

UN NUCLEAR AND MISSILE SANCTIONS AND NORTH KOREAN ILLICIT ACTIVITIES

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I. INTRODUCTION

The year 2006 on the Korean Peninsula will be remembered in history for North Korea's test of its first nuclear device on October 9. Associated with that event were North Korea's missile tests three months earlier, UN sanctions in response to both the missile and nuclear tests, and North Korea's refusal to cooperate in the Six-Party Talks in Beijing after the U.S. took action in late 2005 against a Macau bank for assisting North Korea in money-laundering.

II. UN SANCTIONS AGAINST THE DPRK

"Sanctions" are restrictions applied by one state to punish another state or to seek to force another state to change its behavior. After North Korea invaded South Korea in 1950, numerous states, led by the U.S., applied various sanctions against the Democratic People's Republic of Korea (DPRK or North Korea). Reasons for sanctions against North Korea today range from national security issues to human rights concerns. Many experts categorize sanctions against North Korea on a gradient from the most formal, such as United Nations Security Council (UNSC) resolutions, to the most informal, such as twenty-four international banks voluntarily ceasing transactions with the DPRK during 2006.

Ten days after North Korea test-launched missiles July 4 – 5 (local time), the UNSC passed Resolution 1695. It condemned the tests and called on the DPRK

to return to its self-declared moratorium on ballistic missile tests. UN member states were instructed to "exercise vigilance and prevent missile and missile-related items, materials, goods, and technology being transferred to DPRK's missile or WMD programmes," as well as prevent financial contributions to weapons programs and any transfers of such weaponry from the DPRK to other states. Resolution 1695 further demanded that the DPRK suspend its ballistic missile program and any nuclear programs and return to the Treaty on the Non-proliferation of Nuclear Weapons.

On October 14, the UNSC responded to the DPRK's nuclear weapon test conducted five days earlier by passing Resolution 1718. Building upon Resolution 1695, the new resolution added sanctions against transfers of a broad range of conventional weaponry to the DPRK. Resolution 1718 also called on UN members to prevent the export of luxury goods to North Korea.

The ban on the export of luxury items to the DPRK was unusual and controversial. Each UN member country was to draft its own list of banned items. As a senior Chinese diplomat explained, "It is difficult to tell what is a luxury good because it differs from country to country." Some countries might define luxury goods as items most valued by their own people, while other states might define them as goods especially valued by the DPRK.

Many experts and observers seemed to approve of the new sanction on luxury goods as a means of showing North Korean leaders that the world was aware of the domestic behavior of Kim Jong Il, who favored trusted elites while making inadequate provision for the basic needs of ordinary North Koreans. However, David Straub, a former State Department official who once participated in the Six-Party Talks, disagreed. He commented, "Morally, Kim Jong Il should not purchase luxury goods for himself or his supporters, [but] the ironic result of the luxury sanctions may be to *increase* elite support for Kim in North Korea, since the measure will be taken as proof by the North Korean elite of the United States' intention to "stifle" North Korea with sanctions [M]ost of the other Six Parties and the international community will not seriously attempt to implement . . . the ban of luxury goods, so this part of the resolution detracts from the seriousness with which the UNSC resolution as a whole should be regarded and implemented."

Straub's prediction about the international community's response to the luxury goods ban appeared accurate. As of year's end, fewer than 50 of the UN's 196 member-states had submitted their lists of banned luxury items. Those that were submitted included such items as furs, private planes, motorcycles, cameras, cognac, and iPods.

With no specific incentives or disincentives in place for UN member-states to enforce Resolutions 1695 and 1781, their implementation was spotty. An examination of the motives of some of the main players involved in the North Korean nuclear controversy suggests why some states supported the UNSC resolutions, yet were less than energetic in their application.

1. SOUTH KOREA

Engagement with North Korea remained South Korea's ideal approach to the nuclear problem, even after the North Korean nuclear weapon test, according to various South Korean executive and legislative officials in late 2006. "Economic [cooperation and assistance] policy is a strong focus of North-South cooperation towards unification," commented a Ministry of Unification official.

The "sunshine policy," initiated by then-President Kim Dae-jung in 1998 and continued by his successor President Roh Moo-hyun as the "policy of peace and prosperity," aimed for a so-called "soft landing" for the DPRK. ROK officials claimed that the policy had gradually led North Koreans to understand that living conditions were much better in the South and that the North needed to reform. Even after the North Korean nuclear test, senior ROK government and ruling party officials strongly defended their engagement policy. "Sanctions are working," a leading Uri Party legislator opined. "South Korea suspended rice shipments after the July missile test and North Korea will be 1.5 million tons of grain short. I believe this decision made North Korea decide to return to the Six-Party Talks."

