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## Case Study: United States Busts Likely North Korean Transshipment Scheme

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*The U.S. Justice Department recently announced the arrest of a Taiwanese father and son for allegedly conspiring to export U.S. machine tools that could be used in the production of advanced weapons systems, including weapons of mass destruction. Although the Department of Justice has established that the goods went to Taiwan, past illicit procurement activities of the father could indicate the goods were sent onward to North Korea.*

On May 6, 2013, the U.S. Department of Justice's Attorney for the Northern District of Illinois announced the arrest of a Taiwanese father and son for allegedly conspiring to send U.S. machines relevant to the production of advanced weapons systems to Taiwan in violation of U.S. sanctions put in place against the father in 2009.<sup>1</sup> Since he had a [history of working for](#) North Korea's advanced weapons program procurement arms, the Justice Department believes the goods may have been sent onward to North Korea. According to the Department of Justice press release on the arrests, the father, son, an unnamed associate, and their network of companies were "engaged in the export of U.S. origin goods and machinery that could be used to produce weapons of mass destruction." The U.S. machines sought could be "used to fabricate metals and other materials with a high degree of precision."<sup>2</sup> North Korea has a history of seeking abroad advanced machine tools for its military and nuclear programs.

The father, Hsien Tai Tsai, or "Alex Tsai," 67, resided in Taiwan and was arrested in Tallinn, Estonia at the request of U.S. authorities. His son, Yeuh-Hsun Tsai, or "Gary Tsai," 36, who was born in Taiwan but is a legal permanent resident of the United States, was arrested at his home in Glenview, Illinois. He is alleged to have assisted his father in obtaining the U.S. machines through a trading company in Illinois that he set up for the explicit purpose of obtaining these goods. He would allegedly arrange their export to Taiwan where his father may have re-exported them to North Korea. One prominent North Korean entity is referenced in this case in the context of Alex Tsai's 2009 sanctioning by the United States, the Korea Mining Development Trading Corporation (KOMID), although Alex Tsai may have dealt with other entities. KOMID may have been the recipient of the machines and the Tsais may have acted at its direction.

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<sup>1</sup> U.S. Department of Justice, "Press Release: Taiwanese Father and Son Arrested for Allegedly Violating US Laws to Prevent Proliferation of Weapons of Mass Destruction," May 6, 2013.

<sup>2</sup> Department of Justice Press Release.

KOMID was designated by the United Nations Security Council resolution 1718 Committee in 2009. The State Department indicates that KOMID is “Pyongyang’s premier arms dealer and main exporter of goods and equipment related to ballistic missiles and conventional weapons...KOMID has offices in multiple countries and facilitates weapons sales for the North Korean government.”<sup>3</sup>

According to case documents, Alex Tsai is a major procurement agent for North Korea’s KOMID with activity spanning back to the 1990s.<sup>4</sup> Alex Tsai and two of his companies in Taiwan, Trans Merits Ltd. and Global Interface Company, Inc. were sanctioned in January 2009 by the United States Treasury Department’s Office of Foreign Assets Control (OFAC) for procurements on behalf of KOMID. He and his company, Trans Merits Co., were also indicted in Taiwan in June 2008 for “illegally forging invoices and shipping restricted materials to North Korea.”<sup>5</sup> That year, Alex Tsai and Trans Merits were convicted.<sup>6</sup> Subsequently, Alex Tsai allegedly created new companies, one called Trans Multi Mechanics Co., to act as the claimed end-users of the U.S. machines and thereby evade U.S. trade controls.<sup>7</sup> His son, Gary Tsai, allegedly assisted his father from Illinois by creating his own company that enabled this prolific smuggler to continue doing business, despite the sanctions and his conviction in Taiwan. Another alleged conspirator named as “Individual A” in the indictments, a Taiwanese associate of Alex Tsai, may still be under investigation. The Tsais are each charged with three identical counts of conspiring to defraud the United States in the enforcement of its anti-WMD proliferation laws, conspiracy to violate the International Emergency Economic Powers Act (IEEPA) by evading the U.S. sanctions against exporting to Alex Tsai and his two companies, and money laundering.

