# REPUBLIC OF KOREA

## TRADE SUMMARY

In 2000, the U.S. trade deficit with Korea totaled $12.4 billion, an increase of $4.1 billion from the $8.3 billion trade deficit in 1999. In 2000, Korea was the United States' sixth largest export market. In 2000, two-way merchandise trade between the United States and Korea reached record levels, totaling $68.2 billion, compared with $54.3 billion for 1999. U.S. exports to Korea in 2000 were nearly $27.9 billion, a 21.6-percent increase from the 1999 figure of $23 billion. U.S. imports from Korea in 2000 were $40.3 billion, a 28.9-percent increase from the 1999 figure of $31.3 billion.

U.S. exports of private commercial services (i.e., excluding military and government) to Korea were $5.3 billion in 1999, and U.S. imports were $4.5 billion. Sales of services in Korea by majority U.S.-owned affiliates were $1.1 billion in 1998, while sales of services in the United States by majority Korean-owned firms were $379 million.

The stock of U.S. foreign direct investment in Korea in 1999, the most recent available data, was $8.7 billion, an 18.3-percent increase from 1998. U.S. foreign direct investment is mainly concentrated in manufacturing, banking, and petroleum.

## OVERVIEW

Korean global imports grew rapidly in 2000, jumping 34 percent to $160.5 billion. Exports increased 20.1 percent to $172.6 billion. Korea's global trade surplus narrowed from $24.5 billion in 1999 to $12.1 billion in 2000. In 2001, Korea's trade surplus is expected to narrow slightly to $10 billion.

The Korean economy grew by more than 9 percent in 2000. Inflation remained at moderate levels, although the unemployment rate has been growing and is likely to surpass 4 percent this year. Korea has taken some steps to create a more open, market-oriented economy by breaking unhealthy linkages between government, banks, and *chaebol* (conglomerates). These linkages have impeded competition and market access in Korea and resulted in excessive debt, over-capacity and uneconomic investments. However, political considerations and the Korean economy's initial recovery from the financial crisis have slowed momentum toward reform. Moreover, the Korean Government's extensive involvement in the financial sector, which expanded as many commercial banks were recapitalized with public funds during the financial crisis, has created additional impediments to progress toward a more market-based economy.

## IMPORT POLICIES

### Tariffs and Taxes

Korea bound 91.7 percent of its tariff line items in the Uruguay Round negotiations, and in 2000, Korea's average tariff rate was 8.9 percent. Korea's tariffs on all agricultural products, except rice (HS 1006), are bound, while tariffs on forestry and fishery products remain unbound. Between 1995 and 2004, Korea will lower duties on more than 30 agricultural products of primary interest to U.S. exporters. These products include intermediate- and high-value items, such as vegetable oils and meals, processed potatoes, mixed feeds, feed corn, wheat, fruits, nuts, popcorn, frozen french fries and breakfast cereals.

Under its Uruguay Round commitments, Korea also established tariff-rate quotas (TRQs) intended to either provide minimum access to a previously closed market or maintain pre-Uruguay Round access. (See also "Quantitative Restrictions, TRQs and Import Licensing.") In-quota tariff rates are zero or very low, but over-quota tariff rates on some products are prohibitive. Specifically, natural and artificial honey are assigned an over-quota rate of 253.8 percent; skim and whole milk powder 193.6 percent; barley 340 percent; barley malt 281 percent; potatoes and potato preparations more than 317.6 percent; and popcorn 658 percent.

Duties are still very high on many high-value agricultural and fishery products. Korea imposes tariff rates above 40 percent on many products of interest to U.S. suppliers, including shelled walnuts, table grapes, beef, canned peaches and fruit cocktail, pears and a variety of citrus fruits. Products subject to 30 percent or higher tariff rates include certain meats, most fruits and nuts, many fresh vegetables, starches, peanuts and peanut butter, soups, various vegetable oils, juices, jams, beer and some distilled spirits and dairy products.

By 2004, Korea will reduce bound tariffs to zero on most or all products in the following sectors: paper, toys, steel, furniture, semiconductors and farm equipment. Korea is harmonizing its chemical tariffs to final rates of 0, 5.5 or 6.5 percent, depending on the product. From pre-Uruguay Round levels, tariffs on scientific equipment are being reduced 65 percent. On textile and apparel products, Korea has harmonized and bound most of its tariffs to the following levels: 7.5 percent for man-made fibers, 15 percent for yarns, 30 percent for fabrics and made-up goods and 35 percent for apparel.

Korea uses “adjustment tariffs” to boost its applied tariff rates in order to protect domestic producers, an issue about which the U.S. Government has expressed concern to the Korean Government. In 1997, Korea agreed as a condition of its IMF stabilization package to reduce the number of products subject to tariff adjustments. In 2001, however, Korea renewed adjustment tariffs on 26 of 27 items that received adjustment tariffs in 2000 (reducing the tariff rates for 10 of these 26 items). Most of the remaining items are agricultural products and seafood, including croaker and skate.

The combination of high tariffs and value-added taxes continues to render a variety of products uncompetitive in Korea. One such product motor vehicles, which are subject to a tariff rate of 8 percent – more than three times the U.S. tariff – as well as multiple taxes levied on top of the tariff. Three of these taxes are based on engine size and have a disproportionate impact on imported vehicles. Although Korea eliminated or reduced some motor vehicle taxes based on commitments it made under the 1998 Memorandum of Understanding Regarding Foreign Motor Vehicles in the Republic of Korea, the combination of the tariff and remaining taxes levied on imported cars still severely impedes their price competitiveness.

## NON-TARIFF MEASURES

### Internal Supports

Korea agreed, as part of the Uruguay Round Agreement on Agriculture, to reduce its domestic support (Aggregate Measurement of Support, or AMS) for agricultural products by 13 percent by 2004. The Korean Government substantially increased the level of domestic support it provided to its cattle industry during 1997 and 1998, thereby raising the overall level of support for agriculture as well. The issue of whether Korea had adequately confined domestic support within the constraints of its WTO reduction commitments on domestic subsidies was raised by the United States and Australia in dispute settlement proceedings in 1999. The outcome of the dispute was inconclusive on this question as the WTO Appellate Body was unable to make a specific finding on the consistency of Korea’s subsidy level with the applicable obligations under the WTO Agreement on Agriculture. Nonetheless, the Appellate Body did conclude that Korea has not been computing the current level of domestic support in a manner compatible with the requirements of the Agreement and the United States will be monitoring Korea’s notification of its AMS to the Committee on Agriculture to ensure that the calculation is now in conformity with Korea’s commitments.

## QUANTITATIVE RESTRICTIONS, TRQs AND IMPORT LICENSING

### Quantitative Restrictions

Pursuant to a U.S.-Korea 1993 Record of Understanding (ROU) and Korea's Uruguay Round commitments, the Korean Government committed to liberalize by January 1, 2001 its quantitative restrictions on eight remaining items subject to balance-of-payments protection. These items consist mainly of live cattle (dairy and beef) and beef products (HS 0201 and 0202). Korea did remove its quantitative restrictions on these items in December 2000, but retained a ban on import of mature cattle (both breeding and feeding stock) that have been vaccinated against brucellosis. The U.S. Government initiated WTO dispute settlement procedures in 1999 to ensure that Korea fulfilled its obligation to remove these balance-of-payment restrictions and more broadly that Korea would adhere to WTO rules in the conduct of its beef import and distribution system. The WTO Panel found in favor of the United States, and, after considering an appeal by Korea, the Appellate Body report affirmed most of the findings of the WTO Panel. (See also "Beef" under the TRQ section.) Korea's quantitative restrictions on rice expire in 2004.