While most South Koreans continued to support at least a generic engagement policy even after the North Korean nuclear weapon test, many South Koreans began to express a more critical attitude toward North Korea and the sunshine policy-type of engagement. A former high-level South Korean Foreign Ministry official said in late 2006 that "South Korea wants to exhaust diplomatic means in order to see North Korea's true intentions of either wanting nuclear weapons for the sake of having them or wanting nuclear weapons for bargaining. After this discovery [process], a harder stance should be taken. However, the current post-nuclear situation is an appropriate time to review the impact of engagement and redirect the policy. It is important for South Korea to participate in sanctions because North Korea clearly violated the 1992 [North-South Korean] denuclearization agreement; we have to punish them in one way or another."

Another former Foreign Ministry official advocated "engagement with principles," referring to global norms of non-proliferation, human rights, and market economies. "Without these, North Korean leaders will have hope to continue ... the status quo. Providing goods should come with conditions and pressure for gradual change. This pressure should come through quiet dialogue and quiet diplomacy instead of open criticism."

As the South Korean government implemented UN sanctions against North Korea, however, it remained concerned about the possibility of provoking a military clash with North Korea and continued to believe that increased North Korean dependence on the South would help to ensure peace and stability on the Korean Peninsula. "Inter-Korean trade is still strong despite the missile launch in July and the anger of North Koreans at having conditions put on rice exports," a Ministry of Unification Official disclosed in late 2006. "South Korea doesn't want to sanction interaction like [South Korean-sponsored business and tourist projects in North Korea at] Gaesong and Geumgangsán because they reduce tension and maintain an open military dialogue. Progress has been limited because the DPRK military is limited in what they discuss--it is a small step but a step." South Korea was widely expected to renew food shipments to the North in 2007 before the complete impact of the DPRK's poor rice harvest in 2006 caused starvation.

Apart from the UNSC sanctions, South Korea also felt pressure in 2006 to join the U.S.-led Proliferation Security Initiative (PSI), an informal international effort to prevent the proliferation of weapons of mass destruction. While refusing to become a member or endorse PSI, South Korea observed PSI exercises in April and decided to include interdiction exercises in bilateral U.S.-ROK drills.

A former South Korean government official explained: "Policy-makers fear any confrontation between the two militaries [i.e. of North and South Korea] as a result of PSI. There is a split in the Korean view over the danger of participation in PSI and the possibility of an uncontrollable naval conflict." A U.S. Embassy official commented that he felt the debate about PSI in South Korea had become politicized. The issue of PSI was, he said, "simply an initiative to which countries sign on and comply as much as they want to."

2. CHINA

"China sanctions North Korea because we do not want to see a nuclear peninsula. China agreed to the [UNSC] sanctions because the resolution has two parts:

the first part is about the nuclear issue and the second is on resuming Six-Party Talks and diplomacy. China voted for sanctions *and* diplomacy,” remarked a Chinese foreign ministry official. Considering China’s past reticence to approve international sanctions, its support of UNSC Resolutions 1695 and 1718 suggested its strong disapproval of North Korea’s behavior in 2006. “China wants to slowly change Kim Jong Il’s behavior but, with his continued provocations, China is willing to do more and put itself on the line,” a U.S. political analyst observed.

Other scholars noted how a crisis across China’s border with North Korea could endanger the PRC’s continued development at a time when the country’s leaders felt that physical, political, and financial stability was crucial. An implosion or explosion in North Korean might mean massive flows of North Korean refugees into the PRC, a deployment of China’s armed forces, a drain on China’s economic resources, excruciating diplomatic efforts, the presence of foreign troops at the China-Korea border, and nuclear materials outside the control of the North Korean regime—risks that would be of overwhelming concern to any nation. As an East Asian expert observed, “China [thus] gives enough [assistance to North Korea] to prevent collapse but not enough to make North Korea too comfortable and resistant to sanctions.”

In 2006, China’s oil exports to the DPRK actually increased compared to 2005, while food exports remained at the same level. According to South Korean officials, China provided up to 90% of North Korea’s oil and over 30% of its food. The sale of Chinese luxury goods, including fur, electronics, and cars, to North Korea also increased since October, in spite of UNSC sanctions. Choi Soo-young, a researcher at the ROK’s Korea Institute for National Unification, said, “China holds the key in the push against the North, but it has remained reluctant to squeeze a major lifeline to the North.”

