



Proliferation Finance: Critical Issues and Priorities for Congress

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KEY ISSUES

The lack of effective and universal financial controls to prevent weapons of mass destruction (WMD) proliferation is a gaping security vulnerability for the international community.

The United States has a unique responsibility to combine domestic legislative and regulatory reforms with international leadership in order to strengthen the countering proliferation finance regime. Doing so will require overcoming significant political-will obstacles.

Congress can lead the way by strengthening financial transparency domestically and ensuring that the executive branch is adequately resourced.

SUMMARY

The U.S. government and Congress have long prioritized reducing the risk of weapons of mass destruction (WMD) proliferation, whether from state actors such as North Korea and Iran, or from non-state actors, particularly criminals and transnational terrorist networks.

Despite this concern, however, there remains a significant blind spot: the efforts to prevent the *financing* of WMD proliferation are only in their infancy. The legal framework to prevent the financing of proliferation is weak, and implementation across the world is spotty. The United States in particular suffers from easily fixable deficiencies in its approach to this critical national security issue.

North Korea and Iran in particular have operated (and North Korea continues to operate) egregious, publicly documented, sophisticated global networks of trusted financial agents. These networks are quite sophisticated at evading detection and know how to exploit weak regulations and enforcement in jurisdictions around the world.

These states are creative and diligent in developing new ways to continually disguise their activities, pioneering new technology and networks to sustain themselves and grow. The United States has prioritized dealing with North Korea and Iran as high-level security threats, but the proliferation finance aspect of that strategy has been woefully underdeveloped.

WHAT IS PROLIFERATION FINANCE?

In contrast to the nuclear weapons programs of advanced industrial states, many U.S. adversaries do not have the indigenous research, development, and deployment capacity to constitute WMD programs entirely on their own. As a result, they have to seek financial resources, goods, and know-how elsewhere, including from reputable industrial firms throughout the world, especially from the United States and Europe. The illicit networks that procure these goods and the revenue to sustain illicit WMD programs represent a serious national security threat: financing of proliferation is the essential money trail that enables rogue states, and non-state actors, to threaten peace and security.



Figure 1, which describes Pan Systems and GLOCOM business activities in Asia, demonstrates some of the hallmarks of a North Korean proliferation network:

- » Use of front or shell companies to disguise the controlling entities and to avoid sanctions screening by financial institutions handling the transactions;
- » Strong geographic nexus with China;
- » Use of other vulnerable jurisdictions (Malaysia), or jurisdictions that are global financial and trade centers (Singapore); and
- » Revenue raised from non-military activity (sale of radio equipment) is for the ultimate benefit of the DPRK’s weapons program.

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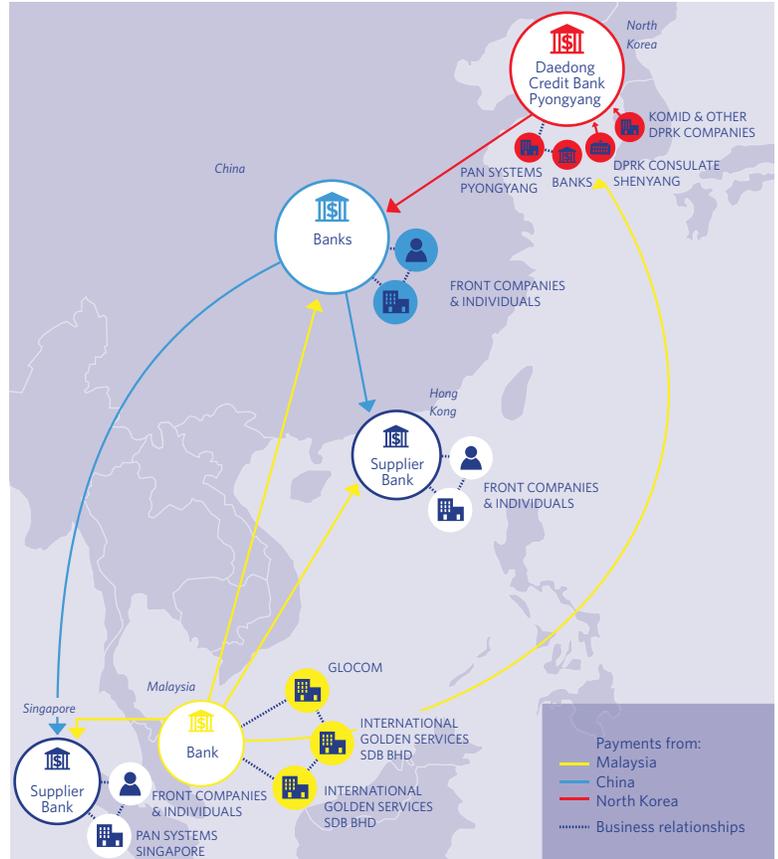


Figure 1: A simplified illustration of North Korea’s sophisticated procurement networks, based in multiple countries. In this case, Pan Systems Pyongyang and its front companies carry out financial activity in multiple jurisdictions, which benefits, among others, the Korea Mining and Development Trading Corporation (KOMID), which is widely considered to be North Korea’s primary arms dealer and main exporter of goods and equipment related to ballistic missiles and conventional weapons. Pan Systems Pyongyang’s involvement in Middle East business is referenced without details (not shown).

