2013 Knowledge Sharing Program with China

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Knowledge Sharing Program

2013 Knowledge Sharing Program with China:

Sharing Experience of the KFTC on Enforcing Competition Laws and Policies

MINISTRY OF STRATEGY AND FINANCE

KDI Korea Development Institute

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Preface

In the 21st century, knowledge is one of the key determinants of a country's level of socio-economic development. Based on this recognition, Korea's Knowledge Sharing Program (KSP) was launched in 2004 by the Ministry of Strategy and Finance (MOSF) and the Korea Development Institute (KDI).

KSP aims to share Korea's experience and knowledge with the partner countries to achieve mutual prosperity and cooperative partnership. Former high-ranking government officials are directly involved in the policy consultation to share their intimate knowledge of development challenges, and to complement the analytical work of policy experts and specialists who have extensive experience in their fields. The government officials and practitioners effectively pair up with their counterparts in the development partner countries to work jointly on pressing policy challenges and share development knowledge in the process. The program includes policy research, consultation and capacity-building activities, all in all to provide comprehensive and tailor-made assistance to the development partner countries in building a stable foundation and fostering capabilities to pursue self-sustainable growth.

In 2013, policy consultation and capacity building workshop were carried out with 36 partner countries covering over 140 research agendas. As a new partner country, Costa Rica, Belize, China, Russia, Hungary, Egypt were selected in consideration of the country's policy demand, growth potential, and strategic economic partnership.

The 2013 Knowledge Sharing Program with China was carried out with the aim of exchanging socio-economic development experience of two countries for improving China's policy making capacity and achieving her socio-economic development. Under the Cooperation Arrangement, the research and seminars were conducted in order to support the establishment of "Sharing Experience of the KFTC on Enforcing Competition Laws and Policies".

I would like to take this opportunity to express my sincere gratitude to Senior Advisor Dr. Won Joon Kim, Project Manager Dr. Kwangshik Shin, as well as the project consultants including Dr. Jae-hyung Lee, Prof. Hwang Lee, and Prof. Mikyung Yun for their immense efforts in successfully completing the 2013 KSP with China. I am also grateful to Executive Director Dr. Hongtack Chun, Program Director Mr. Taihee Lee, and Program Officer Mr. Daehyun Song, and all members of the Center for International Development, KDI for their hard work and dedication to this program. Lastly, I extend my warmest thanks to the Chinese counterparts, the National Development and Reform Commission for showing active cooperation and great support.

In your hands is the publication of the results of the 2013 KSP with China. I believe that KSP will serve as a valuable opportunity to further elevate mutual economic cooperation of China and Korea to a new level. I sincerely hope the final research results on the selected areas could be fully utilized to support China in achieving economic development goal in the near future.

Joon-Kyung Kim
President
Korea Development Institute

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Chapter 3

The 2013 KSP with China

Daehyun Song (Program Officer, Korea Development Institute)

After adopting the market economy in 1978, China has become the global economic center. In August of 2007, China enacted its antimonopoly law and enforced the law since August of 2008. Although the law applies rigorously, China still has lack of experience in fair trade policies. In September of 2012, the 11th Korea-China Economic Ministerial Meeting was held in Beijing and one of main issues was sharing experience of fair trade competition policies. After the National Development and Reform Commission officially requesting the KSP project, the 2013 KSP with China has launched for the first time.

On April and August of 2013, the KSP team went to Beijing carrying out Demand Survey. The KSP team and the officials from China took into consideration of the relevancy of topics, and the two decided three consultation areas for the 2013 KSP with China. Dr. Gwangshik Shin, adjunct professor of Yonsei University managed the project as project manager and Dr. Won Joon Kim, formal Former Deputy General of Competition Policy Bureau(KFTC)/Acting Secretary General of KFTC, headed the team as senior advisor. Considering experiential and academic specialty, the Korean experts were decided as follows:

Under the cooperative arrangement between Korea and China, the procedure and cooperation had decided. Also, The Korean expert have meetings to discuss each area of consultation and desirable result of the project.

From May 12th to 16th of 2014, the Interim Reporting & Policy Practitioners' Workshop was held in Korea. Director General Sukun Lin of the National Development and Reform Commission (NDRC) headed a group of 6 policy

practitioners and scholars. During the Interim Reporting Seminar, Korean experts and Chinese delegation presented their interim findings and engaged in discussions on future directions and developments of the topics. Indeed, Chinese delegation visited Korea Fair Trade Mediation Agency (KOFAIR), Korea Development Institute (KDI) and Korea Fair Trade Commission (KTFC) to meet Korean practitioners and to share experience in relation to each topic.

For the Final Reporting Workshop, the Korean experts went to Beijing from June 25th to 27th of 2014. The Korean delegation successfully shared the result with scholars and officials from NDRC.

Executive Summary

Kwangshik Shin (Yonsei University)

In 2007, People's Republic of China enacted its antimonopoly law which became effective from August 2008. The National Development and Reform Commission (NDRC), one of three competition agencies in the country, is responsible for enforcing the law against price-related monopolistic practices. As a new competition agency which started to apply the competition law in a fast growing economy, the NDRC faces a challenging task of developing a suitable framework for an effective and efficient enforcement of the law. Experience of other nations with a long history of competition law and policy will be of great help as the NDRC strives to enhance the capacity for effective competition policy.

〈Table 1〉 2013 KSP Topics and Researchers

Sharing Experience of the KFTC on Enforcing Competition Laws and Policies Senior Advisor: Dr. Won Joon Kim Project Manager: Dr. Gwangshik Shin	
Consultation Topics	Researchers
Enhancing Enforcement Capacity of Competition Law to Prevent Abuses of Intellectual Property Rights in the IT Industry	Prof. Hwang Lee (Korea University School of Law)
Regulating Abuse of Administrative Power: The Experience of the Korean Fair Trade Commission	Prof. Mikyung Yun (The Catholic University of Korea)
Economic Analysis for Competition Policy	Dr. Jae-hyung Lee (KDI)

Korea enacted its competition law, the Monopoly Regulation and Fair Trade Act (MRFTA), in 1980. The country now has more than 30 years of experience with competition law and policy. Through these years, the Korea Fair Trade Commission (KFTC), an administrative agency with quasi-judicial authority, has been able to develop and establish sophisticated legal rules and analytical frameworks for dealing with complex competition problems in various markets.

Knowledge of Korea's competition law and policy would be valuable to the NDRC in shaping proper competition rules and strengthening enforcement capabilities. This common understanding led the governments of Korea and China to agree upon doing the Knowledge Sharing Program whereby Korea provides its experience and knowledge to the NDRC on three important topics of competition policy, i.e. abuse of intellectual property rights, abuse of administrative authority and economic analysis for competition policy. The product of this program is likely to gain more significance as the NDRC steps up its enforcement efforts in recent years.

Research on Korea's experience in three areas of interest produces important findings which are likely to be quite relevant for the NDRC in formulating effective competition policy. These major findings are as follows:

1. Enhancing Enforcement Capacity to Prevent Abuse of Intellectual Property Rights in the IT Industry.

The development of the digital economy and the globalization are profoundly changing the marketplace. The nature of competition is changing, and innovation and intellectual property rights (IPRs) play a key role in competitive dynamics in many markets. These changes raise new and difficult problems for competition agencies as they try to make sure that the marketplace works competitively.

In the digital economy, the competitive significance of IPRs and the importance of IP laws are much greater than the old economy. Often IPRs are significant competitive weapons. Accordingly, various competitive issues concerning the use of IPRs begin to emerge, and competition agencies are to counter abusive use of IPRs. But competition law and IP law are not without potential conflicts. With the recent patent wars involving smartphone companies, the interface between the competition law and IPRs has attracted a significant amount of attention. These issues are not specific to advanced economies. They are present in developing economies too.

In Korea, the level of IPR protection and competition law enforcement has been set and coordinated in accordance with the developmental stage of the economy. Up to the late 2000s, the policy emphasis was on providing proper protection to IPRs, and this effort, by stimulating innovation, has contributed to the development of high-tech industries. Only recently did the government begin to use the competition law to business practices involving IPRs.

It is worth noting that KFTC's enforcement actions against abuse of IPRs came with its sustained efforts to build capabilities to discern and analyze IP-related competition issues. The agency has forged close cooperation with other government agencies including Korea Intellectual Property Office and Presidential Council on Intellectual Property. The cooperation effort extended to foreign competition authorities as well as to international organizations. The KFTC also developed its analytical framework for IPR abuse in three guidelines about IPR licensing, and has conducted fact-finding surveys in the pharmaceutical, IT, chemical, and machinery industry in 2010 and 2011.

The MRFTA does not apply to the legitimate exercise of IPRs. The report discusses the meaning of the legitimate exercise by examining the landmark GSK decision in 2014. It also explains in detail three IPR guidelines issued by the KFTC, and introduces important cases on IPR abuses. Guidelines on Unfair Exercise of Intellectual Property Rights set out the enforcement standards in the field of IPRs. Guidelines on Fair Patent License Agreements and Model Operating Standards for Standard-Setting Organizations are sub-guidelines to supplement the Guidelines on the Unfair Exercise of Intellectual Property Rights.

The proper protection of IPRs is vital for economic development. Only abuses of IPRs should be prohibited. Given the inherent complexity of IPR-related competition issues, competition agencies are well advised to build analytical capabilities required to discern IPR abuses correctly before it engages in enforcement actions.

2. Regulating Abuse of Administrative Power

Abuse of administrative power constitutes a significant barrier to competition. This is especially true of a country trying to restructure its state-led economy into a liberalized market economy. With many legal and administrative barriers to competition in place, the scope and efficacy of competition law is inevitably very limited. Reducing such barriers is essential to promote an open and competitive environment of the economy. The priority of such an economy is therefore to reduce state intervention through regulatory reform and privatization, while subjecting SOEs to competition law to ensure competition neutrality.

Countering abuses of administrative power require effective and systematic competition advocacy efforts. In general, competition agencies, which are not beholden to any special interest, are best suited for the role of competition advocacy.

As Korea made its transition from a government-led economy to a more market-based economy during the 1980s, reducing pervasive government regulations such as price controls and entry restrictions became an important competition policy issue. Fully-fledged regulatory reform that began in the 1990s and the wave of privatization and economic restructuring in the aftermath of the Asian financial crisis gave impetus to KFTC's growing role in curbing anticompetitive government actions, including those of state owned enterprises (SOEs) with their looming presence in several important sectors.

The KFTC is mandated under the MRFTA to advocate competition principles within the government. The original MRFTA required government authorities to consult with the KFTC before they take any legislative or administrative measure that is likely to restrain competition. This provision serves as a major vehicle for the KFTC to oppose new regulations that unreasonably suppress competition and to advocate competition principles in the government rule making process. After gaining ministerial status in 1996, the KFTC has issued more opinions, and other ministries have accepted a larger proportion of its opinions. From 1998, the KFTC has played competition advocacy role by pushing its competition assessment opinion in the Regulatory Reform Committee of which the KFTC is a member.

The MRFTA as amended in 1996 further empowers the KFTC to develop and implement plans for enhancing competition in markets where monopolistic structure persists for an extended period of time, and to offer its opinions on regulatory reform measures to relevant government authorities. To perform these tasks, the KFTC regularly publishes a report on industrial concentration and occasionally engages in industry studies. In 2008, for example, the Commission took measures to mitigate impediments to competition identified in air transportation, broadcasting, telecommunication, financial service, and insurance sector. Indeed, deregulation has taken place in many sectors through KFTC's competition advocacy efforts. The KFTC has successfully activated competition in many markets by easing or abolishing regulations that limit entry, pricing, or other competitive behavior. A good example is the enactment of the Omnibus Cartel Repeal Act in 1999, which removed 20 legalized cartels under 18 statutes.

The Korean experience shows that where direct economic intervention by the government is prevalent and reliance on SOEs for industrial development is high, active competition advocacy such as regulatory reform and strong enforcement

of competition law against SOEs are effective in curbing abuses of administrative power. This is not the same thing as promoting indiscriminate deregulation or privatization for privatization sake. There are often more competition friendly ways of achieving the same social policy goals, and accurate, transparent cost accounting of public service obligation of SOEs prevents wasting valuable resources.

The prerequisite for successfully advocating competition principles against anticompetitive governmental measures is the competition agency's superior capacity for analyzing competitive effects and welfare consequences of such measures. Comprehensive analyses of abusive administrative power will increase public awareness of its costs and harm to the economy, thereby expanding public support for the open and competitive market economy.

3. Economic Analysis for Competition Policy

Maximizing overall economic efficiency or consumer welfare is generally accepted as the sole or at least the main purpose of competition law and policy. Because everyone in the economy is a consumer, consumer welfare is often taken to be synonymous with people's welfare or national wealth.

The level of consumer welfare depends on how efficiently a society is utilizing its resources. Social welfare is greatest when scarce resources are used in such a way that people are able to satisfy their wants as fully as technological constraints permit. Two types of efficiency in using scarce resources, allocative efficiency and productive efficiency, make up the overall efficiency. Allocative efficiency is about assigning or allocating available productive forces and materials among the various lines of industry. Productive efficiency refers to the effective coordination of various means of production in each industry into such groupings as will produce the greatest result. These two efficiencies are necessary for static, system-wide efficiency.

Business behavior that creates or enhances monopoly power harms consumer welfare by causing allocative inefficiency, while business behavior that creates productive efficiency increases national wealth and can benefit consumers. Most often, business practices that may cause allocative inefficiency can also give rise to productive efficiency gains. In other words, many kinds of ostensibly anticompetitive conduct may enhance overall efficiency. For example, horizontal mergers, while reducing the number of competitors in the relevant market, often enable the merged entity to realize various forms of efficiencies. Vertical restraints on dealers, while restraining intrabrand competition, may enable the manufacturer to distribute its product more effectively, thereby fostering interbrand competition.

It is therefore inevitable that competition agencies analyze likely competitive effects of a business practice before determining its reasonableness. This task must be guided by sound economic theories and analyses. An understanding of the relationship of business behavior to consumer welfare can be gained only through economic theory. Well-developed economic theory shows how firms can interfere with allocative efficiency, how various business practices can create productive efficiency, and provides the means of comparing gains and losses.

Hence, building the capability of economic analysis is vital for the effective and rational implementation of competition law and policy. This is why advanced competition agencies usually have an in-house economic analysis group of professional economists.

The KFTC has continuously been strengthening its capability of analyzing industrial organization and competition problems in the economy. In this process, the Korea Development Institute, a leading government think tank, has systematically supported the KFTC in developing the country's competition policy by producing and analyzing various data on Korea's industrial organization and concentration, by identifying competition problems in the economy, and by advocating specific policy measures. Its research and policy advocacy efforts heavily influenced the shaping of Korea's competition law and policy.

In response to ever increasing complexities of competition issues in the globalized world, the KFTC has stepped up its efforts to enhance its analytical capabilities. These include, inter alia, establishing an in-house economic analysis team, expanding the involvement of outside experts for case-related economic analyses, recruiting people with a doctoral degree in economics, providing more training and education programs for employees, and offering guidelines for economic analysis. The KFTC now routinely engages in economic analysis in important cases, giving much more weight to economic evidence in its decision.

The KFTC regularly publishes data on industrial concentration and market structure such as CR3 and HHI. This information is very useful in understanding the nation's changing industrial organization and competition problems. The Commission also frequently retains outside experts to conduct in-depth studies on specific industries and industry practices. These studies often provide a useful basis for KFTC's law enforcement and competition advocacy programs.

2013 Knowledge Sharing Program with China:
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Chapter 1

Enhancing Enforcement of Competition Law to Prevent Abuse of IPR in IT Industry

Enhancing Enforcement of Competition Law to Prevent Abuse of IPR in IT Industry

Hwang Lee (Korea University School of Law)

Summary

The economic development of Korea, having reached a certain degree, can largely be attributed to the promotion and protection of intellectual property rights (IPR). After moving past the initial development phase, the input-increase strategy of economic growth reaches its limit and IPR becomes more important to increase productivity. As IPR's significance grows and IPR protection is strengthened, the problems of IPR abuse and overprotection come to the fore and fears that warrant the application of competition law begin to emerge. With recent patent wars involving smartphone companies, the interface between competition law and IPR has attracted significant attention. Those issues are peculiar not only to advanced economies, but also applicable to economic development models that emphasize the role of IPR. The symmetry among economic development, IPR and competition policy can be effectively illustrated in the case of Korea, and the Korean experience has important lessons for developing countries.

In each economic development stage, the level of IPR protection and enforcement of competition law were appropriately adjusted to specific economic needs to promote economic development. Although Korea's MRFTA was promulgated in 1980, its active enforcement in IPR began in the late 2000s, which shows that as the level of IPR protection increases, the need to monitor abuse does, too. Attention to the anti-competitive potential of IPR also grew due to the KFTC action against multinational corporations and global development in the interface

of competition law and IPR law.

The recent involvement of the KFTC in IPR matters was accompanied by continuous efforts toward institution building. The watchdog closely cooperated with other government agencies, including the Korea Intellectual Property Office and Presidential Council on Intellectual Property. The cooperation drive extended to tie-ups with foreign competition authorities and international organizations.

Article 59 of the MRFTA stipulates that the Act does not apply to the legitimate exercise of IPR. This report discusses the meaning of legitimate exercise by examining the landmark GSK case that was decided in 2014. The KFTC adopted three guidelines on IPR licensing and utilized fact-finding surveys in the pharmaceutical (2010), IT (2010), chemical (2011) and machinery (2011) industries.

This report will describe in detail the three guidelines that form an analytic framework for IPR abuse. The most important is Guidelines on the Unfair Exercise of Intellectual Property Rights, which set IPR enforcement standards. Guidelines on Fair Patent License Agreements and Model Operating Standards for Standard-setting Organizations for Voluntary Compliance with the MRFTA are sub-guidelines to supplement Guidelines on the Unfair Exercise of Intellectual Property Rights, and give more predictability to IPR holders and potential licensees. Guidelines on Fair Patent License Agreements are intended as an easy-to-understand reference to help SMEs with limited legal capabilities cope with unfair licensing contracts and the Model Operating Standards for Standard-setting Organizations for Voluntary Compliance, in that they recognize the role of a standard-setting organization in remedying IPR abuse in the context of standard setting, though no special duties were imposed.

This report introduces major KFTC cases against IPR abuse in Korea. Earlier cases involved a licensor requiring a licensee to sign a contract irrelevant to the patent, or denying access to new technology in the context of a public construction bidding that incorporated a patented technology. Significant enforcement action against IPR abuse began with Qualcomm in 2009. The telecom giant charged discriminatively high royalties for using non-Qualcomm modem chips in breach of the FRAND commitment and included clauses requiring royalties even if the patents had expired or were invalidated. The GSK-Dong-A case in 2010 involved a patent settlement including a reverse payment agreement. The SK Telecom case in 2011 was about unfair clauses that required SMEs to continue paying royalties regardless of the validity of an SK patent. In a 2014 case involving Samsung, the KFTC found no abuse of standard essential patent rights. The watchdog applied a willing licensee standard to determine whether an injunction by the holder of the standard essential patent subject to the FRAND commitment was illegal under the MRFTA.

This report draws several lessons from the Korean experience in IPR. First, further development of IPR might be helpful in fostering innovative activities and productivity. Second, IPR abuse needs to be regulated at a certain stage of economic development. Third, the inherent complexity of cracking down on IPR abuse needs careful enforcement to prevent errors and problems. Fourth, well-designed procedures are required for both investigations and hearings to prevent enforcement errors. And fifth, building up of the fair trade watchdog's capacity must be prioritized.

The final section of this report deals briefly with the prospect of regulating IPR abuse in Korea with regard to main issues like non-practicing entities, reverse payment and abuse of standard essential patents. Regulation of the interface between IPR law and competition law are constantly evolving in Korea to meet new challenges and reflect recent developments around the globe.

1. Introduction

1.1. IPR's Pivotal Role in Economic Development and Competition Law's Potential to Curb IPR Abuse

Recent years have seen exploding attention to the interface between competition law and IPR law in the context of patent wars between smartphone companies. Novel issues have arisen, such as cases in which a standard essential patent holder subject to a FRAND commitment seeks injunctive relief or exclusion orders or strategic patent acquisitions aimed at competitors, abusive litigation and patent privateering by non-practicing entities. Along with relatively traditional issues like patent ambush and royalty stacking, these issues have become the new center of debate over how far patents should go and what role competition law must play in fixing perceived flaws in the patent system.

Some view such issues to be applicable only to advanced economies, but this might not be true. The role of IPR is imperative for the success of an economy in transitional periods of development, especially when shifting from an input-increase model to that achieved via productivity increase. In this developmental process, competition law can play an important role by preventing IP holders from taking improper measures to illegitimately expand the scope of IPR and ultimately harm consumer welfare and innovation, which IPR is supposed to promote.

Korea is a rare example that shows the importance of enforcing competition policies in developing an economy. On the other hand, its economic development also heavily depended on active IPR policies. The intersection between the two

policies has drawn a lot of policy interest. In this respect, the Korean experience could hold lessons for many developing countries.

1.2. Global Trend of IPR Abuse Regulation

Most fair trade authorities around the world seem to agree that competition law should take the leading role in regulating IPR abuse, and that at the same time, transparent and foreseeable enforcement is imperative to prevent excessive government intervention from harming innovation. As a result, major jurisdictions have promulgated and enforced IPR guidelines. The U.S. Department of Justice and the Federal Trade Commission have been operating Antitrust Guidelines for the Licensing of Intellectual Property since 1995.[1] The European Commission Directorate General for Competition recently revised the Technology Transfer Block Exemption Regulation[2] and accompanying Technology Transfer Guidelines.[3] Japan Fair Trade Commission promulgated Guidelines for the Use of Intellectual Property under the Anti-Monopoly Act[4] in 2007, through an across-the-board revision of Japan's preceding Guidelines for Regulation of Unfair Trade Practices with respect to the Patent and Know-How Licensing Arrangements of 1989.[5]

Although different in details, competition authorities in major jurisdictions broadly agree on several major points.[6] First, certain conflicts exist over the means to be taken, but the goals of competition law and intellectual property law are considered to be along the same lines and not at odds with each other. Both legal regimes share the common goal of promoting innovation and consumer welfare. Second, determining the illegality of IPR licensing requires balancing of the pro-competitive effects (such as innovation) and the suspected anti-competitive effects. Third, the mere existence of IPR does not in itself confer market power. Fourth, the purpose of the safe harbor provision is to promote technology transfer.