There was no consensus among experts as to whether the Chinese aid reflected a unique Chinese relationship with North Korea. Chinese officials generally depicted the relationship as good, but a Chinese graduate student studying international relations in Seoul opined that the PRC actually saw the relationship “as a burden, but North Korea has to be maintained or it will collapse.”

The debate about how much leverage China had on North Korea was also inconclusive. U.S. officials generally said the relationship was close and that the PRC could, if it wished, exercise considerably more pressure on North Korea. Some even likened the Beijing-Pyongyang relationship to that of Washington and London. However, Chinese officials tended to downplay their country’s influence on Kim Jong Il and his elites.

3. JAPAN

Japan was a strong supporter of sanctions against North Korea in 2006 and, with the U.S., led efforts for UN sanctions against North Korea after its missile and nuclear tests. Due to Japan’s proximity to North Korea and tense relations between the two, Japan felt itself to be a potential target of North Korean weapons. Japan appeared even more concerned than the United States about North Korea’s missile program. In August 1998, North Korea had unexpectedly test-launched a long-range Taepo-dong 1 ballistic missile over Japanese territory. The test-launch of a more advanced Taepo-dong 2 missile in 2006 intensified Japanese concerns.

The Japanese government and public also remained deeply disturbed by North Korea’s failure to clarify the fate of Japanese citizens abducted by North Korea during the 1970s and 1980s, and Japanese negotiators told the North Koreans at the Six-Party Talks that they would have to resolve concerns about the abductees before bilateral relations could improve. Shinzo Abe, who succeeded Junichiro Koizumi as Japanese prime minister on September 26, had come to prominence in Japan by taking a tough line toward North Korea on the issue.

In addition to leading the effort for UNSC sanctions against North Korea in 2006, Japan also imposed its own unilateral sanctions against the country, which included a six-month ban on North Korean shipping to and from its harbors beginning in October. By the end of 2006, Japan had already submitted to the UN its list of banned luxury goods to North Korea; luxury items included some of Kim Jong Il’s favorite foods.

4. UNITED STATES

Throughout 2006, the United States continued to take a hard-line approach toward North Korea. The U.S. remained concerned, as President Bush said in his State of the Union address in 2002 after the 9/11 attacks, that rogue states such as North Korea might proliferate nuclear weapons, materials, and technology to other rogue states such as Iran or, directly or indirectly, to terrorist groups. While the U.S. did not exclude the possibility of using force to end North Korea’s nuclear program, it continued to stress the primacy of diplomacy in the form of the Six-Party Talks. “The purpose of sanctions is to induce North Korea to cease its nuclear program,” remarked a U.S. official in Seoul. “The U.S. pushes for sanctions because multilateral talks and bilateral talks are not enough. There needs to be pressure for these talks to have results.” A former high-level South

Korean official, however, explained the Bush administration's motivation differently: "President Bush's moralistic approach proscribes negotiating with immoral people."

5. EFFECTIVENESS OF SANCTIONS

The extremely closed nature of the DPRK made it almost impossible to obtain reliable data about the impact of UN sanctions against it, whether on its political calculations, its economy, or nuclear and missile programs. Analyzing the impact of the sanctions was further complicated by the fact that many sanctions had remained in place against North Korea ever since the Korean War.

According to a foreign exchange student who studied in Pyongyang for a year, North Korean officials portrayed sanctions as the cause of their country's economic failings. "Whatever Kim Jong Il says, everyone believes," he said. North Korean Central TV showed Kim delivering a speech to officials in which he declared: "Sanctions and pressure will never work on [North Korea]. If the hostile forces continue escalating sanctions and pressure against [the North], it will resolutely react to them with stronger countermeasures."

Because of the DPRK's "military first" policy and Kim Jong Il's personal support of the ruling cadre, North Korean elites were unlikely to be seriously discomfited by the sanctions. Even after the imposition of UN sanctions on luxury goods, *The Wall Street Journal* reported North Koreans visiting Dandong, China in December to purchase furs, jewelry, cars, and real estate. The South Korean newspaper *JoongAng Ilbo* in December cited an unnamed source in Macau who claimed that, despite UN sanctions, ten North Korean trading companies there were still providing the North Korean regime with luxury items.

However, Korea expert Bruce Klingner commented: "[The] DPRK's economy is so bad that sanctions can impact the country's economy and financial system. Sanctions affected DPRK behavior when on 31 October 2006 they agreed to rejoin the [Six-Party] Talks." A Chinese official agreed that spillover effects from sanctions targeting the nuclear program would hurt the DPRK economy. "Sanctions, he said, will be impactful because North Korea needs aid North Korea needs to improve relations, especially with its neighbors, to ease the sanctions."

