

An hourglass-shaped graphic with a globe inside. The top bulb is dark blue, and the bottom bulb is light blue. The globe is centered in the narrow neck of the hourglass. The text is centered within the hourglass.

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February 2, 2009

Congressional Research Service

Report RL33885

*North Korean Crime-for-Profit Activities*

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August 25, 2008

**Abstract.** A challenge facing U.S. policy makers is how to balance pursuing anti-drug, counterfeiting, and crime policies vis--vis North Korea against effectively pursuing several other high priority foreign policy objectives, including (1) nuclear nonproliferation negotiations via the Six-Party talks, (2) limiting ballistic missile production and export, (3) curbing terrorism, and (4) addressing humanitarian needs. As the Six-Party process has proceeded in 2008, it appears that the U.S. overriding goal of denuclearization outweighs concerns related to DPRK illicit activity (with the exception of proliferation of nuclear weapons technology and materials). Such illicit activity, however, could surface again as an issue as talks proceed on diplomatic normalization with the DPRK.

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# CRS Report for Congress

## North Korean Crime-for-Profit Activities

**Updated August 25, 2008**

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**Prepared for Members and  
Committees of Congress**

# North Korean Crime-for-Profit Activities

## Summary

Strong indications exist that the North Korean (Democratic People's Republic of Korea or DPRK) regime has been involved in the production and trafficking of illicit drugs, as well as of counterfeit currency, cigarettes, and pharmaceuticals. It appears that drug trafficking has declined and counterfeiting of cigarettes may be expanding. Reports indicate that North Korea may engage in insurance fraud, human trafficking, and wildlife trafficking as a matter of state policy. DPRK crime-for-profit activities have reportedly brought in important foreign currency resources and come under the direction of a special office under the direction of the ruling Korean Worker's Party.

With the caveat that dollar value estimates of clandestine activities are highly speculative, conservative estimates suggest North Korean criminal activity has generated as much as \$500 million in profits per year (about a third of DPRK's annual exports) but has decreased in recent years. A core issue is whether the income from the DPRK's reportedly widespread criminal activity is used to finance the development of weapons of mass destruction or other key military programs, thereby contributing to the DPRK's reluctance to curb its aggregate level of such activity. Some also speculate that the DPRK's criminal smuggling networks could help facilitate the illicit movement of nuclear or other materials in and out of the country.

Policy analysts in the past have suggested that North Korean crime-for-profit activity has been carefully controlled and limited to fill specific foreign exchange shortfalls. However, some concern exists that North Korean crime-for-profit activity could become a "runaway train" that once established could escape control. If the DPRK's crime-for-profit activity has become entrenched, or possibly decentralized, some analysts question whether the current Pyongyang regime (or any subsequent government) would have the ability to effectively restrain such activity, should it so desire. Moreover, some suggest that proposals to shift DPRK crime-related income toward legitimate-source income ignore the fact that the current regime diverts some illicit earnings to slush funds designed to sustain the loyalty of a core of party elite and to underwrite weapons development programs.

A challenge facing U.S. policy makers is how to balance pursuing anti-drug, counterfeiting, and crime policies *vis-à-vis* North Korea against effectively pursuing several other high priority foreign policy objectives, including (1) nuclear nonproliferation negotiations via the Six-Party talks, (2) limiting ballistic missile production and export, (3) curbing terrorism, and (4) addressing humanitarian needs. As the Six-Party process has proceeded in 2008, it appears that the U.S. overriding goal of denuclearization outweighs concerns related to DPRK illicit activity (with the exception of proliferation of nuclear weapons technology and materials). Such illicit activity, however, could surface again as an issue as talks proceed on diplomatic normalization with the DPRK. This report will be periodically updated.

For additional CRS analysis of DPRK issues, see CRS Report RL33590, *North Korea's Nuclear Weapons Development and Diplomacy*, and CRS Report RL33567, *Korea-U.S. Relations: Issues for Congress*, both by Larry A. Niksch.

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# North Korean Crime-for-Profit Activities

## Overview<sup>1</sup>

Allegations of North Korean (Democratic People's Republic of Korea, or DPRK) drug production, drug trafficking, and other crime-for-profit activities have been an issue of concern for Congress, the Administration, the media, and the diplomatic community.<sup>2</sup> The issue is twofold. First is general U.S. interest in halting criminal behavior (upholding the rule of law and protecting U.S. citizens and assets from illicit activity). Second is how to deal with a government suspected of countenancing or sponsoring activity that may threaten U.S. diplomatic and security interests.

A challenge facing policy makers is how to balance pursuing anti-drug, counterfeiting, and crime policies *vis-à-vis* North Korea against effectively pursuing other high-priority U.S. foreign policy objectives, including (1) limiting possession and production of weapons of mass destruction, (2) limiting ballistic missile production and export, (3) curbing terrorism, and (4) addressing humanitarian needs. A core issue is whether the income from the DPRK's reportedly widespread criminal activity has financed the acquisition of weapons of mass destruction and has strengthened the DPRK's ability to maintain, until recently, truculent, no-compromise positions on the issue of its nuclear weapons program. Some also speculate that the DPRK's criminal smuggling networks could help facilitate the illicit movement of nuclear materials in and out of the country.<sup>3</sup> U.N. Resolution 1718 (2006) provides for economic sanctions against persons or entities engaged in or providing support for, including through illicit means, DPRK's nuclear-related, other weapons of mass destruction-related and ballistic missile-related programs.<sup>4</sup>

Counterfeiting, copyright and trademark violations, and other illicit activity occur in virtually all countries of the world, but in the North Korean case, numerous sources indicate that the state apparently had — and may continue to be — sponsoring some of these activities. In this view, if the DPRK is to join the larger international community of nations, it would be expected to cease state-sponsorship

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<sup>1</sup> This report was originally co-authored by Raphael Perl and Dick K. Nanto. Perl retired from the Congressional Research Service in November 2007.

<sup>2</sup> See generally CRS Report RL32167, *Drug Trafficking and North Korea: Issues for U.S. Policy*, by Raphael Perl, and CRS Report RL33324, *North Korean Counterfeiting of U.S. Currency*, by Raphael Perl and Dick Nanto.

<sup>3</sup> Sheena Chestnut, "Illicit Activity and Proliferation: North Korean Smuggling Networks," *International Security*, Vol. 32, No. 1 (Summer 2007), pp. 80-111.

<sup>4</sup> UN Resolution 1718 (2006), Adopted by the Security Council at its 5551<sup>st</sup> meeting, on October 14, 2006 and updated on October 16, 2006.

of such activities and to take appropriate measures against private parties engaged in such production and/or distribution.

As the Six-Party Talks on North Korea's nuclear program have proceeded in 2008, it appears that the U.S. goal of denuclearization has outweighed concerns related to DPRK illicit activity (with the exception of proliferation of nuclear weapons technology and materials). Such illicit activity by North Korea, however, could resurface as the Six-Party process proceeds and attention turns toward normalizing diplomatic ties with the DPRK by the United States, Japan, and South Korea and allowing North Korea to join international financial institutions such as the Asian Development Bank, International Monetary Fund, and the World Bank.