The pendulum of competition law enforcement in IPR has swung over the past century. From the 1930s to 70s, U.S. competition authorities took a hostile

1) U.S. Dept. of Justice and FTC. Antitrust Guideline for the Licensing of Intellectual Property (April 6, 1995).
2) Commission Regulation (EU) No 316/2014 of March 21, 2014, on the application of Article 101(3) of the Treaty on the Functioning of the European Union to categories of technology transfer agreements Text with EEA relevance [2014] OJ L93/17.
3) Guidelines on the application of Article 101 of the Treaty on the Functioning of the European Union to technology transfer agreements [2014] OJ C89/3.
4) Guidelines for the Use of Intellectual Property under the Anti-Monopoly Act (2007).
5) JFTC Guidelines for the Regulation of Unfair Trade Practices with Respect to Patent and Know-How Licensing Arrangements (Feb. 15, 1989; revised in 1999). The first relevant set of JFTC guidelines on IPR was the JFTC Anti-Monopoly Act Guidelines for International Licensing Contracts (May 24, 1968)
6) Sangsup Noh, The Current Status of the Operation of IPR Guideline and Future Tasks, in ICR Law Center, Regulatory Framework for Licensing of Intellectual Property Rights, 2011 ICR Law Center Seminar Series 532-533 (2011); (in Korean)

attitude toward the potential for market power created by IPR protection, which is well exemplified in the "Nine No-nos.[7]" From the 1980s, however, U.S. antitrust authorities took the more permissive view that patents are fully legitimate property rights that are not presumed to create market power and should be subject to the rule-of-reason approach in recognition of its dynamic efficiency. Competition authorities in the EU and Japan followed suit with a slight time lag, and have since moved away from a formalistic and interventionist approach toward one based more on economic effects.

In 21st-century U.S., the pendulum has swung back slightly and recent years have seen a shift in the treatment of patents, which tends to involve a more skeptical evaluation of the strength or quality of a patent.[8] The Actavis decision in 2014 in which the Supreme Court ruled on a pay-for-delay case is considered judicial confirmation of this trend.[9]

Yet the evolution of legal and economic thinking strongly supports deference to IPR in most cases that lack exceptional circumstances, and the enforcement activity of major fair trade authorities including the KFTC are consistent with this global consensus.

1.3. Considerations for Proper Regulations in Accordance with Economic Development

Notwithstanding global trends, developing countries might need a differentiated approach to the patent-competition law interface according to their respective stages of economic development.

A patent right is an exclusive right granted to the patentee for a limited period of time and intended to generate incentives to innovate and encourage patent holders to make public socially beneficial inventions. Hence, there is a potential trade-off between short-term loss of consumer welfare and long-term social benefit. Yet the basic rationale of creating incentives to innovate and general deference to innovation in patent cases might not work well in the situations that developing countries tend to experience.[10] For instance, such countries could lack potential

7) The Nine No-Nos include (i) royalties not reasonably related to sales of the patented products; (ii) restraints on licensees' commerce outside the patent's scope (tie-outs); (iii) requiring the licensee to purchase unpatented materials from the licensor (tie-ins); (iv) mandatory package licensing; (v) requiring the licensee to assign to the patentee patents that may be issued to the licensee after the licensing arrangement is executed (exclusive grant-backs); (vi) licensee veto power over grants of further licenses; (vii) restraints on sales of unpatented products made with a patented process; (viii) post-sale restraints on resale; and (ix) setting minimum prices on resale of the patent products.
8) Alden F. Abbott, The Evolving IP?Antitrust Interface in the USA?the Recent Gradual Weakening of Patent Rights, Journal of Antitrust Enforcement, forthcoming (2014).
9) FTC v Actavis Inc., 133 S. Ct. 2223 (2013).

capital or inventors who can take advantage of innovation incentives, or in certain cases, a domestic investor might not reap the innovation incentives created by the patent system.

Lessons can be drawn from the tendency of IPR protection levels to have a U-shaped correlation to each advanced stage of economic development. One study explained that the initial increase in a country's technological ability has a greater impact on the efficiency of imitating northern technologies than on the efficiency of domestic innovations, making lower-level IPR advantageous for the country. Once technological ability rises above a certain threshold along with advancement in economic development, the innovation effect trumps the imitation effect and the need for better IPR protection rises.[11)]

As the significance of IPR grows and its protection is strengthened, the problems of IPR abuse and overprotection come into the picture, and fears over competition then warrant application of competition law.

1.4. Korea as a Reference for Developing Countries

Korea's history of competition and IPR policy can serve as a reference for developing countries. The nation has a unique past of evolving from a destitute underdeveloped state into an advanced industrial power within a short period of time, thanks to its own efforts. Even given institutional development in association with its socio-cultural development, Korea holds an intermediary position between developed and developing countries. This is even more pronounced when considering that a large portion of the country's recent economic development can be attributed to improved productivity based on increased IPR and an active competition policy. This suggests that productive symmetry among economic development, IPR and competition policy can be effectively illustrated through Korea's case.

So for a country that aims to cultivate an innovation-oriented economy that goes beyond a simple increase in input units, the Korean experience has the potential to fill in the gaps between old systems and fast-growing economies in divergent stages of economic development. The nation might also be a rare case of a developing country that designed and enforced competition policies in coordination with its economic development policies, to considerable success.

10) Thomas K. Cheng, A Developmental Approach to the Patent-Antitrust Interface, 33 Nw. J. Int. L. & Bus. 1 (2012)
11) Yongmin Chen, Thitima Puttitanum, Intellectual Property Rights and Innovation in Developing Countries, 78 J. Dev. Econ. 474, 476 (2005)

2. Development of Economy and Competition & IPR Policies in Korea

2.1. Development of Competition & IPR Policies in Development Stages[12)]

2.1.1. Introduction (1960s to 70s)

Although the Patent Act was introduced in 1946, it remained dormant for a long time. Only in the early 1960s did the Korean government try to make its IPR system effectively work as an ingredient of five-year plans for economic development that officially started in 1962. Following overall revision to the act in 1961, Seoul introduced measures to facilitate catch-up for the Korean economy while promoting an invention-friendly climate. In addition to the Patent Act, the Utility Model Patent System, which grants IPR to inventors of small inventions that do not qualify for patent rights, was extensively utilized. The Employee Invention Compensation System motivated individual inventors. And to stabilize and modernize the patent system, the Patent Attorney Association and the Korean Intellectual Property Office were launched.

Over this period, the scope and degree of IPR protection in Korea were in contrast to that of the 1946 Patent Act, which was modeled after U.S. law. The period of patent protection was shortened from 17 years to 12 years, and foreign patent rights were limited with the intention of protecting domestic industry and developing a stronger technological base. Weak patent protection in this period helped develop indigenous technological capacities by allowing domestic enterprises to imitate advanced foreign technology, while also encouraging minor adaptations and incremental innovations based on foreign inventions.

In this early stage of economic development, Korea pursued an economic policy of export-focused, high-growth development based on strong industrial promotion and trade protection to break away from its underdeveloped state. This policy yielded substantial results against the backdrop of an immature market. Despite these circumstances, no consensus existed on the role or necessity of a competition

12) This chapter summarizes, with minor changes, Jeeyoun Shin, Juyeon Lee, Korea's Intellectual Property Rights System and Its Application to The Phases of Industrial Development: Focusing on The Patent System, KSP Modularization Series 25-30 (2011) and Hwang Lee, Korea's Developmental Experiences in Operating Competition Policies for Lasting Economic Development, 2013 Modularization of Korea's Development Experience (April 2014). See also Keun Lee, Intellectual Property and Economic Development in the Republic of Korea: An Introduction, in World Intellectual Property Organization, The Economics of Intellectual Property in the Republic of Korea, Pub. No. 1031(e), 2012.

policy, and the early form of such a policy before its official introduction in 1980 was mainly utilized as a price control measure.

2.1.2. Rise of Competition & IPR Policies (1980s to mid-1990s)

As Korean companies that were expanding their international market share in knowledge-intensive industries faced growth limitations in relying on simple technology transfers from foreign companies, they began to concentrate greater efforts on R&D. Because of the improved technological capabilities of domestic companies and rise in patent applications, a more advanced IPR system was needed to encourage further technological development in an era of international competition. Hence, Korea began to overhaul its patent system to meet global standards, joining the World Intellectual Property Organization and signing international IP treaties.

Korea's level of IPR protection was substantially heightened to match global standards. Patent protection was extended, and the scope of patentable matter was enlarged to include substance patents. Patent rights protection was further enhanced by incorporating provisions from the WTO/TRIPS in 1995.

As the scale and quality of the Korean economy reached considerable levels by the late 1970s, the limits and side effects of economic development by boosting input and government initiatives began to show. As a result, a more advanced economic model that stressed increased productivity was needed. To overcome these limits and meet political and economic demands, the Monopoly Regulation and Fair Trade Act (MRFTA) was enacted in 1980. In its early stage, the act was not enforced according to its basic purpose of stimulating free market competition, and with the economic policies of developmental economics still leading the way, only partial enforcement was implemented; competition policies primarily concentrated on establishing fair trade practices and alleviating the side effects of industrial policies.

2.1.3. Advancement of Policies (late 1990s to mid-2000s)

The technological innovation capacities of Korean companies reached new highs in the late 1990s, and patent activities showed sound performance domestically and internationally. IPR policies in this advancement period focused on speeding up, streamlining administrative procedures for and improving the quality and efficiency of patent examinations. The e-filing system and three-track examination system (accelerated, regular or customer-deferred) was introduced and the Patent Court was established.

Despite this, the Asian financial crisis that erupted in late 1997 exerted significant influence over the progress of Korea's competition policy. The effort to overcome the crisis led to the adoption of global standards and change in economic policies toward free market principles. As Korea started to participate in and cooperate with international organizations such as the OECD or WTO, demand grew for serious enforcement of competition law based on efficiency and consumer welfare (as opposed to the previous focus on behavioral fairness). Until the mid-2000s, the KFTC tried to move away from intervening in cases considered inherently private and minor, and concentrated its limited resources on cases that would produce the greatest ripple effects on the market. In this process, interest rose in the development of legal enforcement based on economic analyses and advanced legal theories, and the Microsoft case of 2006 was the ultimate result. Through the prosecution of the complex practices of a multinational corporation, the KFTC built the confidence and foundation necessary to pursue subsequent cases involving abuse of market dominance by multinationals such as Intel and Qualcomm.

2.1.4. Spread of Modern Policies to Pursue Advanced Economy (after 2008 Global Financial Crisis to Present)

After the global financial crisis of 2008, Korea faced slowing economic growth and needed a new growth engine to overcome the middle income trap. Korea's focus on manufacturing was deemed no longer reliable to guarantee growth and global competitiveness. Development of an IP-centric industry was identified as the next growth engine. Against this background, the Framework Act on Intellectual Property was enacted in 2011, and a presidential committee on national intellectual property was established for general policy orchestration.

In this period, IPR abuse began to attract the attention of competition authorities, as certain Korean companies became global IT corporations that focused on IPR as their source of competitiveness and foreign multinationals engaged in aggressive licensing tactics.

2.2. Enhancement of IPR Protection in Economic Development Process

While the debate continues over whether different levels of IPR protection have a positive effect on economic growth[13] and the evidence is mixed on this depending on data and methodologies, the Korean experience clearly shows that

13) Some commentators said "there is a growing consensus that stronger IPRs increase economic growth and improve development processes." Keith E. Maskus, Sean M. Dougherty, Andrew Mertha, Intellectual Property Rights and Economic Development in China, in Intellectual Property and Development 297 (World Bank, 2005).

IPR protection contributed to economic development.

Recent research illustrates this correlation with the example of a latecomer playing catch-up.[14)]

In the 1960s and early 70s, Korean companies relied on learning from foreign OEM buyers or through working with foreign direct investment (FDI) companies. Recognizing the limitations of these methods, domestic companies by the mid-1970s turned to technology licensing to learn or get technology transfers from their FDI partners. By the mid-1980s, Korean companies started to establish in-house R&D capacity to outgrow the limitations of technology transfers. Government policy tried to stand alone by mixing up measures to promote public-private R&D consortia, public think tanks, research on existing literature, overseas R&D outposts, co-development contracts with foreign specialists in R&D technology and international M&As.

In the early stages, IPR protection offered little social benefit. With higher technological capabilities and increasing need for technological transfers, however, it became more crucial. Active investment in R&D and the build-up of indigenous R&D capabilities were the result of or coincided with the sudden increase in the level and scope of IPR protection in the mid-1980s.

In sum, IPR played a critical role in Korea's transition from using an input-increase model of economic development to one relying on raising productivity.

2.3. Development Process of IPR Abuse Regulation as Counterbalancing Mechanism

2.3.1. Too early to regulate given low level of IPR protection?

Experts argue that it is too early for Korea to aggressively enforce competition law in the context of IPR because IPR protection is still limited compared to other major jurisdictions. For example, the patent invalidation ratio in Korea is significantly higher than those in the U.S. and Japan.[15)] The level of damages awarded by courts also remains low in Korea.

But strengthened enforcement of competition law cannot be held accountable for the reduction in IPR scope. Rather, it could be considered to promote IPR

14) Keun Lee, Intellectual Property and Economic Development in the Republic of Korea: An Introduction, in The Economics of Intellectual Property in the Republic of Korea (WIPO 2012).
15) Chaho Chung, A Study on the Necessity to Secure Effectiveness of Patent Rights, Report to KIPO (2010). (in Korean)

because competition law shares the common goal of promoting innovation with IPR law. Abusive exercises in IPR that illegitimately extend the scope of IPR and unreasonably hinder follow-up innovation deviate from the basic tenets of IPR protection and could undermine innovation efforts. Thus enforcement of competition law in the context of IPR can help build a competitive marketplace and remove impediments to innovation.

2.3.2. More Focus on Detrimental Effects of IPR Abuse

From the late 2000s, as Korea transitioned into a knowledge-based economy and IPR was recognized as a critical tool for corporate competitiveness, interest rose in the detrimental effects of IPR abuse. As a result, the intersection between competition law and intellectual property law has emerged as one of the most controversial topics among fair trade authorities, practitioners and academics.

The Qualcomm case in 2009 involving the breach of a FRAND commitment by a multinational was a direct example of such a trend.

In a 2009 Task Report to the President of Korea, the KFTC selected the IPR sector as needing tough monitoring. Subsequently, recognizing IPR abuse as a priority in enforcement, the watchdog in 2010 amended its 2000 IPR guidelines. In 2010 and 2011, fact-finding surveys were done in pharmaceuticals, IT, chemicals and machinery. The KFTC also promulgated two sub-guidelines: Guidelines for Fair Patent License Agreements in 2012 and Model Operating Standards for Standard-setting Organizations for Voluntary Compliance with the MRFTA in 2011.

The KFTC's active involvement in IPR abuse cases was clearly affected by global developments in the U.S. and EU, as well as internal demand. But it also shows that a rising level of IPR protection increases the need to monitor abusive behavior.

3. Institutional Aspect of Korean Law in Context of IPR Abuse

3.1. Institution Building of Korea's Fair Trade Commission

The KFTC is the authority in charge of enforcing the MRFTA, which governs IPR abuse. The watchdog is a central governmental agency at the Cabinet level that operates under the umbrella of the Prime Minister's Office. As an independent regulatory body, the KFTC can enforce the MRFTA and related laws while also

functioning as a quasi-legislative organ (as in set legal standards) and quasi-judicial body (as in make decisions that include initial corrective measures to be taken). This structure is similar to that of the U.S. Federal Trade Commission or Japan Fair Trade Commission, but has contrasting aspects to the structure of EU fair trade authorities.

The KFTC has nine top-level executives: the chairman, vice chairman, three standing commissioners and four non-standing commissioners. The Secretariat, with a staff of approximately 500 (as of 2013), supports the commission as a working body. Under the Secretariat are the Administrative Division, Competition Policy Bureau, Consumer Policy Bureau, Anti-Monopoly Bureau, Cartel Investigation Bureau and Corporate Trade Policy Bureau. Among those, the Anti-Monopoly Bureau monitors IPR abuse.

Cases involving the interface between competition law and intellectual property law are considered inherently complex to analyze, and thus require a careful approach to avoid enforcement errors that can negatively affect innovation. Therefore, institution building is considered a key prerequisite in the quest for a balanced approach to the regulation of IPR abuse.

The KFTC's recent involvement in IPR matters did not emerge in a vacuum. Efforts such as consistent arrangement to obtain and foster skilled staff, prioritization and concentration of enforcement resources devoted to IPR investigations, continuous consultations with outside experts and confidence gained from enforcement in cases against multinationals have all substantially contributed to the advancement of competition policies. To deepen its understanding of IPR cases, the KFTC recently hired two patent attorneys to join its corps of experts, including more than 30 attorneys and economists who deal with competition law.

3.2. Cooperation with Other Agencies

3.2.1. Cooperation with Other Government Departments

Given the growing number and importance of cases dealing with the interface between competition law and intellectual property law, close cooperation between authorities responsible for competition and IP is important to ensure proper and coherent enforcement.

The principal authority in charge of administering IP legislation is the Korea Intellectual Property Office (KIPO), an executive agency under the Ministry of Trade, Industry and Energy. KIPO is responsible for the examination and registration of patents, utility models, designs, trademarks and layout designs of semiconductor chips. Also, a tribunal established within KIPO reviews and decides trial cases

involving disputes over eligibility of IP rights registration and the scope and validity of registered IP rights.

The Framework Act on Intellectual Property was enacted in 2011 to ensure unity and consistency of policies on intellectual property that had previously been based on individual statutes. According to this law, the Presidential Council on Intellectual Property (PCIP) was established to devise, review and administer major policies and plans for intellectual property and review and evaluate the progress of such policies and plans. The KFTC chairman is a member of the presidential committee on national intellectual property.

The KFTC has closely cooperated with KIPO and PCIP in developing IPR policy and institutions, but no official cooperation or consultation channel exists for the investigation or review of a case. What is true and important is that the KFTC, when necessary, may consult with KIPO to understand the legal theory underlying a case, the position of a patent authority or global trends related to a case. But as an independent regulator, the KFTC has exclusive authority to determine the facts, illegality of abuse and level of remedies for the IPR cases it pursues, and the watchdog is not subject to external influence.

3.2.2. International Cooperation

To properly tackle issues in licensing practices of multinational corporations, international cooperation is needed with foreign fair trade authorities that share concerns over the potential harm of IPR abuse. The KFTC has proactively cooperated with such authorities through international organizations or bilateral collaboration (with the U.S., EU, Japan or China) to share enforcement experience and data on cases of common interest. This has proven beneficial in improving the quality of regulation.

3.3. Statutory Scheme

The KFTC-governed MRFTA is the law applicable to the illegitimate exercise of IPR.

Article 59 of the MRFTA takes the form of an exemption clause, saying, "The provisions of this Act do not apply to a legitimate exercise of rights under the Copyright Act, the Patent Act, the Utility Models Act, the Design Act or the Trademark Act." This implies that the illegitimate exercise of IPR falls squarely within the ambit of the MRFTA.[16)]

16) Joonbum Kim, Inhye Koh, Important Issues in the Application of Fair Trade Law against The Abuse of Intellectual Property Rights, 150 Journal of Competition 6, 6 (2010). (in Korean)

The KFTC also espouses the view that exercise of IP rights not considered "legitimate" may be subject to investigation and sanctions under the MRFTA. In determining whether an exercise of IP rights is legitimate, the KFTC takes a "rule of reason" approach that requires consideration of (1) whether exercise of an IPR follows the basic purpose of intellectual property laws to promote innovation and development, and (2) what effects such conduct has on market competition and fair trade order.

A debate has lingered over whether the legitimacy of an exercise of IPR should be reviewed from the perspective of IPR law, which means evaluating whether such conduct would be considered a legitimate exercise depends on finding whether it remained within the scope of the IPR, or if such conduct could also be reviewed under liability standards of the MRFTA in addition to the former standard. The KFTC has endorsed the latter position.

In the landmark GSK case decided on February 27, 2014, the Supreme Court held that "conduct deemed not to be a legitimate exercise of the patent right" included conduct that ostensibly seems to be an exercise of patent rights, but in substance departs from the fundamental tenet of the patent system and goes against the institution's essential purpose.[17] The illegitimate exercise of a patent right, the ruling said, should be determined in consideration of the objectives and tenet of the Patent Act, the substance of patent rights, and circumstances including the effects the conduct in question could exert on fair and free competition.

The GSK decision tried to strike a balance between conflicting views. Under general legal principle, the Patent Act takes precedence over the MRFTA because a special law takes precedence over general law; the Patent Act is the special law in this respect. The MRFTA can, however, intervene in exceptional cases where the exercise of the patent right is abnormal and does not contribute to the fundamental purpose of patent protection. In other words, the MRFTA can apply if the exercise of the patent obviously tends to reduce consumer welfare beyond a tolerable degree from the perspective of competition law.

Aside from Article 59 of the MRFTA, Article 32 prohibits international contracts that contain provisions amounting to unfair trade practices, unjust concerted practices or resale price maintenance. Article 33 also allows the filing of a request to the KFTC to review whether an international IPR license contract violates such prohibitions under Article 32. These provisions purport to regulate IPR license contracts with foreign IPR holders. In Korea's earlier stage of economic development, when domestic companies relied on technology transfers from foreign companies, these provisions were intended to give small and mid-

17) Supreme Court 2012du24498, delivered on 27 Feb. 2014 (for the complaint of GSK).

size companies increased bargaining power when negotiating contracts with large foreign licensors. But the benefits from the provisions fell short of initial expectations because of their negative impact on the willingness of licensors to license technologies in high demand. Today, the provisions have outlived their usefulness and no decision has applied Article 32 since 1997. Especially since the extraterritorial application clause was inserted in the MRFTA in 2004, there has been no need for a separate legal basis for applying the MRFTA to international contracts when they affect the domestic market. Only Korea and Japan have a separate regime for international contracts other than extraterritoriality, and this is considered to serve no practical purpose. For these reasons, the KFTC in 2008 repealed its Announcement on the Type and Standard for Unfair Trade Practices in International Contracts. The scheduled repeal of Article 32 and 33 of the MRFTA is also expected to be completed in the first half of 2015.

3.4. Promulgation and Operation of IPR Guidelines

The KFTC adopted three guidelines on IPR licensing. The most significant is Guidelines on the Unfair Exercise of Intellectual Property Rights ("IPR Guidelines"), which were amended in 2010. The revised guidelines contain specific provisions on a wide range of IPR issues, including royalties and licensing, patent pools and cross-licensing, exercise of standard patents, abuse of patent litigation and unfair settlement of patent disputes. The KFTC also has two sub-guidelines: Guidelines on Fair Patent License Agreements released in 2012 and Model Operating Standards for Standard-setting Organizations for Voluntary Compliance with the MRFTA ("SSO Sub-Guidelines") released in 2011.

Unlike U.S. or EC guidelines, the KFTC's IPR guidelines contain no explicit statements like "IP rights are comparable to other forms of property," "IP rights are not presumed to confer market power" or "IP licensing is generally pro-competitive." The KFTC's IPR guidelines, however, are widely considered to share similar views with those of the U.S. in this regard even without explicit announcement.

3.5. Sector-specific, Fact-finding Surveys

The KFTC has utilized fact-finding surveys on IPR abuse in specific industries that have high probability of such abuse. These surveys are a proactive method to assess if a market is well-functioning and useful to detect violations. Such surveys were done in pharmaceuticals (2010), IT (2010), chemicals (2011) and machinery (2011).

Fact-finding surveys can help competition authorities gain a better understanding of industry practices in the exercise of IPR. They can also provide a lead-in to

possible investigations of IPR abuse. The KFTC uncovered the GSK-Dong-A case, which involved a reverse payment, during a survey of the pharmaceutical industry,[18] and the SK Telecom case, in which the patent holder abused its superior bargaining position to extract unfair terms that transferred the risk of patent invalidation to SMEs,[19] during a survey of the telecommunications industry.