### Tariff-Rate Quotas (TRQs)

Most imported goods no longer require government approval, but some products, mostly agricultural/fishery items, face import restrictions such as quotas or TRQs with prohibitive over-quota tariffs. Korea implements quantitative restrictions through its import licensing system. A government export-import notice lists products that are restricted or prohibited.

The U.S. Government has raised concerns about Korea's administration of quotas on rice and its TRQs on citrus and on unprocessed food grade and value-added soybean and corn products. In some cases, including for onions, potatoes, shelled nuts, garlic, Korea uses an auction to allocate in-quota quantities. Such an allocation system adds costs to the permissible charges foreign firms face in entering the Korean market, raising questions about the WTO-consistency of the system.

Korea continues to restrict imports of value-added soybean and corn products. By aggregating raw and value-added products under the same quota, Korea restricts market access for value-added products, such as corn grits and soy flakes, while allowing entry of only the raw product under the in-quota quantity.

### Beef

Pursuant to a 1989 GATT panel ruling against Korea's measures on beef, Korea committed to phase out its balance-of-payment restrictions on beef. Subsequently, in 1990 and 1993, the United States and Korea concluded exchanges of letters and Records of Understanding (ROUs) under which Korea agreed to annual increases in minimum market access levels for beef imports through 2000. The 1993 agreement also guaranteed direct commercial relations between foreign suppliers and Korean retailers and distributors and provided that a growing volume of beef be sold through that channel instead of through a state trading organization. Australia and New Zealand – the other two major suppliers of beef to Korea – entered into identical agreements with Korea. The U.S. and Korean Governments met periodically to review Korea's implementation of the 1993 agreements. Korea failed to meet its minimum market access commitment on beef in 1997, 1998, and 1999.

Senior U.S. Government officials repeatedly sought Korea's elimination of impediments to the entry and distribution of foreign beef and requested WTO dispute settlement consultations in February 1999. These consultations were unsuccessful and a WTO Dispute Settlement Panel on Korea's beef measures was formed in July 1999. Australia joined the U.S. complaint, and Canada and New Zealand participated as third parties.

The United States' complaint focused on Korea's (1) requirements that imported beef be sold only in specialized imported beef stores; (2) laws and regulations restricting the resale and distribution of imported beef by super-groups, retailers, customers, and end-users; (3) discretionary import regime; (4) imposition of excessive duties on imported beef; and (5) failure to fulfill its reduction commitment for domestic support.

On July 31, 2000, the WTO released its panel report, which concluded that Korea's import regime for beef discriminates against imports from the United States and other foreign suppliers. The panel found that Korea's requirement that imported beef be sold in separate retail stores and the imposition of other restrictions only on imported beef are inconsistent with Korea's obligations under GATT Article III:4 because the requirements result in less favorable treatment for imported beef than is accorded to Korean beef. The panel also concluded that Korea provided domestic subsidies to its cattle industry at levels higher than permitted by its commitments under the WTO *Agreement on Agriculture.* The significant increases in domestic subsidies for Korea's cattle producers in both 1997 and 1998 resulted in Korean beef production at levels that would otherwise have been uneconomical, contributing to reduced opportunities for U.S. beef.

Korea appealed the Panel's finding that the dual store system and Korea's domestic support levels are inconsistent with its WTO obligations. However, on December 11, 2000, the WTO Appellate Body sustained the findings of the Panel regarding the discriminatory nature of Korea's retail distribution system for beef and affirmed the Panel's conclusion that Korea must compute the level of domestic support in accordance with the provisions of the Agreement on Agriculture. The Dispute Settlement Body adopted the findings and recommendations of the Appellate Body at its January 10, 2001 meeting. Korea will be allotted a reasonable period of time to bring the measures in question into compliance with its WTO obligations.

In October 2000, the Korean Government passed a rule of origin setting new residency requirements to go into effect at the beginning of 2001 for animals slaughtered for export to Korea. The Korean Government has stated that the new rule is not a public health or animal health requirement. The U.S. Government raised strong concerns about the new requirement and its likely impact on U.S. beef exports to Korea, which total about $500 million. The Korean Government has agreed to delay implementation for one year and to work with the U.S. Government to find a mutually satisfactory resolution to this issue during this time.

**Rice**

The Korean Government continues to exercise full control over the purchase, distribution and end-use of imported rice. The state trading enterprise that administers the WTO-mandated minimum access program purchases only low-quality Asian rice, as Korean law allows imported rice to be used only for industrial or processing purposes. As a result, high-quality U.S. rice is effectively shut out of the Korean market. Korea repeatedly has stated that it will not allow imported table rice to be marketed directly to Korean consumers, raising questions about whether Korea is in compliance with its WTO obligations. The U.S. Government also is concerned with Korea's recent statements that Korean rice policies are “off the table” in the new WTO agriculture negotiations. The United States will continue to actively engage Korea to ensure its full compliance with its WTO obligations on rice and to press for further liberalization of Korean rice policies.

**Tobacco**

The Korean Government is seeking to privatize its national tobacco company, Korea Tobacco and Ginseng Corporation (KT&G). It will abolish KT&G's monopoly status through amendments to the Tobacco Business Act passed by the National Assembly on March 8, 2001. Subsequent privatization of the company through the sale of the Korean Government's 53-percent stake in the company is expected to be completed by the end of the year. In addition, as of July 1, 2001, the Korean Government is scheduled to: (1) allow investment and manufacturing in this sector by private companies, subject to licensing; and (2) reimpose import duties on manufactured cigarettes of up to 40 percent. Tariffs on cigarettes have been maintained at 0 percent since 1988 as per the terms of the U.S.-Korea Record of Understanding (ROU) Concerning Market Access for Cigarettes, which requires that Korea maintain a 0-percent tariff rate until such time as it allows foreign investment in the manufacture of cigarettes.

The U.S. Government has raised this issue with Korea in an effort to clarify our understanding of the licensing requirements to be imposed as investment criteria as well as any other potential restrictions on foreign investment in this sector. Details on these investment criteria will be included in a presidential decree that will issued within the next several months. The Korean Government has assured the United States that it will put the draft presidential decree out for public comment before its finalization. The United States will continue to follow this issue closely to ensure that these changes do not violate the U.S.-Korea ROU and/or discriminate against U.S. manufacturers, although we will remain cognizant of the right of foreign governments to establish sound public health policies and practices and of the U.S. Government's statutory obligations not to promote tobacco abroad.

**Oranges**

Quotas on fresh oranges were liberalized in July 1997 to permit out-of-quota imports. The in-quota tariff rate will remain 50 percent, and the out-of-quota rate will be set at 64.7 percent in 2001 and lowered to 50 percent in 2004. The in-quota quantity for 2001 is 40,046 metric tons and will be expanded at an annual growth rate of 12.5 percent through 2004.

The Ministry of Agriculture and Forestry (MAF) delegated administration of Korea's citrus tariff-rate quota (TRQ) regime to the Cheju Citrus Cooperative (CCC), a Korean producer group. Allowing the CCC to administer the TRQ raises questions about whether the TRQ is being administered in a non-discriminatory manner. In the past, Cheju has filled the quota with most of the imports coming from the United States. In 1999 and again in 2000, the quota was not filled. In 1999, Korea decided to auction a portion of the quota, despite U.S. protests that such an allocation system adds costs to the permissible border charges facing foreign firms entering the Korean market. In 2000, Korea failed to tender the full quota and ignored the U.S. Government and industry queries on the tendering schedule. The United States will actively engage Korea to ensure its full compliance with its WTO obligations on citrus.

