

## Countering Flags of Convenience to Strengthen Sanctions Enforcement



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<b>14. ABSTRACT</b>  Flags of Convenience (FOC) undermine the effectiveness of U.N. sanctions with North Korea, in addition to a number of transnational harms. This paper argues for a multi-layered approach to strengthen the at-sea enforcement of U.N. sanctions with North Korea, which would provide a template for future sanctions regimes and measures to limit the harm posed by FOCs in other shared threats. FOCs come from an incentive structure in the law of the sea that provides nations with preeminent authority over registered ships and broad discretion in the registration and oversight process. This places flag States in competition to register ships, which in turn encourages lax enforcement and oversight by some. To counter this, the paper proposes several steps that the United States can take with the international community to strengthen ship registration standards, improve oversight, and ultimately, strengthen compliance with the rule of law.									
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## INTRODUCTION

United Nations sanctions provide a powerful tool to cooperatively address global security threats, including proliferation, terrorism, and human rights violations.<sup>1</sup> As a key component, sanctions often prohibit the maritime transportation of items, like nuclear weapons materials, arms and military equipment, and revenue-producing commercial goods.<sup>2</sup> But these bans are ineffective when enforcement relies solely on the flag State because of flags of convenience. As a result, the United States must address the unwillingness or inability of flags of convenience to tackle global security challenges.

A flag of convenience is a nation that sets few requirements for ship registration and allows registration regardless of the ship's connection to the country.<sup>3</sup> These lax ship registries provide no transparency over ship ownership and operate as little more than a revenue source for the country, or "flag State."<sup>4</sup> Although international law requires that flag States oversee and enforce the conduct of registered ships, flags of convenience fail to do so because of a lack of interest, capability, or desire to not disturb its reputation as a flag State of choice.<sup>5</sup>

Enforcement that relies solely on a flag State to police its ships does not work because systemic failures in the law of the sea incentivize lax enforcement by flags of convenience and encourage their use by malicious actors to evade accountability. The use of flags of convenience in repeated North Korea sanctions violations illustrates the harm that these registries pose, which

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<sup>1</sup> United Nations Security Council, "Consolidated List," accessed on 21 January 2021, <https://www.un.org/securitycouncil/content/un-sc-consolidated-list>.

<sup>2</sup> Arms Control Association, "UN Security Council Resolutions on North Korea," April 2018, accessed on 12 January 2021, <https://www.armscontrol.org/factsheets/UN-Security-Council-Resolutions-on-North-Korea>.

<sup>3</sup> Tina Shaughnessy and Ellen Tobin, "Flags of Inconvenience: Freedom and Insecurity on the High Seas," *Journal of International Law and Policy* V (2006-2007): 7, [https://www.law.upenn.edu/journals/jil/jilp/articles/1-1\\_Shaughnessy\\_Tina.pdf](https://www.law.upenn.edu/journals/jil/jilp/articles/1-1_Shaughnessy_Tina.pdf).

<sup>4</sup> Matthew Gianni, "Real and Present Danger: Flag State Failure and Maritime Security and Safety," *International Transport Workers' Federation* (June 2008): 6, accessed on 12 January 2021, [https://www.itfglobal.org/sites/default/files/resources-files/flag\\_state\\_performance.pdf](https://www.itfglobal.org/sites/default/files/resources-files/flag_state_performance.pdf); Shaughnessy and Tobin, "Flags of Inconvenience," 8.

<sup>5</sup> George C. Kasoulides, "The 1986 United Nations Convention on the Registration of Vessels and the Questions of Open Registries," *Ocean Development and International Law* 20, no. 6 (1989): 544-45, accessed 12 January 2021, HeinOnline.

mirror similar harms across a range of transnational threats.<sup>6</sup> To address this link between flags of convenience and illicit activity, the United States needs a multi-layered approach that promotes stricter ship registration standards, disincentivizes flag of convenience registries, and diminishes the flag State's normally exclusive authority to inspect ships at sea.