4. Analytic Framework for IPR Abuse under KFTC IPR Guidelines

4.1. Guidelines on Unfair Exercise of IPR

4.1.1. Introduction

In 2000, the KFTC issued Guidelines on the Unfair Exercise of Intellectual Property Rights (IPR Guideline). Due to various reasons including lack of enforcement experience and consensus on the need for regulation and limited scope of the legal provisions, this guideline was rarely utilized. To cover new issues raised after 2000 and strengthen the basis for enforcement, a major revision was made in 2010.

The purpose of the new IPR guideline is to increase consistency and predictability in enforcement of the law and promote fair trade practices. It aims to present general principles and detailed criteria for examination of the exercise of IPR (IPR Guideline sec. I.1).

The IPR guideline recognizes that the IPR system and MRFTA share the common goals of encouraging creative business activities and promoting sound development of the economy (IPR Guideline sec. II.1). The understanding is that if reasonable compensation is not given to innovative technology or if a technology is hard to develop and use due to distorted market structure or conduct, a situation could arise that goes against the basic purpose of the IPR system. Therefore, IPR should be legitimately exercised to the extent that it does not distort market competition, while providing an incentive for new technological innovation. Unreasonable impediment to the use of technology and new innovation is contrary to the basic purpose of not only the MRFTA but also the IPR system. In this regard, the IPR guideline allows the MRFTA to help achieve the common goal that the MRFTA and IPR system pursue by regulating conduct that deviates from the basic purpose of the IPR system, while respecting the legitimate exercise of IPR.

18) See Below 5.3.
19) See Below 5.4.

4.1.2. Scope of Application (IPR Guideline sec. I.2)

The IPR guideline shall apply to the exercise of IPR such as patent rights, utility models, designs, trademarks and copyrights. Though the guideline focuses on patent rights that are representative of IPR for the convenience of description, it may be applied by analogy to the exercise of IPR other than patent rights, accounting for the peculiarity of IPR in each case.

The IPR guideline shall apply to the conduct of foreign enterprises made outside Korea if such activity affects the Korean market. The MRFTA expressly adopts the "effects doctrine" about extraterritorial application.

The guideline also provides that even if a certain exercise of IPR is not specifically provided for in the Guidelines, it shall not be excluded from application of the MRFTA.

4.1.3. Basic Principle

Under Article 59 of the MRFTA, the legitimate exercise of rights based on IPR shall not be subject to the MRFTA. Such exercise of rights based on IPR, however, can be subject to the MRFTA if deemed illegitimate (IPR Guideline sec. II.2.A).

Finding whether the exercise of rights based on IPR is legitimate is mainly determined by concluding (1) whether the exercise of the IPR concerned follows the basic purpose of promoting industrial development by protecting and encouraging new inventions, and striving for the use of relevant technology, and (2) the effect the exercise of IPR has on conditions of competition in the relevant market and fair trade order. But finding whether the relevant exercise of IPR violates the MRFTA shall be determined after review of the separate requirements for illegality under relevant provisions (IPR Guideline sec. II.2.B).

If the exercise of IPR results in impeding fair trade[20] and higher efficiency at the same time, finding whether the exercise violates the MRFTA shall be determined, in principle, after balancing both effects. If the effect of increasing efficiency exceeds that of impeding fair trade as a result of the exercise of IPR, the exercise of IPR can be considered a non-violation of the MRFTA (IPR Guideline sec. II.2.C).

But clear evidence and not vague speculation must show that such effects are highly likely to occur (IPR Guideline sec. III.C).

20) The effects of impeding fair trade on the market as a result of the exercise of IPR can be observed in the specific form of either anti-competitiveness or unfairness depending on the type of law violation (IPR Guideline sec. III.B.1).

4.1.4. Specific Criteria for Determining Illegality

In contrast to the provisions in its 2000 version, the latest IPR guidelines have gone beyond providing for specific forms of violations and included considerations and examples.

〈Table 1-1〉 Structure of IPR Guidelines Applied to Specific Violations (Examples)

IPR Guidline sec. III. 3. Exercise of Patent Rights Related to Technical Standards	
(1) Basic Considerations	. . . Generally, the consultation for technical standard selection and exercise of patent rights related thereto create pro-competitive effects in that they promote the use of the relevant technology and contribute to consumer welfare by creating efficiency. But such acts are likely to impede fair trade in the relevant market, including through abuse of the standardization procedure or demanding unfair terms after adoption as the technical standard, and consequently can be deemed going beyond the legitimate scope of patent rights
(2) Applicable Provisions	But whether a certain act violates Article 3-2 (Prohibition of Abuse of Market Dominant Position), Article 19 (Prohibition of Unfair Collaborative Acts), Article 23 (Prohibition of Unfair Trade Practices) and Article 26 (Prohibited Activities of Enterprisers' Organization) of the MRFTA shall be determined by comprehensively considering the separate requirements for illegality set forth in each provision.
(3) Type of Abuse	a. An act of unduly agreeing on certain terms such as price, quantity, territory, opponents and restriction on technological improvement during consultation for technical standard selection; b. An act of unduly refusing to disclose information about the related patent application or registered patents owned by oneself to increase the chance of being selected as the technical standard or avoid prior consultation on licensing terms . . .
(4) Examples	<Example 3> An act of not disclosing a patent during the technology standardization process "A" is a patent holder of a technology involving the exchange of information between the CPU of a computer and peripheral devices (e.g., video device). In considering the selection of A's patented technology as a standard, the standardization organization for video electronic products surveyed its members, including A, on whether there were patents related with the relevant technology. A falsely represented that it had no related patents, and the organization took A's word for it and selected the relevant technology as the standard.

The IPR guidelines provide no conclusive standard for illegality within its provisions but serve as a bridge that leads to the KFTC determining the illegality of conduct by applying specific provisions of the MRFTA. As described in Table 1, the guidelines adopted a four-stage approach. In the first stage, the rationale for and concerns of competition in regulating problematic conduct and basic considerations in determining illegality are put forth. The second stage prescribes the applicable provisions of the MRFTA. In the third stage, the type of conduct that can be assessed to be abuse is stipulated. This is not a categorical prohibition and each conduct must be subject to the rule-of-reason approach to find liability under relevant MRFTA provisions in addition to IPR guidelines. And in the fourth stage, detailed examples are given, when appropriate, of potentially problematic conduct based on domestic and foreign cases with modifications to help comprehension of the guidelines.

4.1.5. Guideline's Approach to Licensing Terms

4.1.5.1. Royalty for License (IPR Guideline sec. III.1.A)

The IPR guideline recognizes that obtaining a patent through innovative development of technology requires a considerable amount of time, money and investment risk. Considering the need for just compensation for patent holders' technological accomplishments and inducing new technological innovation, the IPR guideline generally considers imposition of royalty as a legitimate exercise of patent rights.

On the other hand, practices likely to impede fair trade in the relevant market, such as making unfair demands for payment in exchange for licensing, can be considered going beyond the legitimate scope of patent rights.

(1) An act of unduly deciding, maintaining or changing royalty in collaboration with another enterprise;
(2) An act of charging an excessively unreasonable level of royalty in light of customary commercial practice;
(3) An act of discriminatorily charging royalty depending on factors such as the licensee's identity;
(4) An act of unduly charging royalty for parts that have not used the technology licensed;[21)]

21) The act of including the use of a competitor's technology in calculating royalty for licensed technology can increase the cost for using the competitor's technology; moreover, it can decrease demand for the technology, which is most likely to be considered an anti-competitive act. Exceptions can be made when such methods of calculating royalty are acknowledged as inevitable (e.g., due to limitations in measuring the volume of licensed technology use). (IPR Guideline sec. III.1.A.(4) note)

(5) An act of unduly charging royalty for a term including the period after the expiration of patent rights; and
(6) An act of allowing the patent holder to decide or change royalty calculation methods without clearly stating them in the contract.

4.1.5.2. Refusal to License (IPR Guideline sec. III.1.B)

To provide just compensation for a patent holder's technological accomplishments and promote new technological innovation, the patent system grants a patent holder exclusive monopoly over the use of the relevant invention. Hence refusal to grant a license by a patent holder to protect its rights can be considered a legitimate exercise of patent rights.

But practices likely to impede fair trade in the relevant market, such as unduly refusing to license, can be considered going beyond the legitimate scope of patent rights.

(1) An act of refusing to license a certain enterprise together with a competitor without a legitimate reason;
(2) An act of unduly refusing to license a certain enterprise;[22] and
(3) An act of refusing to license to secure the effectiveness of other unfair acts, like refusing to grant a license to another party if the latter rejected unreasonable conditions imposed by the patent holder.[23]

4.1.5.3. Limitations on License Scope (IPR Guideline sec. III.1.C)

A patent holder may not only refuse to license within a reasonable scope, but also set bounds on the use of patented inventions, allowing only partial implementation. This limitation can result in the pro-competitive effect of promoting trade of a patent holder's technology whose owner would otherwise refuse granting the license. Hence a patent holder's granting of a license with reasonable limitations (e.g., number of licenses, territory or period for protecting the patent holder's rights) can generally be considered a legitimate exercise of patent rights. But practices likely to impede fair trade in the relevant market, such as unfair restriction on the scope of the license, can be considered going beyond the

22) In cases where (1) the purpose of the refusal to trade relates to restraining competition, (2) the refused technology is an essential element of business activities, (3) the technology is extremely influential in the relevant market (e.g., technology standard), (4) use of the technology has been excessively impeded through a refusal to grant licenses though the patent holder itself did not have the intent to use the technology, the act will probably be considered unfair (IPR Guideline sec. III.1.B.(2) note)
23) The conditions stated as examples in "III. 1. C. Limitations on Scope of License" and "D. Imposition of Anti-Competitive Conditions when Licensing" can be included in the "unreasonable conditions" stated above.

legitimate scope of patent rights.

(1) An act in which the patent holder and licensee make an agreement with unreasonable conditions, like restricting the number of licenses, territory and period related to either products concerned with the license ("contracted products") or technology ("contracted technology");

(2) An act of unduly regulating the supply in the relevant market by restricting the number of licenses, territory and period related to the contracted products or technology; and

(3) An act of discriminatorily restricting the number of licenses, location and duration related to the contracted products or technology depending on the other party in the transaction.

4.1.5.4. Imposition of Unreasonable Conditions when Licensing (IPR Guideline sec. III.1.D)

In addition to being able to restrict the scope of use of patented inventions by granting a partial license, a patent holder may impose conditions not directly related to specifying the scope of the license. In general, what can be considered a legitimate exercise of patent rights is a patent holder imposing terms within a reasonable scope to effectively materialize the relevant patented invention, enhance the safety of contracted products or prevent the technology's appropriation.

But practices likely to impede fair trade in the relevant market, as listed below, such as imposition of unreasonable conditions when licensing, can be considered going beyond the legitimate scope of patent rights.

(1) Restrictions on prices of contracted products[24)]
(2) Restrictions on suppliers of raw materials[25)]
(3) Restrictions on purchasers of contracted products[26)]
(4) Restrictions on trade of competing goods or technology[27)]

24) III.1.D.(1) of the IPR guideline provides that restricting the minimum resale price is deemed illegal and II.2.C of the IPR guideline provides that in principle, the minimum resale price maintenance is deemed illegal without further analysis of the effects of impeding fair trade and efficiency enhancing effects. But in a case involving Hanmi Pharmaceutical in 2010, the Supreme Court held that the minimum resale price maintenance is not illegal per se (Supreme Court 2009du9543, delivered on Nov. 11, 2010). Thus the provision should be revised.
25) However, exceptions can be made for situations where the restriction of suppliers for raw materials etc. has been enforced for the guarantee of quality or performance of the contracted products.
26) Exceptions can be made for situations where the other party in the dealing of contracted products is inevitably restricted within a reasonable scope due to licensing by limiting the number of licenses, territory, term and others of the contracted products to guarantee the patent holder's rights.

(5) Tie-in sales
(6) Imposition of non-assertion obligation[28)]
(7) Restrictions on improving technology and research activities (including grant-back)[29)]
(8) Restrictions on use after expiration of patent rights
(9) Provisions on termination of contract or disputes

When determining whether the patent holder's addition of terms in licensing a grant is anti-competitive, the following factors shall be considered:

(1) Whether the attached conditions are essential in implementing the relevant patented invention (i.e., relationship between patented invention and imposed conditions), (2) whether the relevant conditions contribute to promoting implementation of the relevant technology, and (3) whether the patent rights about the appropriate conditions have been exhausted.

In general, once the licensee sells the contracted products, patent rights for sold contracted products are considered exhausted. Imposing restrictive conditions on an area in which patent rights have been exhausted, such as on the resale of an already sold product, can be considered going beyond the scope of legitimate exercise of patent rights. Likewise, it is difficult to consider imposing conditions on the licensee even after the patent rights' expiration or on areas irrelevant to the concerned patent rights as legitimate exercise of patent rights.

4.1.6. Treatment of Patent Pools and Cross Licensing (IPR Guideline sec. III.2)

A patent pool refers to an arrangement of multiple patent holders putting together individual patents for cross licensing or collective licensing to third parties. IPR guidelines recognize that through integrated operation of complementary technologies, patent pools can create the pro-competitive effects of boosting efficiency in relevant markets and promoting technology use by cutting the search cost in the relevant technical field or expenses needed for negotiating with

27) Exceptions can be made for situations where the act is deemed inevitable to protect the patent holder's confidential business information from being revealed or leaked to competitors or a third party by dealing competing products or technology together, and where the scope of restriction is limited to the minimum only to protect the patent holder's rights.
28) Exceptions can be made when the infringement of the patent rights in question is agreed to be notified to the patent holder, or when the licensee can assume a defense suit or must cooperate with the patent holder's defense suit.
29) Exceptions can be made if the patent holder is acquiring the licensee's achievements under mutually equal conditions or through payment of a reasonable price, or if the restrictions on improving technology are inevitable due to the performance guarantee of the contracted products or technology or to protect the patent holder's trade secrets.

multiple patent holders, and also reducing the risk in technology use caused by infringement.

But practices that are likely to impede fair trade in the relevant market through patent pools, as listed below, can be considered going beyond the legitimate scope of patent rights.

(1) An act of unduly agreeing during the operation of the patent pool on certain related terms such as price, quantity, territory, opponents and restriction on technology improvement;
(2) An act of unduly refusing to grant licenses or executing a license agreement containing discriminative terms with other enterprises that did not participate in the patent pool;
(3) An act of unduly requiring the other enterprise to share its independently acquired knowledge, experience and technical achievements during the operation of the patent pool;[30)]
(4) An act of coercing package licensing by unduly including invalid or non-essential patents in the patent pool;
(5) An act of causing excessive disadvantage to the licensee by imposing a lump-sum royalty that is excessively higher than that for each patent included in the patent pool.

Specifically, determination of illegality in the exercise of IPR in a patent pool is to be mainly based on technologies that compose such a pool, the form in which the technologies are licensed, and method of operation.

For technologies that compose the patent pool, the exercise of rights of the relevant patent pool will most likely be deemed unfair if the technologies that compose such a pool can be mutually substituted or the patent pool includes non-essential or invalid patents.

On the form in which the patent pool technologies are licensed, the exercise of rights of the relevant patent pool will most likely be deemed unfair if package licensing of the relevant technologies is the only viable method and independent licensing of each technology is prohibited.

On the method of operation, the exercise of rights of the relevant patent pool will most likely be deemed unfair if the patent pool is independently operated by a

30) This is highly likely to be deemed unfair especially if one is required to share knowledge about other technology that can substitute the technology included in the patent pool, if one is required to share knowledge about technology not directly related with the patent pool, or if the sharing of such knowledge excludes enterprises outside the patent pool.

specialist group separate from the patent holders.

Cross licensing is an arrangement among multiple patent holders to grant mutual licenses for patents held by each patent holder, and often used as a settlement tool especially in patent disputes. Cross licensing is similar to patent pools in that it can impede fair trade through enabling collaborative acts between enterprises and excluding third-party competitors, notwithstanding its pro-competitive effects such as promoting technology use and cutting transaction costs. Accordingly, the provisions applicable to patent pools under 2.A.(1), (2) and (3) of the Guidelines may be applied with proper modifications to cross licenses.

4.1.7. Special Issues in Exercise of Standard-related Patent Rights (IPR Guideline sec. III.3)

Once a technology is adopted as a standard, it can have enormous and lasting influence in the relevant market partly because a considerable switching cost might be needed to replace it. If a technical standard is protected as a patent with exclusive/monopolistic characteristics, this could seriously impede fair trade in the relevant market. To tackle these fears, numerous standardization organizations usually require relevant patent data to be disclosed in advance before selecting technical standards. Prior consultation is also needed to ensure fair, reasonable and non-discriminatory (FRAND) licensing terms if the technology is protected by patents. The disclosure of and prior consultation on licensing terms are necessary to prevent abuse of patent rights selected as a technical standard, and compliance thereof is an important consideration when judging fairness in exercise of the patent rights related to the technical standard.

Generally, consultation on selection of technical standards and exercise of patent rights related thereto create pro-competitive effects in that they promote use of the relevant technology and contribute to consumer welfare by creating efficiency.

But acts likely to impede fair trade in the relevant market, as listed below, including abuse of the standardization procedure or demanding unfair terms after adoption of the technical standard, can be considered going beyond the legitimate scope of patent rights.

(1) An act of unduly agreeing on certain terms such as price, quantity, territory, opponents and restriction on technology improvement during consultation on technical standard selection;
(2) An act of unduly refusing to disclose information about the related patent application or registered patents owned by oneself to increase the possibility of being selected as the technical standard or avoid prior consultation on

licensing terms

(3) An act of unduly refusing to grant licenses for a patented invention widely used as the technical standard

(4) An act of unduly discriminating licensing terms for a patented invention widely used as the technical standard or imposing an excessive royalty

4.1.8. Abuse of Patent Actions (IPR Guideline sec. III.4)

Legal procedures such as patent infringement actions are important means for guaranteeing patent holders' rights. Such actions incur considerable losses of time and expenses, however, and could further interfere with the parties' business activities by influencing their reputations in the relevant market. So abuse of legal/administrative procedures/actions, including those of illegitimate patent infringement, and fair trade impediment in the relevant market could be deemed considered going beyond the legitimate scope of patent rights. If infringement action is brought when the patent holder is aware of non-infringement or social norms make it objectively clear that no infringement has occurred, this is highly likely to constitute IPR abuse. Yet if the patent holder's expectation of legal action is deemed reasonable and justified, the sole fact that the patent holder failed to prevail in legal action is not automatically determined as proof of abuse of a patent action.

4.1.9. Anti-Competitive Agreements During Patent Dispute (IPR Guideline sec. III.5)

Settlement over a patent's validity and infringement can be effective for guaranteeing a patent holder's rights to resolve a dispute between the patent holder and interested parties. This is because it can reduce the cost of the lawsuit and risk in technology use.

But settlement with the effect of unduly sustaining the exclusive authority of the invalid patent and unduly preventing the entry of competing enterprises into the market can be considered going beyond the legitimate scope of patent rights.

In the following cases where (1) the parties to the settlement agreement are competitors, (2) the purpose of the settlement is related to restriction of competition in the relevant market, (3) market entry of the relevant enterprises is delayed until after the patent rights expire, (4) the entry of related enterprises into the market not directly related to the patent is delayed, or (5) the parties to the settlement are aware that the disputed patent is invalid or it is objectively obvious that it is invalid, such a settlement agreement for the relevant patent dispute is likely to be deemed unfair.

4.1.10. Assignment of Patent Rights that Constitute Major Business (IPR Guideline sec. III.6)

The IPR guidelines acknowledge that an agreement on the assignment of patent rights that constitute a main part of a business or an exclusive license that generates the same effect will undergo review per relevant merger review provisions.

4.2. Guidelines on Fair Patent License Agreements[31)]

On January 17, 2012, the KFTC promulgated Guidelines on Fair Patent License Agreements. The IPR guidelines set basic enforcement standards but because of an effect-based approach, the guidelines, in practice, lack specificity for contracting parties who lack legal expertise to understand and directly rely on. Another fear was that small and medium-size enterprises (SMEs), with their inferior legal capabilities or bargaining power (compared to large corporations), end up accepting licensing contract forms drafted by big companies with limited bargaining and focused on royalty rates. Thus the implication of grant-back clauses or consequences of patent invalidity are often not fully considered, and even if a contracting party finds the clauses problematic, it frequently confronts difficulty in negotiating terms. Against this background, the KFTC adopted Guidelines on Fair Patent License Agreements that include examples and explanations on what can be viewed as fair licensing practices and recommended provisions. This guideline was expected to minimize the risk of MRFTA violation by providing greater predictability and help SMEs cope with unfair licensing contracts. By using this guideline as an easy-to-understand reference and best practices, contracting parties are expected to easily determine whether a certain clause is unfair or can use it as a standard form contract to avoid regulatory risks. Guidelines on Fair Patent License Agreements are advisory, so violation does not necessarily mean the conduct is unlawful. The illegality of certain conduct should be determined under the MRFTA and PR guidelines.

Guidelines on Fair Patent License Agreements identify five types of potential MRFTA violations: (1) restriction on competition by joint conduct (2) restriction on competition by unilateral conduct, (3) unfair agreement through abuse of superior bargaining position, (4) use of unfair competition methods and (5) concentration of economic power through supporting affiliates.

Guidelines on Fair Patent License Agreements provide clause-by-clause analysis of ten typical clauses found in patent licensing agreements. The ten are:

31) On May 21, 2014, the KFTC announced that this guideline will be removed by the end of September the same year, leaving required parts incorporated into the IPR license guideline. As a result, this section should be changed as soon as the plan's implementation is made available.

(1) Clauses on licensing fees (discriminatory fees imposed on competitors and their business partners and significantly favorable terms for affiliates)
(2) Request to produce proof of licensing fee
(3) Clause on purchase of raw materials
(4) Restriction on territory
(5) Restriction on sale price and volume of relevant product
(6) Clause on restriction on trade of competing products or technology
(7) Clause conditioned on and tied to other products
(8) Clause on grant-back of improved technology
(9) Clause on treatment in case of patent invalidation
(10) Non-challenge clause

As described in <Table 1-2>, an analysis structure for each specific clause includes (1) case example, (2) basic purpose of relevant clauses, (3) risk of violating the MRFTA, (4) fair licensing guidelines and (5) best practices.

〈Table 1-2〉 Structure of Guidelines on Fair Patent License Agreements (Examples)

8. 8. Clause on Improved Technology (Grant-back)	
(1) Case Example	"A" holds patent rights on x1, the core fundamental technology ("x1") necessary to manufacture Product X ("X"). A's patent right on x1 is expected to expire in five years. Ninety percent of X distributed in the market is manufactured by using A's x1, which has been widely used as the most efficient technology to produce X for a long time. Three years ago, A signed an agreement with "B," an X manufacturer, in which A would grant license of x1 to B. As the contract period recently expired, A is considering renewing the agreement. In the review process, A learns that B is conducting research on x2, which has improved x1 and would radically reduce the manufacturing cost of X. While renewing the agreement, A (i) adds a new provision on technology improvement in which if B makes improvements to the relevant technology, A still holds the patent rights to the technology, and (ii) A further clarifies that the agreement shall be renewed subject to and conditioned on the aforementioned provision. B needs x1 to maintain its business operations, and would face substantial cost in switching the base equipment if it substitutes x1 with another technology. As a result, B signs and executes the renewal agreement as proposed by A. With the provision on technology improvement included in the agreement, B loses the incentive to improve x1 on its own cost and research on x2, the improved technology, is suspended. Afterwards, A renews agreements with enterprises other than B with the same provision on technology improvement in agreements. Among the enterprises, several were later found to improve x1 and the improved technologies were registered as A's patent rights.