The role of Congress in this issue includes overseeing U.S. policy, eliciting information and raising public awareness of the issue, and balancing U.S. interests when foreign policy goals may conflict with anti-crime activities. Congress also authorizes and appropriates funds for humanitarian and other economic assistance for North Korea.

Areas of DPRK criminal activity commonly cited have included production and trafficking in (1) heroin and methamphetamine; (2) counterfeit cigarettes; (3) counterfeit pharmaceuticals (e.g., "USA" manufactured Viagra®); and (4) counterfeit currency (e.g., U.S. \$100 bill "supernotes").<sup>5</sup> Media reports also have indicated that North Korea may be engaged in insurance fraud, endangered species trafficking, and human trafficking as a matter of state policy.<sup>6</sup> News reporting on the subject reached its height in 2003, when the Bush Administration was actively raising the issue of DPRK's crime-for-profit activities at the highest levels. Since then, fewer public reports have surfaced to indicate that DPRK illicit activities are continuing. At the same time, no public reports indicate that DPRK has completely halted its crime-for-profit activities.

In 2008, the State Department reports that while DPRK's drug trafficking appears to have declined substantially, "DPRK-tolerance of criminal behavior may exist on a larger, organized scale, even if no large-scale narcotics trafficking incidents

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<sup>5</sup> Note that in addition to citing the likelihood of past DPRK state involvement in illicit drug production and trafficking, the U.S. Department of State in its March 2006, *International Narcotics Control Strategy Report* (INCSR) stated that:

Indictments in the United States issued in 2005 and the ongoing work of several corporate investigative teams employed by the holders of major United States and foreign cigarette and pharmaceutical trademarks have provided compelling evidence of DPRK involvement in trademark violations carried out in league with criminal gangs around the world, including trafficking in counterfeit cigarettes and Viagra. The DPRK is also associated with production of high-quality counterfeit U.S. currency ("supernotes").

On the issue of counterfeiting of U.S. currency, in July 2004, for example, the U.S. Secret Service reportedly uncovered a network selling counterfeit North Korean made cigarettes, pharmaceuticals, and \$100 bills. See Frederik Balfour et al., "Fakes," *Business Week*, February 7, 2005. Criminal indictments subsequently ensued. See generally *BBC News*, "What is a Superdollar?," June 20, 2004.

<sup>6</sup> See section on insurance fraud, *supra*.

involving the state itself have come to light.”<sup>7</sup> The estimated aggregate scale of DPRK’s crime-for-profit activity has been and may still be significant — and arguably provides important foreign currency resources to the heavily militarized North Korean state. DPRK crime-for-profit activities are reportedly orchestrated by a special office charged with bringing in foreign currency under the direction of the ruling Korean Worker’s Party.

North Korean drug trafficking, trade in counterfeit products, and the counterfeiting of U.S. currency, to the extent that it does indeed exist, have been a matter of concern in Asian, European, and U.S. law enforcement, foreign policy, and national security communities. At least 50 documented incidents, over decades, many involving arrest or detention of North Korean diplomats, have linked North Korea to drug trafficking. Such activity, particularly production and trafficking of methamphetamine and trade in counterfeit cigarettes, appears to be continuing.<sup>8</sup>

With the caveat that dollar value estimates of clandestine activities are highly speculative, conservative estimates suggest North Korean criminal activity generates as much as \$500 million in profit per year, with some estimates reaching the \$1 billion level. One recent economic study by Stephan Haggard and Marcus Noland, however, places current illicit activity at a much lower level and considers the lower end of the various published estimates of profit as the upper bound. For example, the Haggard/Noland study estimates drug trafficking in 2005-2006 at about \$20 to \$35 million.<sup>9</sup>

In contrast, the (South) Korea Institute for Defense Analysis reportedly stated that North Korea earns between \$700 million and \$1 billion per year from exporting weapons and trading drugs and counterfeit money.<sup>10</sup> In 2003, an official from U.S. Forces Korea reportedly stated that North Korea’s annual revenue from exports of illegal drugs was estimated at \$500 million and from counterfeit bills at \$15 to \$20 million. The official also stated that in 2001, North Korea exported ballistic missiles worth \$580 million to the Middle East.<sup>11</sup> More recently, some sources report that North Korea has been exporting conventional military weapons to Burma (Myanmar) in contravention to current U.N. prohibitions against North Korea.<sup>12</sup>

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<sup>7</sup> U.S. Department of State, *INCSR* (2008).

<sup>8</sup> For more details, see CRS Report RL33324, *North Korean Counterfeiting of U.S. Currency*, by Raphael Perl and Dick Nanto, and CRS Report RL32167, *Drug Trafficking and North Korea: Issues for U.S. Policy*, by Raphael Perl. See also U.S. Department of State, *INCSR* (2008).

<sup>9</sup> Haggard, Stephan and Marcus Noland. “North Korea’s External Resources and Constraints” in *Korea’s Economy 2008, Volume 24, c. 2008. Pp. 83-91*.

<sup>10</sup> “PSI ‘Will Hit N. Korea Where It Hurts,’” *The Chosun Ilbo* [digital version], October 27, 2006.

<sup>11</sup> “USFK Details DPRK’s Drug, Missile Exports, Counterfeit Bills,” *Chosun Ilbo* (Internet Version-WWW), May 12, 2003. Translated by Open Source (Article No. KPP20030514000056).

<sup>12</sup> See for example “Oslo-Based Website: Burma’s Purchase of North Korean Arms (continued...)”

One basis for the \$500 million to \$1 billion figure for illicit exports is that it can be inferred from international trade data and from reported anecdotes that markets in Pyongyang have ample supplies of imported foreign goods. In 2004, North Korea is estimated to have incurred a trade deficit of \$1.8 billion. This deficit rose to about \$2.0 billion in 2005, dropped to an estimated \$1.3 billion in 2006, and rose to an estimated \$2.7 billion in 2007.<sup>13</sup> Some of this imbalance is financed through food and other aid, capital inflows, borrowing, remittances from North Korean laborers working abroad (especially in Russia and the Middle East), and tourism. Pyongyang, however, does little borrowing on international markets, and Tokyo has been cracking down on remittances from ethnic North Koreans in Japan. Inflows of capital also seem small, although they are rising as China and South Korea invest in enterprises in the North. As a result, some surmise that in some years as much as \$1 billion has been financed by illicit activity.<sup>14</sup>