**Import Clearance Procedures**

U.S. suppliers of food and agricultural products, including products for which market access was liberalized under bilateral or multilateral trade agreements, continue to encounter market access barriers in Korean ports despite the steps the Korean Government has taken in this area in the past few years. After WTO dispute settlement consultations with the United States between 1995 and 1999, the Korean Government revised its import clearance procedures by (1) expediting clearance for fresh fruits and vegetables; (2) instituting a new sampling, testing and inspection regime; (3) eliminating some non-science-based phytosanitary requirements; (4) revising the Korean Food and Food Additives Codes, for example, to bring Korean pesticide residue level standards for citrus into conformity with CODEX Alimentarius standards; and (5) requiring ingredient listing by percentage for major, rather than for all, ingredients.

In December 1999, the Ministry of Health and Welfare (MHW) revised the ministerial ordinance of the Food Sanitation Act. This revision changed the food inspection period to two days for document review, three days for organoleptical testing, five days for random testing, and 10 days for laboratory testing. Food products requiring incubation testing are held up to 18 days.

In 2000, the Korea Food and Drug Administration (KFDA) revised the Food Code, the Food Additives Code, and the Labeling Standards for Food, addressing many of U.S. industry's concerns, such as the elimination of mandatory Korean-language labeling of product type for most products and excessive restrictions on food. Additional work is needed to bring Korea's food code standards up to international standards, however, specifically those standards related to food additives *(e.g.*, Korea has not effectively adopted the "generally recognized as safe" standard).

In October 2000, the U.S. Government worked closely with the KFDA and the Ministry of Agriculture and Forestry (MAF) to reassure them that the U.S. Government would help them minimize the risk of importing U.S.-origin food-grade corn and corn-based food products that tested positive for the "Starlink" protein. In late December, KFDA guidance to field inspector helped ease, although not eliminate, port clearance delays caused by confusion over Korea's import requirements regarding Starlink.

Despite the steps the Korean Government has taken in this area over the past couple of years, import clearance of agricultural products at Korean ports remains generally slow, and procedures continue to be arbitrary. Surveys of U.S. trading partners in Asia indicate that import clearance for most agricultural products requires less than three to four days. In Korea, import clearance for new products still typically takes 10 to 18 days, and four to six months if a food additive is not specifically recognized in Korea's Food Code for use in that product. (Any unauthorized additive must go through a formal approval process before it can be approved for use in a particular food).

The Korean Ministry of Agriculture and Forestry (MAF) and its agencies responsible for administering plant, animal and animal product inspection, including the National Plant Quarantine Service and National Veterinary Research and Quarantine Service, account for the greatest delays in import clearance. MAF imposes numerous requirements that restrict access or delay import clearance, such as incubation testing for non-quarantine pests and product detention based on administrative errors on export certificates – which add costs for importers and, ultimately, for consumers.

The United States will continue its dialogue with the Korean Government on import clearance procedures until clearance times in Korean ports are comparable to those in other Asian ports and Korean procedures are based on science and consistent with international trade rules and norms. (See also "Standards and Conformity Assessment Procedures.")

**Customs Procedures**

The Korea Customs Service (KCS) frequently classifies "blended products" under the Harmonized System (HS) heading for the major ingredient of that product rather than the HS heading for the blended product, which has a lower tariff rate. "Blended products" disadvantaged by this practice include potato flakes, soybean flakes, flavored popcorn and peanut butter chips.

KCS's repeated misclassification of potato preparations under the HS heading 1105, which has essentially stopped U.S. exports of these products to Korea. Preparations of potato flour, flakes, granules or pellets should enter Korea under the unrestricted HS 2005 heading, with an applied tariff rate of 20 percent and a bound rate of no more than 31.5 percent in 2004. Instead, KCS has been classifying these products under the more restrictive HS 1105, which is subject to a tariff-rate quota (TRQ) with an in-quota quantity of 60 metric tons and an over-quota tariff in excess of 300 percent. Although the Korean Government agreed in a letter to classify potato preparations according to internationally recognized criteria, they have failed to do so. The U.S. Government will continue to seek resolution of this issue.

U.S. exporters have faced classification issues on other products as well. KCS also recently announced that imported skate and ray, if not accompanied by a government-issued inspection certificate that identifies the fish by its scientific name, will automatically be classified as skate, which is subject to a 50-percent adjustment tariff, and not as ray, which has a 10 percent general tariff. U.S. exports of soda ash also have been misclassified, thus resulting in a higher tariff.

In addition, KCS routinely rejects customs clearance applications on administrative grounds (wrong print, font size, erasure marks on application, etc.), thereby delaying the official start of the customs clearance process. Finally, Korean regulations often require local trade associations to certify or approve import documentation. In addition to requiring the importer to pay a processing fee, which is used to help fund the association, this rule requires importers to submit confidential business information, to which their local competitors then have access.

## STANDARDS, TESTING, LABELING AND CERTIFICATION

### Standards and Conformity Assessment Procedures (Sampling, Inspection, Testing and Certification)

Korea maintains standards and conformity assessment procedures, such as sampling, inspection, testing and certification, that deviate from international norms and appear to have a disproportionate impact on imports.

In September 2000, the Ministry of Agriculture initiated a revision of the Processing Standards and Ingredient Specifications for Livestock Products. Korea notified the WTO but failed to consider comments from major dairy supplying countries in the final revision. Korea explained that it did not incorporate these comments because limited Ministry resources did not allow officials to conduct an adequate review before the Ministry-determined publication date. Comments submitted by major beef supplying countries regarding unscientific restraints on beef storage also were apparently ignored.

In 2000, the Korea Food and Drug Administration (KFDA) revised the Food Code, Food Additive Code, and Labeling Standards to make them more consistent with international standards, but these changes were insufficient to remove many existing trade barriers. The United States has continually expressed concern about the Food Code's prohibition of many ingredients in food and food manufacturing that are generally recognized as safe by international standards. (See also "Import Clearance Procedures.")

Market access for a variety of products continues to be hampered by Korea's certification requirements. Market access for in-shell walnuts has been delayed by Korea's requirement for an extensive pre-clearance inspection program. Market expansion for shelled walnuts is also being held up while Korea considers information documenting the phytosanitary efficacy of the U.S. industry's fumigation program, which has been accepted by other U.S. trading partners worldwide. Access for apples is hindered by Korea's delay in reviewing documentation on pest mitigation provided by the United States. Korea continues to maintain government-mandated shelf-life requirements for items such as bottled water.

Korean Government agencies require pre-approval for pharmaceuticals, chemicals, computers, telecommunications equipment and other products. While many other countries require pre-approval for some products, the range of affected products is exceptionally large in Korea, and companies must submit documentation that is extraordinarily detailed. In the past, information by importers as part of the pre-approval/certification process often was not adequately protected. The Korean Government revised the Pharmaceuticals Affairs Act in July 2000 to allow data submitted for approval/certification be protected upon written request, with disclosure punishable by fine and imprisonment. However, these revisions do not require the Korean Government to protect data when such protection is deemed contrary to the vague assertion of "public interest," the definition of which remains extremely vague (See also "Intellectual Property Rights Protection").

For pharmaceuticals, recent regulatory changes should reduce somewhat the delays companies have typically experienced in obtaining approval from KFDA for the local sale of drugs developed outside of Korea. Specifically, KFDA now permits firms to begin local clinical trials prior to issuance of a Certificate of Free Sale (CFS) by the country of origin. However, local testing requirements are still onerous. The KFDA had made assurance that regulations released in December 1999 would comport with the spirit of the International Conference on Harmonization (ICH) guidelines and, therefore, would render Korea's rules on foreign data and testing more science based. Contrary to the ICH, the regulations fail to include Koreans as members of the general Asian population for drug testing and presumes that drugs are ethnically sensitive unless proven otherwise. Guidelines on this issue for the regulations released in December 2000 fail to make clear when such bridging studies are required.