〈Table 1-2〉 Continue

8. 8. Clause on Improved Technology (Grant-back)	
(2) Basic Purpose of Relevant Clauses	If a licensee of the patent holder's technology improved the technology through R&D, an issue can be raised over who will own the patent right of the improved technology. In this respect, the patent holder has an incentive to request the sharing of rights to improved technology to (i) prevent its technology from turning obsolete and being driven out of the relevant market due to the new technology, and (ii) receive its contribution to the new technology by providing the licensee with the original technology.
(3) Risk of Violating MRFTA	In this example, A has held the dominant market position for a long time through its x1 in the technology market relevant to the manufacture of X. So A signs an agreement whereby it shall solely own the patent right of the improved technology to maintain its dominant market position. Because of the execution of such an agreement, the licensee has reduced incentive to innovate while the patent holder maintains/strengthens its dominant position in the technology market by stacking patent rights on technology improved by the counterparty as well. Restricting competition like this can exceed the scope of legitimate exercise of patent rights and violate the MRFTA.
(4) Fair Licensing Guidelines	If the licensee made improvements to that technology, the improved technology contains both the contribution of the patent holder who developed the original technology and that of the counterparty who completed the improved technology through follow-up innovation. Thus the provision on improved technology must simultaneously (i) guarantee the initial contribution of the patent holder, and (ii) sufficiently guarantee incentive for follow-up innovation by the licensee.
(5) Best Practices	If the licensee improved the patented technology on its own, the patent right for the improved technology shall belong to the party who made such improvements. Per the original patent holder's request, however, the improving party shall grant a non-exclusive license with reasonable terms and conditions considering the improved technology's value.

4.3. Model Operating Standards for Standard-setting Organizations for Voluntary Compliance with MRFTA[32)]

4.3.1 Basic Principles

The KFTC in December 2011 implemented the Model Operating Standards for Standard-setting Organizations for Voluntary Compliance with the MRFTA ("Model Operating Standard"). The aim is to clarify violations of the MRFTA that could arise during the standard-setting process. The watchdog also intends to propose a Model Operating Standard that enterprises and businesses participating in the standard-setting process and SSOs (standard-setting organizations) may refer to,

32) On May 21, 2014, the KFTC announced that this Model Standard will be removed by the end of September the same year, leaving necessary parts incorporated into the IPR license guideline. As a result, this section should be changed as soon as the plan's implementation is made available.

thereby preventing violation of the MRFTA and promoting fair business practices. The Model Operating Standard is a recommendation that has no binding legal effect. This does not imply that SSOs are subject to special duties in the case of legal dispute between an SSO and private party (Model Operating Standard I.2.1)). Nevertheless, the Model Operating Standard is important in that it recognizes the SSO's role in preventing abuse of standard essential patents.[33)]

The Model Operating Standard is primarily applicable to agreements and exercises of IPR among private parties that occur during the standard-setting process. It neither applies to actions of the government or other public institutions as well as to the exercise of a technology accepted as a de facto standard due to its widespread use in the industry (Model Operating Standard I.4.1).

4.3.2. Risks of MRFTA Violation

The Model Operating Standard recognizes the pro-competitive effects of standard setting, such as reducing the risk of duplicate investment, promoting technological innovation and reducing production cost by securing product compatibility (Model Operating Standard II.1.A). But it says the standard-setting process can be distorted due to lack of information or deception. Further, the difficulty of replacing standard technology with another due to significant switching costs can cause fears over competition when IPR holders unreasonably restrict use of the standard technology (Model Operating Standard II.1.B).

A standard's market power can be measured by its share in the relevant technology market, but when this is difficult, the market share of products or services that use the standard can be relied on for the calculation. The market power of a standard cannot be presumed by the mere ability to exercise IPR with respect to a specific standard. Instead, the determination should be based on a comprehensive review of how widespread the standard's adoption is, the substitutability of the standard and the essentiality of the relevant IPR (Model Operating Standard II.1.C).

The Model Operating Standard offers examples of behavior during the standard-setting process that could violate the MRFTA. In addition to unreasonable collaborative acts such as price fixing, exclusion of competitors during the standard-setting process such as restricting participation in the standard-setting process, restricting the adoption of a specific technology and limiting the development of competing standards can violate the MRFTA. Restriction on the availability of the adopted standard can be also illegal, and examples of such conduct include patent

33) For the role of SSOs in preventing patent hold-ups in the context of standard setting, see Kai-Uwe Kühn, Fiona Scott Morton, Howard Shelanski, Standard Setting Organizations Can Help Solve the Standard Essential Patents Licensing Problem, Antitrust Chronicle (March. 2013).

ambush and breach of FRAND commitment (Model Operating Standard II.2).

4.3.3. Model Operating Standards

The Model Operating Standard sets out three basic principles for voluntary compliance: (1) the opportunity to participate in the standard-setting process, (2) transparency in the operation of the process, and (3) fair availability of the standard (Model Operating Standards III.1). The Model Operating Standard advises in this regard (1) to keep any restrictions on participation in the standard-setting process to a minimum and only if necessary for the SSO's reasonable attainment of its goals; (2) ensure that conditions unnecessary for the reasonable attainment of its goals, such as price or output, are not directly or indirectly discussed among competitors, and (3) establish and implement a reasonable and clear IPR policy to ensure that future use of the standard is not restricted by a specific party's interests.

The Model Operating Standard provides the following details on operating standards.

- Limitation on participants: SSO rules on participation must be objective and clear, and should be implemented in a non-discriminatory and reasonable manner.

- Limitation on discussion scope: SSOs must be prohibited from collectively determining matters that directly affect market competition. To prevent illegal information exchange, the licensing administration is recommended to be operated by an independent third party with no direct ties to participants in the standard.

- Decisions to designate a standard: The process of selecting technologies to be included in a standard must be conducted in a fair manner and through objective evaluation procedures. Disclosure of any designations of standards is advised to help interested parties easily determine details of the relevant standard technology and the scope of relevant essential IPR, as well as the possibility of future licensing.

- IPR Disclosure Policy: SSOs may establish and implement internal regulations that (1) require all participants in the standard-setting process and their agents to disclose information on essential IPR included in the standard being developed, and (2) prevent amendments to IPR strategies and acts that restrain fair use of the standard by unreasonably using information shared during the process of essential technology designation.

- FRAND commitment: SSOs need to require essential IPR holders to submit an irrevocable written commitment to granting licenses for their standard technology on FRAND terms before making a final determination on the scope of standard technologies. SSOs may implement a policy whereby participants make an across-the-board FRAND commitment to license their essential IPR, regardless of whether they have been disclosed. SSOs need to encourage the transferee to comply with FRAND terms when IPR subject to a FRAND commitment is transferred. SSOs can also require participants to provide clear notification of the commitment to transferees in the event of a transfer of rights.

- Ex Ante Disclosure of Licensing Conditions: To prevent holders of essential IPR from unfairly exercising their rights after the standard has been designated, participants in the standard-setting process may individually disclose the conditions of the essential IPR, such as maximum royalties.

- Establishment of Effective Enforcement Measures: If a IPR holder fraudulently concealed its IPR or avoided submitting or refused to make a FRAND commitment, SSOs should provide procedures for the exclusion of such technology from the standard and discussions on other reasonably substitutable technologies.

- Restrictions on External Activities by Participants: SSOs may not restrict their participants from involvement in the development of substitute standards without reasonable grounds or restrict participant participation in the development of products and services that use such substitute standards.

5. Major Cases of IPR Abuse

This section introduces cases of the KFTC's regulatory enforcement over IPR abuse from the early stages to recent developments. The focus of findings of liability has been observed to have migrated from fairness in conduct in earlier cases to anti-competitive effects on the market. It reflects the development of competition law enforcement from a historical perspective.

On anti-competitive effects the KFTC depicts to find illegality, the watchdog has paid major attention to the exclusionary effects by market dominant players based on a rule-of-reason standard as opposed to simple pricing problems. In most cases, the high licensing fee of IPR alone was not considered a major interest of the KFTC. This is because the applicable regulatory scope for excessive pricing by a market dominant business is extremely narrow under the MRFTA, and subtle legal and

economic grounds exist for price regulation.

5.1. Earlier Cases

Earlier cases in the mid-2000s mostly involved a licensor requiring a licensee to sign a contract irrelevant to the patent, or denying access to the new technology in the context of public construction bidding that incorporated a patented technology.

In Rainbow Scape[34] decided on July 26, 2005, the KFTC ruled against a licensor who forced licensees to sign subcontracts with licensors for construction work to which the patented technology did not apply. Rainbow Scape owned a patent for a method of installing fountains. Certain municipal governments required use of Rainbow Scape's patented technology as a qualification for participating in fountain construction biddings. Taking advantage of its superior bargaining position that stemmed from the necessity of the patent to win the bid, Rainbow Scape demanded that prospective licensees sign subcontracts with the company covering not only portions of work involving the patented technology but also portions of work irrelevant to the patent, and this equaled 74 percent of the combined construction work. The KFTC found that (1) the patent did not confer the power to condition licensing on the subcontracting of unrelated works and that (2) this practice was at odds with the patent protection's purpose to encourage innovation and technological development.

Kobec[35] involved a similar issue with Rainbow Scape. In exchange for the licensing of a patented technology incorporated in bridge improvement work, Kobec was found to have required subcontracting of excessive portions of work to Kobec or a company it designated, and to prepay part of the proceeds in cash. Although the KFTC left open the possibility that requiring licensees to subcontract construction covered by a patent to a capable company can be justified on the grounds of preventing non-use of the patented technology and safety, it also held that designating the party to whom the work should be subcontracted, the high proportion of subcontracting and excessive amounts of prepaid money went beyond the legitimate scope of the patent and would thus be deemed an impediment to fair trade.

In Insung Industry[36] decided on September 9, 2005, at issue was refusal to license a technology to the successful bidder of a public construction work. To pass the qualification examination, the successful bidder was required to submit a technology use agreement with Insung Industry. At first, Insung refused to license

34) KFTC Decision No. 2005-151, 2005. 7. 26.
35) KFTC Decision No. 2006-266, 2006.11.23.
36) KFTC Decision No. 2005-174, 2005.9.9.

based on inappropriate timing of the construction, but even after the defect was remedied, it refused to license on other unreasonable grounds. The KFTC held that the company's conduct was an illegal refusal to deal. Such conduct, the watchdog said, was beyond the limit of the freedom to choose trading partners since the respondent could have been compensated for its technology by incorporating its capital investment and the technology cost in calculating royalties. Similar issues in the Insung case also emerged in Space.[37)]

The four cases above were deemed in violation of Article 23 of the MRFTA, which prohibits unfair trading practices. But in one case, the KFTC applied the provision on abuse of dominant position as prescribed in Article 3(2) of the MRFTA. In Royal Information Technology Corporation (RITCO),[38)] Hyundai Engineering & Construction, which was awarded a land improvement contract from a local government, gave a public bid notice for installing automatic fire detectors. The project was designed to use a specific model of fire detectors manufactured by a Swiss company, which was exclusively distributed by RITCO. Three companies bid and RITCO was the third-lowest bidder. The lowest bidder contacted RITCO to order supplies of the fire detector, but got no response and eventually had to abandon the contract. Then the second-lowest bidder also gave up the contract after receiving an estimate from RITCO that it deemed too expensive. Hyundai had no choice but to sign the contract with RITCO. The KFTC found that RITCO's conduct constituted refusal to deal under Article 3(2) of the MRFTA.

5.2. Qualcomm: Abuse of Standard Essential Patent by Breaching FRAND Commitment

The first significant enforcement action against IPR abuse by the KFTC was sanctions against Qualcomm for its CDMA technology patent licensing in 2009.[39)]

The KFTC imposed a corrective order and fine of USD 210 million on Qualcomm for (1) charging discriminatively high royalties for using non-Qualcomm modem chips rather than its modem chips, (2) offering loyalty rebates on the condition that licensees meet a great portion of their demand with Qualcomm modem chips and RF (radio frequency) chips, and (3) requiring royalties even after the expiration or invalidation of the relevant patents.[40)] The first and third issues were related to IPR

37) KFTC Decision No. 2006-166, 2006.7.26.
38) KFTC Decision No. 2006-221, 2006.10.10.
39) KFTC Decision No. 2009-281, 2009.12.30.
40) Press Release, Korean Fair Trade Comm'n, Qualcomm's Abuse of Market Dominance (Jul. 23, 2009)
41) Failure to disclose the application digital signal processor interface was also raised, but the KFTC closed the investigation on that issue as Qualcomm voluntarily pledged to disclose the interface to third parties.

licensing.[41]

The KFTC found that Qualcomm was a dominant player in the Korean market for code division multiple access ("CDMA") modem chips and that Qualcomm charged discriminatively high royalties for export models when it licensed its CDMA technology to mobile handset makers. For example, the company charged a 5-percent royalty when a handset maker used Qualcomm modem chips and a 5.75-percent royalty when non-Qualcomm modem chips were used. In addition, Qualcomm discriminatively set a royalty ceiling of $20 for handset makers using Qualcomm modem chips and $30 for handset makers that incorporated competing modem chips. And the company netted the price of its modem chip when calculating royalties applied to the handset for domestic use. In this case, the KFTC referred to Qualcomm making a written FRAND commitment to the Telecommunications Technology Association, a standard setting body for CDMA.

On the third issue, the license agreement provision in question provided under the title of "Invalid or Expired Patents" said, "The obligation for LICENSEE to pay royalties to QUALCOMM under Section 5.2 shall be reduced by XX percent (XX%) of the applicable royalty rate in the event all patents that are licensed hereunder by QUALCOMM and used by LICENSEE have expired or are invalid." The KFTC found that the provision constituted abuse of superior bargaining position under Article 23, Paragraph 1, Item 4 of the MRFTA ("unduly takes advantage of its bargaining position to harm others").

The final review of this case remains pending with the Supreme Court.

5.3. GSK-Dong-A: Anti-competitive Patent Settlement

Inspired by the pharmaceutical sector's inquiry into the European Commission in 2009, the KFTC in 2010 conducted a market-wide survey to gather information about patent licensing agreements and legal disputes among pharmaceutical companies. The inquiry involved 30 multinational and 18 domestic companies, and eventually included all major pharmaceutical companies doing business in Korea.[42] After a lengthy analysis of the results, the KFTC concluded that GlaxoSmithKline Korea (GSK), one of the world's largest pharmaceutical multinationals, and Dong-A Pharmaceutical Co. (Dong-A), Korea's industry leader, had violated Article 19, Paragraph 1, Item 4 (Limiting the Territory of Trade) of the MRFTA by agreeing not to sell generic drugs, something which resulted in high prices and harm to consumer

42) See KFTC Press Release, 'Beginning of IPR Licensing Market Inquiry of Pharmaceutical Industry' (June 2010). Text available at http://www.ftc.go.kr/news/ftc/reportView.jsp?report_data_no=3938&tribu_type_cd=&report_data_div_cd=&currpage=2&searchKey=1&searchVal=%C1%A6%BE%E0&stdate=&enddate.¼ (in Korean).

interests.

GSK developed Ondansetron, an ingredient that fights nausea, and subsequently produced and sold Zofran, which uses Ondansetron as an active pharmaceutical ingredient (API). Subsequently Dong-A developed Ondaron, a medication that used Ondansetron API that was claimed to be developed by a different method. In a subsequent patent dispute, both parties settled on the condition that in exchange for the withdrawal of the patent lawsuit, GSK would grant Dong-A (1) exclusive rights to sell Zofran to national and public hospitals in Korea and (2) exclusive domestic rights to sell Valtrex, a separate medication. The duration of the settlement agreement went beyond the expiration date of the GSK patent. Dong-A also agreed not to develop, produce or sell any medication with identical or similar ingredients to Zofran or Valtrex.

The KFTC imposed fines of USD 2.9 million on GSK and USD 2 million on Dong-A, along with a cease-and-desist order in November 2011.[43] Both companies filed appeals to overturn the KFTC decision with the Seoul High Court, which had exclusive jurisdiction for cases dealing with KFTC actions.

The Supreme Court largely affirmed the KFTC decision and held that (1) the agreement at issue was that GSK provided Dong-A, who disputed the validity of the patent GSK held and put on sale a competing product, with a significantly larger scale of economic benefit than the cost of the patent lawsuit in exchange for withdrawing the competing product from the market and restricting its sale beyond the term of the patent, and (2) the agreement affected fair and free trade by providing a portion of the monopoly profit to the other party in return for maintaining its monopoly power, and (3) the agreement was not deemed a legitimate exercise of patent rights, (4) thus the MRFTA is applicable to the conduct, and (5) harm to consumers did exceed efficiency. The Supreme Court said the KFTC found an anti-competitive agreement for the other new drug (Valtrex), which bore no relationship to the patent for Ondansetron without properly defining the market or assessing the anti-competitive effect, and repealed part of the KFTC decision.[44]

43) KFTC Decision 2011–300, delivered on Dec. 13, 2011. Full text available at http://www.ftc.go.kr/laws/book/judgeSearch.jsp. (in Korean). For details of the case in English, see KFTC Press Release, 'Nation's first crackdown on collusion blocking the entry of cheap generic drugs' (October 2011). Text available at http://eng.ftc.go.kr/bbs. do?command=getList&type_cd=52&pageId=0201. (in English, search by the term 'generics'). Both companies filed appeals to overturn the KFTC decision with the Seoul High Court, which had exclusive jurisdiction for cases dealing with KFTC actions. After a tough trial, the two panels of the court in October 2012 dismissed most of the points in both appeals.

44) Supreme Court 2012du24498, delivered on 27 Feb. 2014 (for GSK's appeal). Supreme Court 2012du27794, delivered on 27 Feb. 2014 (for Dong-A's appeal).

5.4. SK Telecom: Unfair Licensing Practices for SMEs

On November 11, 2011, the KFTC issued a corrective order against SK Telecom, Korea's largest telecommunication carrier, for abusing its superior bargaining position to conclude "unfair" technology transfer agreements with SMEs that needed SK's technology to deliver gap-fillers ordered from the telecom giant.[45] This action followed a sweeping fact-finding survey on IPR abuse in the IT industry.

The licensing contract at issue included an unfair clause that the validity of SK patents would not affect the contract, and thus meant that the licensee should continue to pay royalties regardless of the patents' validity. But if SK used the patented technology of its contracting party, a clause effectively exempted SK from paying royalty after the patent expired or was invalidated. The KFTC found that SK abused its superior bargaining position to unilaterally transfer the risk caused by the uncertainty around the patent's invalidity and unreasonably restrain use of the technology after invalidation, which the other party would otherwise be free to use.

5.5. Samsung Electronics: No Abuse of Standard Essential Patent

On February 25, 2014, the KFTC announced that the injunction filed by Samsung Electronics against Apple based on the standard essential patent did not constitute abuse of market dominant position or unfair trading practices under the MRFTA.

Samsung was deemed to maintain monopoly in each of the four essential patent technology markets and thus would be considered a market dominant operator in the mobile telecommunication device market. But the KFTC rejected all of Apple's arguments on the illegality of Samsung's conduct

The KFTC made clear that FRAND commitments did not automatically exclude the right of patent holders to file an injunction against potential licensees. The critical issue was whether the potential licensee negotiated in good faith (willing licensee standard). But Apple had filed a patent infringement lawsuit during negotiations and proposed unfavorable license terms that underestimated patent value. Apple also showed an unwillingness to pay any royalty before the conclusion of the suit, which the KFTC called a typical example of a reverse hold-up.

The KFTC concluded after review that the standard essential patent held by Samsung did not amount to be an "essential factor." Samsung lacked exclusive

45) KFTC Decision No. 2011-120, 2011.11.30.

control over them because it was obliged to license to any potential licensee on FRAND terms and more than 50 companies held 15,000 standard essential patents for 3G mobile communication technologies. In addition, the KFTC found that Samsung did not fail to disclose its patent properly in the standardization process by intentionally withholding patent information.

6. Lessons from the Korean Experience

6.1. Need to Develop IPR to Improve Productivity Along with Development

The international economic landscape has significantly changed since the years Korea achieved its miraculous growth. And most developing countries have no similarities in their technological innovative capacity, and an export-led growth model might not always work. So sweeping generalizations must be avoided.

The Korean experience, however, could provide useful insight into how developing countries could use IPR strategy to increase innovation and productivity. Despite having few resources and small land size, Korea stepped up from being a poor country providing cheap labor to emerge as a global leader in major industries including IT and cars. No coincidence that Korea's transformation from a labor-intensive economy to one stressing high technology based on knowledge occurred amid the dramatic growth in IPR.

6.2 Need to Regulate IPR Abuse at Certain Stages of Development

Few empirical studies have connected the need for regulation of IPR abuse to a certain stage of economic development. As stated earlier, however, Korea has developed effective regulations on competition law over IPR after certain stages of economic development as protection of IPR was strengthened. In the beginning stages, the KFTC began to handle cases of unfair denial of access to new technology and was not fully in line with traditional competition-related concerns. With Korea's patent protection levels reaching global standards, however, industries demanded proper regulation of suspect conduct, and as the KFTC built up its enforcement capacity, it began to enforce the MRFTA in IPR with a focus on exclusionary effects.

6.3. Inherent Complexity of IPR Abuse Regulation and Calls for Careful Enforcement to Prevent Errors

PR abuse is a notoriously complex area for competition law enforcement in any jurisdiction worldwide. In addition to the need to understand highly technical information, authorities must consider that excessive enforcement could have a negative effect on investment, innovation and risk-taking incentives over the long run. A quick fix to correct competition-related fears without making significant enforcement errors is hard to find, and an approach careful not to impede innovation is needed. Competition authorities should fully analyze the rationale behind certain licensing practices, consider dynamic efficiencies and base their decisions on sound economic theory with full balancing of conflicting effects.

6.4. Well-designed Procedures for Both Probes and Hearings to Prevent Enforcement Errors

The KFTC has been consistent in carefully dealing with cases of IPR regulation to determine anti-competitive effects that outweigh efficiencies. This rule-of-reason approach is usually adopted because the watchdog is well aware of the great risk of enforcing on a false positive that could lead to inhibiting innovation. Such procedural carefulness is necessary due to the highly complicated and fact-intensive aspect of case analyses, difficulty in analyzing effects of market competition and the dynamically changing characteristics of technology markets.

One of the most noticeable examples in this respect was the Microsoft tying arrangement case in 2005. Although not directly dealing with IPR regulation, the case possessed similar aspects in factual complexity and difficulty in analyzing competitive effects. To make a decision on liabilities for three illegal tying arrangements in this case, the KFTC held seven hearings, each lasting nearly a full day over several months, following a four-year investigation by a task force organized solely for this case. Even after the hearings, the KFTC convened many times for nearly two months to conduct full analysis of the case. In oral arguments before the commission, both sides and interested parties presented a variety of testimonies by foreign experts and domestic professionals and oral debates.