## Illicit Drug Production and Trafficking

### Allegations of State Involvement

There has been evidence to suggest that the North Korean government is supporting drug production and trafficking as a matter of state policy. Since 1976, North Korea has been linked to more than 50 verifiable incidents involving drug seizures in at least 20 countries.<sup>15</sup> A significant number of these cases has involved arrest or detention of North Korean diplomats or officials. Concerns about North Korean drug trafficking and production were further expressed in the International Narcotics Control Board's 1997 annual report, which referred to such DPRK drug trafficking incident claims as "disquieting." In 1999, substantial seizures of North Korean methamphetamine occurred in Japan (35% of the total methamphetamine seizures in Japan that year). Large seizures of heroin and methamphetamine with a link to the DPRK have since occurred in Taiwan, and in April of 2003, the "Pong Su," a DPRK state enterprise-owned, sea-going vessel of around 4,000 metric tons apparently delivered a large quantity of DPRK-trafficked and also possible DPRK-

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<sup>12</sup> (...continued)

Threatens Stability," *BBC Monitoring Asia Pacific*, April 6, 2008; "Thai-Based Website: U.S. Concerned over Reports of North Korean Weapons to Burma," *BBC Monitoring Asia Pacific*, April 6, 2008; and Michael Green and Derek Mitchell, "Asia's Forgotten Crisis: A New Approach to Burma," *Foreign Affairs*, Vol. 86, Iss. 6 (November/December 2007). Note that the United Nations does not have an arms embargo on Burma.

<sup>13</sup> CRS Report RL32493, *The North Korean Economy: Background and Policy Analysis*, by Dick Nanto and Emma Chanlett-Avery.

<sup>14</sup> For example, see Statement of David L. Asher, Ph.D., Before the Subcommittee on Federal Financial Management, Government Information, and International Security, Senate Homeland Security and Government Affairs Committee, April 25, 2006, footnote 2.

<sup>15</sup> Statement of William Bach, Office Africa, Asia, and Europe Programs, Bureau for International Narcotics and Law Enforcement, State Department, before the Subcommittee on Financial management, the Budget, and International Security, Senate Government Affairs Committee, May 20, 2003.



origin heroin to Australia. Although members of the vessel's North Korean crew were subsequently acquitted on charges relating to the smuggling of the drugs, experts have little doubt of a North Korean connection to the drug shipment.<sup>16</sup>

Since 2003, however, no incidents definitively and directly linking the DPRK State apparatus to such drug trafficking activity have come to light. The State Department's March 1, 2008, *International Narcotics Control Strategy Report* states that drug trafficking with a connection to North Korea "appears to be down sharply and there have been no instances of drug trafficking suggestive of state-directed trafficking for five years."<sup>17</sup>

Many analysts suggest that any decline in DPRK state-linked drug trafficking activity would likely be in response to enhanced international attention paid to such activity in the wake of the April 2003 seizure of heroin carried on the North Korean Vessel the "Pong Su." Others, however, remain skeptical and offer an alternative explanation. They suggest that the decline in seizures is because North Korean source methamphetamine is now regularly being mistakenly identified as "Chinese source," given growing links of Chinese criminal elements to North Korea's drug production/trafficking activities. In line with such a conclusion are press reports in late 2006 of the arrests in China in differing locations of North Korean nationals involved with Chinese criminals in the trafficking of methamphetamine. However, it is not clear from the reports whether the drugs were of DPRK origin or whether the North Koreans arrested had links with DPRK officials.<sup>18</sup>

## Reported Scope of Illicit Drug Activity

North Korea has reportedly produced three main types of illicit drugs: (1) opiates, including opium and heroin; (2) synthetic drugs, especially methamphetamine; and (3) counterfeit pharmaceutical drugs. In 2008, the amount of illegal drug production and trafficking is unlikely to be large enough for North Korea to be cited on the State Department's drug "majors list," which could make Pyongyang subject to the drug certification process applicable to "major" producers and potentially liable to discretionary trade sanctions and restrictions on non-humanitarian aid.<sup>19</sup>

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<sup>16</sup> Notable here is the DPRK registry of the Ship, the DPRK nationality of its crew, and the presence on the ship of as least one DPRK non-crew political officer. For more detail see CRS Report RL32167, *Drug Trafficking and North Korea: Issues for U.S. Policy*, by Raphael Perl.

<sup>17</sup> U.S. Department of State, *INCSR* (2008).

<sup>18</sup> See "China Busts Huge N. Korean Drug Ring," *Bangkok Post*, January 11, 2007 [DPA report]. Note, however, that it is not clear from the reports whether the drugs were of DPRK origin or whether the North Koreans arrested had links with DPRK officials.

<sup>19</sup> Since 1992, Congress has required that the President submit annual reports, which identify major drug transit and major drug producing countries, known as the "drug majors." Major illicit drug producing countries are defined by section 481(e)(2) of the Foreign Assistance Act of 1961 (22 U.S.C. 2291(e)(2)) as a country in which (1) 1,000 hectares or more of illicit opium poppy is cultivated or harvested during a year, (2) 1,000 hectares or more of

(continued...)

**Opiates.** According to press reports and North Korean defectors, farmers in certain areas have been ordered to grow opium poppies in the past. In 2006 congressional testimony, a representative of the State Department reported that North Korea cultivates 4,000 to 7,000 hectares of opium poppy, producing approximately 30 to 44 metric tons of opium gum annually.<sup>20</sup> Though such estimates appear reasonable, they are nevertheless based on indirect and fragmented information. With the caveat that conclusive “hard” data is lacking, U.S. government investigative agency sources estimate North Korean raw opium production capacity at 50 tons annually. North Korean government chemical labs reportedly have the capacity to process 100 tons of raw opium poppy into opium and heroin per year.<sup>21</sup>

**Methamphetamine.** North Korea’s maximum methamphetamine production capacity is estimated to be 10 to 15 metric tons of the highest quality product for export. This coincides with a time when markets for methamphetamine are dramatically expanding in Asia, especially in Thailand, Japan, the Philippines, and more recently in Cambodia and China.<sup>22</sup>

**Pharmaceuticals.** North Korea also has an advanced pharmaceutical industry, and it is widely believed that large-scale production of expertly packaged pharmaceuticals such as knock-off erectile enhancement drugs (particularly, Viagra® and Cialis®) has been orchestrated by Pyongyang. However, public source data on such alleged activity is sketchy. At issue is not the existence of the knock-off drugs,

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<sup>19</sup> (...continued)

illicit coca is cultivated or harvested during a year, or (3) 5,000 hectares or more of illicit cannabis is cultivated or harvested during a year, unless the President determines that such illicit cannabis production does not significantly affect the United States. Major drug-transit countries are defined by section 481(e)(5) of the Foreign Assistance Act of 1961 (22 U.S.C. 2291(e)(5)) as a country (1) that is a significant direct source of illicit narcotic or psychotropic drugs or other controlled substances significantly affecting the United States, or (2) through which are transported such drugs or substances. A second certification process was enacted by Congress as part of the Combat Methamphetamine Epidemic Act of 2005. This law amends the Foreign Assistance Act of 1961 to require the State Department to report the five largest importing and exporting countries of two precursor drugs, ephedrine and pseudoephedrine, commonly used to produce methamphetamine, and certify whether these countries are fully cooperating with the United States on methamphetamine chemical precursor control. Nations deemed not to be fully cooperating face a loss of U.S. bilateral assistance and U.S. opposition to multilateral assistance in the multilateral development banks.