Finally, Korea has impeded market access for foreign pharmaceuticals by requiring redundant local test data for three lots of imported pharmaceuticals, vaccines and biologics with the dossier for product registration. Moreover, once registered, every lot of the drug imported into Korea for commercial purposes must be tested. The United States will continue to emphasize the need for the Korean Government to implement international guidelines on the acceptance of foreign clinical test data, make the drug approval process for new drugs more science-based and shorten the overall drug approval process in Korea (see also "Intellectual Property Rights Protection" and "Pharmaceuticals").

Korea's motor vehicle standards and certification procedures continue to serve as market access barriers for U.S. and other foreign auto manufacturers. Consistent with the 1998 U.S.-Korea Memorandum of Understanding (MOU) on market access for foreign motor vehicles, Korea has taken steps to simplify and streamline its standards and certification procedures, such as safety compliance thresholds and environmental certification. In October 2000, Korea joined the Global Agreement, an agreement intended to encourage the international harmonization of motor vehicle standards. However, the U.S. Government continues to be concerned about various standards issues in the automotive sector, including: (1) the Korean Government's plan to implement a pass-by-noise standard that does not comply with the 1998 U.S.-Korea MOU on autos; (2) changes to Korea's fuel economy labeling laws; and (3) the potential application of new standards to minivans with the Korean Government's reclassification of minivans as passenger vehicles. The U.S. Government also is closely monitoring the Korean Government's development of a self-certification system, which Korea committed to implementing by 2002.

Under Korea's current system of testing and certification procedures, imported tires are subject to burdensome and lengthy inspection procedures, which can delay entry into the market by up to two weeks. Under its previous system, Korea had recognized U.S. tire importers' self-certification to the U.S. Department of Transportation (DOT) standard. On December 29, 2000, Korea's National Assembly adopted an amendment to the Quality Management Promotion Act, which will become effective on July 1, 2001. Currently under revision, the Presidential decree and Ministerial ordinance to implement the amended Act will be subject to a notice and comment period before implementation. In drafting the implementing regulations, we will urge the Korean Government (1) to exempt from testing requirements products designated with internationally recognized marks, such as the "DOT" mark and (2) to merge the current two-test system into a single test, and (3) to amend the fee structure.

**Labeling Requirements**

U.S. exporters cite Korea's nontransparent and burdensome labeling requirements as barriers to entry, despite recent changes to these requirements. The U.S. Government will continue to express concerns to the Korean Government regarding these issues as well as its non-science based labeling standards.

In July 2000, KFDA revised its food labeling standards to bring Korea's labeling standards more in line with international standards. For example, mandatory Korean-language labeling of product type for most products was eliminated. The new labeling standards is to be implemented after an 18-month grace period. In addition, new packaging and labeling standards for food became effective January 1, 2001. Aimed at protecting the environment, the standards prohibit the use of PVC-shrink wraps. The Ministry of Environment (MOE) addressed U.S. Government concerns about the restricted use of PVC-shrink wrap on some products, including frozen products. The U.S. Government will to monitor implementation of these standards.

In 1999, the Korean National Assembly passed legislation authorizing the Ministry of Agriculture and Forestry (MAF) and the KFDA to label food products enhanced through biotechnology – known as genetically modified organisms (GMOs). MAF has authority for labeling requirements on unprocessed GMOs, while KFDA has authority for the conduct of safety assessments on such products. Proposed labeling standards, which mirror European standards, would become effective in March 2001. MAF's labeling standards would initially apply only to unprocessed corn, soybeans and soybean sprouts, but also would apply to potatoes in March 2002. KFDA labeling standards apply to 27 categories of processed products if made from the above four biotech-produced ingredients. MAF and KFDA labeling standards both have significant flaws – including different tolerance levels for GMO content and no guidance for companies on how to verify GMO content – that leave room for arbitrary and inconsistent interpretations of certification requirements by Korean officials.

**GOVERNMENT PROCUREMENT**

Korea joined the WTO Agreement on Government Procurement (GPA) on January 1, 1997 and agreed to cover procurement of goods and services over specific thresholds by numerous Korean central government agencies, provincial and municipal governments and some two dozen government-invested companies. Korea's GPA coverage currently does not include Korea Telecom's purchases of telecommunications commodity products and network equipment. Procurement of satellites will be included in Korea's coverage beginning on January 1, 2002.

Practices applied by Korea in procurements for construction of the new Inchon International Airport project appear to favor Korean firms over foreign firms. These practices, such as the use of domestic partnering, short deadlines and certain licensing requirements restrict the ability of U.S. and other foreign firms to participate meaningfully in bidding opportunities and to win contracts. In 2000, the WTO Dispute Settlement Body determined that procurements for the Inchon project are not covered by Korea's GPA commitments.

**EXPORT SUBSIDIES**

Korea has aggressively promoted exports through a variety of policy tools, including export subsidies. It has committed to phasing out export subsidy programs that are not permitted under the WTO Agreement on Subsidies and Countervailing Measures. Under its IMF economic stabilization package, Korea eliminated, earlier than originally planned, four WTO-prohibited export subsidies. Korea is rationalizing its overall subsidy regime, including through the notification of 19 programs to the WTO, as required by reporting obligations, and the elimination or reduction of the benefits available in 68 others.

**Government Corporate Refinancing Program**

The Korean Government, through the Korea Development Bank (KDB), has initiated a program aimed at providing direct financial support to several large companies that are encountering severe cash flow problems. The KDB is expected to purchase about $1.2 billion worth of bonds during the first quarter of this year of which about $400 billion represent bonds issued by Hyundai Electronics Industries (HEI). The bonds have a maturity of one year. The Korean Government maintains that the KDB support will terminate at the end of 2001. It also insists that only viable companies will benefit from temporary KDB support, and that HEI and other beneficiaries are getting their financial houses in order now because they will be made to "sink or swim" on their own in 2002.

The U.S. Government has expressed its concern to the Korean about the negative implications of this type of government-directed lending for Korea's restructuring efforts and the Korean economy. The United States has noted that a significant share of the early benefits under this program have been provided to companies that are largely export focused and has raised with Korea its concerns over the potential inconsistency of this intervention with the WTO Agreement on Subsidies and Countervailing Measures. The Administration is currently studying this matter to determine whether additional steps are appropriate.

**INTELLECTUAL PROPERTY RIGHTS PROTECTION**

In spring 2000, Korea was elevated to the Special 301 "priority watch list" as a result of continuing concerns regarding inadequate IPR enforcement, lack of protection for clinical drug test data, lack of full retroactive protection for pre-existing copyrighted works and pharmaceutical patents, problematic amendments to Korea's Copyright Act and Computer Program Protection Act, lack of coordination between Korean health and IPR authorities on drug product approvals for marketing, and continued counterfeiting of consumer products.

In January 2001, the Korean Government passed amendments to the patent, trademark and utility model laws that increased monetary penalties for infringement cases from five years imprisonment and a 50 million won fine to seven years imprisonment and a 100 million won fine. The revisions also generally made it easier to calculate damage amounts in infringement cases.

More specifically, the Patent Act changes both strengthened and streamlined the patent application process. The revision also gave the Korean Industrial Property Office (KIPO) more power to protect technologies exchanged through the Internet. In 2000, KIPO also increased the number of examiners on duty, thus apparently shortening the examination and registration period substantially from 1-2 years to 10 months. Overall, while the patent law is fairly comprehensive and offers protection to most products and technologies, U.S. industry still believes that deficiencies remain in the interpretation of claims and in the treatment of dominant and subservient patents.

Trademark Act changes were made to bring Korea into compliance with the Madrid Protocol on International Registration of Marks (as the country prepares for membership in 2002) and the Ttrademark Law Treaty. The revision also simplified application procedures for international applications and introduced an ex post facto damage compensation system for registrants.

The change in the Design Act permits registration without examination for internationally famous designs.