III. ILLICIT ACTIVITIES

The U.S. government moved strongly against the DPRK's illicit activities in 2005-2006. Experts said that the DPRK had long been engaged in the counterfeiting of U.S. currency and the manufacture and smuggling of illicit drugs and counterfeit cigarettes.

The prime question concerning North Korean illegal activities was the degree of control exercised by the regime. Harvard University researcher Sheena Chestnut posited four possible scenarios:

A lack of state control where individual officials and citizens had the incentive and opportunity to pursue criminal activity for personal gain.

The state condoned but did not involve itself in the activity; criminal activity was understood to be a "perk" of certain positions within the North Korean state structure but was not centrally supported or coordinated in any way.

The state might know about the activity and control it to a certain extent, but gave organizations a certain degree of latitude in running criminal operations.

The North Korean leadership had pursued a deliberate policy of drug trafficking and counterfeiting, based on either ideological motivations or the need for financial survival, and supported the activity with the full array of assets and personnel available to the central government.

With North Korea's high degree of surveillance of the population and insistence on conformity, it appeared unlikely that the state lacked control over persons engaging in such sensitive international matters. The second scenario also seemed unlikely given the scope and expense of a program producing high-quality counterfeit goods in large quantities. Regarding the third and fourth scenarios, many defectors' testimonies pointed toward a deliberate official policy of illicit activities, but the lack of credible information made a final conclusion impossible.

1. CURRENCY COUNTERFEITING

The DPRK's motivations for counterfeiting U.S. currency were unknown. Speculation included a need for foreign exchange due to sanctions and a failed economy, a desire to maintain the living standard of the ruling elite, procurement

of funds for its nuclear program, and a means of attacking the U.S. economy. In any event, counterfeiting of currency by a foreign state could be labeled an act of war.

The amount of North Korean-counterfeited U.S. dollars, sometimes called “supernotes” due to their high quality, was unknown, but \$50 million had been detected in circulation. Analysts believed that this apparently low volume posed little threat to the U.S. economic system. In the case of smaller economies, however, it could cause damage. Both Taiwan and Ireland experienced a local crisis in confidence in the dollar when supernotes were found in circulation there.

Of additional concern in the case of the supernotes was the means of their distribution. In 2005, the U.S. government conducted Operation Smoking Dragon and Operation Royal Charm against criminal rings in the U.S. distributing counterfeit cigarettes, methamphetamines, and counterfeit Viagra. The gangs had promised undercover agents that they would provide them with supernotes and surface-to-air missiles. United States Attorney Debra Wong Yang said on November 9, 2005: “Today’s indictment shows a willingness of the smugglers to acquire practically anything for importation – no matter how dangerous or destructive.”

2. BANCO DELTA ASIA

On September 15, 2005, the U.S. Treasury Department designated a bank in Macau, Banco Delta Asia (BDA), as a “primary money laundering concern” under the USA Patriot Act for having “been a willing pawn for the North Korean government to engage in corrupt financial activities.” North Korea cited the designation as justification for its refusal to participate in Six-Party Talks during most of 2006. U.S. law enforcement and intelligence officials later approached banks and businesses in China, Hong Kong, Macao, Singapore, South Korea, and Vietnam, cautioning them against financial dealings of any sort with North Korea.

Media reports often termed the freezing of the approximately \$24 million in North Korean funds in BDA and the subsequent refusal of many banks to handle North Korean accounts as U.S. “sanctions.” In fact, the U.S. government itself did not freeze any overseas North Korean accounts. Financial markets themselves reacted to maintain their reputation and avoid regulatory risk. For example, twenty-four banks voluntarily ceased transactions with the DPRK in September.

The U.S. could lift the designation against BDA, but such a step still might not guarantee market confidence in BDA or other institutions dealing with North Korean accounts. In a letter sent to the U.S. Treasury on October 18, the Macau

government and BDA jointly said that BDA would not return North Korean funds in its accounts to North Korea regardless of U.S. actions because the funds would almost certainly be frozen under UN Resolution 1718. A Macau financial official also noted that it was up to the government of Macau, rather than the U.S., to unfreeze North Korea’s accounts.

Some U.S. officials told the media that the consequences of U.S. action against BDA were much greater than anticipated. “Because the North Korean leadership placed so many of their foreign exchange eggs in the BDA basket, the sanctions on BDA that prompted the closure of these accounts have had an unusually effective impact,” said Brad Babson, a retired World Bank expert on East Asia. A Chinese official commented that “twenty-four million dollars is a lot to North Korea when you look at their foreign currency reserve.” The subsequent refusal of many other financial institutions to handle North Korean accounts compounded the damage to North Korea.