Alex Tsai is expected to be extradited from Estonia to the United States. Although it is unclear why he was in Estonia, U.S. authorities have previously lured illicit procurement agents to third party countries with amenable extradition policies or treaties with the United States, where they are arrested by cooperating local authorities. U.S. Immigration and Customs Enforcement (ICE) agents have posed as suppliers or middlemen that claim to want to make illicit deals for U.S. goods with the targeted procurement agents, luring them to the third party country on the pretense of a meeting to discuss business. For example, in 2007, a three year ICE [operation](#) against Iranian procurement agent Amir Hossein Ardebili led to his arrest in Tbilisi, Georgia after he unsuspectingly met with U.S. officials and admitted criminal intentions while under video surveillance. Ardebili was extradited to the United States, pled guilty to fourteen charges, and received a sentence of five years in prison.

## The Scheme and Procurements

Starting in 2008, Alex Tsai in Taiwan, and Gary Tsai, his son in Illinois, began procuring U.S. machine goods. According to the indictments, the alleged criminal acts took place between August 2009 and August 2010, after Alex Tsai was sanctioned by OFAC in January 2009. After his designation, Alex Tsai allegedly created a company in Taiwan called Trans Multi Mechanics Co. and used it interchangeably with Trans Merits in an attempt to thwart U.S. sanctions. The indictment of Alex Tsai indicates that

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<sup>3</sup> U.S. Department of State, “Fact Sheet: United States Sanctions Individuals Linked to North Korean Weapons of Mass Destruction Programs,” March 8, 2013. <http://www.state.gov/t/isn/205879.htm>

<sup>4</sup> Department of Justice Press Release.

<sup>5</sup> United States District Court in the Northern District of Illinois, Eastern Division, *Indictment: United States of America v. Hsien-Tai Tsai aka Alex Tsai*, October 23, 2012, p. 3.

<sup>6</sup> *United States of America v. Alex Tsai*, p. 3.

<sup>7</sup> Department of Justice Press Release.

the alleged scheme “attempted to hide Alex Tsai’s and Trans Merit’s involvement in those transactions by conducting business under different company names.”<sup>8</sup>

In September 2009, Gary Tsai created an import/export company called Factory Direct Machine Tools. The indictment alleges that Alex Tsai and Individual A were partners in Factory Direct.<sup>9</sup> The indictment claims that Factory Direct was used by Gary Tsai to negotiate machinery purchases on behalf of front companies Trans Merits and Trans Multi Mechanics and to import goods into the United States for unknown buyers. The three allegedly conspired to visit specific U.S. machine companies and purchase machinery from them. Gary Tsai would request from Alex Tsai payment for goods procured. The goods were allegedly exported to Taiwan to Trans Merits/Trans Multi Mechanics and then may have been sent on to North Korea.

### ***Pre-OFAC Designation Transactions***

Gary Tsai assisted with several transactions that preceded Alex Tsai’s January 2009 OFAC designation. In August and September 2008, Gary Tsai arranged the export of a used Sansei 20” SS-501 rotary surface grinder from a U.S. company located in Michigan. The indictment explains that this machine “is used to produce precision ground surfaces” and could be used “to produce rocket parts.”<sup>10</sup> Gary Tsai arranged its export from Los Angeles, California to Taiwan using Air Tiger Express. Trans Multi Mechanics in Taiwan sent funds in the amount of \$12,000 to pay for this machine.

In September and October 2008, Gary Tsai arranged the purchase of another used Sansei 20” SS-501 rotary surface grinder from a U.S. company in Santa Paula, CA. Alex Tsai and Individual A flew from Taiwan and joined Gary Tsai in an inspection of the machine. Trans Multi Mechanics’ bank account was the source of payment for this item, which was sold for \$10,500. The machine was exported to Trans Merits Co. Ltd. in Taiwan using Air Tiger Express.

In September and October 2008, Gary Tsai negotiated the purchase of a Mitsui Seiki HT-4A Horizontal Machining Center, which is “a machine tool capable of producing extremely accurate machine parts,” from a company in Barberton, Ohio.<sup>11</sup> Alex Tsai allegedly sent \$36,650 for the machine from Taiwan.

### ***Post-OFAC Designation Transactions (Alleged Crimes)***

Following his designation by OFAC in January 2009, three days later, Gary Tsai allegedly signed up to begin receiving e-mail notifications from OFAC which contained information about designations. Thus, he was likely aware of his designation. The American Institute in Taiwan also sent to Tsai’s home a letter notifying him that his U.S. visa had been cancelled due to the designation.

