

# ***Training Materials***

## ***Countering North Korean Procurement Networks through Financial Measures: Role of Southeast Asia***

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# Introduction

- SE Asia's relative geographic proximity & rudimentary export and financial controls make it vulnerable to DPRK abuse
- SE Asia's financial system were used for the payments of North Korea-based Ocean Maritime Management (OMM)
  - Singapore: Chinpo Shipping, Senat Shipping
  - Thailand: Mariner's Shipping
  - Malaysia: Pak In Su
- Awareness and understanding regarding CPF is limited in the region



## Part I

# Role of Financial Measures in Countering Proliferation Finance CPF

# Financial Dimension

- Every illicit trade transaction ultimately requires payment
- Use of formal financial system rather than informal sector due to acquisition from legitimate suppliers
- Operate for financial profit and vulnerable to disruption of funding

# Role of Financial Measures in CPF

- Financial transactions leave footprints
  - Investigative value: Authorities obtain documents
  - Analytical value: Uncover broader proliferation networks
  - Deterrent value: Proliferators fear of being discovered
  - Preventive value: Production of WMD impeded



# **Part II**

## **International Legal Framework**

# International Legal Framework

- UN Security Council
  - Resolution 1540
  - Resolutions on North Korea and Iran
    - Financial Provisions of the Resolutions
- Financial Action Task Force (FATF)
  - Recommendation 2 and 7
- US Regulations
  - Secondary Sanctions



# **United Nations Security Council (UNSC)**

# UNSC Resolution 1540

- Operative Paragraph 2 requires to adopt and enforce laws to prohibit the financing of certain actions related to nuclear, chemical or biological weapons and their means of delivery: manufacturing, acquiring, possessing, developing, transporting, transferring, or using.
- Operative Paragraph 3 obligates to have “controls on providing funds and services” that could contribute to WMD and related missile capabilities.
- Resolution 1540 did not elaborate how to achieve these requirements

# Implementation of 1540

- Implementation lagging
- Implementation Challenges
  - Political will
  - Lack of capacity & resources
- No enforcement mechanism
  - 1540 Committee's task is to oversee the implementation

# UNSC Resolution 1540

- 1540 Committee monitors implementation status of Resolution 1540 with national reports and reports to the Security Council
- 1540 Committee publishes
  - Committee's report without detailing countries status
  - Country matrices based on country reports
    - UNSCR1540 Matrix
      - SE Asian countries CPF legislation incorporated into anti-money laundering and countering terrorism financing legislation (AML.CPF)

# Criminalization of Proliferation Finance by Southeast Asian Countries

South East Asian Countries	1540 Matrices (Approved by December 2015)
Malaysia	Criminalized under AML/CFT Law and Penal Code
Singapore	Criminalized under AML/CFT Law, Terrorism Act
Indonesia	Criminalized under AML/CFT Law (Uncertain)
Cambodia	Criminalized under AML/CFT Law (Uncertain)
Thailand	Criminalized under AML/CFT Law
Philippines	Criminalized under CFT Law, nuclear weapons financing criminalized under another legislation
Vietnam	Criminalized under AML Law (Uncertain)
Myanmar	Criminalized under AML/CFT Law
Brunei (Brunei Darusselam)	Criminalized under Anti-Terrorism Law, Internal Security Act (Uncertain)
East Timor (Timor Leste)	Penal Code, Funding of Terrorism, Constitution, AML/CFT Law
Laos (Lao People's Democratic Republic)	Penal Law (Uncertain)

“Uncertain” refers to the questioning by the 1540 Committee regarding the pertinence of the measures taken by the country, or the term signifies that the Committee has not reached out the legislation to which the country claims.