Another example was the Qualcomm case in 2009. For the final decision, a fully-dedicated task force at the KFTC investigated the case for more than three years and held six hearings that included many opportunities for oral arguments and presentations in self-defense. During the hearings, many expert testimonies produced by both parties were allowed and encouraged.

Such careful steps were considered critical for Korea because experts and the KFTC fully recognized the requirements for a rule-of-reason analysis. Because such demand is common in most jurisdictions, the KFTC's experience should serve as a good reference.

6.5. Capacity Building of Competition Authority

Monitoring the dynamic and fast-evolving IT sector and applying competition law to the exercise of IPR can often be a challenging task for a competition authority with limited enforcement resources. Capacity building for such a watchdog must be prioritized to make efficient use of limited resources as well as ensure effective enforcement in this complicated area. Internally, consistent efforts to obtain and foster high-quality staff are crucial. The well-organized body and skilled staff of the KFTC have substantially contributed to the advancement of competition policies in Korea.[46] Close cooperation and information exchange with other competent authorities in charge of IPR policies and foreign counterparts can help make up for the shortage of expertise and enforcement experience in this area to ensure proper and coherent implementation.

6.6. Future of Korean Regulation of IPR Abuse

Regulations on the interface between IPR and competition law are constantly evolving in Korea to meet new challenges and reflect recent developments around the globe.

In its work plan for 2014, the KFTC announced that it would take a closer look at potentially abusive practices of non-practicing entities (NPEs).[47] It expressed concerns about (1) excessive exercise of patent rights by companies that used to manufacture and sell products on a global scale but are now behaving more like NPEs after withdrawal from the market, and (2) acquisitions and abuses of standard essential patents by NPEs.

The KFTC also pledged to closely monitor patent abuse in the pharmaceutical sector and improve relevant institutions.[48] With the passage of the free trade

46) For more information on the Korean experience in capacity building, see Hwang Lee, Korea's Developmental Experiences in Operating Competition Policies for Lasting Economic Development, 2013 Modularization of Korea's Development Experience (Apr. 2014), http://ksp.kdi.re.kr/common/attdown.jsp?fidx=405&pag=0000700003&pid=131.

47) Korea Fair Trade Commission, Work Plan for 2014 (Feb. 20, 2014), pp. 23-24, http://www.ftc.go.kr/common/download.jsp?file_name1=/news/report/2014&file_name2=0220 2014년 업무계획 서면보고서2.PDF&file_path=news_report_path (text in Korean) (Work Plan); Korea Fair Trade Commission, KFTC News No. 1 (Apr. 1, 2014), http://eng.ftc.go.kr/bbs.do?command=getList&type_cd=70&pageId=0306.

48) Id., at 18.

agreement with the U.S., the patent regulatory linkage system has been introduced to Korean law modeled after the Hatch-Waxman Act of the U.S. Along with the new system, patent disputes between the brand name drug giants and generic companies will grow more prevalent and lead to large settlement payments disproportionate to litigation risk. Based on the recent Supreme Court case (most notably GSK), the KFTC is expected to monitor reverse payment and develop standards for determining illegality in such practices.

The Samsung-Apple case, although dismissed by the KFTC, set an important regulatory precedent in determining the illegality of seeking injunctive relief by the FRAND-encumbered standard essential patent holder. The KFTC will continue to develop the criteria in keeping pace with developments in its major jurisdiction.

The revision of Guidelines on the Unfair Exercise of Intellectual Property Rights could take place soon, possibly by the first half of 2015, to accommodate cumulative demand to meet new regulatory demands.

Over the long run, the KFTC can be expected to strengthen competition law enforcement for both domestic and foreign businesses to ensure sound and creative economic development, which is the top priority of national economic policy amid a maturing Korean economy. Major cases abroad were extracted in the IT industry, owing to both the sector's high patent density and fast development. Since IT is a crucial sector for Korea, the country must maintain creativity and competitiveness. This policy demand requires careful watch by a competent watchdog and will lead to vigorous enforcement in this industry. Private litigation to check competitor abuse of IPR among major IT companies is also envisioned to grow, and global Korean IT companies will be major players in the arena. In turn, this will attract the attention of competition authorities.

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Competition Laws and Policies

Chapter 2

Regulating Abuse of Administrative Power: The Experience of the Korean Fair Trade Commission

Regulating Abuse of Administrative Power: The Experience of the Korean Fair Trade Commission

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Summary

Abuse of administrative power, leading to restraints on competition, can be a serious issue in countries that are trying to restructure their economies from a state-led, planned model to a liberalized, market-led one. This has been the experience of both Korea and China. It is very difficult to enforce competition law when such legal restrictions on competition are in place. The priority of an economy in transition is therefore to first eliminate the legacies of state intervention through regulatory reform, and contain state power in important industrial sectors through privatization. To ensure competitive neutrality, state-owned enterprises (SOEs) must also be subject to competition policy, thus promoting private-sector initiatives in general.

In these circumstances, the advocacy of competition policies by government agencies can be vital. "Competition advocacy" refers to any activities undertaken by those agencies, besides the enforcement of competition law, that promote fair competition. Since it is often impossible for a competition agency to enforce competition law directly against other ministries, which frequently have a mandate to meet other important social goals, reining in those bodies' anti-competitive behavior requires persuasion, consultation and recommendation?i.e. the precise tools of competition advocacy.

The experience of the Korea Fair Trade Commission (KFTC) shows that strong

provisions in the Monopoly Regulation and Fair Trade Act (MRFTA) allowed the KFTC to actively conduct a competition advocacy role. The three basic competition advocacy provisions are mandatory consultation and a mandatory competitive impact assessment prior to the legislation of new regulations, along with a mandate to reform monopolistic markets.

Besides a strong legal mandate, competition advocacy requires the relevant agency to be independent, enjoy high status and show intellectual leadership (including the capacity for economic analysis). A strong enforcement of competition law against SOEs also greatly helped the KFTC in promoting its own initiatives.

One of the most important issues regarding the regulation of SOEs is competitive neutrality. Competitive neutrality refers to a situation where no entity operating in a market has undue competitive advantages or disadvantages. To ensure competitive neutrality, and enhance allocative efficiency in the overall economy, it is essential to separate the commercial and non-commercial activities of SOEs. Not only will this help prevent cross-subsidization between the two sectors, it will maximize the SOEs' transparency and accountability. It is of course important to recognize the SEOs' public service obligations and account for any costs these activities will incur. However, in their commercial activities, SOEs must be forced to pursue a commercial rate of return, so as to prevent them from undercutting private competitors with the aid of public funds. Tax, regulation, financial access and public procurement are also crucial points in ensuring competitive neutrality.

The concept of competitive neutrality is flexible in that it acknowledges the need for government assistance to SOEs in fulfilling their public service obligations. Thus, it would make sense to apply the ideal only in cases where SOEs face competitors, potential or otherwise, from the private sector, where they are the dominant company in their field, or where the costs of anti-competitive measures would overwhelm the social benefits gained through the SOE's activities. Although competitive neutrality as a concept has not received much theoretical treatment in Korea, it is in fact largely achieved by making all SOEs subject to the MRFTA.

Competition agencies can also play a constructive role in expanding the scope of the private sector by pushing for privatizations, which by their nature tend to promote competition. The Korean experience shows that introducing institutional reforms both before and after the privatization is very important. For competition to take root, constant vigilance is required toward those sectors that were recently liberalized from the grip of SOEs. Where regulations still exist, the competition agency needs to push for structural reform and vigorously enforce competition laws. This work must be divided appropriately between the competition agency and the regulatory body, which needs to become independent of the related ministry to

avoid regulatory capture.

1. Introduction

Different jurisdictions vary in their treatment of administrative restrictions on competition, depending on their government structures, legal traditions and historical legacies. This chapter focuses on the experience of Korea and how Korean competition authorities dealt with administrative actions with anti-competitive consequences. As Korea transitioned from a government-led to a market-based economy during the 1980s, dealing with pervasive government regulations, such as price controls and anti-competitive entry-restrictions, became an important competition-policy issue. Fully-fledged regulatory reform that began in the 1990s, along with the wave of privatization and economic restructuring in the aftermath of the Asian financial crisis, gave impetus to the Korea Fair Trade Commission (KFTC)'s growing role in regulating anti-competitive government actions, including those of SOEs in particular sectors.

In the following section, we explain the legal basis on which anti-competitive administrative practices are regulated under Korea's Monopoly Regulation and Fair Trade Act (MRFTA). Section 3 discusses the role of the KFTC in regulatory reform pursuant to its competition advocacy mandate, and presents cases representative of the Korean experience. Section 4 explores the KFTC's experience in enforcing competition law against SOEs, and discusses issues and concepts relevant to effective enforcement in this area. Section 5 concludes by drawing policy implications from the Korean experience of regulating anti-competitive administrative actions.

As such, this paper does not deal with regulatory reform or privatization per se. (There is much more to say about regulatory reform and privatization as independent topics.[49]) Here, the boundary is drawn, by looking at the experience of the KFTC, at drawing implications for competition policy in dealing with the abuse of administrative power.

The Korean experience shows that when direct government intervention in the economy is prevalent, and the country relies heavily on SOEs for rapid industrial development, active competition advocacy and strong legal enforcement against SOEs are effective in curbing abuses of administrative power. This is not the same as promoting indiscriminate deregulation or privatization for its own sake. It is of

49) On these topics, see recent publications from the Knowledge Sharing Program: Ha, B.K. et al (2012), 2011 Modularization of Korea's Development Experience: Regulatory Reform and Economic Development-Korea's Experience in Regulatory Reform, and Nam, I.C. (2013), Governance of SOEs and Public Institutions in Korea.

course important to recognize the need for regulations governing such areas as safety and equitable income distribution, and for SOEs to pursue broader public service responsibilities. But it is also important to acknowledge that other methods use competition to achieve those goals, and that accurate, transparent accounting in SOEs prevents the waste of valuable resources.

2. How the MRFTA Deals with the Abuse of Administrative Power

2.1 Treatment of Activities of the State and Actions in Compliance with Law

The MRFTA applies to entrepreneurs (MRFTA Art. 1). An entrepreneur is a person who "conducts a manufacturing business, service business, or other businesses." This definition does not preclude public entities with administrative power such as the state or local governments. That is, to the extent that such public entities participate in the market as party to a business, they are subject to the MRFTA. However, the state or local governments as a sovereign or market regulator are not subject to the substantive rules of the MRFTA. Instead, the MRFTA contains explicit competition advocacy provisions to deal with monopolistic conditions created by the government. Competition advocacy refers to any actions other than explicit enforcement of competition law undertaken by the competition authority to promote competition. These actions may take the form of giving advice to other government agencies during the process of legislation, or participating in the regulatory reform or privatization processes to facilitate a competition friendly outcome. Activities to build a competition culture in general, such as undertaking national campaigns to demonstrate benefits of competition, or conducting research and publicizing the harm done by anti-competitive behavior, are other important examples of competition advocacy. Korea's experience with competition advocacy in regulatory reform is discussed in more detail in Section 3.

On the other hand, actions in compliance with the law or administrative orders may be exempt from MRFTA even if such actions have anti-competitive consequences. Article 58 (Lawful Acts Conducted Pursuant to Acts and Subordinate Statutes) states that "This Act shall not apply to lawful acts of an enterprise or an entrepreneur's organization conducted in accordance with other acts and subordinate statutes." For example, in the recent debate on the renewed government zeal for regulatory reform, the KFTC has emphatically reconfirmed that social and economic regulations aimed at supporting the disadvantaged. That is, the so called "ckakhan (good)" regulations that may inhibit open competition

but are firmly based on statute, are not the subject of regulatory reform from the perspective of competition policy.

Actions in compliance with law or administrative orders are not automatically exempt, however. Actions that unnecessarily and seriously limit competition, and go far beyond the spirit of the law, may come under the purview of the MRFTA. For example, in a case where the Korea Association of Beobmusa[50] Lawyers allocated cases to its members in an orderly fashion, and prevented its members from accepting cases from organizations that did not consult the Association in advance, the Supreme Court ruled such actions to be anti-competitive and subject to the MRFTA, even though those actions had been in compliance with Association rules, which in turn had legal basis under the Certified Judicial Scriveners Act.[51] While the MRFTA can, in theory, be used to prosecute serious anti-competitive practices in line with the law or regulations, in practical terms, competition advocacy would be important when the actions at issue have a firm legal basis. Further, in the telecom price fixing cases uncovered in 2005, the KFTC strongly refuted the "administrative order" defense made by the telephone companies, reasoning that the administrative order in question was merely a recommendation and not a binding order.[52]

2.2 Treatment of SOEs

State-owned enterprises, classified as public entities undertaking business, have never been explicitly exempt from the MRFTA. However, before the 1980s, the majority interpretation of Article 58 was that since SOEs had clear mandates under special statutes, and because they were regulated by their respective authorities, SOEs need not be regulated under the MRFTA. Further, until 1999, the MRFTA Art. 1 defined "business" subject to the MRFTA narrowly, by providing an explicit list of covered industries. When the MRFTA was first promulgated in 1980, this list included "manufacturing, retail and wholesale, transportation and warehousing businesses." This gave categorical exemption to major SOEs operating in public utilities and the financial sector. In 1990, the MRFTA was amended to include most industries, except primary industries.[53] Other businesses could be added to the list by the Enforcement Decree. This listing approach came under criticism for defining covered industries too narrowly, and was scrapped in 1999. Since then, all businesses

50) Beobmusa refers to certified scriveners.
51) Kim, D.J. (2002: 167-171). "A Study on Exemptions from the Monopoly Regulation and Fair Trade Act."
52) For more detail on the telecom price fixing cases, see Section 4.3.
53) The list included "manufacturing; electricity, gas, water, and construction business; wholesale, retail and repair services; catering; transportation, warehousing and telecommunication; finance and insurance, real estate and business services; education services, health and social welfare business; social and private services, domestic services, and briquette manufacturing.

in all fields have become subject to the MRFTA.

More recently, "competitive neutrality" has gained currency in the international community as the core concept for regulating SOEs. Competitive neutrality refers to a situation where "no entity operating in an economic market is subject to undue competitive advantages or disadvantages."[54] As private firms are increasingly competing in industries traditionally dominated by SOEs, ensuring competitive neutrality between SOEs and their private-sector rivals has become an important policy issue. At the same time, many emerging economies use SOEs as instruments to develop national champions through industrial policy. This has prompted their trade partners to attempt to incorporate competitive neutrality as an important principle in free trade agreements.

To ensure competitive neutrality, it is paramount that a government's commercial activities be separated from its non-commercial ones. If this isn't done, it would be difficult to enforce competition law against the government's commercial activities. Because of this, the best way to maximize transparency and accountability is often to incorporate commercial government activities into an entity that is independent from the government. If physical separation is difficult, a separate accounting system, at least, should be adopted. In the case of unincorporated entities conducting commercial activities, it is important that they identify the direct costs of their functions. It should be also be acknowledged that even when they operate in a competitive environment, SOEs have public service obligations, for which they should be adequately compensated in a way that avoids market distortions. By having separate premises and distinct accounting procedures, SOEs can be compensated for their public service obligations with a minimized risk of their using that money to cross-subsidize other non-commercial activities.

At the same time, competitive neutrality requires SOEs to earn market rates of return on their commercial activities, with their performance benchmarked against similar activities in the same industry. If they are allowed to operate in the face of persistently low profits or losses, SOEs would be able to undercut their private sector competitors. Competitive neutrality also means that government businesses must bear equivalent tax and regulatory burdens. Neutrality should be extended to the availability of finance. SOEs should be made to pay the same interest rate under similar circumstances. Competitive neutrality is impaired when SOEs receive outright subsidies or subsidized credit, or are able to obtain cheaper finance in the market because they are perceived to be low risk thanks to implicit government backing. Likewise, in the case of public procurement practices, enforcing a competitive, transparent and non-discriminatory bidding process is the most important factor in

54) OECD (2012a: 10). "Competitive Neutrality: National Practices."

ensuring competitive neutrality.[55]

The concept of competitive neutrality is flexible in that it acknowledges the need for government assistance to SOEs to fulfill their public service obligations. It arguably makes sense to apply the competitive neutrality benchmark only when: SOEs are engaged in commercial activities for which private sector competitors already (or potentially) exist; SOEs are nonetheless dominant; and the costs of anti-competitive practices outweigh the overall social benefits the SOE creates. The discussion on competitive neutrality shows that the concept is multi-disciplinary in nature, with its broad scope extending far beyond competition policy proper. Nevertheless, the Korean experience shows that subjecting SOEs to the full extent of competition law is an essential aspect of leveling the playing field between government-owned entities and private companies. KFTC's experience in enforcing competition law against SOEs is discussed in more detail in Section 4.

3. Regulatory Reform and Competition Advocacy in Korea

3.1 The Legal Provisions for Competition Advocacy

As explained in the preceding section, anti-competitive practices carried out by the government are not addressed through a strict enforcement of NRFTA rules, but rather through competition advocacy. Only a few competition laws in the world contain explicit mandatory provisions for competition advocacy. In the Korean case, the MRFTA provides three basic mechanisms for competition advocacy: mandatory consultation prior to the legislation of new regulations, a mandate to reform monopolistic markets, and mandatory competitive impact assessments prior to introducing new regulations.

The provisions of competition advocacy have been strengthened over time, as summarized in <Table 2-1>. They began with the mandatory prior consultation provision, which itself became more specific and detailed in the 1986 MRFTA amendment in defining the nature of anti-competitive factors caused by regulation subjected to prior consultation. Competition advocacy expanded to include rules and regulations in the 1996 amendment. With the formal separation of the KFTC from the Economic Planning Board in 1990, it became possible for other Ministries to consult with the KFTC directly, further strengthening the body's authority to conduct competition advocacy vis-a-vis other government offices. The provisions stipulating the mandate to reform monopolistic markets and the mandatory

55) For greater detail on competitive neutrality, see Appendix 2 at the end of this chapter.

competitive impact analysis were added in 1996 and 2009, respectively. On the basis of these strong legal foundations, the KFTC became actively involved in government initiatives for regulatory reform and the promotion of competition.

〈Table 2-1〉 Strengthening Competition Advocacy Provisions of the MRFTA

Year	Legal and Institutional Changes
1980	<Promulgation of the MRFTA, including Article 51 (former version of the current Art. 63)> - Consultation on Enactments of Acts: the chief-officer of the competent administrative authority shall seek, in advance, consultation with the *Economic Planning Board*, when he intends to propose legislation or an amendment of enactments containing anti-competitive factors, as well as when he intends to make approvals or other measures containing anti-competitive factors against an enterprise or an enterprise's organization.
1986	<Anti-competitive factors due to enactments that are subject to prior consultation provision is defined in greater detail> - Enactments or amendments, administrative approvals or measures resulting in "undue collaborative acts" and "exclusionary practices" by enterprises' organizations are subject to prior consultation.
1990	- Amendment of the MRFTA: Article 51 becomes Article 63 - Authority of the KFTC is strengthened: the KFTC become independent of the *Economic Planning Board*, and ministries can now directly consult with the KFTC, without first consulting the *Economic Planning Board*. - *The Committee of Economic Regulatory Reform (later the Regulatory Reform Committee)* is established. KFTC heads the Committee during 1997-1998.
1995	<Elevation of KFTC status> - The KFTC becomes a central administrative body, with its Chairman elevated to Minister status. The KFTC is therefore further empowered to conduct competition advocacy vis-a-vis other ministries through ministerial and vice-ministerial meetings.
1996	<Expansion of the coverage of the prior consultation provision and related KFTC authority> - In addition to undue collaborative acts and exclusionary practices of enterprise organizations, enactments or amendments restraining prices and terms of transactions, market entry or business activities, becomes subject to prior consultation. - Further, the competent authorities must notify the KFTC when they intend to enact or amend competition restricting rules or regulations. The KFTC can give advice regarding the rectification of such anti-competitive factors. Further, the KFTC can give similar advice even when there has not been any prior notification. <Article 3 is newly introduced into the MRFTA (Mandate to Reform Monopolistic Market Structures)> - The KFTC is to establish and implement action plans to promote monopolistic markets, and give advice to the chief-officer of competent authorities, regarding the competitive reform of such markets.

〈Table 2-1〉 Continue

Year	Legal and Institutional Changes
1998	<Enactment of the Framework Act on Administrative Regulations> - *The Regulatory Reform Committee*, directly reporting to the President, is established to oversee all regulatory reform work. The Chairman of the KFTC is a permanent member of the Committee.
2000	<Establishment of the Task Force for Reforming Anti-Competitive Regulation> - A task force devoted to competition advocacy under the KFTC is established as stipulated by the *Prime Minister's Decree*. The Task Force undertakes any investigative or research projects requested by the Regulatory Reform Committee. The Task Force also oversees anti-competitive rules and regulations at the regional level.
2009	<Competitive Impact Assessment> - "The Guidelines for Regulatory Impact Analysis" at the *Prime Minister's Office* were amended to include a competitive impact analysis as a part of the mandatory prior regulatory impact assessment.

Source: Compiled by the author, by consulting the amendment history of the MRFTA and the *White Paper on Fair Trade*, various years.

3.1.1 Prior Consultation

Article 63 of the Monopoly Regulation and Fair Trade Act (MRFTA) stipulates that when administrative agencies wish to propose or amend legislation, rules or other administrative measures that restrain competition, they should consult the Fair Trade Commission in advance. Where restraint of competition is recognized, the KFTC may give advice to the heads of the relevant administrative agencies on how to rectify any anti-competitive elements. The same applies to provisions already enacted or amended without prior notice or requests for consultation. The MRFTA thus provides the KFTC with a firm legal foundation to intervene in the process of regulatory reform.

The Korean Fair Trade Commission has put a lot of effort into implementing Article 63, seeing it as an important pillar of the Commission's competition advocacy role. As a result, it has been quite influential in shaping the regulatory process to reflect competition concerns. This role was strengthened in 1990 when the KFTC became a central administrative agency, independent from the former Economic Planning Board, and again in 1995 when the status of its chairman was raised from vice-ministerial to ministerial level. Since then, the KFTC has actively participated in ministerial and vice-ministerial meetings to present its views. The KFTC Chairman is also one of the four members of the Economic Ministries Council, which advises on regulations that fall under the remit of the Ministry of Finance and Economy. From 1997 to 1998, the KFTC headed the inter-ministry Committee of Economic

Regulatory Reform. A task force attached to this Committee made over 100 proposals for reform.

In 2000, the Task Force for Reforming Anti-Competitive Regulation, a body devoted to competition advocacy, was established under the KFTC as part of the Prime Minister's Decree. The Task Force undertakes any investigative or research projects requested by the Regulatory Reform Committee, and tackles anti-competitive rules and regulations at the regional level. The latter task became especially salient as criticism mounted that efforts by central government to shed anti-competitive regulations were being undercut by local governments, which simply reinstated the rules at the regional level.