In September 2009, Gary Tsai, Alex Tsai, and Individual A allegedly worked to arrange the export of a U.S.-origin Bryant Center Hole Grinder from a company in Skokie, Illinois using the name Trans Multi Mechanics, the alleged alias for the sanctioned Trans Merits. The indictment does not indicate whether this machine could be used to produce advanced weapons systems. It could be used to

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<sup>8</sup> *United States of America v. Alex Tsai*, p. 4.

<sup>9</sup> *Ibid.*

<sup>10</sup> *Ibid.*, p. 7.

<sup>11</sup> *United States of America v. Alex Tsai*, p. 13.

“grind a center hole, with precisely smooth sides, through the length of a material.”<sup>12</sup> A centrifuge expert advising ISIS thought that the machine could be useful to making gas centrifuge components.

Alex Tsai in Taiwan allegedly claimed in e-mail communications that he was an agent working for Trans Merits to procure for Trans Multi Mechanics. Gary Tsai in Chicago allegedly claimed that he worked for Trans Multi Mechanics, the front company created by his father, but provided the supplier with a business card stating Trans Merits. It is unknown why the U.S. company did not check that Trans Merits was sanctioned by the United States before making this export. The Tsais are accused of laundering \$7,200 from Taiwan to the United States to pay for the procurement.

The indictments claim that the alleged conspirators used the company name Factory Direct Machine Tools of Chicago to attempt to procure and import goods into the United States for unspecified purposes. Importations of any goods involving the designated Alex Tsai would also be a violation of U.S. law. E-mail communications indicated that Gary Tsai considered his father to be “the boss” of Factory Direct despite the company being in his name.<sup>13</sup> In early 2010, the alleged conspirators arranged the import of LED traffic lights and related parts into the United States. In August 2010, Gary Tsai allegedly imported an oil pump into the United States for unknown purposes. Also that month, he allegedly imported a Vickers pump into the United States and discussed sending money to Alex Tsai’s bank account in Hong Kong.<sup>14</sup>

## Lessons and Observations

As the likely end-user of the goods named in this case, North Korea is evidently in the market for Western-made machines and other goods to outfit and supply its advanced weapons programs. Western nations and suppliers and their subsidiaries worldwide must investigate any suspicious equipment requests with claimed East Asian trading company end-users and be on watch for schemes involving common East Asian transit points, such as China, Hong Kong, and Taiwan.

Many major North Korean illicit procurement schemes which have been brought to light involve obtaining goods from or via China in violation of UN Security Council sanctions resolutions, Chinese export controls, or the domestic export laws of Western nations. This case indicates that North Korea does not rely solely on China as a transit country, or country of diversion concern, to obtain needed supplies for its advanced weapons programs from high technology supplier states. It also may use Taiwan as a transit country for U.S., European, and Japanese goods. Taiwanese officials need to redouble efforts at policing the activities of the many trading companies on their territory and better examine re-exports heading for North Korea. This case implies that they have not done enough. In particular, one question is, why was Alex Tsai able to continue operating his illicit procurement schemes unhindered after being indicted and convicted?

By the exploitation of the poorly enforced trade control laws of its neighbor, China, North Korea has hidden from Western intelligence agencies many of its procurements for its advanced weapons and nuclear programs. This case highlights that North Korea is not self-sufficient at producing

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<sup>12</sup> United States District Court in the Northern District of Illinois, Eastern Division, *Indictment: United States of America v. Yueh-Hsun Tsai aka Gary Tsai*, April 19, 2013, p. 4.

<sup>13</sup> *United States of America v. Alex Tsai*, p. 30.

<sup>14</sup> *Ibid*, pp. 29-34.

domestically the goods it requires for its advanced weapons programs. In particular, it requires machine tools. This should serve as a reminder that although North Korea's foreign procurements are not detected as regularly as Iran's, that relative absence of detection does not mean that North Korea is not procuring from abroad or that it is not dependent on foreign supply for its military and nuclear programs.

The United States continues to have successes in carrying out and conducting sting operations to stop illicit procurement agents worldwide. Its arrests of smugglers in third party countries with friendly extradition treaties and policies remain a creative way to circumvent the current inadequate international rules and laws governing prosecutions of illicit procurement agents working for sanctioned countries.