<sup>20</sup> Statement of Peter Prahar, Office Africa, Asia, and Europe Programs, Bureau for International Narcotics and Law Enforcement, State Department, before the Subcommittee on Federal Financial Management, Government Information, and International Security, Senate Homeland Security and Government Affairs Committee, April 25, 2006.

<sup>21</sup> See generally, *INCSR*, March 2000, p. VIII-39 and CRS Report RL32167 (archived), *Drug Trafficking and North Korea: Issues for U.S. Policy*, by Raphael Perl, pp. 8-9.

<sup>22</sup> See generally, *INCSR*, March 2006 and CRS Report RL32167, *Drug Trafficking and North Korea: Issues for U.S. Policy*, by Raphael Perl, pp. 8-9.

but whether the DPRK is indeed the manufacturer, with some speculating that China may be the source of production.<sup>23</sup>

## Rising Domestic Drug Production and Abuse?

An emerging genre of reports, yet to be substantiated, suggests that as state control of drugs in the DPRK becomes looser, a growing amount of stimulants for domestic sale and consumption are being produced privately by scientists in the DPRK and funded by private investors. Some reports suggest drug abuse is becoming widespread among senior military officials and also among the poor as a means to dull hunger. Others suggest that drug addiction is spreading among cadres such as the officer corps of the People's Army Security Department and high-ranking party officials. A scenario is being presented of drugs sold openly at farmers markets, at times being used instead of currency in transactions.<sup>24</sup>

## Manufacture and Distribution of Counterfeit U.S. Currency

Besides the production and distribution of illicit drugs, DPRK appears to have been involved in the production and distribution of counterfeit foreign currencies as a means of generating foreign exchange.<sup>25</sup> The United States has accused DPRK of counterfeiting U.S. \$100 Federal Reserve notes (supernotes) and passing them off in various countries.<sup>26</sup> Officials familiar with the bogus currency in question note its

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<sup>23</sup> Note that “knock-off” Viagra® and Cialis® are readily available in China, notably in Dandong on the DPRK border. For allegations/reports linking the DPRK in the past to such activity, see Statement of David L. Asher before the Subcommittee on Federal Financial Management, Government Information, and International Security of the Senate Homeland Security and Government Affairs Committee, April 25, 2006. See also, *U.S. News and World Report*, White House Week, May 30, 2005.

<sup>24</sup> See “Widespread Drug Use in North Korea; Drug Control; Domestic Circulation, Alternative to Food Shortage,” *Sankei Shimbun* (Internet Version), June 20, 2006, TO3:13:10Z.

<sup>25</sup> For detail, see CRS Report RL33324, *North Korean Counterfeiting of U.S. Currency*, by Raphael F. Perl, and Dick K. Nanto. Note that allegations have been reported that Russia protects an “array of sophisticated criminal networks stretching from Russia through Georgian territory” (South Ossetia) that includes counterfeit U.S. \$100 bills “minted” at a press inside this area. See Michael Bronner, “When the war Ends, Start to Worry,” *New York Times*, August 16, 2008, p. 19.

<sup>26</sup> Several sources, however, refute the U.S. position. For example, in 2006, South Korea's intelligence agency, the National Intelligence Service, reportedly claimed it had no evidence that North Korea has made forged supernotes since 1998. In May 2007, Switzerland's federal law enforcement agency, the Bundeskriminalpolizei, also reportedly cast doubts on DPRK's ability to print supernotes. Most recently in January 2008, an independent news agency conducted its own ten-month investigation and reported that evidence to support DPRK counterfeiting claims as “uncertain at best.” See “N Korea ‘Not Forging US Dollars,’” *BBC News*, February 2, 2006 and Kevin G. Hall, “U.S. Counterfeiting Charges (continued...)”

exceptional quality — so good that many cashier-level bank personnel would likely not be able to detect the forgeries.

In an April 2008 hearing, a Treasury official stated that it has continued to work with the U.S. Secret Service to counteract North Korea's counterfeiting of U.S. currency and that high-quality counterfeit bills produced by North Korea, known as the "Supernote," continue to surface.<sup>27</sup> Media reports indicate that counterfeit \$100 bills are used in North Korean markets as currency and are valued at about the equivalent of \$70.<sup>28</sup> It is not clear, however, whether the counterfeit bills circulating are from existing stocks or are currently being produced. The anti-counterfeiting security features incorporated into new U.S. bills make counterfeiting much more difficult.

In 2006, U.S. officials cited the figure of \$45-\$48 million detected or seized since 1989.<sup>29</sup> However, because counterfeiting is a form of clandestine criminal activity and North Korea is a closed society, the amount of alleged DPRK-produced counterfeit currency in circulation is speculative at best. Estimates of the profit such transactions bring to the Pyongyang regime — to the extent they are based on open source material — are also speculative. Amounts commonly cited, which take into account many factors, range from \$15 million to \$25 million in profit per year.

## Incidents Linking the DPRK to Counterfeiting Activity

At least 13 reported incidents between 1994 and 2005 show North Korean involvement in counterfeiting and smuggling or distributing U.S. currency. All of these incidents occurred in either Asia or Europe. The use of DPRK diplomatic passports and the involvement of DPRK diplomats, embassy personnel, and employees and officers of DPRK state-owned and -operated trading companies connect most of these incidents to the government of North Korea in varying degrees.

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<sup>26</sup> (...continued)

against N. Korea Based on Shaky Evidence," *McClatchy Newspapers*, January 10, 2008.

<sup>27</sup> U.S. Department of the Treasury, Under Secretary for Terrorism and Financial Intelligence Stuart Levey, Testimony Before the Senate Committee on Finance, April 1, 2008, Press Release HP-898.

<sup>28</sup> Kwo'n Cho'ng-hyo'n and Sin Chu-hyo'n, "Counterfeit Dollars Are Being Circulated as Official Currency' in North Korean Markets — Inflation Is Extreme — [People] Pay With Supernotes," *The Daily NK* (Internet version), July 31, 2007. Translated by Open Source Center, document # KPP20070831031008.

<sup>29</sup> See Esther Pan, *North Korea's Capitalist Experiment*, Council on Foreign Relations Backgrounder, June 8, 2006. David L. Asher, Statement, April 25, 2006, op. cit. Statement of Peter A. Prahar, Director, Office of Africa, Asia and Europe Programs, Bureau for Narcotics and Law Enforcement Affairs, Department of State, Before the Subcommittee on Federal Financial Management, Government Information, and International Security, Senate Homeland Security and Government Affairs Committee, April 25, 2006.