The number of prior consultations increased from just 430 cases in 2004 to 1,178 cases in 2010. In 2010, the KFTC submitted opinions on 55 cases (4.78%), recording a success rate of 76.8%. The success rate increased to 87.9% in 2011 (see <Table 2-2>). The KFTC also monitors public notifications and directives on a quarterly basis, to spot any anti-competitive regulations that may require remedial action. This led to recommendations that 25 public notifications and directives be reformed in 2010. Examples include a regulation limiting the number of financial organizations that can issue certification of the capital status of information and communications businesses, and a regulation limiting sales of medicine to certain locations.[56)]

Some of the major recent overhaul efforts include reviewing anti-competitive regulations at the regional government level, with the aid of academic associations. As a result, the KFTC and local governments at the metropolitan and provincial level agreed to reform 41 anti-competitive regulations throughout 2009-2010. At the district and county level, a total of 985 ordinances were designated for reform. In 2011, these efforts led to an 87% success rate for governments at the metropolitan and provincial levels, and a 78.48% success rate for governments at the district and county levels.[57)] These success rates are fairly high, given the average success rates in similar initiatives of 57% for developing countries and 75% for developed countries.[58)]

56) KFTC (2011: 580). Trace of Market Economy Development: Korea Fair Trade Commission, a History of 30 Years.
57) KFTC (2012: 267-268). White Paper on Fair Trade.
58) Advocacy Working Group (2002: 64). "Advocacy and Competition Policy." Report presented at International Competition Network Conference's Conference, Naples, Italy.

〈Table 2-2〉 Trend in prior consultation

Year	Total Number of prior consultations	Number of KFTC submissions (%)	Success rate (%)
2002	381	36(5.7)	22(61.1)
2003	361	49(7.5)	42(85.7)
2004	430	44(10.2)	37(84.1)
2005	658	46(12.7)	38(82.6)
2006	634	36(9.4)	34(94.4)
2007	635	45(7.1)	30(66.7)
2008	827	36(4.4)	18(50.0)
2009	1,097	29(2.6)	27(93.1)
2010	1,178	55(4.7)	46(83.6)
2011	1,624	33(2.0)	29(87.9)

Source: KFTC (2012: 281), KFTC (2007: 237)

Note: Number of prior consultations is based on legislation introduced by government ministries only, and does not include those introduced by National Assembly representatives. Including that legislation would raise the total number of, e.g., prior consultations to 2,096 cases in 2010 and 1,761 cases in 2011.

In a recent survey commissioned by the KFTC and undertaken by the Korea Society for Regulatory Studies, most common forms of competition-restricting regulations at the regional level were found to be associated with the promotion of regional industries or certain social agendas.[59] Such regulations work to the advantage of specific entrepreneurs by firstly introducing an ordinance, presumably with a social agenda (e.g., supporting regional construction, environmentally friendly agriculture or other green growth projects, cooperatives, women's business groups, and social enterprises). Then, a specific entrepreneur is favored, by being designated as eligible to receive subsidies under these ordinances. Often, subsidies go beyond the purpose of supporting R&D, community development or environmental protection to actually cover production costs, which has a direct effect on competitors in the private sector. By protecting specific producers, these subsidies serve to significantly restrict competition rather than promote an industry in general, especially if the selection criteria and process is based on regional or personal ties rather than merit. Examples include the Specialty Agricultural Products Exhibition Shop, set up by the Daegu City Ordinance, which restricted participation

59) Kim, J.K. "Anti-competition Regulations of Regional Governments and their Reform." A Research Report submitted to the KFTC. 2013.

by specifying tight criteria for entry; and the Designation and Support of Special Development Projects Ordinance in Jeju, which gave a competitive advantage to firms selected to undertake certain development projects. It seems certain that there are better, less anti-competitive ways to promote social goals or regional development.

3.1.2 Mandate to Reform Monopolistic Markets

In 1999, the MRFTA was amended to adopt Article 3, which gives the KFTC the mandate to reform monopolistic or oligopolistic market structures. The provision stipulates that the KFTC "shall establish and implement action plans to promote competition in markets in which monopolistic or oligopolistic situations have continued for a long time in relation to the supply or demand of goods or services." The KFTC may also "give opinions to the chief officers of the competent administrative authorities as to the introduction of competition or other measures necessary to improve market structures, where it appears to be necessary for the Commission to carry out" the above "action plans." In addition, the KFTC shall research the market structures and announce the results in order to establish and promote the "action plans." This provision gives power to the KFTC to effectively carry out competition advocacy in areas where monopolistic conditions are already entrenched, in addition to the ability to screen regulations that may have anti-competitive effects prior to their legislation.

Most recently, the KFTC's main emphasis has been on removing entry barriers in industries where a monopolistic market structure has become entrenched. For example in 2009, the KFTC and relevant Ministries agreed to allow private operators' entry into the market of liquefied natural gas (LNG) refueling, which had formerly been a monopoly of the Korea Gas Corporation, an SOE. Further, in a move that ended a 40 year duopoly, two new tax cork producers were designated. Altogether, a total of 26 projects to lower entry barriers, including one related to marine shipping by large, bulk consignment shippers, were submitted to the Presidential Council on National Competitiveness. In 2010, the KFTC successfully concluded an agreement with the relevant authorities to remove entry barriers to services that employ large numbers of people, such as the LPG import business, and to expand the realm of private competition in what had been government monopolies. The latter provision led to an increase in the number of institutions that can provide precision safety diagnosis and 12 other projects designed to eliminate public monopolies.[60)]

60) KFTC (2011), op. cit.

3.1.3. Competitive Impact Assessment

As the reform effort expanded beyond economic regulations to non-economic issues, the regulatory reform project was transferred to the Prime Minister's Office. Although there had been concerns that this shift in focus would narrow the scope of input from competition policy, the Chairman of the KFTC still holds a permanent position on the Regulatory Reform Committee. According to the Framework Act on Administrative Regulations, a regulatory impact assessment must be undertaken prior to the enactment or amendment of a regulation. In 2009, the Guidelines for Regulatory Impact Analysis at the Prime Minister's Office were amended to include a competition impact analysis as part of this impact assessment. This strengthened the role of the KFTC, which is responsible for carrying out the impact analysis.

The KFTC conducted a total of 415 competitive impact assessments in 2011, and 58% of its proposed reforms were reflected, a fairly high success rate compared with the OECD average (see <Table 3.3>). It is interesting to note that while the number of assessments increased from 2009 to 2011, the KFTC's submissions for reform declined, with the success rate remaining stable. This seems to suggest that any new regulations are less likely to contain anti-competitive elements, and, by further implication, that competition advocacy in the area of regulatory reform has been quite effective.

〈Table 2-3〉 Trends in Competitive Impact Assessments

Year	CIA cases	Submission for reform (cases)	Success rate (%)
2009	330	25	68.6
2010	277	36	54.8
2011	415	13	58

Source: KFTC (2011: 580), KFTC (2012: 276)

The competitive impact assessment is undertaken in two stages. First, a preliminary inspection is undertaken to identify potential anti-competitive effects of proposed regulation. This is achieved by checking whether the regulation produces any of the following four categories of anti-competitive effects:

1) The proposed legislation limits the number or range of suppliers (e.g., awards exclusive grants, licenses or permits, limits eligibility, significantly raises costs of entry or exit, creates a geographic barrier).

2) The proposed legislation limits the ability of suppliers to compete (e.g., puts controls on price, advertising, or quality standards, raises production costs for some suppliers (newcomers) compared to others (incumbents).
3) The proposed legislation reduces the incentive of suppliers to compete (e.g., creates self-regulatory or co-regulatory regimes, requires information on supplier outputs, prices or costs to be published, provides exemption from competition law).
4) The proposed legislation limits the choices and information available to consumers (e.g., limits consumers' ability to decide who they buy from, reduces customer mobility between suppliers by increasing the cost of changing suppliers, fundamentally changes information required by buyers to shop).

If anti-competitive effects are found in any of the four areas above, an in-depth investigation is conducted. In this second stage assessment, the relevant market is defined and the potential overall impact of the proposed regulation on competition is considered in detail. If the social cost of limiting competition is deemed to be greater than the social benefits of the regulation, the search begins for alternative ways to achieve the regulatory goal while minimizing any negative, anti-competitive effects. The competitive impact assessment process includes field visits, meetings with stakeholders and consultations with related industries.

One significant example of a competitive impact assessment that reflected the KFTC's opinion is the reform of the designation system for Certified Electronic Documents Centers. The KFTC's reform measure was included in an amendment to the Framework Act on Electronic Commerce, which had restricted entry to the industry by stipulating that only companies whose business plans had been approved could gain the documents center designation. Another example is the Act on Distribution and Price Stabilization of Agricultural and Fishery Products, which had proposed that the government should allow wholesalers to limit the method of bidding and price bands for successful tender bids when there was a sudden increase or decrease in the price. The KFTC recommended that the government should only impose direct controls on the prices of agricultural goods in highly exceptional situations such as natural disasters. The reform of the proposed amendment to the Enforcement Decree of Medical Appliances, which had prohibited advertising using free gifts, is another good example of the success of competitive impact assessments. The KFTC was of the opinion that such advertisements provided useful information about the product to consumers, and a uniform ban on them would act as an entry barrier by limiting the freedom of suppliers.[61)]

61) KFTC (2012), op. cit.

3.2. KFTC's Role in Regulatory Reform

It is unusual for competition law to contain such explicit and mandatory competition advocacy provisions. That this situation exists in Korea attests to the fact that the founders of MRFTA considered competition advocacy to be an indispensable role of competition authorities. The economic conditions in which the MRFTA was born provide a clue as to why competition advocacy, especially with regards to government intervention in the economy, was considered so important. As Korea fumbled its way from a government-led development paradigm towards market-led growth, it had to shrug off the chains of government regulation that had shackled many industries, hindering the emergence of a vibrant private sector.

In a bid to foster economies of scale, government policy frequently placed restrictions on entry to certain industries. At the same time, price stabilization had been a policy priority throughout the 1970s, especially due to the two oil shocks, and the government found price controls to be a convenient tool in achieving this. The now defunct Price Stabilization and Fair Trade Act was promulgated in 1975 to stabilize prices after the first oil shock. The government applied this law to regulate prices in monopolistic markets, which the Act defined as industries with total sales of more than KRW 2 billion, in which the top three firms held a collective share of more than 60%.

However, by directly intervening in price setting while failing to address the monopolistic structure of markets, the Act failed to bring down prices. Enforcing entry barriers and price controls actually ended up creating monopolistic markets rather than weakening them. Regulations once adopted to promote new industries now served to protect entrenched incumbents. Extensive regulations also created a wave of wasteful rent seeking activities and vested interests. As a result, prices were not stabilized, precipitating even more government intervention to steady the market.

A good example of this vicious circle is the alcohol industry, which required decades of regulatory reform to make it competitive. Until the late 1990s, the alcohol industry was among the most heavily regulated of all. No fewer than 103 types of regulations plagued the industry.[62] While alcohol is universally recognized as having health and safety concerns that require some regulation, many of the regulations imposed on the industry in Korea before the late 1990s seriously impaired competition without seriously addressing the social concerns.

Much of the regulation in the alcohol industry consisted of entry restrictions

62) For details on the regulatory reform of the alcohol industry, see Ji, D.C. (2004).

such as limitations on the number of licenses issued, minimum production floors, and legal regional monopolies. These entry restrictions were adopted initially to prevent "excess competition" from small firms who supposedly couldn't produce high-quality products. However, persistent entry restrictions allowed a few large firms to dominate the industry, and had a highly negative impact on competition. Promotion of competition in the industry had to begin with the elimination of these regulations, which were fostering monopolies and various market distortions. As it would have been extremely difficult to scrap all the regulations at once, the industry was deregulated over the course of a decade. Details of regulatory reform in the alcohol industry are listed in <Box 2-1> below. Deregulation led to the entry of many new companies, especially small ones, which in turn saw the emergence of more differentiated products and brands, and lower prices.

〈Box 2-1〉 Examples of Pro-competitive Regulatory Reform in the Alcohol Industry

- New licenses were issued beginning in 1991, then in 1993-1994.
- Minimum sized stipulation on production floors were eliminated during 1990-1995.
- Detailed production specifications were abolished during 1990-2002.
- The Mandatory Purchase system, whereby soju wholesalers were forced to procure more than 50% of their total soju stock from their home city or country, was abolished in 1996.
- The regional (city, province) monopoly system for rice wine was abolished completely in 2001 through the implementation of the Omnibus Cartel Repeal Act.
- Two more new firms were designated as tax cork producers in 2010 and 2011. This market had been monopolized by two incumbents for more than 40 years.
- Internet sales of traditional wine were allowed from 2010.

Source: Ji, D.C. (2004); KFTC (2012).

It is easy to see why the normal enforcement of competition policy would have been difficult in the alcohol industry, and that deregulation or regulatory reform had to take place before effective enforcement could be carried out. As it would have been equally challenging to enact laws that were administered by different Ministries while also being subject to competition law, not lease because the industries under those Ministries' purview could have fallen prey to regulatory capture, a specific mechanism to address the problems of administrative restrictions had to be to found. The drafters of MRFTA found the answer in the prior consultation provision, which, as discussed above, was expanded and strengthened in the years following the first promulgation of the MRFTA.

To justify the need for the competition advocacy provision, the drafters of the MRFTA took pains to show, through extensive field studies, that there genuinely was a close relationship between the regulated industry (represented by various

industry associations and cooperatives) and the regulating Ministries.[63] Competition advocacy therefore played a pivotal role in restricting the spread of administrative restrictions and allowing market mechanisms to take root in the Korean economy. In so doing, it paved the way for Korea to make its transition from a government-led to a market-based economy.

Increasing trade liberalization and globalization required further structural reforms to promote competition in the 1990s; as the new civilian government took power in 1993, regulatory reform became a national priority. The Omnibus Cartel Repeal Act of 1999 represents a landmark reform of this era. This is an example of the KFTC using its quasi-legislative power to eliminate, in a single swoop, most of the exemptions from the MRFTA that were still prevalent at the time. Among many other things, the Act revised a provision allowing premium-fixing by insurance companies, and limited coordination directives to cases of compliance with intergovernmental agreements or the export of military equipment. Further, the Act abolished governmental coordination of bidding for overseas construction projects and the territorial allocation of unsterilized rice wine.[64]

The law also ended the long time practice of fee-setting arrangements in a number of professional services, such as lawyers, certified public accountants, architects, certified tax accountants, patent attorneys, customs brokers, certified labor services, administrative recorders and veterinarians. According to a follow-up survey conducted by the KFTC in 2003 under its Clean Market Project, although fees charged by professional service providers became somewhat differentiated depending on the range and quality of services provided, a substantial overall decrease in the fees was not forthcoming even after these cartel-like practices had become illegal.[65] Some professions were actually able to reverse the decision, with architects using fee-setting arrangements again from 2001, albeit in a less restrictive form. For notaries and engineers, too, fees are set through regulation rather than market competition. Eliminating regulations restraining competition in professional and services sector remains a challenge.

In carrying out these competition advocacy activities, the KFTC was assisted by public research think tanks and academia, which provided intellectual ammunition and helped build social consensus on the necessity of competition policy. Having an intellectual basis supported by economic analysis is critical in competition advocacy, as officials of other Ministries have to be convinced, vested and entrenched interests

63) Lee, K.U. (2003: 191-215), "Introduction of Competition Policy" in Kim, K.S ed. Cases in Policy Research by KDI: Recollections of the Past 30 Years. Korea Development Institute
64) KFTC (2011: 63) op.cit
65) OECD (2007:2), Reviews of Regulatory Reform: Korea: Progress in Implementing Regulatory Reform.

overcome, and the general public won over.[66]

In particular, during the MRFTA's early years, the role of the Korea Development Institute (KDI) was crucial. The KDI collaborated in drafting the MRFTA, and was a key driver of regulatory reform during the 1980s and the 1990s. According to testimony from a pioneering competition policy expert, the KDI's role in preparing the ground for competition law dates back to the 1970s, when the Economic Planning Board commissioned the KDI to select monopolistic industries that should be subject to the Price Stabilization and Fair Trade Act of 1975. During the drafting of the MRFTA, many compromises were necessary between the economically minded KDI experts, who foresaw a progressive strengthening of the implementation, and the legalistic bureaucrats who wanted stronger regulation. Further, when the KDI initiated the 1988 regulatory reform process, it chose the sector-independent KFTC as its government partner.[67] It is important to note that the first initiative for regulatory reform came from the KDI, which was able to provide an intellectual basis for promoting competition, rather than any government Ministry.

4. Enforcement of MRFTA with Respect to State Owned Enterprises

4.1 KFTC's Policy Towards SOEs

Since different countries use different definitions, it is difficult to describe exactly what SOEs are. Several laws are involved in overseeing the management of public organizations in Korea, but the main legislation regulating SOEs is the Act on Management of Public Organizations (2007). This Act defines public organizations as any bodies that meet the following criteria: those established by law and to which the government provides financial assistance; those whose revenues from government-mandated activities are greater than 50% of their total revenue; those in which the government has a majority share or minority share and the power to appoint directors; those that are established by any of the public organizations defined above. Of these, public organizations with more than 50 employees and whose "own revenue" (i.e. excluding revenues from government mandated activities) is greater than 50% of total revenues are categorized as SOEs. As of 2010, there were 286 such SOEs in Korea. Among this group, companies that have assets exceeding KRW 2 trillion and whose "own revenue" is greater than 85% are

66) For details on how the KFTC built up its capacity for expert economic analysis, see the chapter on "Economic Analysis for Competition Policy" in this volume.
67) The 10 industries that came under scrutiny were advertising, cosmetics, bus transportation, automobile repair, finance, securities, insurance, deep-sea fishery, shipping and construction.

categorized as "market-oriented SOEs." As of 2010, 44 public organizations were designated as market-oriented SOEs.

This is a narrow definition of SOEs, as it does not include those established by regional or local governments and associations or cooperatives that are closely affiliated with the government. Further, this definition neither includes the Korea Broadcasting Corporation nor the Korea Educational Broadcasting Corporation, which are regulated separately by special laws. According to an internal memo of the KFTC, the number of "public enterprises" that were potentially subject to its ex-officio investigations came to more than 700. This included companies in which the government had minority holdings, or that were owned by regional governments, partially government funded (e.g., public research institutions and hospitals), affiliates of SOEs, or quangos such as cooperative federations, incorporated foundations, and associations with a close affiliation with the relevant government department. Therefore, the public sector under the purview of the MRFTA is much broader than the narrow, legal definition of SOEs.

As the preceding discussion notes, enforcement of the MRFTA against SOEs strengthened over time, especially with the beginning of full-scale regulatory reform in the 1990s, and gained further momentum from the economic restructuring and privatization that took place following the Asian financial crisis. The KFTC conducted 10 rounds of ex-officio investigations of unfair trade practices of SOEs during the 1997-2002 period. Additional ex-officio investigations of several large SOEs and more than 20 regional SOEs were undertaken in 2004 and 2009. Based on the first rounds of ex-officio investigations in the late 1990s, the KFTC in 1999 established a list of screening criteria to identify anti-competitive elements in unfair trade practices by SOEs.[68] The list was prepared with the aim of ensuring objective and transparent enforcement, and preventing anti-competitive practices ex-ante by publicizing to SOEs and their contractors the kind of actions that would result in prosecution.

Ex-officio investigations of SOEs are high on the KFTC's agenda once again in 2014. The KFTC is placing special emphasis on regulating anti-competitive trade practices such as unfairly exploiting a trade position and providing assistance to affiliated firms or individuals with special connections. Privatized former SOEs in market-dominant positions will also be subject to investigation.

SOEs were categorically exempt from being designated "market dominant," but this changed in 1993 when they became subject to the same designation as private firms.[69] Market dominant firms are prohibited from abusing their dominance according to Article 3(2), which lists the following specific categories of

68) KFTC (1999), "Judging Criteria for Unfair Trade Practices of Public Enterprises."

anti-competitive conduct: setting unreasonably high prices compared to changes in market conditions, unreasonably withholding supplies, unreasonable interference with the business activities of other entrepreneurs, unreasonably impeding the participation of new competitors, and engaging in transactions that unfairly exclude competitive entrepreneurs or that entail considerable harm to the interests of consumers. Categories or standards for abusive acts are determined by the Presidential Decree.

Enforcement against SOEs under this provision was further strengthened in 2001 when the Enforcement Decree of the MRFTA was amended to include, as a category of unreasonable interference in the business activities of other entrepreneurs, the unreasonable limiting of or refusal to give access to "essential facilities". Many essential facilities, including telephone networks, railways and power systems, are owned by SOEs or privatized, former SOEs. This provision, however, has not yet been invoked in a competition case.

SOEs meeting the relevant criteria are also prohibited from cross-shareholding and cross-debt guarantees, a provision originally targeted at large private business groups. Article 9 of the MRFTA prohibits enterprises with total group assets of more than KRW 5 trillion from cross-shareholding with another independent company. Fourteen SOEs were subject to this prohibition as of 2014.[70] Further, Article 10(2) prohibits such enterprises from cross-debt guarantees. Leaving aside the debate on whether it is desirable for such corporate governance provisions to be included in the competition law, this is an example of ensuring regulatory neutrality between SOEs and their private competitors.

4.2 Regulating Anti-competitive Practices of SOEs

The most frequent category of violation committed by SOEs comes under MRFTA Article 23 (Prohibition of Unfair Trade Practices). This provision prohibits enterprises from: discriminating against or refusing to deal with certain commercial partners; the unfair exclusion of competitors; unfairly coercing or inducing customers of competitors to use the enterprise's services; unfairly taking advantage of its position in trade; trading under terms and conditions which unfairly restrict or disrupt

69) In the same year, the designation system was changed to a system where the entrepreneur can be presumed to be dominant in the market when its market share in the relevant market is greater than 50%, or if the sum of three entrepreneurs in the relevant market exceeds 75%. In the latter case, a firm whose market share is less than 10% is excluded. An entrepreneur whose annual sales or procurement in the relevant market is less than KRW 4 billion is excluded (MRFTA Art. 4).

70) They are: Korea Land and Housing Corporation, Korea Electric Power Corporation, Korea Expressway Corporation, Korea Railroad Corporation, Korea National Petroleum Corporation, Seoul Metropolitan Rapid Transit Corporation, Korea Gas Corporation, K-Water, Nonghyup, Incheon Development and Tourism Corporation, Incheon International Airport Corporation, Seoul Metro, Busan Port Authority, Korea District Heating Corporation.

business activities; assisting a person with a special interest or other companies by providing advanced payment, loans, manpower, immovable assets, securities, goods, services, rights to intangible properties, or otherwise transacting under substantially favorable terms. These are illustrative examples; any other act which threatens to impair fair trade is prohibited, with the categories or standards for unfair trade practices determined by the Presidential Decree.

KFTC's investigations show that of the unfair trade practices seen at SOEs, the most common were various forms of unfairly exploiting their dominant position in trade and providing favorable terms to affiliate firms. For example, the KFTC found that 98% of all transactions between SOEs and their affiliate firms were based on private contracts rather than open bids. Ultimately, institutional changes, such as reforms to laws that allow SOEs to execute private contracts with their affiliates, will be needed. Some limitations have already been imposed in this regard. A 1999 reform carried out according to KFTC recommendations[71] has had the effect of expanding market opportunities in areas formerly monopolized by SOEs and their affiliate firms. As there is a danger that, vis-a-vis their private competitors, affiliate firms receiving preferential treatment from SOEs could in effect be benefiting from government support for SOEs public service obligations, this is an area that requires special attention in the context of competitive neutrality. In light of this, the emphasis on regulating support for affiliate firms in the KFTC's 2014 agenda seems well judged.