## BACKGROUND

North Korea faces a comprehensive sanctions regime because of its nuclear weapons program.<sup>7</sup> Starting in 2006 and steadily expanding since, these sanctions target a range of activities, goods, and financial transactions in an effort to deprive the regime and its military of support.<sup>8</sup> The sanctions prohibit the importation of a number of items, including luxury goods, military equipment and technology, and limiting oil, natural gas, and petroleum products.<sup>9</sup> The sanctions also target the regime's funding by barring exports of military equipment, textiles, food products, coal, metals, and minerals.<sup>10</sup> The United Nations maintains the international law framework found in the law of the sea and requires that flag States enforce the sanctions regime on their registered ships.<sup>11</sup>

Despite these bans, foreign-flagged ships continue to trade with North Korea.<sup>12</sup> For example, a Sierra Leone-flagged ship recently made three trips to North Korea to deliver fuel and a Panama-flagged ship transferred fuel to a North Korean vessel during a prohibited at-sea

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<sup>6</sup> Robert Huish, "The Failure of Maritime Sanctions Enforcement against North Korea," *Asia Policy* 23 (January 2017): 150, accessed 8 December 2020, JSTOR.

<sup>7</sup> Eleanor Albert, "What to Know About Sanctions on North Korea," Council on Foreign Relations, 16 July 2019, accessed on 10 January 2021, <https://www.cfr.org/backgrounder/what-know-about-sanctions-north-korea>.

<sup>8</sup> Huish, "The Failure of Maritime Sanctions Enforcement," 137; Arms Control Association, "UN Security Council Resolutions on North Korea."

<sup>9</sup> Arms Control Association, "UN Security Council Resolutions on North Korea."

<sup>10</sup> Arms Control Association.

<sup>11</sup> Arms Control Association.

<sup>12</sup> Albert, "What to Know About Sanctions"; Huish, "The Failure of Maritime Sanctions," 145.

rendezvous.<sup>13</sup> These examples illustrate the 56 prohibited maritime transfers that took place in just the first quarter of 2020, resulting in delivery of total of “600,000 to 1.6 million barrels” of refined petroleum.<sup>14</sup> These latest violations reflect North Korea’s continued use of flags of convenience to advance its nuclear program; a trend starting in the early 2000s.<sup>15</sup> Flags of convenience registries often linked to illicit transfers, include: Panama, Belize, Comoros, Equatorial Guinea, Sierra Leone, Tanzania, Togo, Mongolia, and Russia.<sup>16</sup>

### **THE LAW OF THE SEA INCENTIVIZES FLAGS OF CONVENIENCE**

The North Korea sanctions regime follows international law by relying on individual nations, as “flag States,” to regulate the activity of their ships.<sup>17</sup> Under this international law framework, flag States must maintain a registry, exercise jurisdiction and control over registered ships, and “adhere to standards of international law.”<sup>18</sup> Once registered, a ship enjoys freedom from interference by other nations during its voyage and activity at sea.<sup>19</sup>

Implementation of those broad standards is largely a matter of prerogative for each flag State.<sup>20</sup> This combination of a flag State’s preeminent authority and autonomy encourages abuse, or flags of convenience. The system allows these nations to broadly extend registry services and sovereign protection to ships throughout the world, regardless of any meaningful connection to

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<sup>13</sup> United Nations Security Council, “Report of the Panel of Experts Established Pursuant to Resolution 1874 (2009),” S/2020/840, (August 28, 2020): 11, accessed on 10 January 2021, [https://www.securitycouncilreport.org/atf/cf/%7B65BFCF9B-6D27-4E9C-8CD3-CF6E4FF96FF9%7D/s\\_2020\\_840.pdf](https://www.securitycouncilreport.org/atf/cf/%7B65BFCF9B-6D27-4E9C-8CD3-CF6E4FF96FF9%7D/s_2020_840.pdf).

<sup>14</sup> United Nations Security Council, “Report of the Panel of Experts (2020),” 11.

<sup>15</sup> Michael Richardson, “Crimes under Flags of Convenience,” *Yale Global Online*, 19 May 2003, <https://yaleglobal.yale.edu/content/crimes-under-flags-of-convenience>, accessed on 10 January 2021.

<sup>16</sup> David Albright, et al., “56 Countries Involved in Violating UNSC Resolutions on North Korea during the Last Reporting Period,” Institute for Science and International Security, 6 June 2019, 14, accessed on 11 January 2021, [https://isis-online.org/uploads/isis-reports/documents/DPRK\\_Report\\_June\\_6,\\_2019\\_Final.pdf](https://isis-online.org/uploads/isis-reports/documents/DPRK_Report_June_6,_2019_Final.pdf).