Taken collectively, the link is seen as even stronger. Of these 13 incidents, 6 occurred after 1999.<sup>30</sup>

Counterfeiting of foreign currency is apparently a phenomenon that is not new to the government of North Korea. Seoul's War Memorial Museum reportedly contains DPRK-manufactured South Korean currency from the 1950s, the production of which reportedly continued into the 1960s. South Korean media reports cite a 1998 South Korean National Intelligence Service (IS) Report to the effect that North Korea had forged and circulated U.S. \$100 banknotes worth \$15 million a year. Subsequent reports to the South Korean National Assembly in the same year and in 1999 are cited in the media as stating that North Korea operates three banknote forging agencies and that more than \$4.6 million in bogus dollar bills had been uncovered on 13 occasions between 1994 and 2005.<sup>31</sup>

Arrests and indictments point to DPRK trafficking in bogus U.S. currency as recently as 2005. In August 2005, federal law enforcement authorities completed two undercover operations that focused on the activities of members of China's Triad criminal syndicates. The operations, named Royal Charm and Smoking Dragon, reportedly netted some \$4 million in supernotes believed to be of North Korean origin. Illicit narcotics, counterfeit brand cigarettes and pharmaceuticals were seized as well. U.S. government authorities indicate there is the potential that any scheduling of trials and/or the plea bargaining process will reveal direct links between some of the smugglers and North Korean officials or government entities.<sup>32</sup>

## **Banco Delta Asia Bank Action**

The Banco Delta Asia (BDA) bank is located and licensed in the Macau Special Administrative Region of China. According to the U.S. Treasury Department, BDA played an important role in laundering money that had been derived from DPRK's crime-for-profit activities. Treasury claims that senior BDA officials worked with DPRK officials "to accept large deposits of cash, including counterfeit U.S. currency, and agreeing to place that currency into circulation."<sup>33</sup> In addition, BDA clients were reportedly known to include a DPRK front company, which had been involved for more than a decade in distributing counterfeit money, smuggling counterfeit tobacco products, and suspected in being involved in drug trafficking.

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<sup>30</sup> See "The 'Soprano State?' North Korean Involvement in Criminal Activity and Implications for International Security," by Sheena E. Chestnut (hereinafter cited as *Chestnut*), Stanford University Honors Thesis, May 20, 2005, p. 144-145.

<sup>31</sup> See "Seoul's U-Turn on N. Korean Counterfeiting Could be Fatal," *Chosun Ilbo* (English Edition), December 25, 2005. The title of the 1988 report is cited as "A New Threat in the 21<sup>st</sup> Century: Realities and Responses to International Crimes."

<sup>32</sup> See generally, remarks of Acting Assistant Attorney General, John C. Richter of August 22, 2005, available at [[http://www.usdoj.gov/criminal/press\\_room/speeches/2005\\_4193\\_rmrksOprSmokngDrgnNroylChrm082405O.pdf](http://www.usdoj.gov/criminal/press_room/speeches/2005_4193_rmrksOprSmokngDrgnNroylChrm082405O.pdf)].

<sup>33</sup> The Department of the Treasury. Treasury Designates Banco Delta Asia as Primary Money Laundering Concern under USA Patriot Act. Press Release JS-2720. September 15, 2005.

On March 19, 2007, the Treasury Department finalized a rule based on Section 311 of the USA PATRIOT Act (31 U.S.C. 5318A), which prohibited U.S. financial institutions from opening or maintaining correspondent accounts for or on behalf of BDA.<sup>34</sup> This order, which continues to remain in effect, has also led banks, not only from the United States but from other nations as well, to refuse to deal with even some legitimate North Korea traders. North Koreans appear to have moved some of their international bank accounts to alternative banking institutions, including those in China, Austria, and Switzerland.<sup>35</sup> The DPRK also enacted an Anti-Money Laundering Law partly to ease foreign concerns over alleged money laundering by North Korean entities.<sup>36</sup>

Pyongyang cited the BDA action in the past when it refused to return to the Six-Party Talks on its nuclear program and received a pledge by the United States as an aside in the process of negotiating the Six-Party Agreement of February 13, 2007, to resolve the BDA issue.<sup>37</sup> In the process of seeking to resolve the issue, the United States agreed to release blocked assets — some \$25 million — to DPRK authorities. After considerable effort, the \$25 million in Banco Delta funds were returned to North Korea via the U.S. Federal Reserve and a Russian bank in June 2007 as a condition for restarting the Six-Party talks.<sup>38</sup> This decision was both praised and criticized by observers. Some described the release of funds as one of the Administration's "notable foreign-policy successes" because it was seen as having contributed to bringing DPRK back to the negotiating table for the Six-Party Talks.<sup>39</sup> Others argued that returning the funds to North Korea compromised the spirit of international agreements the United States has supported, including U.N. Resolution

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<sup>34</sup> *Federal Register*, Vol. 72, No. 52, March 19, 2007 (Final Rule), pp. 12730-12740. See also, The Department of the Treasury, Treasury Designates Banco Delta Asia as Primary Money Laundering Concern under USA Patriot Act, Press Release JS-2720, September 15, 2005; *Federal Register*, Vol. 70 No. 181, September 20, 2005(Notices), p. 55214; and FINCEN Advisory of December 13, 2005, on Guidelines to Financial Institutions on the Provision of Banking Services to North Korean Government Agencies and Associated Front Companies Engaged in Illicit Activities which encourages financial institutions worldwide to take precautions that they are not used as a conduit for the laundering of proceeds of DPRK illicit activities.

<sup>35</sup> "Major Chinese Banks Refrain From Dealing with N. Korean Firms," *Kyodo News*, March 13, 2006.

<sup>36</sup> "Foreign Trade of the Democratic People's Republic of Korea (via Naenara Internet), May 13, 2008. Open Source Document No. KPP20080513971062.

<sup>37</sup> King, Neil Jr. And Evan Ramstad. "Politics & Economics: What Drove the North Korea Deal; U.S. Hungered for Diplomatic Victory, Pyongyang for Financial Relief," *Wall Street Journal*, February 14, 2007, p. A.4. See also David L. Asher, Statement Before the Subcommittee on Federal Financial Management, Government Information, and International Security, Senate Homeland Security and Government Affairs Committee, April 25, 2006.

<sup>38</sup> "N Korea Confirms Funds Transfer," BBC News (International Version On line), June 25, 2007.

<sup>39</sup> See, for example, John K. Cooley, "N. Korea: Tell The Truth on Forged Dollars," *The Christian Science Monitor*, Op-ed, November 19, 2007.