As large-scale buyers, SOEs also have a role to play in preventing bid-rigging in public procurement. To prevent the formation of cartels among bidding firms, the KFTC recommended that SOEs should include in their notice of tender a clause claiming indemnity if bid-rigging is found. The Korea Electric Power Corporation (KEPCO) and K-Water introduced such a clause in 2011.[72] These examples show the close relationship between competition-friendly regulatory reform and competition law enforcement. Strong enforcement leads to the uncovering of anti-competitive practices, which in turn becomes the basis of detailed recommendations for more structural reform. At the same time, regulatory reform enhances the ability of competition agencies to enforce the law.

Some representative cases of the abuse of dominant trade positions by large SOEs are presented in <Box 2-2>. Common practices include SOEs unilaterally setting unfavorable terms of trade, such as delays in payment, contract cancellations, contracts containing unfair terms, and discrimination in favor of affiliate firms. One example of this was the refusal of KEPCO to provide opportunities for engineer training, a prerequisite for firms looking to bid for its contracts. As an electricity

71) KFTC (2011: 412), op. cit.
72) KFTC, White Paper on Fair Trade, 2012: 202-203.

provider, KEPCO could have been deemed an essential facility, but the KFTC did not explicitly invoke the essential facility clause. In fact, the KFTC has yet to invoke the essential facility doctrine in any of its decisions.

In <Box 2-2>, cases of preferential treatment by SEOs to affiliate firms are presented. For example, the partially privatized KEPCO provided unfair favors to an affiliate by subsidizing its labor cost. Similarly, the Korea Land and Housing Corporation and the Korea Gas Corporation subsidized the real estate rental costs at one of its subsidiaries. Using private contracts rather than open bidding to award contracts at above-market rates is another common form of support SEOs offer their subsidiaries. Such preferential treatment by market dominant SOEs serves to artificially inflate the competitiveness of subsidiaries, ultimately crowding out private competition or preventing entry by new firms. Further, unfair dealings such as these mean that SOE resources that could have been used to lower prices, invest in new facilities, or adopt cost-cutting technology and management systems, are lost.

〈Box 2-2〉 Examples of unfairly taking advantage of trade position

1) Unfair trade practices by Korea Land and Housing Corporation (LH)*

LH is designated as market dominant in housing construction. In 1998, a KFTC inspection found LH to be abusing its dominant market position via various unfair trade practices in its transactions with suppliers of construction material. These abuses included unilaterally cancelling orders on elevators and other construction materials without paying compensation, delaying payments, refusing to pay compensation for indirect costs arising from its changes in design, and refusing to pay interest on returned payments due to contract cancellation. On account of these violations and LH's discrimination in favor of affiliate contractors, achieved by making irregular advanced payments to them, a surcharge of KRW 276 million was imposed.

2) Delayed payments by Korea National Petroleum Corporation (KNPC)**

KNPC has a monopoly in the exploration, drilling, and development of petroleum in Korea, thus also enjoying a monopsony position in piping works, the non-destructive inspection of pipes and various other related construction works. Contractors wishing to participate in these works have little bargaining power to resist unfair demands by the KNPC. In 2003, the KNPC failed to pay compensation for contract delays it was liable for under the contract for under-sea non-destruction inspection. At the same time, the KNPC unilaterally reduced payments for the construction of an oil storage tank by unduly changing construction specifications after the work was completed. A surcharge of KRW 20 million was imposed for the two violations.

〈Box 2-2〉 Continue

3) Refusal to deal by Korea Electric Power Corporation***

In its bidding contracts with electric work subcontracting firms, KEPCO stipulated that the bidding subcontractors had to hire a certain number of engineers who had completed training in live wire operation at training institutions designated by KEPCO. At the same time, KEPCO selected trainees using its own criteria, and dispatched them to electric work subcontracting firms by region. The Corporation subsequently recognized only these trainees as live wire operation engineers, denying training opportunities for other engineers.

The KFTC concluded that this constituted a refusal to deal by KEPCO, with respect to subcontracting firms that wanted to bid for KEPCO's electric work orders. The KTFC recommended a series of corrections.

Source: * KFTC Case No. 9805독관0763
** KFTC Case No. 2004독관3679.
*** Lee, J.H. (2005: 74-75); KFTC Case No. 9706독관0963.

〈Box 2-3〉 Unfair Assistance to an Affiliate Firm by KEPCO (2001)

1) Korea Electric Power Corporation (2001)*

KEPCO over-priced its indirect labor costs in dealing with its subsidiary, KEPCO Plant Services and Electric Engineering Ltd (KEPCO KPS). KEPCO enjoys a dominant position in electric power generation and related industries, and owns several subsidiary firms. For example, it still has a monopoly in power transmission, distribution and sales. Further, KEPCO has monopsony power in machinery and equipment for electric distribution, constituting around 80-90% of total demand. KEPCO was given a correction order, and was fined KRW 3.6 billion.

2) Korea Land and Housing Corporation (2003)**

The Korea Land and Housing Corporation provided unfair economic advantage by renting out real estate to a subsidiary, the Korea Construction Management Corporation (KCMC), at more than half the market rental rate. In 2003, the country's 556 construction inspection companies faced severe competition, having all been hit by a slump in demand in the wake of the economic crisis. The KCMC itself was facing management difficulties. Under the circumstances, support from LH would have given a substantial competitive edge to the KCMC.

3) Korea Gas Corporation (KOGAS)***

KOGAS is designated as market dominant; it has a monopoly in natural gas supply in the Korean market, and has monopsony power in the construction of gas-supply-related facilities. The unfair advantages that KOGAS provided the Korea Gas Technology Corporation, one of its four subsidiaries, included an uncontested contract for the construction of gas supply facilities, resulting in a much higher price than would have been the case in an open bid (1998, 2008). KOGAS also leased apartments to Korea Gas Technology Corporation employees without charging rent. Nor did KOGAS collect any maintenance fees on an office building rented out to the Korea Gas Technology Corporation.

Source: * KFTC Case No. 2001거감0099.
** KFTC Case No. 2003독관2338
*** KFTC Case No. 9904독관0497, 2001조일0226, 2007조이1374

4.3 KFTC's Role in Privatization

As is common in many developing countries, Korea also relied heavily on SOEs for investment during the early years of the country's development. SOEs constituted around 33% of total fixed capital formation in the mid-1970s[73], compared to around 8.6% in 2012.[74] The privatization of SOEs in Korea started as early as 1968, and formed an important part of regulatory reform implemented by the new government in 1993. However, the results were less than impressive. Fully fledged privatization began, with a renewed sense of urgency, as part of the fundamental economic restructuring that took place in the aftermath of the Asian financial crisis. Between 1998 and 2002, eight SOEs, some of which had resisted past attempts at privatization, and 66 SOE affiliates were privatized.

The privatization plan of 1998-2002 was overseen by the inter-ministerial Committee for Privatization of Public Enterprises. The Committee, headed by the Minister of the then Ministry of Strategy and Budget (MoSB), constituted the Department Head of Government Reform of MoSB, Vice Ministers from the Ministries regulating relevant SOEs, the Vice-chairman of the KFTC, the Vice President of the Korea Development Bank and two participants from the private sector.[75] It was significant that the KFTC could directly participate in the privatization process from the planning stage. Efforts by the Committee to devise an appropriate institutional environment including competitive market conditions, the continuance of public services, and rational price mechanisms prior to privatization set its efforts apart from previous privatization drives.

The KFTC set up a special taskforce, which was charged with drawing up plans to introduce competition in SOE-dominant sectors, in accordance with four principles: the elimination of regulations restricting market entry or allowing interventions in pricing; the separation of vertically integrated SOEs by region or function; the application of the same M&A review principles to SOEs; and strengthening the monitoring of abuses of market-dominant positions or unfair trade practices among privatized entities.[76] These principles were established to prevent public monopolies turning into regulated private monopolies. In short, the main role of competition policy in privatization is ensuring competitive market conditions take

73) Sakong, I. and Song, D.H. (2003: 135), "Reforming Corporate Governance of SOEs" in Kim, K.S ed. op. cit.
74) Bank of Korea 2014. Total fixed capital formation here refers to that of 169 non-financial SOEs (over 50% of (sales/cost) is compensated by the government or proportion of sales to the government is less than 80%), categorized according to the guidelines of the 2008 System of National Accounts (SNS) by the Bank of Korea to estimate public sector financial account.
75) Park, H. and S. Park. (2011: 91), Evaluation of Privatization of SOEs and Future Challenges, Korea Institute of Public Finance.
76) Ju, S.S. (2002: 15), "Privatization and Competition Policy," Fair Trade

root in the privatized industry, rather than participating directly in the privatization procedure itself (e.g., issuing and selling shares). The competition authority needs to consider the competitive effects of suggested privatization methods, given the particular details of the relevant market structure and governance of the relevant SOE. As the competitive effects of different privatizations depend on many specific circumstances, it's not realistic to declare certain methods of privatization anti-competitive or otherwise in advance.

In accordance with the principles it has set, the KFTC presented views on how to introduce competition in the utilities sector (with respect to the privatization of the Korea Gas Corporation (KOGAS), Korea Telecom (KT), Korea Electric Power Corporation (KEPCO) and KT&G, contributing to the formation of a competitive market structure in the industries in which these SOEs operated.

With respect to the Korea Gas Corporation, which in the end was only partially privatized, the KFTC recommended structural separation of its wholesale, pipes and retail sectors, along with the adoption of an Open Access System, where the sharing of essential facilities would be obligatory. For KT&G, the KFTC recommended the abolition of its monopoly on tobacco manufacturing, along with changing the tobacco price approval system to a notification system. Both measures were reflected in the 2001 amendment of the Tobacco Business Act.[77)]

In the case of the privatization of Korea Telecom, the KFTC suggested a plan to enhance competition by dividing business units by geographic coverage (e.g., by intra-city, inter-city, and international call services) and selling them separately.[78)] Although this recommendation was not accepted at the time due to technical difficulties, KT became completely privatized by 2002 (see <Box 2.4> below for details on introducing competition in the telecommunication sector).

77) White Paper on Fair Trade (2002 : 141-142).
78) Ibid, pp. 15-17.

〈Box 2-4〉 Introducing Competition in the Telecommunications Sector

Competition in the telecoms sector was introduced early on when Dacom was allowed to enter the international call service market in 1991. Subsequently, Dacom was allowed to enter the long distance call service market in 1996, and Hanaro was allowed to enter the local call service market in 1999. Further, the sector became open to foreign competition in 1998. Thus, KT was already exposed to competition before it became fully privatized in 2002 through a share flotation. This complete privatization of Korea's telecoms sector is remarkable given that many developed countries still haven't succeeded in fully privatizing their telecoms sectors.

Reforms since 2000 include the introduction of number portability, local loop unbundling, a policy framework for Voice over Internet Protocol (VoIP) and universal service, as well as the use of long-run incremental costs to determine interconnection charges. These changes have substantially improved competitive conditions in the industry, which no longer has any entry restrictions.

Source: Park, H. and S. Park (2011: 211-218).

The KFTC enforced competition law vigorously in the telecommunications sector even after the complete privatization of Korea Telecom. A prominent example is the three price-fixing cases from 2005.[79] In the first, to narrow the price difference between the two operators in the local call market, Hanaro agreed to increase its tariff rates in exchange for receiving subscribers from KT. The companies were fined a total of KRW 115,196 million, with KT receiving the heavier fine (KRW 113 billion), the highest fine imposed on a single firm to date. In the second, three operators in the international call market, acting in response to low tariff levels offered by resellers, colluded on the level of discount rates offered for several destinations. The companies were fined KRW 5.4 billion. Finally, four operators in the long-distance call market, in a bid to minimize tariff-based competition, conspired to ensure they all offered the same deals to consumers seeking an unlimited, flat-rate service[80]. The KFTC levied fines of KRW 20.4 billion for this violation. KT, which was a dominant operator in all sectors of the telephony market except international calls, was involved in all three cases.

In the long-distance collusion case, operators claimed that the violation (for example, offering the same flat-rate service) resulted from a binding administrative order. The telecoms sector was still regulated, and KT was obliged to pass on details of its tariff rates to the then Ministry of Information and Communication (MIC). The MIC advised KT to explain the new flat-rate service to other operators before marketing it, and to consider lowering its access fees to the three operators that didn't have their own long-distance network, so as to enable them to compete

79) See the White Paper in Fair Trade (2006: 174-179) for a summary of these three price fixing cases.
80) KT's flat rate service had consumers pay a fixed fee in addition to their monthly payment, which gave them unlimited use of the long-distance service.

with KT's new flat-rate service. Accordingly, latecomers would be at a disadvantage in flat-rate services, as they would have to pay fees for a service that is essentially free to customers. KT argued that it was acting in accordance with the MIC's administrative guidance. Further, KT argued that the guidance was based on the MIC's power to determine the criteria for setting access fees and other terms of access, which in turn, derived from the *Telecommunications Business* Act.[81)]

However, the KFTC concluded that KT was merely using the MIC's administrative guidance as an excuse, and that KT was trying to prevent more competitive flat-fee services being offered by other operators. KT, the KTFC decided, was just using the lower access fees to coerce other operators to market exactly the same flat fee service as that of KT, effectively restraining price competition in the long-distance telephony market. Further, the KFTC presumed that the MIC's guidance was intended only as a recommendation, not a binding order. Supporting this assertion, Hanaro Telecom had gone ahead and offered a more competitive form of flat-fee service in opposition to KT's wishes.[82)]

These were landmark cases that helped competition take root in the telecoms industry. They also sent out a strong message that the KFTC would take a stern position toward any "administrative order" defense not firmly based on statute. Through the staggered liberalization of the telecommunication sector, the privatization of KT, and several competition cases, it can be said that a competitive market structure has been constructed in the telecoms industry.

By contrast, the electric power industry is still heavily regulated, inefficient and in need of competition (see <Box 2-5> for details). Although the sector is not exempt from competition law, and while the KFTC has brought several competition cases against KEPCO, they are mostly in regard to minor violations involving unfair trade practices. The KFTC hasn't been able to initiate a major restructuring of the industry to promote competition. It remains unclear how effectively competition law can be enforced in a market that remains so heavily regulated and structurally non-competitive. Clearly, the KFTC needs to take a stronger advocacy role in this sector to promote greater competition and ensure competitive neutrality.

In regulated sectors, most countries have set up specialized regulatory bodies. These bodies often share regulatory responsibilities with competition agencies. In Korea's case, the KFTC and the Korea Communications Commission (KCC), under the Ministry of Information and Communications, share regulatory responsibility with respect to unfair trade practices in the ICT sector. The Telecommunications

81) KFTC (2005). "Decision on the Unfair Collaborative Act by Four Long Distance Telephony Service Operators." (Decision No. 2005-331; Case No. 2005단체0162).
82) Ibid.

Business Act stipulates that the KCC can regulate unfair activities. On the other hand, the KFTC is entitled to regulate all unfair business practices, such as cartels, abuse of dominant position, and violations of consumer protection laws. Mergers and acquisitions are coordinated between the two organizations. Therefore, it is possible that both regulators could investigate the same case and reach a different conclusion. Given that the KCC is not completely free from the influence of the MIC, it would be desirable for the KCC to become an independent regulatory body and leave competition-related matters completely to the KFTC. However, an understanding between the two regulators seems to preclude the possibility of dual penalties for the same violation. Further, for matters related to access to essential facilities, the telecoms legislation takes precedence over competition laws. Other matters are open to consultation and discussion.

Regarding the electric power sector, the Korea Electricity Commission (KREC) was established in 2001 to temporarily undertake regulatory functions. The KFTC's shared role in regulating this sector is not as clear as its role in the telecommunications sector. KREC purports that it has the "dominant position and main role" in promoting a competitive market, including regulating the abuse of a market-dominant position and the protection of consumer welfare. Devising an efficient mechanism of shared responsibilities between specialized regulatory bodies and the competition agency therefore becomes an important competition policy issue, especially in instances where a privatized or partially privatized sector still needs to be regulated.

While not all of the KFTC's recommendations went through, and the privatization process stalled after 2002,[83] the important thing to note here is that the privatization process institutionalized the participation of the KFTC, ensuring that, at the very least, views from the perspective of competition policy could be heard.

〈Box 2-5〉 Absence of Competition in the Electric Power Sector

In 2001, the electricity industry was vertically split up, with the separation of power generation from transmission, distribution and retailing. Competition was introduced to the power generation market, where six regional subsidiaries of KEPCO, SK, GS and POSCO compete with a number of small to medium-sized utilities. KEPCO itself still has a monopoly over transmission, distribution and retailing. Although six District Electric Power Businesses (DEPBs), with their own generation and distribution facilities, entered the retail market in 2004, their arrival has done relatively little to promote competition.

Many argue that the lack of competition in the electricity industry has resulted in under-investment, chronic supply shortages, excess demand, and large-scale deficit accumulation by KEPCO. Scholars point to three main deficiencies. First, under the current pricing system, estimated cost is used as the bidding price, limiting direct price competition between generators in the wholesale market. Second, KEPCO's subsidiaries are allowed to use a lower price, discounted by a correction factor depending on the type of generator being used. This discrimination between SOE subsidiaries and private utilities distorts incentives to invest in power generation facilities and affects profitability. Third, in the spot market for capacity, price is determined based on opportunity cost, but this opportunity cost is way out of line with current costs.

The regulatory system put in place in 2001 was meant to be temporary, and accompanied by a specialized regulatory body independent of the *Ministry of Trade, Industry, and Energy*. This has not materialized however, as the privatization process has come to a halt.

Source: Nam (2013).

5. Conclusion

Abuses of administrative power that serve to restrain competition can be a serious issue in countries that are trying to transition their economies from a state-led, planned economy to a liberalized, market-led one. This has been the experience of both Korea and China. Industrial policies that promote strategic industries via large economies of scale will, by their nature, involve erecting barriers to entry. In many cases, industrial-promotion projects such as these are undertaken using SOEs, which benefit from government subsidies and other preferential treatment regarding access to scarce economic resources, protection from competition, and gaining an advantageous market position vis-a-vis their private counterparts. Rapid economic development also results in high inflation, and governments often use direct price controls to stabilize the macro-economy and contain social unrest.

It is very difficult to enforce competition law when such legal restrictions on competition are prevalent. This is clearly seen in the case of the alcohol industry, as well as in the contrasting experiences of the telecommunications and electric power sectors discussed in the preceding sections of this paper. The priority of an economy in transition is, therefore, to eliminate the legacies of state intervention

through regulatory reform, contain state power in important industrial sectors through privatization, and subject SOEs to competition policy. All of these initiatives are aimed at promoting private sector initiatives in general. In these circumstances, the advocacy role of competition agencies can be vital. Competition advocacy refers to any competition-promoting activities undertaken by the competition agency, other than the enforcement of competition laws. Since it is often impossible for a competition agency to enforce competition law directly against Ministries in charge of independent statutes, which are frequently charged with implementing other important social goals, reining in anti-competitive behavior needs to be done through persuasion, consultation and recommendation, that is, using the tools of competition advocacy.

From the perspective of competition policy, another important concept in disciplining SOE-dominated sectors is competitive neutrality. Competitive neutrality refers to a situation where no entity is in an unduly advantageous or disadvantageous position in an economic market. As competition is introduced into sectors previously dominated by SOEs, it is crucial that competitive neutrality is maintained between them and their private-sector competitors. To enable competitive neutrality, it is of paramount importance that state-backed commercial activities be physically separated and corporatized; if this isn't possible, at the very least, their accounts should be clearly separated from those of the government. Cross-subsidizing commercial enterprises using funds from government-subsidized activities, impairs competitive neutrality by artificially inflating the competitiveness of the government-backed sector vis-a-vis private competitors. On the other hand, cross-subsidizing the non-commercial sector with profits from commercial-sector activities would weaken the competitiveness of SOEs in general.

Further, when the boundary between the commercial and non-commercial activities of SOEs is blurred, it becomes very difficult to enforce competition law. Competition law, after all, is only intended to target commercial activities.

Requiring SOEs to earn a commercial rate of profit from their commercial activities, and compensating them fully and accurately for their non-commercial public service duties, minimizes potential distortions from misplaced economic incentives. Competitive neutrality in the areas of taxation, regulation, access to finance and public procurement are also important. Of course, competitive neutrality is only meaningful when there is a potential or actual private competitor, when the SOE is dominant in the industry, or when the social benefits outweigh the costs of any anti-competitive effects.

This paper showed the experience of the KFTC in dealing with abuses of administrative power; in particular, it detailed how the KFTC actively participated in

the privatization process, used the competition law's strong competition advocacy provision to spearhead regulatory reform, and vigorously enforced competition law against SOEs, especially in the MRFTA's early years, when Korea moved from a state-led to a market-based economy. Although the KFTC did not always win, its success in this area has been outstanding, and may offer lessons to competition agencies in other developing countries.

Below, this study looks at some of the policy implications, drawn from the Korean experience, thought to be especially salient in making a competition agency better equipped to regulate abuses of administrative power:

1) Strong legal mandate for competition advocacy:

» The Korean competition law provided a strong and firm legal mandate for competition advocacy, and has been strengthened in the years since its inception.

- Specific mechanisms of competition advocacy include prior consultation, a mandate to restructure monopolistic markets, and competitive impact assessments.

- The most prominent initiatives the KFTC undertook include various regulatory reform campaigns at both the central and local government levels, and the introduction of the Omnibus Cartel Repeal Act.

2) Strong intellectual leadership:

- The KFTC was able to take advantage of a wide network of think tanks and scholarly expertise from academia. The contribution of the KDI was especially valuable during the KFTC's early years.

- Intellectual leadership supported by economic analysis is crucial in implementing competitive advocacy, because Ministry heads have to be convinced, vested and entrenched interests fought off, and public opinion won over.

3) Independence and status of the competition agency:

» For the competition agency to effectively carry out competition advocacy activities, and to avoid regulatory capture, it must be independent from other administrative organs, especially the Ministries in charge of regulating the respective industries. It also needs to wield sufficient status and power to be

able to aggressively present its views to other Ministries.

- In Korea, this was achieved early on, with the KFTC being separated from the Economic Planning Board. Subsequently, the KFTC was elevated to Ministerial status, and given permanent membership in important state organs such as the Four Economic Ministers Council, the Regulatory Reform Committee, the Inter-Ministerial Committee for Privatization, and the Presidential Council on National Competitiveness. The KFTC was thus able to actively participate as a full member in these key national-level government bodies, enabling it to carry out its competition advocacy mandate vis-a-vis other official organizations and bureaucrats.

- The KFTC is given quasi-judicial and quasi-legislative powers, in addition to the power to enforce laws under its jurisdiction. The KFTC's investigative powers have been strengthened, but not as much as recommended by some international organizations.

- The KFTC operates specialized units devoted to competition advocacy, and is able to set up special task force teams when necessary, for example, to handle cases of privatization.