In December 2000, the Korean National Assembly passed revisions to the Computer Programs Protection Act (CPPA). While the amendments addressed various U.S. Government concerns, including decompilation and protection against circumvention, the United States continues to press the Korean Government to address issues in the CPPA such as "temporary copies" and enforcement-related legislation. There are also concerns regarding the consistency, transparency and effectiveness of Korean anti-piracy enforcement efforts regarding software and other products in the Korean market.

In July 2000, Korea implemented a revised copyright law. However, there are continuing concerns regarding the legislation, including the issue of reproduction in libraries. Korea also apparently still fails to provide full retroactive protection to pre-existing copyrighted works of life plus 50 years, or 50 years from publication, as required under the WTO TRIPS Agreement.

U.S. publishers remain concerned over rampant book piracy in Korea. Despite Korea's new copyright law, the situation faced by U.S. book publishers has continued to deteriorate over the past few years. According to industry, the losses to U.S. publishers inflicted by book piracy in the Korean market in 2000 totaled an estimated $39 million, a 56 percent increase from 1995. Industry also remains concerned that massive piracy continues at universities nationwide through small copy shops serving professors and students alike. The U.S. Government will continue to urge Korea to improve its enforcement against book piracy, including the imposition of deterrent penalties.

Although Korean laws on unfair competition and trade secrets provide some trade secret protection in Korea, these statutes remain deficient. For example, U.S. firms, particularly some manufacturers of chemicals, candy and chocolate, face continuing problems with government regulations requiring submission of very detailed product information, i.e., formulae or blueprints, as part of registration or certification procedures. U.S. firms report that although Korean law forbids the release of business confidential information, submitted information has not been given sufficient protection by government officials and, in some cases, has been made available to Korean competitors or to their trade associations.

The Korean Government has taken steps over the years to remedy data or patent protection problems that affect pharmaceuticals, but problems remain, including the lack of coordination between Korean health and safety (KFDA) and intellectual property (KIPO) officials that result in the granting of marketing approval for products that infringe existing patents. Moreover, it is as yet unclear whether Korea provides protection against unfair commercial use for test data submitted for marketing approval, as required by Article 39.3 of the TRIPS Agreement. Indeed, Korea has been unable to confirm that such protection exists in its legal regime.

The Trademark Act contains provisions for prohibiting the registration of trademarks without the authorization of foreign trademark holders by allowing examiners to reject registrations made in "bad faith." However, the legal procedures that U.S. companies must pursue in order to have infringing trademarks canceled are seen as complex, time-consuming and costly. This has apparently discouraged U.S. companies from pursuing legal remedies to address infringement in Korea. As such, problems still arise with respect to "sleeper" trademark registrations. In January 2000, trademark infringement became a major issue for a dozen U.S. citrus packers who discovered their brands had been secretly registered by a Korean company. The Korean company invoked its brand registration rights to block citrus distribution by the U.S. owner of the trademark. KIPO declined to intervene, noting the legal remedy was through the Korean Court system.

Korea has long been a source of exports of infringing goods. Textile designs generally receive protection under the Korean design law, not copyright law. However, additional protection for textile designs was afforded in the July 1, 2000, revision to the Copyright Act. Protections still remain suspect, however, and some Korean companies allegedly pirate U.S.-copyrighted textile designs and export them to third countries, where they compete with genuine U.S.-produced goods.

In February 2001, Korean President Kim publicly ordered the Ministries of Information and Communications and the Ministry of Justice to strengthen their copyright enforcement efforts. President Kim explicitly tied the success of Korea's domestic software industry to a strong regime for the protection of intellectual property rights. The U.S. Government is encouraged by these actions and will continue to urge Korea to ensure that its enforcement of intellectual property rights protection is non-discriminatory, transparent, and sustained.

## SERVICES BARRIERS

Korea continues to maintain restrictions on some service sectors through a "negative list." In these sectors, foreign investment is prohibited or severely circumscribed through equity or other restrictions. (See also "Investment Barriers.")

### Construction

The construction and engineering markets in Korea were first opened to foreign competition in 1996. Foreign companies may bid on public projects, including the massive capital projects designed to improve basic infrastructure in Korea. Foreign firms still report problems with attempts to renegotiate accepted bid prices, however, as well as with registration and bonding procedures, which are excessively burdensome.

### Advertising

The government-affiliated Korean Broadcasting Advertising Corporation (KOBACO), which has a monopoly over the allocation of television and radio advertising time, launched a new rate system for advertising time in April 2000. The new "Global Standard " system offers advertising air time in various time-lengths and provides more purchasing flexibility in terms of upfront contract requirements, preemptibility, and designation. However, since most advertising contracts are still offered only on a monthly basis, spot buying, although theoretically possible, is rare.

The Korean National Assembly is now considering legislation, the "Broadcasting

Advertising Law," which would end KOBACO's monopoly and allow the creation of a competing media agency whose ownership would include non-government organizations and corporations.

In August 2000, the Korea Advertising Review Board, which includes many members of the Korean advertising industry, took control of advertising censorship procedures from the Korea Broadcasting Committee. The August 2000 amendments to the Broadcasting Law improved censorship procedures but the law still provides considerable discretion, a particular problem given that Korean advertising industry is controlling the censorship process. All television and radio advertising must first be submitted in its final, fully produced form for censorship approval rather than at the "storyboard" stage. The unpredictability of the censorship process considerably increases the risk and costs of developing new advertising campaigns and of introducing new products.

In some product categories, e.g., cosmetics, the Ministry of Health and Welfare (MHW) allows the local manufacturers' association to review advertising copy in advance of airing or publication. The approval guidelines are vague, and the process notifies competitors of future marketing activity, including for new products. The types of advertising campaigns permitted also are circumscribed. For cosmetics and pharmaceuticals, "before and after" demonstrations of product effectiveness are not permitted, nor are direct efficacy claims for pharmaceuticals and over-the-counter medicines or advertising of prescription drugs to the general public.

**Screen Quotas**

Korea maintains screen quotas on imported motion pictures, requiring that domestic films be shown in each cinema a minimum number of days per year (currently, 146 days with reductions to 106 days possible if certain criteria are met). The quota discourages trade, cinema construction, and the expansion of theatrical distribution in Korea. In January 1999, the National Assembly passed a resolution introduced by the Culture and Tourism standing committee that a relaxation of the screen quota should only be considered if and when Korean films achieve a 40-percent market share. In December 2000, a similar resolution was introduced by the Unification and Foreign Affairs and Trade standing committee and passed by the entire Assembly. Reduction of Korea's screen quotas has held up negotiation of the U.S.-Korea Bilateral Investment Treaty.

**Foreign Content Quota for Free Terrestrial TV**

Korea restricts foreign activities in the free TV sector by limiting the percentage of monthly broadcasting time (not to exceed 20 percent) that may be devoted to imported programs. Annual quotas also limit, at a maximum of 75, 70, and 45 percent respectively, broadcast motion pictures, animation and popular music. Foreign investment is not permitted for terrestrial television operations.

**Foreign Content Quota for Cable TV**

Korea restricts foreign activities in the cable TV sector by limiting per channel airtime for most foreign programming to 50 percent. Annual quotas for broadcast motion pictures are set at 70 percent and animation at 60 percent. The Korean Government also restricts foreign ownership of cable television-related system operators and program providers to 33 percent and network operators to 49 percent. For satellite broadcasts, foreign participation is limited to 33 percent.

**Satellite Re-transmission**

The Integrated Broadcast Law mandates that Korean firms that wish to re-broadcast satellite transmissions of foreign programmers must have a contract with the foreign program provider in order to obtain approval from the Korean

Broadcasting Commission (KBC). The Korean Government is currently not requiring that Korean firms pay fees for such transmissions.