<sup>17</sup> Kasoulides, “The 1986 United Nations Convention,” 543; Shaughnessy and Tobin, “Flags of Inconvenience,” 1-2.

<sup>18</sup> Kasoulides, “The 1986 United Nations Convention,” 548-49; Shaughnessy and Tobin, “Flags of Inconvenience,” 7.

<sup>19</sup> Tamo Zwinge, “Duties of Flag States to Implement and Enforce International Standards and Regulations – And Measures to Counter Their Failure to Do So,” *Journal of International Business and Law* 10, no. 2 (2011): 299-300.

<sup>20</sup> Kasoulides, “The 1986 United Nations Convention,” 543, 548.

the flag State by the owners, crew, or location of operation.<sup>21</sup> In return, the flag of convenience receives a revenue source, which can be significant.<sup>22</sup> For example, Panama, the world's largest registry, receives \$500 million in annual "fees, services, and taxes" from its registry.<sup>23</sup>

This creates an incentive for flag States to compete for ship registration revenue, which in turn encourages weaken standards and oversight to attract ship owners.<sup>24</sup> For legitimate owners, like merchant ships, these registries reduce costs through low taxes and business-friendly policies, especially related to labor costs.<sup>25</sup> But these registries also offer less transparency over ship ownership by combining limited disclosure of ownership in the registration processes with other laws that shield banking, finance, and businesses from foreign scrutiny.<sup>26</sup> Most troubling for transnational challenges, like sanctions enforcement, flags of convenience help ship owners and operators evade accountability for criminal activity through lax enforcement and oversight.<sup>27</sup>

The problem of ships registering in more lenient countries to skirt criminal prohibitions is as old as the law of the sea.<sup>28</sup> But the trend is getting worse.<sup>29</sup> Today, international maritime governance interests have increased in complexity and implicate a range of issues, like vessel safety, pollution prevention, port security, sustainable fishing, and transnational crime.<sup>30</sup>

Addressing these concerns imposes restraints on ship owners, which in turn, encourages ships to seek out less stringent flag States. Today, ship owners have even greater access to a multitude of

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<sup>21</sup> Kasoulides, 548.

<sup>22</sup> Kasoulides, 546; United Nations Conference on Trade and Development, *Review of Maritime Transport (2015)*, (Geneva: UNCTAD, 15 October 2015): 41, accessed on 10 January 2021, <https://unctad.org/webflyer/review-maritime-transport-2015>; Shaughnessy and Tobin, "Flags of Inconvenience," 2.

<sup>23</sup> BBC News, "Why So Many Shipowners Find Panama's Flag Convenient," 5 August 2014, accessed on 12 January 2021, <https://www.bbc.com/news/world-latin-america-28558480>.

<sup>24</sup> Gohar A. Petrossian, et al., "Flags for sale: An empirical assessment of flag of convenience desirability to foreign vessels." *Marine Policy* 116 (2020): 2, <https://doi.org/10.1016/j.marpol.2020.103937>.

<sup>25</sup> Economist, "Follow the Flag of Convenience," Vol. 342, 8005, 22 February 1997, 75-76, ProQuest; Jessica Ford and Chris Wilcox, "Shedding light on the dark side of maritime trade – A new approach for identifying countries as flags of convenience," *Marine Policy* 99 (2019): 298. <https://doi.org/10.1016/j.marpol.2018.10.026>.

<sup>26</sup> Gianni, "Real and Present Danger," 19-20.

<sup>27</sup> Ford and Wilcox, "Shedding light," 298; Economist, "Follow the Flag of Convenience," 75.

<sup>28</sup> Shaughnessy and Tobin, "Flags of Inconvenience," 7; Kasoulides, "The 1986 United Nations Convention," 544.

<sup>29</sup> Kasoulides, "The 1986 United Nations Convention," 544; Economist, "Follow the Flag of Convenience," 76.