# UN Resolutions on DPRK and Iran

- Resolution 2231(2015) on Iran lifted nuclear-related sanctions
  - Missile related sanctions remain
- Resolution 2371(2017) and Resolution 2375(2017) on DPRK
  - Toughest sanctions ever imposed
  - Terminates banking relationship with DPRK banks
  - Targets hard currency earnings
    - Through limiting coal, iron, other imports from DPRK
    - Through expulsion of certain diplomatic personnel

# Financial Provisions of UN Resolutions

- 1- Targeted Financial Sanctions
- 2- Activity-based Financial Sanctions
- 3- Vigilance Measures
- 4- Other Provisions

# 1- Targeted Financial Sanctions

- Focused on specific parties
- Seek to disrupt suspect transactions and punish parties to illegal trade by
  - Freezing assets of specific individuals and entities
  - Denying the access to the international financial system



# 1- Targeted Financial Sanctions

- Goal
  - Make resources unavailable for WMD support
  - Deter designated parties from pursuing WMD activities
  - Initiate further investigation
- Rapidly implementation after designation is crucial

## 2- Activity-Based Financial Sanctions

- Aim at preventing the Member States from providing financial services, financial resources or financial assistance to the concerned countries that could contribute its prohibited activities and programs.
- Risk-based approach
  - Identification of high-risk clients and transactions
  - Conduct enhanced due-diligence
  - Follow-up actions
    - Terminate business relationship
    - Suspend transactions
    - Freeze accounts

# Enhanced Due Diligence

- **Obtain additional information to avoid violations:**
  - Parties to the transaction
  - Details on end-use or end-user of the item
  - Export control info (license, end-user certificate)
  - Source of funds
  - Beneficial ownership of the counterparty
  - Purpose of the transaction or payment

# 3- Vigilance Measures

- Vigilance over
  - North Korean banks and entities
  - North Korea affiliated accounts and transactions
  - DPRK diplomats working for DPRK banks
  - North Korean nationals working abroad to earn hard currency for DPRK's nuclear and related missile programs

# 4- Other Financial Measures

- Prohibition of grants, financial assistance or loans
- Terminating banking relationship
  - Closing DPRK banks' existing branches, representative offices in Member States
  - Closing foreign bank's branches, representative offices in DPRK
  - Prohibiting opening of new ones unless UN 1718 Committee approves
  - Terminating joint ventures, ownership interests, corresponding banking relationships
- Limiting DPRK diplomats' banking accounts to one

# Financial Action Task Force (FATF)



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# FATF

- FATF: Inter-governmental body established by G7 in 1989 with 36 members/22 observers, including the UN
- Mandate: Renewed in April 2012 (through 2020)
- Objectives are to set standards and promote effective implementation of legal, regulatory and operational measures for combating money laundering, terrorism financing, and proliferation financing.

# FATF Standards

- FATF Standards: The FATF 40 Recommendations “International Standards on Combating Money Laundering and the Financing of Terrorism and Proliferation”
- Standards first developed in 1990,
- Standards revised in 1996, 2001, 2003, 2012 revisions
- Internationally recognized standards for an effective AML/CFT/CPF framework
- Covers APF in Recommendations 2 and 7.



# FATF

## ■ FATF standards relating to CPF

- Recommendation 2 (National cooperation and coordination)
- Recommendation 7 (Targeted financial sanctions related to proliferation)

## ■ FATF guidance and other tools to assist implementation of UNSCRs

- Guidance Paper on UNSCRs Implementation (2013)
- Typologies Report on Proliferation Financing (2008)
- Status Report on Policy Options (2010)
- Best Practices on National Coordination & Information Sharing (2013)

# FATF Recommendation 2

- National cooperation and coordination
  - Identify and coordinate relevant competent authorities for combating the financing of proliferation
  - Effective mechanisms to coordinate on the development and implementation of policies and activities to address proliferation financing

# Key Agencies for National Cooperation

- Key Agencies
  - Export control & Customs/Border Control
  - Intelligence Services
  - Financial Intelligence Units & Financial Institutions
  - Law Enforcement & Prosecution Agencies
  - Financial Supervisors
  - Government Policy Departments/Designations
- Need to Coordinate on Investigations, Policy Development, Responses to Key Threats

# FATF Recommendation 7

- Implementation of **targeted financial sanctions (TFS)** to comply with UNSCRs relating to the prevention, suppression and disruption of proliferation of WMD and its financing.
- TFS: asset freezing and prohibitions to prevent funds from being available for the designated persons/entities
- R7 aims to support the implementation of UNSCRs on Iran and the DPRK
- Ensure that freeze includes all funds or assets owned or controlled, directly or indirectly
- Identify additional targets and assets for designation
- Focus is prevention, to stop the flow of financing of proliferation related funds.