1718, which condemns the alleged use of crime-for-profit activities to finance DPRK's nuclear ambitions.<sup>40</sup>

In addition to the issue of returning the frozen funds, some analysts claim that the BDA issue brought to the surface lingering questions about the way the international banking community treats DPRK accounts. Specifically, the financial effects of the BDA action were larger than expected. It caused a run on accounts at the bank that compelled the government of Macau to take over BDA's operations and place a temporary halt on withdrawals. It also appears to have obstructed some legitimate North Korean financial interests, as the BDA action caused other banks around the region, including Chinese, Japanese, Vietnamese, Thai, and Singaporean banks, to impose voluntarily more stringent regulations against North Korean account holders. As North Korean traders and others move forward, some question whether the situation will return to "business as usual," "business with caution," or remain as "no business at all." In the case of China, a media report indicates that the country is allowing North Koreans to open bank accounts in China to settle business transactions in Chinese yuan. This enables them to conduct transactions in the Chinese currency.<sup>41</sup>

## Other Illicit Activity

### Counterfeit Cigarettes

Counterfeit cigarette production may have replaced illegal drug trafficking as a major source of crime-for-profit revenue for North Korea. In 2008, the State Department reports that "the continuing large-scale traffic in counterfeit cigarettes from DPRK territory suggests, at the least, that enforcement against notorious organized criminality is lax, or that a lucrative counterfeit cigarette trade has replaced a riskier drug trafficking business as a generator of revenue for the DPRK state."<sup>42</sup> Reports from the past several years have charged the DPRK with producing counterfeit cigarettes for export of seemingly genuine Japanese brand cigarettes (Mild Seven) and U.S. brands such as Marlboro. According to the *Wall Street Journal*, U.S. authorities seized more than a billion of the "fake smokes" in California in 2005. Millions more packs of fake Marlboros, Mild Sevens, and other cigarettes made in North Korea have been seized in Taiwan, the Philippines, Vietnam, and Belize.<sup>43</sup> Officials from Philip Morris, which launched a major undercover operation to investigate the trade, have been cited as stating that DPRK-made knock-offs of its Marlboro brand have been discovered in more than 1,300

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<sup>40</sup> David L. Asher, Statement before a joint hearing of the Committee on Foreign Affairs, U.S. House of Representatives, Subcommittee on Terrorism, Non-proliferation, and Trade, and Committee on Financial Services, Subcommittee on Domestic and International Monetary Policy, April 18, 2007.

<sup>41</sup> Reuters. "New China system eases N. Korea sanctions," April 7, 2008.

<sup>42</sup> U.S. Department of State, *INCSR* (2008).

<sup>43</sup> See "Dispatch: Export boom: Tobacco Companies Trace Fake Cigarettes to North Korea," by Gordon Fairclough, *Wall Street Journal*, January 27, 2006.

places. They cite DPRK knock-off cigarette production capacity as being in the range of more than two billion packs a year, making Pyongyang one of the largest producers of such contraband in the world.<sup>44</sup>

Press reports cite a confidential report prepared by a consortium of tobacco manufacturers to the effect that the DPRK regime could be earning some \$80 to \$160 million in payoffs alone from manufacturers of such counterfeits. Gross revenues from such sales, according to the report, could generate between \$520 and \$720 million annually. One of the main hubs of such activity is reportedly Rajin, a free trade zone port city on North Korea's east coast.<sup>45</sup> Many of the cigarette factories in Rajin are reportedly owned and financed by Chinese criminal groups. According to one report, the DPRK regime allows specific deep-sea smuggling vessels to use its ports and provides the gangs with a secure delivery channel.<sup>46</sup> North Korean state-owned enterprises, mostly located in the Pyongyang area, also reportedly produce contraband cigarettes.<sup>47</sup>

A 2006 article on North Korean cigarette production found that DPRK cigarette manufacturers have been turning more toward producing domestic low-priced brand cigarettes instead of counterfeit products. The article states that relative to the price of rice, the price of a package of cigarettes has been falling and their quality has been rising.<sup>48</sup> In 2007, the DPRK imported \$12.95 million (\$14.1 million in 2006 and \$13.5 million in 2005) in tobacco products from China. Domestic brands now are taking market share from imports, and North Korean cigarette producers — even the factories operated by the No. 39 Department of the Workers' Party, which accumulates and manages Kim Jong-il's slush funds — reportedly have been producing more for the domestic market than counterfeits of brands such as Mild Seven, Crown (both Japanese brands), and Dunhill.<sup>49</sup>

Media reports indicate that Greek authorities seized some four million cartons of contraband cigarettes through the fall of 2006, of which three million were aboard North Korean vessels. For example, on September 25, 2006, Greek officials detained

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<sup>44</sup> Ibid. Note that legal cigarette production and distribution in North Korea is done partly by a joint venture between the British American Tobacco company and Sogyong General Trading Corporation, a Pyongyang-based state trader. See Lora Saalman, "Smoke Signals From BAT's North Korea Venture," *Online Asia Times*, February 8, 2006.

<sup>45</sup> See, for example, U.S. Department of State, *INCSR* (2008).

<sup>46</sup> See *Production of Counterfeit Cigarettes in the Democratic People's Republic of Korea* (DPRK), June 29, 2005, potentially available from Philip Morris, USA, the American tobacco unit of New York-based Altria Group, Inc. Note that the report does not touch upon the potential role played by South Korean authorities, who, whether by design or lack of customs, law enforcement resources, or political will, may facilitate or countenance the trade.

<sup>47</sup> Fairclough, Gordon. "Dispatch: Export boom: Tobacco companies trace fake cigarettes to North Korea," *Wall Street Journal*, January 27, 2006.

<sup>48</sup> Moon, Sung Hwee. "North Korean Cigarette Production: Chinese Cigarettes Disappear," *The Daily NK* (in English), August 12, 2008.

<sup>49</sup> Ibid.



a North Korean freighter that was carrying 1.5 million cartons of contraband cigarettes and arrested the seven seamen on board. According to information from Greek customs authorities, the ship's load of counterfeit, duty-unpaid cigarettes would have brought 3.5 million euros in taxes.<sup>50</sup>

## Insurance Fraud

Media reports from late 2006 suggested that the DPRK may be involved in insurance fraud as a matter of state policy. Some industry experts are concerned that claims for property damage are vastly overstated; circumstances of accidents are being altered; and that claims for deaths are not accident-related.<sup>51</sup>

A recent example cited in media reports of possible DPRK state involvement in insurance fraud involves a ferry accident that reportedly occurred in April 2006 near the coastal city of Wonsan. After the accident, North Korea declared that 129 people had died, all of whom were provided life insurance coverage when they bought a ticket. It was claimed that most of the victims had died of hypothermia, although weather data apparently indicated that temperatures were warmer than reported by Pyongyang's Korea National Insurance Corporation.<sup>52</sup> In another case, in July 2005, a medical rescue helicopter apparently crashed into a government owned disaster supply warehouse, setting it on fire. It reportedly took the DPRK authorities only 10 days to file a claim that included a detailed inventory of hundreds of thousands of items — a task which insurance industry officials say normally takes most governments many months.<sup>53</sup>

Although a practice of North Korean state initiated insurance fraud has not been confirmed, criminal conduct of this nature would appear consistent with a well-established pattern of DPRK crime-for-profit activity. One industry source estimated in 2006 that the extent of fraudulent DPRK insurance claims could have exceeded \$150 million.<sup>54</sup>

## Endangered Species Trafficking

Several reports link North Korean officials with trafficking in endangered species, which is in contravention to the U.N. Convention on International Trade in

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<sup>50</sup> Note that the Greek Merchant Marine Ministry reported that the ship, the *Evva*, was discovered about eleven kilometers southwest of the port of Katakolo on the Peloponnesus Peninsula in southern Greece. The cargo appeared to be destined for Greece. See "N. Korean Ship with Contraband Cigarettes Nabbed," *Chosun Ilbo*, September 26, 2006.