**Accounting**

Korea restricts the establishment of foreign accounting firms by requiring that a company be comprised of at least five Korean-certified accountants/partners. Foreign Certified Public Accountants (CPAs) are required to fulfill the same requirements as Korean CPA, including: (1) obtaining Korean certification; (2) completing a two-year internship; and (3) registering with the public accountants association. Any established accounting firm in Korea is prohibited from making an investment in or providing a debt guarantee to any other firm in excess of 25 percent of the accounting firm's paid-in-capital.

**Engineering**

Although there are no restrictions on foreign engineering services specified in Korean law or regulation, procuring agencies (national, local and private) can specify particular conditions and/or requirements for engineers and engineering services depending on the nature of the project. Such specifications can be written to favor domestic engineering services firms. Except in the area of architectural design, the Ministry of Construction and Transportation (MOCT) imposes no requirements that engineering services be provided on a joint venture basis.

**Legal**

At the time of Korea's accession to the OECD in 1996, the Korean Government amended the "Lawyers Act" to permit non-Koreans to be licensed to practice law in Korea, provided that they meet the same criteria that are applied to Korean nationals. The Korean Government also amended the "Regulation on Foreign Investment" in 1997 to allow for foreign investment in the legal sector. Any individual not qualified as a lawyer under Korean law is prohibited from providing legal services to Korean and foreign clients in Korea and from establishing a law firm/office in Korea. There is no provision for "foreign legal consultants" in Korean law, although in practice there are many foreign attorneys in Korea who perform a legal advisory function of sorts.

**Financial**

As a condition of its IMF economic stabilization package, Korea agreed to bind its OECD commitments on financial services market access in the WTO. Korea's revised schedule of WTO financial services commitments entered into force in September 1999. The U.S. Government will continue to work with Korea to ensure that it meets its WTO and OECD financial services commitments and to bring about more liberal treatment of foreign financial services providers.

Foreign-based, non-financial businesses in Korea face burdensome and costly procedural requirement that are inappropriate to Korea's level of development and financial sophistication. For instance, virtually all inter-company transfers are subject to certification, a cumbersome, costly and unnecessary requirement, particularly for transactions between subsidiaries.

**Insurance**

After Japan, Korea is the second largest insurance market in Asia, with $50.4 billion in premiums paid in the fiscal year ending March 31, 2000. The environment for foreign insurance companies has improved considerably since Korea implemented a series of regulatory changes after its 1996 OECD accession. Korea incorporated many of these changes, including expanded market access and national treatment, into the 1997 WTO Financial Services Agreement.

The 1997-98 financial crisis led to a restructuring of the Korean insurance industry. In 1998, the newly established Financial Supervisory Commission (FSC), the Korean Government's financial watchdog and center for financial reform, revoked the licenses or forced the merger of many insurance companies on the grounds of insolvency. In addition, 16 life and non-life insurance companies entered FSC-supervised workout programs. (A workout program is a voluntary, out-of-court debt-restructuring framework, which may or may not involve government oversight.) In 2000, after failing several times to sell Korea Life Insurance to foreign buyers, the Korean Government nationalized it, taking over management control.

The Korean Government is gradually liberalizing foreign entry into the life and non-life insurance markets and has lifted some restrictions on partnering with Korean insurance companies and on hiring Korean insurance professionals. In April 1998, Korea liberalized insurance appraisals and activities ancillary to the management of insurance and pension funds. Korea's brokerage market was opened to foreign firms in April 1998. Several foreign reinsurance firms like Reliance and ARIGA have since entered the market.

**Banking**

In September 2000, the Korean Government commenced the "second round" of bank restructuring. The National Assembly authorized the formation of financial holding companies in October and in December granted authority for the government to spend another 50 trillion Korean won in public funds to recapitalize ailing financial institutions. Unlimited deposit insurance, which had been introduced to shore up confidence in banks during the 1997-98 financial crisis, was revoked on January 1, 2001, and replaced with a per-account limit of 50 million Korean won.

In the aftermath of the economic crisis, the Korean Government injected over 20 trillion won of public funds into most of the commercial banks, effectively nationalizing their management. Currently, three of these banks remain under government management (Seoul, Hanvit, Peace). Under present plans, after injecting 6 trillion won as bank recapitalization, the government will combine five banks (Cheju, Kyongnam, Kwangju, Peace, Hanvit) in a state-run holding company in the first quarter of 2001. The Korean Government also retains significant ownership in Korea First, Korea Exchange, and Chohung Banks. (In January 2000, the Korean Government sold 51 percent of Korea First Bank to Newbridge Capital.) Foreign banks can establish subsidiaries or direct branches. Although foreign investors may legally become majority owners of Korean banks, this has proven to be difficult in practice. In 1998 and 1999, the Korean Government opened the capital markets to foreigners, permitting foreign financial institutions to engage in non-hostile mergers and acquisitions of domestic financial institutions.

Korea continues to restrict the operations of foreign bank branches based on branch capital requirements. These restrictions limit: (1) loans to individual customers; (2) foreign exchange trading; and (3) foreign-bank capital adequacy and liquidity requirements. Foreign banks are subject to the same lending ratios as Korean banks, which require them to allocate a certain share of their loan portfolios to Korean companies other than to the top four *chaebol* and small and medium enterprises.

All banks in Korea continue to suffer from a non-transparent regulatory system and must seek approval before introducing new products and services – an area where foreign banks are most competitive.

On January 1, 2001, the Korean Government further deregulated foreign exchange transactions by easing the Capital Transaction Permission System, thereby providing new opportunities to foreign banks. The April 1999 Foreign Exchange law introduced the first phase of foreign exchange and import-export transaction liberalization.

### Securities

On June 24, 2000, the Korean Government removed limits on local currency issues of stocks and bonds by foreign firms. The Korean Government places no limits on foreign ownership of listed bonds or commercial paper, no longer restricts foreign ownership of securities traded in local markets and has removed almost entirely foreign investment ceilings on Korean stocks. Despite this liberalization, foreign securities firms in Korea continue to face some non-prudential barriers to their operations.

## INVESTMENT BARRIERS

The Kim Government has made a strong commitment to create a more favorable investment climate and to facilitate foreign investment. It removed restrictions on the direct purchase of land by foreigners through the 1998 revision of the Alien Land Registration Acquisition Act. Non-Koreans, however, still cannot produce certain agricultural products for commercial purposes, nor can agriculturally-zoned land be taken out of agricultural production.

The 1998 Foreign Investment Promotion Act: (1) increased the number of business sectors open to foreign investment (currently, four remain fully closed, including inshore fisheries, coastal fisheries, TV and radio stations; and 17 partially closed, to FDI); (2) provided more tax incentives; (3) simplified investment procedures; and (4) established Foreign Investment Zones. The Korean Government must automatically approve a foreign investor's notification unless the activity appears on an explicit "negative list" or is related to national security, the maintenance of public order or the protection of public health, morality or safety. Since May 1998, foreigners have been permitted to engage in hostile takeovers and may purchase 100 percent of a target company's outstanding stock without consent of its board of directors.

Capital market reforms have eliminated or raised ceilings on aggregate foreign equity ownership, on individual foreign ownership and on foreign investment in the government, corporate and special bond markets, and have liberalized foreign purchases of short-term financial instruments issued by corporate and financial institutions. However, the Korean Government still maintains foreign equity restrictions with respect to investments in various state-owned firms and many types of media, schools and beef wholesalers.

The Korean Government has taken several important steps to privatize state-owned corporations. Beginning April 1, 2001, foreign investment limits for Korea Telecom will be increased from 33 percent to 49 percent. In addition, the National Assembly passed legislation in December 2000 that sets the stage for the privatization of KEPCO, the state-owned electric power utility. The government also divested its stakes in Hanjung Heavy Industries.