<sup>30</sup> Ford and Wilcox, "Shedding light," 298.

flag of convenience registries, which now register more than 70% of the global, commercial fleet.<sup>31</sup>

### **FLAGS OF CONVENIENCE HELP CIRCUMVENT SANCTIONS**

The U.N. Panel of Experts overseeing the North Korea sanctions identified illicit transfers by “foreign-flagged vessels using flags of convenience” as the “primary method of sanctions evasion.”<sup>32</sup> This reflects a common theme across a range of transnational problems, like smuggling, pollution, and illegal fishing, where flags of convenience fail to effectively control the conduct of registered ships.<sup>33</sup> Relying solely on enforcement by flag States invites evasion through the use of flags of convenience.<sup>34</sup>

Flags of convenience help North Korea evade sanctions in three ways. First, these countries simply fail to investigate and enforce violations. In several instances, flags of convenience, like Sierra Leone and Equatorial Guinea, ignored U.N. inquiries about ships engaged in illicit trade.<sup>35</sup> Others, like Panama, simply de-registered ships after receiving information about a violation without further consequence to the owners or crew.<sup>36</sup> Once de-registered, ships can easily register in a new flag of convenience and continue their illicit voyages. As a result, the lack of enforcement interest by flags of convenience creates a practical safe haven for illicit activity because ship owners realize the low likelihood of criminal or civil consequences.

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<sup>31</sup> Ford and Wilcox, 298.

<sup>32</sup> United Nations Security Council. “Report of the Panel of Experts Established Pursuant to Resolution 1874 (2009).” S/2019/171 (March 5, 2019): 7, accessed on 25 November 2020, [https://www.securitycouncilreport.org/atf/cf/%7B65BFCF9B-6D27-4E9C-8CD3-CF6E4FF96FF9%7D/s\\_2019\\_171.pdf](https://www.securitycouncilreport.org/atf/cf/%7B65BFCF9B-6D27-4E9C-8CD3-CF6E4FF96FF9%7D/s_2019_171.pdf).

<sup>33</sup> Gianni, “Real and Present Danger,” 9-12; Ford and Wilcox, “Shedding light,” 298.

<sup>34</sup> Albright, et al., “56 Countries Involved in Violating UNSC Resolutions,” 16.

<sup>35</sup> United Nations Security Council, “Report of the Panel of Experts (2020),” 13; United Nations Security Council, “Report of the Panel of Experts (2019),” 12.

<sup>36</sup> United Nations Security Council, “Report of the Panel of Experts (2020),” 21.

Second, weak registry standards and a lack of transparency help malicious actors, like North Korea, obscure illicit activity and frustrate enforcement efforts. Registration in a flag of convenience can be as simple as completing a form, paying a fee, and raising a new flag of sovereign protection. Weak registry standards in these nations obscure the identity of individuals accountable for the ship's voyage and activity by not requiring disclosure of ship owners and allowing registration through complex, corporate structures.<sup>37</sup> This ease of access and lack of transparency makes it impossible to investigate illicit activity and impose accountability.<sup>38</sup> As a result, North Korea seeks out flag of convenience registries for "increasingly complex" transfer schemes that use multi-layered corporate shells to hide its involvement and hinder enforcement.<sup>39</sup>

Third, flags of convenience exercise poor control over their registries making them more prone to fraudulent use. The profit motive that underlies a flag of convenience registry results in little oversight over the registry itself.<sup>40</sup> Many also outsource operation of the registry to private, overseas companies, further removing these registries from oversight by government authorities.<sup>41</sup> The lack of control over the registry makes these countries attractive options for fraudulent use by malicious actors, like North Korea.<sup>42</sup> For example, in 2019, North Korea disguised one of its ships by changing its name, homeport, and registry information to match a Sierra Leone registered ship.<sup>43</sup> A weak registry, like Sierra Leone, is less likely to identify the fraudulent use, cooperate with international partners, or take enforcement action to protect its registry.

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<sup>37</sup> Gianni, "Real and Present Danger," 19-20.

<sup>38</sup> United Nations Security Council, "Report of the Panel of Experts (2020)," 25.

<sup>39</sup> Albright, et al., "56 Countries Involved in Violating UNSC Resolutions," 20.

<sup>40</sup> BBC News, "Why So Many Shipowners Find Panama's Flag Convenient."