<sup>51</sup> See George Russell, "North Korea Suspected of Collecting Millions in Reinsurance Fraud," *Fox News* report of December 4, 2006, which cites Michael Payton, an attorney representing several of the insurance companies involved with the DPRK.

<sup>52</sup> *Ibid.* See also North Korea's Insurance Fraud, *Dong-A Ilbo*, 22:23 GMT, December 5, 2006.

<sup>53</sup> *Ibid.*

<sup>54</sup> Russell, "North Korea Suspected of Collecting Millions in Reinsurance Fraud," *op. cit.*

Endangered Species of Wild Fauna and Flora (CITES).<sup>55</sup> The DPRK is not a member of CITES; however, DPRK diplomats allegedly have been caught trafficking in CITES-protected species between treaty member states, including France, Russia, and Kenya.<sup>56</sup> According to the State Department, known DPRK violations of CITES began in the 1980s and have mainly involved trafficking in elephant ivory and rhino horn.<sup>57</sup> Although some may argue that cases of endangered species smuggling by DPRK diplomats may have been for personal use, the sheer size of confiscated shipments — as much as several hundred kilograms each — suggests that endangered species trafficking could have been planned by a North Korean government entity.<sup>58</sup>

## Human Trafficking

According to the State Department, North Korea is a source country for men, women, and children trafficked for forced labor and commercial sexual exploitation and has been listed by the U.S. government as a “Tier 3” country for as long as it has been included in the State Department’s *Trafficking in Persons* annual reports. As a Tier 3 country, North Korea reportedly does not comply with minimum standards for eliminating trafficking and is not making significant efforts to do so.

It remains unclear to what extent DPRK profits from human trafficking activities as a source of revenue. However, the State Department indicates that North Korea directly contributes to labor trafficking by maintaining a system of force labor prison camps inside the country, where an estimated 150,000 to 200,000 prisoners are forced to log, mine, and tend crops.<sup>59</sup> According to Mark Lagon, Director of the U.S. Office to Monitor and Combat Trafficking in Persons, the most common form of DPRK trafficking are North Korean women and children who voluntarily cross the border into China and are picked up by trafficking rings and sold as brides in China

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<sup>55</sup> See generally CRS Report RL34395, *International Illegal Trade in Wildlife: Threats and U.S. Policy*, by Liana Sun Wyler and Pervaze A. Sheikh.

<sup>56</sup> “Smuggling of Specimens of CITES-listed Species by Diplomats,” CITES 42<sup>nd</sup> Meeting of the Standing Committee, Lisbon (Portugal), 1999, Doc. SC.42.12.7, at [<http://www.cites.org/eng/com/sc/42/42-12-7.pdf>].

<sup>57</sup> Statement of Peter Prahar, Office Africa, Asia, and Europe Programs, Bureau for International Narcotics and Law Enforcement, State Department, before the Subcommittee on Federal Financial Management, Government Information, and International Security, Senate Homeland Security and Government Affairs Committee, April 25, 2006.

<sup>58</sup> For arguments to this effect, see Statement of William Bach, Office Africa, Asia, and Europe Programs, Bureau for International Narcotics and Law Enforcement, State Department, before the Subcommittee on Financial management, the Budget, and International Security, Senate Government Affairs Committee, May 20, 2003.

<sup>59</sup> U.S. Department of State, *Trafficking in Persons Report*, section on “country narratives,” June 2007, at [<http://www.state.gov/g/tip/rls/tiprpt/2007/82806.htm>]. According to the State Department, a trafficking victim “need not be physically transported from one location to another” in order for the crime to fall within Congress’ definition of “severe forms of trafficking in persons” (as defined in the Trafficking Victims Protection Act of 2000, P.L. 106-386, as amended).

and elsewhere, including Russia and Mongolia.<sup>60</sup> The 2007 *Trafficking in Persons* report further states that North Korean women and girls may also be lured out of DPRK with promises of food, jobs, and freedom, only to be forced into prostitution, marriage, or exploitative labor arrangements in China.

## Policy and Prospects

U.S. policy has addressed North Korea's crime-for-profit activities through several tracks, including diplomacy, law enforcement, economic sanctions, and economic incentives. In some instances, the various tracks may overlap considerably, while in other cases, they may work at cross-purposes. Congress has played an active role in the oversight of U.S. policy toward North Korea and may further consider evaluating U.S. efforts to reduce North Korea's crime-for-profit activities or explore in more detail the dynamics and trends related to the regime's illicit financial channels.

One strategy on the diplomatic front has been to use fora such as the Six-Party Talks on nuclear proliferation to address issues such as North Korea's illicit activities. This was the initial preference of the Bush Administration, but since sometime after the BDA action in 2007, this tactic no longer appears evident. As the Bush Administration comes to a close, denuclearization is the primary emphasis of policy on North Korea. Also, if the DPRK is able to earn foreign exchange and receive more economic assistance, the pressure to generate foreign currency through illicit activities arguably will diminish.

The policy debate heretofore has been divided between those who argue to pressure North Korea with unilateral tactics that cut DPRK off from access to its illicitly generated profits through economic sanctions<sup>61</sup> and a second group of policymakers more in favor of engagement who seek to resolve the North Korean problem mainly by negotiations. Its goal is to change DPRK's "bad behavior" by bringing the country into the circle of peaceful nations and inducing it to act in accord with international standards.<sup>62</sup> In 2008, the latter argument seems to be carrying the day.

Following recent developments in the Six-Party talks, a continued policy challenge for the United States is to receive a commitment by Pyongyang to curtail its alleged crime-for-profit activities. A possible vehicle for this discussion could be the working team on the normalization of diplomatic relations between the DPRK and the United States. Since Japan, South Korea, and China also have considerable interest in protecting themselves from North Korean illicit activity, it also may be

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<sup>60</sup> "Director Lagon Speaks at Woodrow Wilson International Center for Scholars," *U.S. Fed News Service*, March 3, 2008.

<sup>61</sup> See for example, John R. Bolton, "Salvaging Our North Korea Policy," Op-ed, *The Wall Street Journal*, March 17, 2008.