While the more liberalized Korean investment regime has increased U.S. investor interest in Korea, additional changes, such as enhanced labor-market flexibility, better intellectual property protection, a more transparent regulatory environment, and significant progress on structural reform and market opening would greatly improve Korea's attractiveness as a destination for foreign investment.

## ANTICOMPETITIVE PRACTICES

### Competition Policy

Korea's enforcement of competition policy is generally weak, despite the increased role of the Korea Fair Trade Commission's (KFTC's) role as enforcer of Korea's competition law and advocate of competition policy and corporate restructuring. KFTC's powers to conduct investigations and to impose tougher penalties were enhanced in January 1999 with the revision of the Monopoly Regulation and Fair Trade Act. The Act was subsequently revised in December 2000 to broaden KFTC's authority in corporate and financial restructuring and to raise substantially the administrative fines for violations and for failure to cooperate with KFTC investigations. With its new authority, the KFTC, in December 2000, imposed fines of about $36 million on the "Big Four" *chaebol* for illegal subsidies to affiliated firms**.** In August 2000, the KFTC also fined seven mid-ranking *chaebols* about $14 million for illegally subsidizing affiliates.

Despite KFTC's heightened level of enforcement activity, it still is relatively weak compared to other ministries. For competition policy to take root in Korea, a stronger KFTC is a prerequisite. In addition, the KFTC should more evenly apply the Monopoly Regulation and Fair Trade Law.

**ELECTRONIC COMMERCE**

In March 1995, Korea initiated a project to construct a high-speed information network linking 144 calling zones with broadband fiber optic cables. The expected benefits from such investment include: a more transparent public sector through the realization of e-government, the digitization of traditional industries to make them more value-added, and a greater equity in educational opportunities. Results of this initiative are beginning to take form as Korea has seen a sharp increase in internet usage in the past two years, from just under 11 million in 1999 to about 19 million in 2000. Households with high-speed internet access has risen from just over 50,000 in 1998 to more than 4 million in 2000. Korea ranks among the top countries for internet usage in Asia.

Korea's Electronic Commerce Basic Law and the Electronic Signatures Law went into effect in July 1999. These laws encourage private sector development of electronic commerce and codify authorization of electronic signatures as legally binding on consumers and businesses. Korea stated its intention not to impose customs duties on the flow of information by electronic means in the November 1998 U.S./Korea Joint Statement on Electronic Commerce. In 2000, the Korean Government enacted additional regulations and directives to buttress the 1999 legislation. In 2001, the Electronic Commerce Basic law is expected to be revised to reflect the changes seen in e-commerce since the law's first passage.

Growing dependence on the information and communication infrastructure has led the Korean government to propose the Information Infrastructure Protection Act to combat cyber attacks. The proposed legislation will likely take effect in 2001. Another area of concern for the Korean government is data privacy. They have proposed the Act on Promotion of Utilization of Information and Communication Network and Data Protection to take effect in 2001. The proposed act would require full disclosure to data subjects about how their personal information would be utilized and consent before transferring to a third party. Moreover, data subjects would have the right to access their personal data to make corrections if determined to be inaccurate.

Korea currently has three licensed certificate authorities and uses a full scale public key infrastructure (using digital signature technology) to ensure security, integrity, and consumer confidence on electronic commerce transactions. The U.S. Government has encouraged Korea to allow various types of authentication technologies (not just digital signatures) to be used. The U.S. Government also has urged Korea not to enact laws or regulations that discriminate against electronic authentication methods or providers from other jurisdictions or erect trade barriers to the provision of authentication services by foreign companies. In addition, the United States has encouraged Korea to recognize the importance of flexible private-sector solutions to authentication and certification, and should not require licensing of certification entities.

## OTHER BARRIERS

### Lack of Transparency

The lack of transparency in rulemaking and in Korea's regulatory system continues to hamper foreign firms' ability to compete in the Korean market. Many Korean trade-related laws and regulations lack specificity. Korean officials exercise a great deal of discretion in applying broadly drafted laws and regulations, resulting in inconsistency in their application and uncertainty among businesses. Imported food products remain particularly susceptible to capricious interpretation of ambiguously worded labeling and product categorization standards. Internal guidance, developed by relevant ministries but rarely published, directs their implementation and sometimes the regulations themselves are not made public. In addition, the Korean Government has failed to produce advance or timely notification of planned or actual changes to laws and regulations. While Korea has made progress on transparency issues, *e.g.*, by the Korea Food and Drug Administration (KFDA) in its approach to revamping Korea's Food and Food Additive Codes and labeling standards, additional improvement is necessary.

### Frugality Campaigns and Anti-Import Bias

Frugality campaigns, ostensibly directed at limiting individual consumption, serve to discourage imports. While the Korean Government is no longer directly involved in anti-import campaigns and has taken steps to discourage overt anti-import activity, serious concerns about anti-import biases remain. The legacy from past anti-import campaigns along with Korea's prevalent economic nationalism has proven difficult to overcome. A survey released in February 2001 conducted by an international marketing firm revealed that attitudes toward imported cars have worsened since1999. According to the survey, the main factor driving down import car sales in Korea is social pressure and the negative public image of foreign cars in Korea. The Korean Government has taken action to improve Korean attitudes toward foreign cars, including sponsoring the first-ever Korea Import Motor Show in Seoul, which attracted more than 500,000 people. The Korean Government has agreed to sponsor a one-year joint study by a U.S. and Korean research institutes, to be conducted this year, to gain a better understanding of the benefits the foreign auto industry has brought to Korea, and to educate Korean policymakers and consumers on these issues. While this study is a useful step, the Korean Government will need to take additional active steps in this area.

In August 2000, the National Agricultural Cooperative Federation (NACF), a quasi-government producer group that allocates Ministry of Agriculture (MAF) policy directed loans, participated in a boycott led by Korean farmer associations against goods manufactured by Korean companies that imported citrus. The U.S. Government expressed concern about NACF's role in the boycott given its government links. Farmer associations also approached the Cheju Citrus Cooperative, the administrator of Korea's citrus import quota, regarding importing citrus that the farmers claimed undermined prices of various domestic fruits and vegetables. The Cheju Citrus Cooperative subsequently canceled its last tender for quota citrus, the second year Korea did so. More recently, the Korean Pharmaceutical Manufacturers Association (KPMA) sent a letter to 38,000 Korean doctors and hospitals urging them to prescribe domestic rather than foreign drugs in consideration of the economic difficulties of Korean firms. The Korean Government should make it clear to the KPMA and the public that it does not sanction such letters.

**Motor Vehicles**

On October 20, 1998, the United States and Korea concluded a Memorandum of Understanding (MOU) to improve market access for foreign motor vehicles. Under this MOU, Korea agreed to: (1) to reduce its 80- percent bound tariff rate and bind in the WTO its 8-percent applied tariff rate; (2) lower some of its motor-vehicle-related taxes and to eliminate others through the development of a long-term plan to substantially reduce the tax burden on motor vehicle owners; (3) streamline its standards and certification procedures and adopt a manufacturer-driven self-certification system by 2002; (4) establish a new mortgage mechanism to make it easier to purchase motor vehicles in Korea; and (5) actively and expeditiously address instances of anti-import activity and proactively educate Korean citizens on the benefits of free trade and competition.

The United States and Korea have held three reviews of the MOU since the agreement was signed, most recently in August 2000. Although the Korean Government has implemented the commitments it made on specific tax and tariff issues, the United States expressed its strong concerns about the lack of progress toward the key goals of the agreement, which include: (1) substantially increasing market access for foreign motor vehicles; and (2) establishing conditions so that the Korean motor vehicle sector operates according to market principles. While Korean imports into the U.S. market hit record levels in 2000, more than doubling over the past two years to about 470,000 vehicles or 2.7 percent of the U.S. market, import sales in Korea totaled 4,414 vehicles, representing 0.31 percent of the market. Moreover, the lack of growth of imported vehicles occurred despite the more than 12 percent growth of the overall Korean auto market.