With North Korea refusing to cooperate in Six-Party Talks until the U.S. arranged for the return of all its accounts in BDA, tensions began to rise between the U.S., on the one hand, and Six-Party partners China, Russia, and the ROK, on the other. Reflecting media reports of disagreement between the U.S. State and Treasury Departments and his own skepticism of the Bush administration’s North Korea policy, South Korean President Roh said: “The U.S. Department of State did not seem to be aware of the Treasury Department’s action [against BDA] in advance. On the other hand, the move might have been a joint plot between the two departments.” A Chinese official referred to supernotes and BDA as a “U.S.-NK issue” and expressed a desire for the U.S. to be more “flexible” so progress could be made in Six-Party Talks. He described the financial action against North Korea as “a touchstone issue.” “North Korea wants to see if . . . it can have confidence in the U.S. It wants to be shown that the US is doing something to improve relations with North Korea.”

Under such pressures, the U.S. held a round of bilateral talks with the DPRK on the BDA issue during the Six-Party Talks in December 2006. The talks suggested a change in the Bush administration’s hard-line approach toward the DPRK in general and the BDA issue in particular. A second round was planned for January 22, 2007.

3. ILLICIT DRUG AND COUNTERFEIT PHARMACEUTICALS SMUGGLING

In its 2006 International Narcotics Control Strategy Report (INCSR), the U.S. Department of State reaffirmed that the DPRK government likely sponsored production and trafficking of opium, heroin, and methamphetamines (“meth”).

Most North Korean-produced meth ended up in Japan, where it was distributed by criminal organizations. Traditionally, 30-40% of meth seized in Japan was tied to the DPRK. More recently, the share of North Korean meth on the Japanese market was declining, apparently due to increased meth production in China or because DPRK meth was attributed to China because of Chinese criminal organizations' middle-man role. North Korean drugs were also trafficked into China, and North Korea served as a primary source of illicit drugs, including heroin, crystal meth, ecstasy, and ketamine, to Taiwan. South Korea received very few controlled substances from North Korea due to their closed border.

The year 2006 saw the trial in Japan of two Japanese men and a South Korean man charged with smuggling 180 kilograms of meth. Japan's National Police Agency (NPA) reported that the men's cargo ship had made many trips from North Korea to Japan since 2000 and that it was used to carry hundreds of kilos of amphetamines. The drugs were packed in bundles, then dropped in waters off Japan for fishing boats to retrieve and take to shore.

In July 2006, the NPA concluded that North Korea's drug trade involved DPRK government participation, based on an investigation into seven cases over nine years. Smugglers claimed that their actions had been overseen by the North Korean government. The NPA believed that three or four secret plants in North Korea were the source of most meth trafficked to Japan. The Japanese investigation was continuing as of the end of 2006.

According to the 2006 INCSR, there was "compelling evidence of DPRK involvement in trademark violations carried out in league with criminal gangs around the world, including ... trafficking in counterfeit Viagra." Because of high prices and demand for Viagra, North Korea presumably made a substantial profit from the sales. While no significant events related to counterfeit Viagra or other pharmaceuticals were disclosed during 2006, investigation into DPRK activities in this arena was ongoing.

4. CIGARETTE SMUGGLING

The Japan Coast Guard confirmed in May 2006, for the first time, that inspectors had found counterfeit cigarettes aboard ships whose last port of call was North Korea. Japanese newspapers reported a new assignment for the special task force investigating the Japanese abductees issue: Uncover how North Korean-made Mild Seven-brand cigarettes were manufactured and distributed in Japan.

Time Magazine in January 2006 disclosed a 2005 investigative report commissioned by major U.S., European, and Japanese tobacco corporations and compiled by undercover agents, informants, and industry experts. The report estimated that 10-12 factories in the DPRK produced 41 billion counterfeit cigarettes per year, with estimated profits of \$80-\$160 million. It also pointed to the DPRK military and domestic security services as owning some of the factories, while foreign crime organizations owned others. David Asher, who had served as senior advisor to the former Assistant Secretary of State for East Asia and Pacific Affairs James Kelly, claimed that the sale of counterfeit cigarettes constituted the DPRK's biggest source of foreign currency.

IV. CONCLUSION

North Korea's criminal activities to earn foreign revenue appeared unlikely to end soon, despite pressures from the U.S., Japan, and other members of the international community. International sanctions, including those by the UNSC in response to the nuclear and missile tests, did not appear to be well coordinated or carefully implemented, and North Korea, long accustomed to international sanctions, repeatedly stressed that it would not be pressured.