<sup>62</sup> See for example, David Sanger, "Questions without Answers: The Korean Conundrum," *The New York Times*, January 19, 2006.

addressed in the working team on normalizing relations between the DPRK and Japan as well as in other negotiations. So far, however, the working teams have not appeared to have addressed North Korean crime-for-profit activities.<sup>63</sup>

On the law enforcement side are actions such as the prosecution of criminal behavior and those resulting from the Bush Administration's Illicit Activities Initiative (IAI). The IAI was established in 2003 as an interagency effort aimed at curtailing North Korean involvement in narcotics trafficking, counterfeiting, and other illicit activities. The major purposes of the initiative have been to provide policy support for the Six-Party Talks and to hold North Korea to internationally accepted standards of behavior by enforcing relevant U.S. and other laws. The IAI has come to involve fourteen different U.S. government departments and agencies, and it has received cooperation from fifteen different governments and international organizations.<sup>64</sup> The Banco Delta Macau action stemmed partly from the work of the IAI.

The United States and other nations also are taking direct measures to halt shipments of illicit cargo from North Korea. The Proliferation Security Initiative (PSI), for example, is aimed at stopping shipments of weapons of mass destruction, their delivery systems, and related materials by tracking and searching suspected ships or other conveyances transporting such cargo.<sup>65</sup> Fourteen nations have signed on to the PSI, and many more have endorsed the principles.<sup>66</sup> Although not directed at illicit activities per se, the prospect of ships being inspected complicates North Korean efforts to smuggle items such as illegal drugs, fake pharmaceuticals, and counterfeit currency.<sup>67</sup> A weakness of the PSI, however, is that the DPRK's immediate neighbors, China and South Korea, have not joined the effort, though there is some speculation that Seoul may join under new President Lee Myung-bak. In addition, no North Korean ships or airplanes have been halted by a PSI operation.

The role of Congress in this issue includes oversight of U.S. policy, eliciting information and raising public awareness of the issue, and in balancing U.S. interests when foreign policy goals may conflict with anti-crime activities. Congress also may be asked to provide funding for energy and food assistance to North Korea as part of

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<sup>63</sup> For the status of current and ongoing political developments involving the DPRK see CRS Report RL33567, *Korea-U.S. Relations: Issues for Congress*, by Larry Nicksch and CRS Report RL33590, *North Korea's Nuclear Weapons Development and Diplomacy*, by Larry Nicksch.

<sup>64</sup> See David L. Asher, Statement Before the Subcommittee on Federal Financial Management, Government Information, and International Security Senate Homeland Security and Government Affairs Committee, April 25, 2006.

<sup>65</sup> See also CRS Report RL34327, *Proliferation Security Initiative (PSI)*, by Mary Beth Nikitin.

<sup>66</sup> U.S. Department of State. *The Proliferation Security Initiative*, June 2004. [<http://usinfo.state.gov/products/pubs/proliferation/>]

<sup>67</sup> The White House. Proliferation Security Initiative, Fact Sheet. September 4, 2003. U.S. Department of State. U.S. Notes First Anniversary of Proliferation Security Initiative. Press Release, June 1, 2004.

a resolution of the DPRK's nuclear weapons program, because some contend that additional supplies of energy and food could reduce the need to rely on illicit activities in some North Korean quarters. Congressional action also could be required to enable North Korea to earn more foreign exchange through an increase in its legitimate exports or by attracting investments from U.S. businesses. This could include, for example, granting the DPRK normal trading nation status (most favored nation status) with respect to U.S. import duties,<sup>68</sup> or by allowing goods from North and South Korea's Kaesong Industrial Complex to be included in the proposed Korea-U.S. Free Trade Agreement.<sup>69</sup>

For those assuming that the Pyongyang regime wants to curb its crime-for-profit activity, an important question yet unresolved is the degree to which the leadership will be able to do so. Analysts point out that in nations or regions where the crime has become institutionalized, income from such activity often becomes "addictive" to those involved in the criminal conduct. In such instances, a class of criminal entrepreneurs is created and, in the case of North Korea, analysts point to the systematic criminalization of the state, over years, and its growing intimate relationships with organized crime elements throughout Asia.<sup>70</sup> That is not to say that North Korean criminals, like other criminals, would not be able to switch emphasis from risky criminal activity, such as narcotics trafficking, to less risky and potentially even more lucrative large-scale manufacture and trade in counterfeit cigarettes and pharmaceuticals — a trend that may well be underway. Indeed, state countenanced — if not state sponsored — production of seemingly genuine Japanese and U.S. cigarettes appears to be flourishing, as may large scale production of expertly packaged pharmaceuticals such as Viagra®.

Whereas the capacity to produce opium is dependent on the availability of suitable land and climatic conditions, methamphetamine production and a wide range of counterfeiting activities are not limited by agricultural production constraints. Reports of substantial DPRK imports of ephedrine — an essential precursor for methamphetamine production — support the theory that the DPRK has developed a significant production capacity for methamphetamine. Such activity is occurring at a time when (1) North Korea urgently needs foreign currency, and (2) the southeast Asian methamphetamine market continues to expand.

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<sup>68</sup> Only Cuba and North Korea do not have normal trade relations (NTR) status with the United States. Usually, countries first normalize relations with the United States, then sign a trade agreement that provides temporary NTR status, and then seek permanent NTR status. Without NTR, imports are assessed the duties that were applied to U.S. imports in the 1930s before being reduced by various rounds of multilateral negotiations and other agreements.

<sup>69</sup> See CRS Report RL34330, *The Proposed U.S.- South Korea Free Trade Agreement (KORUS FTA): Provisions and Implications*, coordinated by William H. Cooper.

<sup>70</sup> Note that in the case of drug trafficking relationships, indications are mounting that the DPRK is using Chinese criminal groups to traffic in — and mask the source of — DPRK produced drugs. See for example, China 'Ailing' from North Korean-Made Drugs — Drugs now bigger problem than North Korea Escapees by Kang Ch'ol-hwan, Seoul *Chosun Ilbo* (Internet Version), October 9, 2004.

Some see promise in the efforts by the international community to entice and/or pressure Pyongyang into reducing its involvement in crime-for profit activity.<sup>71</sup> Others, however, argue that the more legitimate the source of income, the greater the pressure for accountability on the regime, since revenue from illicit activities does not usually enter official records. Hence, they maintain that proposals to shift DPRK crime-related income toward legitimate-source income ignore the fact that the current regime diverts some illicit earnings to slush funds designed to sustain the loyalty of a core of party elite and to underwrite weapons development programs. They suggest, therefore, that prospects for a decrease in crime-for-profit activity are not good and that the current regime is likely to be neither willing nor able to change its dependence on income where no accountability is involved. Still, it appears that Pyongyang is reducing much of its illicit activity as it finds other means to export and earn foreign exchange.

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<sup>71</sup> For information on the internal dynamics and situation in the DPRK, see *Assessing Internal North Korea* by Larry A. Niksch, a paper prepared for a conference on North Korea sponsored by the Keck Center for International and Strategic Studies, Claremont McKenna College, October 26-27, 2006.