels also do not have IMO numbers. **Vessels conducting ship-to-ship transfers with North Korean vessels will typically disable their AIS transponders** to mask their movements and facilitate illicit trade.

Conclusion

4.0

Financial institutions can mitigate the risk of inadvertently facilitating illicit North Korean commercial activity by conducting effective enhanced due diligence procedures that are informed by international guidance and risk typologies.

Leading guidance recommends the following best practices to strengthen internal controls as part of an effective sanctions compliance program:

+ Screening against relevant sanctions lists, such as the U.S. or U.N. sanctions lists, is an essential initial step of a financial institution's internal controls.
+ Use of structured data that provides ownership and beneficial ownership can then be used to strengthen screening capabilities.
+ Ongoing training is essential to an effective anti-money laundering program and to detect sanction evasion activities. A well-developed training program should ensure that sanctions compliance responsibilities are communicated to employees and that all appropriate staff are equipped with the required knowledge and resources to effectively conduct due diligence.
+ Financial institutions can send circulars to appropriate personnel that include new regulatory requirements, updated guidance, and the latest typologies and case studies regarding North Korea-related sanctions evasion techniques.

Key Sources Used for This Report

5.0

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ABOUT US

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