# FATF's Country Assessments

- FATF assesses country's implementation of the 40 Recommendations, including R.2 and R.7.
- A country would be assessed against:
  - **Technical compliance** with 40 Recommendations
    - Legal/institutional AML/CFT framework of the country; powers/procedures of competent authorities etc.: compliant (C), largely compliant (LC), partially compliant (PC), or non-compliant (NC)
  - **Effectiveness**
    - How well the AML/CFT system is working in practice in the country: high, substantial, moderate, or low level of effectiveness

# FATF's Country Assessments

- Peer reviews
- Publicly available report
- “High-risk and non-cooperative jurisdictions” list
- Motivation for countries to enact laws and implement them

	Technical Compliance Ratings (Rec. 2)	Technical Compliance Ratings (Rec. 7)	Effectiveness Ratings (Proliferation Financing Financial Sanctions)
Singapore	Compliant	Largely Compliant	Substantial
Malaysia	Compliant	Partially Compliant	Moderate

# Challenges in Implementing FATF Recommendations 2 and 7

- **R.7 requires freezing ‘without delay’**
  - UN sanctions list need to be transposed into domestic laws/regulations: it always adds time to implement the sanctions.
- **Fulfilling requirements under R.2/R.7 is not straightforward**
  - Mechanisms to cooperate/coordinate, involving all relevant authorities, both those supervising financial sector and export/border control agencies, may not exist.
  - Communicate designations promptly to obligated entities (financial institutions & other relevant bodies)

# US Regulations



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# US Regulations

- Complements and provides enforcement to UN Security Council sanctions
- Secondary sanctions enable to target non-US parties supporting DPRK's illicit programs
  - Freezing of assets, imposing fine, denying access to US financial system
  - US Department of Treasury has been more aggressive in imposing secondary sanctions to DPRK's third party enablers
    - Designated a Chinese company for supporting DPRK's nuclear program
    - Designating Chinese banks facilitating DPRK's prohibited program



# **Part III**

## **Role of Southeast Asia**

# Requirements for SE Asian Countries in Counter Proliferation Financing (CPF)

## ■ Requirements for all UN Members

- Resolution 1540
  - Adopt controls to counter proliferation financing
- Country-based sanctions (NK, Iran [missiles])
  - Implement list-based financial sanctions
  - Implement activity-based financial sanctions
  - Exercise vigilance
  - Implement other financial provisions

## ■ FATF Recommendations (CPF added 2012)

- Incorporate interagency cooperation in CPF (Rec. 2)
- Freeze the assets of designated persons by UN “without delay” (Rec. 7)

## ■ US Regulations (Sanctions)

- Comply with US regulations, particularly re NK

# Latest Developments Affecting SE Asia

- After Iran's nuclear deal, enhanced vigilance/due diligence should apply
  - To enforce missile sanctions/embargo against Iran
  - To ensure Iran compliance with JCPOA
- New UN and US North Korea sanctions should stimulate greater attention to issue
  - To avoid US secondary sanctions
    - US secondary sanctions now apply to transactions with facilitators of North Korean nuclear/missile activities

# Risks for SE Asian Countries

- If proliferation finance unchecked
  - Risks from spread of WMD and associated delivery systems
- If failure to comply with
  - UNSC resolutions
    - Reputational damage in international community
  - FATF Recommendations
    - Naming and shaming
    - Exposure to countermeasures
  - US Regulations
    - Secondary sanctions
      - Asset freezing
      - Denial of access to US financial system

# Challenges to Implementing CPF Measures in SE Asia

- Lack of awareness and understanding of proliferation finance and countermeasures
  - Lack of specific legislation for CPF
    - Some states subsume this under Anti-Money laundering (AML)/Countering Financing of Terrorism (CFT)
      - 1540 Committee is not certain about some states' measures
- CPF is low on the agenda of regional bodies
  - No typologies (sanitized or fictional case studies) distributed
  - Until the APG's 2016 workshops, no workshops, meetings on CPF

# Recommendations

- Introduce specific legislation or specific measures in the existing legislation in line with the FATF criteria
- Introduce institutional framework with identification of responsible institutions and procedures
- Specify financial institutions obligations and enable them to comply with US regulations



**Thank you...**



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