It is possible to detect and track the financing of proliferation. By going outside their own national borders to find support for illicit weapons programs, proliferating states leave themselves open to discovery by the international community. If moving money in exchange for goods is essential to building a weapons of mass destruction program, then it becomes possible for financial regulators, law enforcement, and intelligence agencies to track and disrupt it, and, where possible, to apprehend members of the proliferation networks. Ultimately, cracking down on the financing of illicit activities is an effective way to stop the illicit activity itself.



THE ROLE OF THE UNITED STATES

The United States is well placed to correct this misperception and make a meaningful difference to check the global nuclear threat. The dollar is the global currency of choice for trade, investment, and as a reserve currency, and the U.S. financial sector is the largest globally.

The United States deserves credit for attempting to address this situation, but must do much more to focus maximum effort on constraining rogue countries' ability to pursue an illicit weapons capability, including increasing global cooperation to address this issue. This includes specific enforcement actions domestically, such as strengthening rules around financial transparency, extending safe harbor provisions for banks working creatively on finding proliferation finance typologies internally, and increasing resources for national law enforcement, and regulatory and intelligence agencies.

NEXT STEPS

- » Congress should pass legislation requiring the reporting to law enforcement of the ultimate beneficial ownership of corporate entities that are created in the United States. Doing so would provide an invaluable tool for information gathering about illicit financial actors, including proliferation networks. The existing Customer Due Diligence Rule is insufficient because it only requires certain financial institutions to collect such information, without a mandate that it be automatically transmitted to government authorities.
- » Congress should consider advancing a financial requirement to mandate the declaration of all cross-border payments, possibly including information that would be relevant to bridging the gap between data about financial transactions and the physical shipment of potentially proliferation-related goods. As currently formulated, the Travel Rule is only for transactions above \$3,000 and requires only retention, not transmittal to relevant authorities. U.S. partners Canada and Australia already operate significantly tougher Cross-Border Transfer Rules.
- » Congress should use its significant oversight responsibilities to ensure the administration's timely implementation of the Customer Due Diligence Requirements for Financial Institutions Rule, which became effective in May 2018. The rule strengthens the requirement for financial institutions to verify the identity of account holders, requiring the ongoing monitoring of customer accounts for suspicious transactions.
- » Congress should prioritize additional increases on a yearly basis for the Treasury Department's Office of Terrorism and Financial Intelligence (TFI) in order to more adequately provide resources for activities to counter proliferation finance. TFI's activities include the formulation and enforcement of all financial measures to counter weapons of mass destruction.
- » Congress is currently taking steps to require the administration to create a Virtual Currency Task Force; it should mandate that such a Task Force produce analysis on the impact of financial technology on financial crimes compliance, including its specific application to countering proliferation finance.

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- » Congress should appropriate more resources to expand technical assistance programs run by the Departments of State (Export Control and Related Border Security or the Bureau of International Security and Nonproliferation) and Defense (Defense Threat Reduction Agency). These programs enable partner countries to tighten their regulatory and legal regimes to combat proliferation finance.
- » Congress should use its significant oversight ability to ensure that U.S. diplomatic engagement with North Korea adequately addresses Pyongyang’s abuse of the international financial system.

FURTHER READING

- » Elizabeth Rosenberg, Neil Bhatiya, Claire Groden and Ashley Feng, “Financial Networks of Mass Destruction,” (Center for a New American Security, January 2019) <https://www.cnas.org/publications/reports/financial-networks-of-mass-destruction>.
- » Jonathan Brewer, “The Financing of WMD Proliferation: Conducting Risk Assessments,” (Center for a New American Security, October 2018), <https://www.cnas.org/publications/reports/the-financing-of-wmd-proliferation>.
- » Jonathan Brewer, “The Financing of Nuclear and other Weapons of Mass Destruction Proliferation,” (Center for a New American Security, January 2018), <https://www.cnas.org/publications/reports/the-financing-of-nuclear-and-other-weapons-of-mass-destruction-proliferation>.