At the last review, the United States also raised concerns about a range of issues, including: (1) continuing anti-import sentiments and negative perceptions that serve as significant barriers to the purchase of a foreign car, including the perception of Korean consumers that there is a link between such a purchase and a Korean Government income tax audit; (2) the lack of a plan to reduce or eliminate engine-displacement-based taxes as Korea committed to do under the MOU; and (3) a range of standards and certification issues, including the Korean Government's plan to implement a pass-by-noise standard that does not comply with the 1998 U.S.-Korea MOU on autos, changes to Korea's fuel economy labeling laws, and the potential application of new standards to minivans with the Korean Government's reclassification of minivans as passenger vehicles. The United States Government requested that the Korean Government keep the U.S. Government and industry apprised of its work to develop a self-certification system for autos, the process for which is underway. The U.S. Government provided Korea with proposals in many of these areas and the two sides are continuing to discuss ways to address U.S. concerns. The United States will continue to urge the Korean Government to take meaningful actions to open this important sector.

The United States and Korea also discussed the lack of meaningful corporate restructuring in the Korean motor vehicle sector. Daewoo Motor, which went bankrupt in July 1999, continues to operate through the goodwill of its creditor banks, many of which are owned by the Korean Government. The U.S. Government will continue to urge Korea to rely on market-based solutions to the restructuring of this and other sectors and will closely monitor Korean actions as they have a direct impact on the ability of U.S. firms to compete in the Korean market.

**Pharmaceuticals**

U.S. concerns on trade in pharmaceuticals with Korea primarily deal with lack of protection of intellectual property rights (IPR), particularly with respect to clinical data and patents. On July 1, 2000, Korea implemented a revised

Pharmaceutical Affairs Act, whereby data submitted to the KFDA can be protected upon the written request of firms. However, U.S. industry remains concerned that the KFDA still will be able to use the originators technical data to support local competitors' product registrations. In essence, the new law does not remedy harm caused by the lack of effective coordination between health and intellectual property authorities and allows products that infringe existing patents to be approved for marketing in Korea.

Korea has taken a number of steps in the past year to improve the business climate in the pharmaceutical sector, including introduction of a new system to reimburse hospital for drugs at "Actual Transaction Prices" system to eliminate the illegal hospital margins that were applied only to domestic drugs. Korea also implemented last fall a new policy separating the responsibilities of prescribing and dispensing between doctors and pharmacists, respectively, to curb abuses in the system and ensure patients obtain the proper medical diagnosis and treatment.

To address the problem of hospitals illegally profiting from prescription drugs by demanding that the drugs be discounted below the reimbursement rate, the Ministry of Health and Welfare (MHW) in late 2000 announced that it would make across-the-board price cuts on all pharmaceuticals. The U.S. Government was encouraged by Korea's efforts to monitor and enforce the ATP system. Nonetheless, both the U.S. Government and industry had concerns about the potential unfairness of such across-the-board cuts, which would have penalized those companies that had not been engaged in illegal price discounting. In response, MHW agreed to revise the plan. Instead, it has provided companies the option of being audited to see if their drugs were being priced at the Actual Transaction Price (ATP) and, after the audit, if illegal discounts were uncovered, prices would be adjusted. While U.S. companies received less than a 5-percent reductions in their ATP, the lack of transparency of the process remains problematic. MHW has been unwilling to provide pharmaceutical companies with access to the audit data or a detailed explanation of the rate cuts. U.S. companies also remain concerned that MHW is grouping drugs that contain the same chemical entity in the audit process, rather than auditing on a product by product basis. The U.S. Government will continue to closely watch how this issue develops.

**Cosmetics**

While there is a positive trend toward self-regulation in this sector, obstacles remain to the entry and distribution of foreign cosmetic products in Korea. Korea has excessive and burdensome testing and import authorization requirements and new packaging requirements that appear to limit the use of outer containers considered vital to the protection, preservation and presentation of cosmetics. Korea established an independent cosmetics law effective July 21, 2000, which separates cosmetics-related provisions out of the existing pharmaceuticals law. The new law categorizes and regulates cosmetics and cosmetic ingredients claiming to have a functional or therapeutic effect and requires companies to label their products as cosmeceuticals. Companies must prove efficacy in order to obtain permission from the Korea Food and Drug Administration (KFDA) to sell their products in Korea.

U.S. industry is concerned about the new law because of its vagueness. The definition in the law is unclear about product categories, when a product should be designated as therapeutic, and the standard that must be met in order to prove efficacy, although the failure to meet the standard is subject to penalty. There are no provisions in the new law to protect proprietary information, which companies may find necessary to submit to prove efficacy. The U.S. Government will continue to urge the Korean Government to work with U.S. and other cosmetic manufacturers to clarify these regulations.

**Steel**

The United States has long been concerned with the Korean Government's extensive involvement in, and support for, Korea's steel sector and its steel-using industries. These policies led to export surges to the United States, especially during the recent Asian economic crisis.

In 2000, the United States continued its bilateral dialogue on steel with Korea, holding working level meetings in May and November. The overall objectives of these consultations continue to be: (1) the end of Korean Government involvement in Korea's steel industry, including complete privatization of POSCO; (2) the market-based restructuring of Korea's steel industry, including finalization of the sale of Hanbo Steel and operation of Hanbo without Korean Government direction or support; and (3) fair trade in steel products.

The government-owned Korea Development Bank (KDB) sold its remaining 6.84 percent of POSCO shares in October 2000. With this sale, the Korean Government asserts that it has completed the privatization of POSCO. Recent reports also indicate that foreign investors now control more than 50 percent of POSCO. However, the Korea Industrial Bank (KIB), of which the Korean Government owns 98 percent, remains the largest single shareholder of POSCO, holding a 4.1 percent stake in POSCO. The U.S. Government continues to urge full privatization of POSCO. In addition, POSCO's size and monopoly producer status in Korea of some key steel products and recent allegations that POSCO refused to supply certain products to all customers continue to raise concerns of possible unfair practices.

In September 2000, a U.S.-led consortium abandoned its bid to purchase Hanbo Steel. Recent press reports indicate that the Korea Asset Management Corporation and other creditors of Hanbo are now prepared to sell individual parts of the Hanbo Company to qualified foreign and domestic purchasers. The U.S. Government will continue to monitor the disposition of Hanbo to ensure that the Korean Government fulfills its assurances that Hanbo will not receive any support and will be sold through a market-based process.

**Telecommunications**

The Korean Government has taken an active role in determining the standards for third generation (3G) wireless services. In 2000, it announced that it would issue three licenses, one for the U.S.-developed cdma-2000 technology, one for the EU-developed W-CDMA technology, and one in which the operator would be free to choose the technology. Three companies submitted qualified bids for licenses using W-CDMA technology and, in December 2000, the top two were awarded licenses (one for the W-CDMA mandated license and one for the free choice license). One company submitted a bid for the cdma-2000 license, but it was judged not qualified. The Korean Government plans to re-tender the cdma-2000 license. The U.S. Government has urged Korea to allow all licensees to choose their own technology.

Korea has accelerated its WTO-agreed schedule for increasing the amount of foreign investment permitted in Korea's telecommunications services operators, including Korea Telecom, but still maintains a 49-percent limit on total foreign investment in any one company and a 10-percent limit on the holdings permitted by any single foreign investor. These restrictions serve to limit the interest of many foreign investors in Korea's telecom services market by making it virtually impossible for foreign investors to have managing control of the companies in Korea.