<sup>41</sup> Michael B. Krakat, "The Many Parallels of CBI and Flags of Convenience," Investment Immigration Insider, 14 October 2020, accessed on 24 January 2021, <https://www.imidaily.com/analysis/the-many-parallels-of-cbi-and-maritime-flags-of-convenience/>.

<sup>42</sup> United Nations Security Council, "Report of the Panel of Experts (2019)," 108.

<sup>43</sup> United Nations Security Council, "Report of the Panel of Experts (2019)," 108.

## MEASURES TO CURB FLAGS OF CONVENIENCE

The United States can improve maritime sanctions, and strengthen maritime governance across a range of transnational threats, by taking steps to curtail the use of flags of convenience by illicit actors. First, the United States can support more stringent ship registration standards, like those in the proposed United Nations Convention on Conditions for the Registration of Ships.<sup>44</sup> That proposal requires that flag States identify ship owners for improved accountability and require a nationality connection between the flag State and the owners or crew.<sup>45</sup> These standards would reduce the current ease of foreign registration by limiting the registries available to foreign ship owners, improve transparency for investigation and accountability, and encourage flag States to exercise greater oversight because of the stronger citizenship connection to the ship.<sup>46</sup>

Second, the United States should use diplomatic and economic tools to change the incentive structure for smaller flag of convenience registries, like Sierra Leone, Togo, and Tanzania. For example, ships once widely used Cambodia's flag of convenience in support of a number of illicit activities, including smuggling, illegal fishing, human trafficking, and North Korea sanctions violations.<sup>47</sup> Facing "pressure from the European Union" and "international scrutiny" from these links to illicit activity, Cambodia closed its registry to foreign ships in 2016.<sup>48</sup> The United States can work with partners and allies to alter the incentive structure for smaller registries by providing incentives or imposing costs. Measures could include: foreign aid

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<sup>44</sup> Kasoulides, "The 1986 United Nations Convention," 559.

<sup>45</sup> United Nations Conference on Trade and Development, "United Nations Convention on Conditions for Registration of Ships," (February 7, 1986): Articles 5-9, accessed on 10 January 2021, [https://unctad.org/system/files/official-document/tdrsconf23\\_en.pdf](https://unctad.org/system/files/official-document/tdrsconf23_en.pdf).

<sup>46</sup> Kasoulides, "The 1986 United Nations Convention," 554-56.

<sup>47</sup> Kali Kotoski, "Flag of Convenience Scheme Retired," *Phnom Penh Post*, 1 September 2016, accessed 24 January 2021, <https://www.phnompenhpost.com/business/flag-convenience-scheme-retired>.

<sup>48</sup> Kotoski.

conditioned on registry action; development assistance to build oversight and enforcement capacity; barring imports or port entry by weak registry ships; or sanctioning financial transactions tied to the flag of convenience's registry system. Sufficient inducement or pressure could lead smaller registries to reconsider their flag of convenience status, and close or take enforcement obligations more seriously.

For larger registries, the United States can develop cooperative agreements for at-sea sanctions enforcement; a model used for a number of transnational threats like illegal fishing, drug smuggling, and counter-proliferation. For example, the United States and major registries, like Panama and Liberia, have cooperative agreements to inspect ships suspected of trafficking weapons of mass destruction.<sup>49</sup> The United States build on established cooperative relationships and expand existing agreements to include sanctions enforcement. The United States can develop new agreements with other registries where the size or strategic relationship makes diplomatic and economic pressure inappropriate. Cooperative agreements would lead many illicit actors to move to a new registry because of the increased risk of accountable enforcement action. For those that continued their illicit activity, sanctions enforcement agreements would provide a practical means to curtail illicit activity through at-sea inspection, seizures of banned goods, and other enforcement action.

Finally, the United States should encourage the U.N. Security Council to authorize at-sea inspection and seizure of prohibited goods by the international community. The Security Council can change international law, including the law of the sea's traditional exclusive jurisdiction of flag States.<sup>50</sup> It has done so in other sanction regimes. For example, the Security Council

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<sup>49</sup> U.S. Department of State, "Signing of the U.S.-Panama Ship Boarding Agreement to Support the Proliferation Security Initiative (PSI)." 12 May 2004, accessed on 25 January 2021, <https://2001-2009.state.gov/t/us/rm/32413.htm>; Milan Vesely, "Liberia's Flag of 'Inconvenience'," *African Business*, April 2004, 24, ProQuest.

<sup>50</sup> Arms Control Association, "UN Security Council Resolutions on North Korea"; Devon Whittle, "The Limits of Legality and the United Nations Security Council: Applying the Extra-Legal Measures Model to Chapter VII

allowed the international community to enforce bans on charcoal exports from Somalia without requiring approval from the flag State.<sup>51</sup> The continuing inaction by flags of convenience highlights the need for expanding authority to other nations to inspect and enforce sanctions.

## COUNTERARGUMENT

A proposed U.N. resolution to authorize international enforcement of illicit maritime smuggling would likely be blocked by Russia and China. Both countries reportedly aid North Korea with “sanctions evasion assistance,” and harbor nationals and business entities that frequently violate a range of sanctions prohibitions.<sup>52</sup> Reflecting this complicit support, the current North Korea sanctions have been “watered down” to avoid vetoes from these two permanent members of the U.N. Security Council.<sup>53</sup> Weaker sanctions support strategic interests in Russia and China by reducing risks of a North Korea regime collapse and preventing foreign enforcement against their nationals.<sup>54</sup>

The threat of a veto in the Security Council should not dissuade the United States from incremental steps to address the harm caused by flags of convenience. First, cooperative engagement to strengthen registry procedures and bilateral measures for at-sea enforcement with key flags of convenience would not be impacted by China or Russia non-cooperation. Second, the United States can work to normalize the importance of at-sea enforcement of U.N. sanctions in other sanctions regimes with less direct threat to Chinese and Russian interests. Including provisions for at-sea enforcement, regardless of a ship’s flag, in future sanctions would build

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Action,” *The European Journal of International Law* 26, no. 3. (2015), 672, <https://academic.oup.com/ejil/article/26/3/671/2599590>.

<sup>51</sup> United Nations Security Council, “Resolution 2182,” S/RES/2182 (2014), 6, accessed on 12 January 2021, [https://www.securitycouncilreport.org/atf/cf/%7B65BF9B-6D27-4E9C-8CD3CF6E4FF96FF9%7D/S\\_res\\_2182.pdf](https://www.securitycouncilreport.org/atf/cf/%7B65BF9B-6D27-4E9C-8CD3CF6E4FF96FF9%7D/S_res_2182.pdf).

<sup>52</sup> Albright, et al., “56 Countries Involved in Violating UNSC Resolutions,” 2.

<sup>53</sup> Albert, “What to Know About Sanctions.”

<sup>54</sup> Albert, “What to Know About Sanctions.”

international support around the idea that maritime transportation bans require implementation with concrete action at-sea. Third, the United States can initially target specific flags of convenience in a way that avoids directly challenging interests of Russia or China. For example, improved sanctions could authorize international inspections on ships registered in specific countries other than China or Russia, linked to repeat violations non-responsiveness to U.N. inquiries, like Sierra Leone or Equatorial Guinea.<sup>55</sup>

## CONCLUSION

The international community, often led by the United States, uses sanctions against maritime transportation to address a number of global security challenges, including proliferation, regional instability, and terrorism. Increasingly global security threats make future sanctions likely in this inter-connected world. To remain a viable measure in the United States' foreign policy toolkit, sanctions cannot rely on flag States alone for effective at-sea enforcement. Otherwise, the inherent incentives in the law of the sea will facilitate evasion through flags of convenience.

The United States needs a multi-layered approach to address the undermining effect of flags of convenience on global security challenges, like sanctions enforcement. Building international support for standardizing ship registration and improving transparency will facilitate greater enforcement and make individuals accountable for a ship's illicit activities. Diplomatic and economic tools can alter the incentive structure and pressure flags of convenience to take greater enforcement action. Finally, measures for international enforcement, taken in cooperation with flag States or at the direction of the U.N. Security Council, can provide the at-sea enforcement required to implement any international ban. Although some countries,

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<sup>55</sup> United Nations Security Council, "Report of the Panel of Experts (2020)," 13.

particularly Russia and China, may resist, the United States can build international support among partners and allies for the need to challenge the harmful effects of flags of convenience. These steps would strengthen North Korea sanctions, create a more effective template for future sanctions regimes, and strengthen maritime governance across a range of transnational threats.

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