4) Enforcement of competition law against SOEs:

» As discussed, competitive neutrality is a useful concept in policing SOEs. The KFTC has achieved regulatory neutrality by not exempting SOEs from the enforcement of competition policy, and by treating them in the same way as private enterprises. The KFTC has strengthened enforcement against SOEs over time, sometimes through ex-officio investigations.

- It is important not to uniformly exempt strategic industries, which are usually dominated by SOEs, as a way of exempting SOEs from competition law. SOEs should be fully subject to competition law, not least because it is the best way to ensure their economic health and competitiveness in the long run, companies spurred on by foreign competition will, almost invariably, be stronger than those relying on government protection. Where important policy concerns exist, exceptions can be made, e.g., in times of economic restructuring, economic crisis, fostering R&D, etc., but dominant players shouldn't be categorically exempted.

- In the Korean experience, SOEs that subsidize and give preferential treatment to affiliate organizations have been a common channel for cross-subsidies between the public and commercial sectors. This precludes the entry of

private firms into sectors where SOEs have monopsony power, and so required particular scrutiny by the competition authority.

- The enforcement of competition law becomes more important after privatization. As the experience of Korea's telecoms sector shows, continued vigilance is needed to maintain competition in a sector formerly dominated by an SOE.

- An important goal of privatization is to introduce competition, so a public monopoly should not merely be replaced with a private monopoly. Since the incumbent can enjoy a dominant position even after privatization, these sectors will still require regulation.

- In such cases, many countries have set up specialized regulatory bodies, and devising an efficient system of shared regulatory responsibilities with the competition agency becomes an important policy issue.

  • To avoid regulatory capture, it is important for these specialized bodies to be independent from the Ministries governing the relevant sector.

  • Those bodies must also share regulatory powers with the competition agency, delegating competition matters to the latter. Korea has adopted this structure, but still needs to make specialized regulatory bodies such as the Korea Communications Commission and the Korea Electric Commission fully independent from their related Ministries.

- All this said, regulation in SOE-dominant sectors where competition has been introduced should not remain in place for too long. It is important to eliminate direct regulation over price and entry, especially when it is discriminatory, as soon and as much as possible. If this isn't done, it becomes difficult to fully enforce competition law in the regulated sector. In this regard, the KFTC seems to have done better in the telecoms sector than in the electric power sector; in the latter, the KFTC was only able to regulate minor unfair trade practices carried out by KEPCO, and hasn't taken a leading role in making the industry more competitive.

5) Promotion of competition culture at a broad level:

» Competition advocacy must not only target the public sector, but society at large, especially as it bids to overcome regionalism. Competition policy should also be coordinated with overall reform efforts, industrial policy and SOE policies.

- The competition agency cannot do the job alone. The Korean experience shows that overall social consensus, appropriate political conditions and demand (by consumers, by small business) need to be present to ensure the strong implementation of competition law.

- Sometimes, pressure for reform comes from the outside. For Korea, the Asian financial crisis is a case in point. While external pressure is not the most pleasant way to carry out reform, its dynamics can be used strategically to undermine entrenched domestic interests and stimulate reform.

- In China's case, liberalization and free trade agreements could be strategically used to stimulate domestic reform.

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Appendix

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1. Administrative Monopoly in China's Anti-Monopoly Law

Pervasive administrative monopoly is considered a serious problem in China, and the Anti-Monopoly Law (AML) devotes a whole chapter to this subject (Chapter 5, Articles 32-37). Administrative monopoly refers to conduct by administrative authorities (or other organizations authorized by laws or regulations to administer public affairs) that eliminates or substantially restricts competition in the market.

If not necessary for meeting other legitimate policy objectives within the general provisions of the AML, such conduct constitutes an abuse of administrative power. Such abuses are prohibited under the AML. Under the general provision of Article 8, "No administrative organ or organization empowered by a law or administrative regulation to administer public affairs may abuse its administrative power to eliminate or restrict competition." Chapter 5 of the AML further specifies categories of governmental actions that would be prohibited: mandated use of products and services, regional blockades, restrictions on bidding, restrictions on market entry, and restrictions on competition. Box A.1 presents an example of mandated use.

Prosecuting such abuses is the responsibility of the relevant superior agencies, and while those responsible can be punished by law, the competition authorities can only give advice to the superior agencies on the appropriate penalties. That is,

the competition authority cannot directly enforce the relevant AML provisions (AML Art. 51). Administrative monopoly can also be regulated under the Anti-Unfair Competition Law (AUCL) (1993), which stipulates that courts have jurisdiction over civil disputes caused by anti-competitive conduct.

Industries controlled by SOEs, and strategic industries concerning national security and the "lifeline of the national economy," are exempt from the AML (Article 7). However, they are still subject to supervision and regulation by the government, and must conduct their business in accordance with law, be honest, and not hurt the interests of consumers by virtue of their dominant status or state-trading status.

〈Box A-1〉 The AQSIQ Case (2008): An Example of Mandated Use of Products

The General Administration of Quality Supervision, Inspection and Quarantine (AQSIQ) case was the first attempt to apply the AML to a case of administrative monopoly. Four companies in the anti-counterfeiting business complained that by promoting the proprietary product identification, authentication and tracking system (PIATS) and mandating through an administrative order that all companies in the anti-counterfeiting business had to join PIATS, AQSIQ was having an anti-competitive effect on the market. PIATS was operated by a company called CITIC Inspection Information Technology Co. Ltd., in which AQSIQ held a 30% share. PIATS levied charges both on companies, as "data maintenance fees," and on consumers for inquiry fees and call tolls.

In 2008, AQSIQ declared that companies that don't join PIATS could neither obtain a production license nor pass the compulsory product certification process. Since an estimated 87,000 companies were subject to this order, it was expected generate significant revenue. The plaintiffs claimed that AQSIQ had abused its administrative powers by designating only one company to operate the electronic quality-control business, ultimately impeding competition in the market by precluding other competitors. Indeed, following the order, a number of anti-counterfeiting companies closed while CITIC Inspection presumably enjoyed substantial profits. Although the case could not go to trial on procedural grounds, AQSIQ announced in 2008 that it had withdrawn all of its investment from CITIC Inspection.

Source: Xu, S. and B. Zhang (2013: 271-286).

2. International Discussions on Competitive Neutrality

Early discussion of competitive neutrality is found in the OECD (2004), which emphasized the need to regulate state-owned enterprises that often enjoy privileged positions in the economy. SOEs are often found to be monopolistic or have dominant positions in the market vis-a-vis their private competitors. Thus, there is a greater likelihood that SOEs will abuse their market dominance and engage in various anti-competitive activities. Because such SOEs tend to be large,

the impact of their anti-competitive behavior also tends to be sizeable. Even if they do not directly engage in anti-competitive behavior, SOEs that compete with private enterprises thanks to assorted benefits they receive from the government, ranging from direct subsidies to subsidized finance and tax exemptions, will still impair economic efficiency. This is because high cost SOEs may outcompete their lower cost private competitors, which will lead to market distortions. OECD (2004) refers to this market distortion as the "competitive neutrality problem."

The OECD has been a major forum for discussing this theme over the years, through several policy round tables and publications of policy papers. The most recent studies on competitive neutrality by OECD include a series of publications made in 2012. In the "Competitive Neutrality: National Practices (2012a)," the OECD provides a more concrete definition of competitive neutrality as a situation where "no entity operating in an economic market is subject to undue competitive advantages or disadvantages." The study also finds that most countries deal with aspects of competitive neutrality through competition laws and policies. Most of these policies give public and private businesses "equal rights and obligations," but differ in the extent of the scope of application and exemptions available to different types of government businesses. A minority of countries have explicitly built the enforcement of competitive neutrality into their national policies, while a few nations (e.g. Australia) have established a comprehensive and formal legal framework.

The OECD has continually emphasized the importance of establishing the principle of competitive neutrality as the standard for "fair" competition, especially with respect to OECD firms competing with SOEs from emerging economies. This stance is fully reflected in "Competitive Neutrality: Maintaining a Level Playing Field between Public and Private Business (2012b)," which highlights existing competitive neutrality practices and policy challenges in leveling the playing field between public and private businesses.

The report identifies the enhancement of allocative efficiency throughout the economy as the main economic rationale behind ensuring competitive neutrality. Competitive neutrality also has a political rationale that is linked to "governments' role as universal regulators in ensuring that economic actors are 'playing fair' (where state-owned corporate assets are concerned and vis-a-vis other market participants), while also ensuring that public service obligations are being met." At the same time, the report identifies eight "building blocks" or areas of challenge to maintaining competitive neutrality: streamlining the operational form of government business, identifying the direct costs of any given function, achieving a commercial rate of return, accounting for public service obligations, tax neutrality, regulatory neutrality, debt neutrality, and public procurement.

The third publication "*Competitive Neutrality: A Compendium of OECD Recommendations, Guidelines and Best Practices (2012c)*," attempts to provide a full perspective on existing OECD instruments related to competitive neutrality. It does this by synthesizing all the related OECD recommendations on the aforementioned eight priority areas or "building blocks" of competitive neutrality identified in OECD (2012b). The following is a short summary of the core of this report:

1) *Streamlining operational form of government business:* When SOEs are engaged in both public service provision and commercial business activities, questions arise about whether their business activities are consistent with market principles. To level the playing field, the OECD recommends the structural separation of commercial and non-commercial activities, to the extent that benefits outweigh costs, noting that physical separation is not always feasible or economically efficient. The OECD also recommends corporatizing commercial activities and, if feasible, non-commercial units which operate on a commercial basis, and exposing them to competitive, open markets to the greatest extent possible, mostly to ensure transparency and accountability.

2) *Cost identification:* For credible enforcement of competitive neutrality, identifying the costs of any given function of commercial government activity is important. For incorporated SOEs, the most important issue is accurately accounting for the costs associated with public service obligations, so as not to under- or over-compensate for the cost if it is subsidized by government funds. For unincorporated units of general government that share costs between commercial and non-commercial activities, the concern is that the attribution may often not be feasible. OECD recommendations include disclosing the proportion of shared costs and assets that are attributed to commercial activities, making transparent the degree of subsidies disbursed by the state, and removing any cost advantages or disadvantages which may exist due to public ownership.

3) *Commercial rate of return:* To prevent cross-subsidizing between commercial and non-commercial activities of SOEs or government, the OECD recommends that SOEs should be forced to achieve commercial rates of return and to benchmark similar business activities in the same industry. Clarifying any non-business objectives the SOE may be required to pursue is also important, so that they aren't used to undercut actual or potential competition. The OECD also recommends that where SOEs do not maximize profits or are allowed to earn lower rates of return, non-traditional competition law-based approaches, such as appropriate cost-accounting mechanisms and performance comparisons, may also be usefully applied.

4) *Public service obligations:* the competitive neutrality problem becomes most evident when SOEs are required to provide essential public goods alongside commercial activities. Competitive neutrality requires accurate costing, pricing and regulation of parts of the service provision that take place on a commercial basis. This suggests removing privileged access that SOEs may have and compensating the companies accordingly. The main OECD recommendations regarding this issue include: ensuring sufficient transparency and disclosure around public funds used to pay for fulfilling public service obligations; subjecting the use of public resources to budget oversight and monitoring; providing adequate compensation for the public policy priorities SOEs are obliged to undertake, while disbursing compensation in a manner that can be accounted for separately, and establishing reliable cost calculation methods that avoid cross-subsidization.

5) *Tax neutrality:* Giving public and private business activities equal tax treatment is important in maintaining competitive neutrality. Governments should not have perverse financial incentives, for example, by favoring purchasing goods and services from itself to avoid taxes. The OECD International VAT/GST Guidelines suggest that in cross-border trade, businesses in similar situations carrying out similar transactions should be subject to similar levels of tax. When equal tax treatment is impossible, the second best practice is to ensure transparency around tax exemptions, thus making it possible to address any advantages that stem from such exemptions.

6) *Debt neutrality:* Many SOEs benefit from preferential access to credit, because of the perceived low risk of lending to companies with government backing. Fully leveling the playing field thus requires subjecting SOEs to full financial market discipline. The main OECD recommendation here is that SOEs should be made to access credit on the same terms as private enterprises. Debt neutrality adjustments used in jurisdictions such as Australia are considered best practice: in that country, debt rating agencies provide credit evaluations of government businesses under a counterfactual assumption of private ownership, and require SOEs to pay debt guarantee fees to offset any cost advantages that stem from its ownership.

7) *Regulatory neutrality:* If SOEs are incorporated according to company law, they should be subject to the same regulatory treatment as private businesses. However, where SOEs are created according to statutory authorization, or where commercial activities remain integrated with general units of government, certain legal regulatory exemptions may result in violating competitive neutrality. Where this is the case, the OECD recommendation is to extend the remit of regulations to apply to SOEs, or to have them applied on

a voluntary basis. Another important recommendation is to conduct periodic evaluations of government participation in regulated markets, especially where SOEs retain monopoly rights. Financial regulations should be consistent and neutral irrespective of ownership, institution, sector and markets, applying equally to government-controlled or owned financial institutions. Not only competition agencies, but trade and investment authorities all have a role to play in enforcing competitive neutrality.

8) *Public procurement:* Procurement policies and procedures should be competitive, non-discriminatory and uphold high standards of transparency to be consistent with competitive neutrality. The OECD recommends that general procurement rules should apply to SOEs as they would apply to other companies, and that clear selection criteria should be put in advance. Where discriminatory preferences exist, they should be made transparent in the selection criteria and be shared with potential bidders in advance. In contracting-out government services, in-house bids should be treated the same as outside bids. The OECD stresses integrity and ethics as essential in the procurement process.

The competitive neutrality concept has come to receive greater attention recently in international forums other than the OECD, in particular in trade agreement negotiations. With the progress of privatization and industrial liberalization, SOEs have increasingly started competing with private firms. At the same time, many emerging economies use SOEs as instruments to develop national champions through industrial policy. As their trade partners have responded with attempts to incorporate competitive neutrality as a key principle in free trade agreements, tensions have grown.

Several free trade agreements already contain provisions for competition policy and regulation of SOEs. The FTAs between Korea and the US, and Korea and the EU are examples. Following NAFTA, most FTAs the US has concluded with developing countries also contain competition policy chapters, including provisions for national treatment, non-discrimination, and transparency. The US-Singapore FTA contains extensive transparency provisions in addition to the usual NAFTA provisions, mostly applicable only to Singapore. In the Regional Comprehensive Economic Partnership (RCEP) negotiations, Korea and Australia have led moves to include provisions on competition policy and SOEs, albeit in a mild form.

While provisions on competition and SOEs have become commonplace in trade agreements, not many refer explicitly to "competitive neutrality." FTAs Australia has concluded are exceptions, usually containing explicit clauses on competitive neutrality, perhaps reflecting the strong implementation of competitive neutrality

in Australia. The Korea-Australia FTA is an example: Article 14.4 in the Competition Policy chapter, entitled "Competitive Neutrality," states that the parties recognize "the importance of ensuring that governments at all levels in their territories do not provide any competitive advantage to any state enterprise in their business activities as a result of their being a state enterprise." It also states that the article "shall apply to the business activities of state enterprises and not to their non-business, non-commercial activities," and that the application of this article "shall not obstruct the performance of the particular public tasks assigned to them."

Competitive neutrality has been most forcefully pursued in the *Trans Pacific Partnership* (TPP) negotiations. Developed countries such as the US and Australia have pushed for the inclusion of provisions on competition policy and SOEs. According to Seshadri (2013), clauses on competition are expected to require the establishment of national competition laws, authorities and procedural fairness aimed at providing a level playing field for companies from TPP member countries. Further, a provision on SOEs in the TPP is expected to include the principle of competitive neutrality, whereby SOEs receive no competitive advantages beyond those enjoyed by private sector companies, and that they operate on a commercial basis. Specific methods have been proposed, similar to those used in the WTO Subsidy Agreement, to test the harm caused by violations of competitive neutrality and determine remedies. Such strong conditions on SOEs are difficult to accept for countries such as Vietnam, a formerly centrally planned economy where SOEs are known to take up around 40% of its output.

It is likely that increasing international discussions on competitive neutrality would put similar pressure on China, as it becomes more engaged in negotiating free trade agreements. Although China has significantly privatized some sectors such as telecommunications, it still envisions SOEs as playing a key role in various strategic sectors. As in many other countries, applying the Anti-Monopoly Law vigorously against SOEs may constitute an important first step in implementing competitive neutrality, enabling China to better deal with pressures from its trading partners. At the same time, it could enhance allocative efficiency in China's overall economy, as well as improving the international competitiveness of the country's major SOEs, which increasingly need to compete in the international market on their own merit rather than on the basis of preferential treatment from central or regional governments.

2013 Knowledge Sharing Program with China:
Sharing Experience of the KFTC on Enforcing
Competition Laws and Policies

Chapter 3

Economic Analysis of Competition Policy

Economic Analysis of Competition Policy

Jae-hyung Lee (Korea Development Institute)

Summary

Considering that the objective of competition policy is economic efficiency, it is essential to evaluate the influence of the problem according to a certain policy or fair trade law. The effects on the economy of a certain corporate action can be judged via careful analysis. At this point, economic analysis supports formulation and implementation of competition policy on an academic and empirical basis. Economic analysis is necessary to evaluate the effects of the issued entrepreneur's action academically and empirically, and also plays an important role as policy infrastructure in the process of formulation and implementation of competition policy.

On top of that, economic research and investigation are essential not only for the development of policy on competition law, but also for the enhancement of the overall competitive atmosphere of national industry (i.e., competition advocacy). From the late 1990s, as the enforcement of fair trade law was strengthened, corporations that had given a passive response to the actions of the Fair Trade Commission began to react more actively. In this process, economic analysis was widely applied. The commission also tried to develop plans to enhance economic development capacity in response to such changing conditions. They also founded an economic analysis organization for strengthening specialties, developed programs for fostering highly skilled employees and built up a network with external expertise.

On top of that, the Fair Trade Commission enacts and operates the submission of an economic analysis report as an institutional framework for such analysis. They utilize economic analysis for judgment on law violations and use analytical tools and econometric models for market definition and proof of abuse of market dominant position. The commission has won several crucial cases against large multinational corporations such as Microsoft on the basis of economic analysis, and this has paved the way for the commission to gain more confidence in economic analysis. Especially in the case of cartels, economic analysis is widely utilized for levy calculation. For the effective promotion and execution of competition policy, the nation's market and industrial situation and comprehensive corporate information are needed. The commission reinforces economic analysis of the entire economy and market. In Korea, statistics and company information supports economic analysis, and the watchdog actively utilizes them. The commission writes up and presents a statistics report on market structure including comprehensive information on the evaluation of competitive status throughout the economy. And in-depth research is done on a specific industry and institutional framework. Use of this economic analytical method has been a huge contribution to the development of Korea's competition policy.

Despite its short experience, competition policy in Korea has sharply progressed over the last 30 years mainly because of constant functioning of research and analysis. The government is responsible for active leadership on the reformulation of the Korean economy, executing these functions and arming the people with absolute knowledge of theory. So the economic analysis function should be further developed.

1. Introduction: Competition Policy and Economic Analysis

The objective of competition policy is efficiency in the national economy through the promotion of competition. In a market economy, monopolistic and oligopolistic profits decrease and dead-weight loss, a negative effect of a monopoly and oligopoly, is eliminated when competition is achieved effectively. Also, consumer benefits are maximized and national resources are most efficiently distributed. Competition policy brings the economy closer to this condition by eliminating artificial risks such as abuse of market dominant power, anti-competitive corporate mergers, illegal cooperative actions and unfair transactions.

As the final objective of a competition policy is efficiency, it is crucial to evaluate how specific policies or actions against competition policy affect efficiency. Actions that look similar on the surface can have different effects on competition according

to the economic environment or market conditions, and when such effects can be more precisely evaluated, competition policy can contribute to the economy more effectively. In other words, actions that negatively affect the economy and competition order must be regulated while punishment of actions that have positive effects need to be avoided. The economic effects of specific corporate actions can be evaluated only through precise analysis and in this respect, economic analysis can offer theoretical and practical support for the setting and execution of competition policies.

In general, economic analysis in competition policy in a theoretical or practical manner analyzes the effect or degree of a business operator's actions on markets, competitors and consumers based on economics. In other words, the emphasis is on theoretically or practically estimating and calculating the economic effect - whether there is any restriction on competition and its degree - of the problematic action of a business operator in case of procedures such as the decision to go to trial and the trial itself. Including economic analysis on such an enforcement process, this report aims to deal with economy analysis in the sense of covering all economic investigations and research needed for conducting competition policies.

An economic approach to establish and enforce competition policies plays an important role in several aspects.

First, such an approach is needed for theoretical and practical evaluation of the effects that the problematic actions of a business operator have. Economic analysis is an important proof material for deciding whether a specific action causes anti-competitive effects in trial decisions and litigation on the execution of competition policy, which are cases against fair trade law. Defining market boundaries, whether they are the specific actions of a market dominant business operator, corresponds to abuse, and whether a corporate merger restricts competition can only be accurately decided through precise economic analysis.

Second, economic research and investigation form policy infrastructure in establishing and executing competition policy. To effectively push ahead with a competition policy, general data on industrial and market conditions is required. If information on the distribution of corporate groups that need extra attention in competition policy, changes in the degree of overall competition (market structure) of the nation and industries likely to have problems with competition law are identified beforehand, fair trade policymakers can preemptively deal with the problems of restriction on competition.

Third, economic research and investigation are important not only for the development of systems related to competition law, but also for enhancing the

overall competitive atmosphere of national industries, that is to say advocating competition. For example, when advancing regulatory reforms for market function activation, a thorough economic analysis is needed for the entire process from production to consumption of a specific industry to devise regulations that have pro-competitive effects and support reform theoretically and practically. In this way, support for regulation reform can be achieved on a national level.

This report is composed as follows. Following the introduction, efforts of fair trade policymakers to reinforce economic analysis capability in competition policy in Korea are presented in Chapter Ⅱ. Chapter Ⅲ covers how economic analysis was used in trial decisions and litigation involving competition law violations. In Chapter Ⅳ, research and analyzing functions that the Fair Trade Commission enforce are explained as basic information for policy infrastructure, and Chapter Ⅴ deals with evaluation and future assignments.

2. Fair Trade Commission's Efforts for Strengthening Economic Analysis Capacity

2.1. Rising Need for Stronger Fair Trade Law and Economic Analysis

Enforcement of competition law is a process of ① interpreting legal provisions, ② deciding whether specific actions deemed problematic by law can occur, and ③ deciding whether a specific competent action violates the law. In executing competition law, economic analysis is used as practical supporting evidence ③, and as indirect evidence to estimate the existence of ②.

As information, computer and communication technology is seeing innovative development and corporate acts are becoming more complex and diverse with the emergence of new business models. So the number of cases that require in-depth economic analysis is increasing. In this situation, scientific economic analysis to procure rationality and objectivity is an essential factor in the execution of competition law. Economic analysis can be understood as a task that results in legal output based on economic input.

The Monopoly Regulation and Fair Trade Act ("Fair Trade Act"), the main competition law in Korea, was enacted in April 1981. At that time, this law was an unfamiliar system in the Korean economy, so most entrepreneurs lacked deep understanding of it. So if the KFTC exposed actions that restricted competition or unfair transactions and determined that such actions violated the law, business

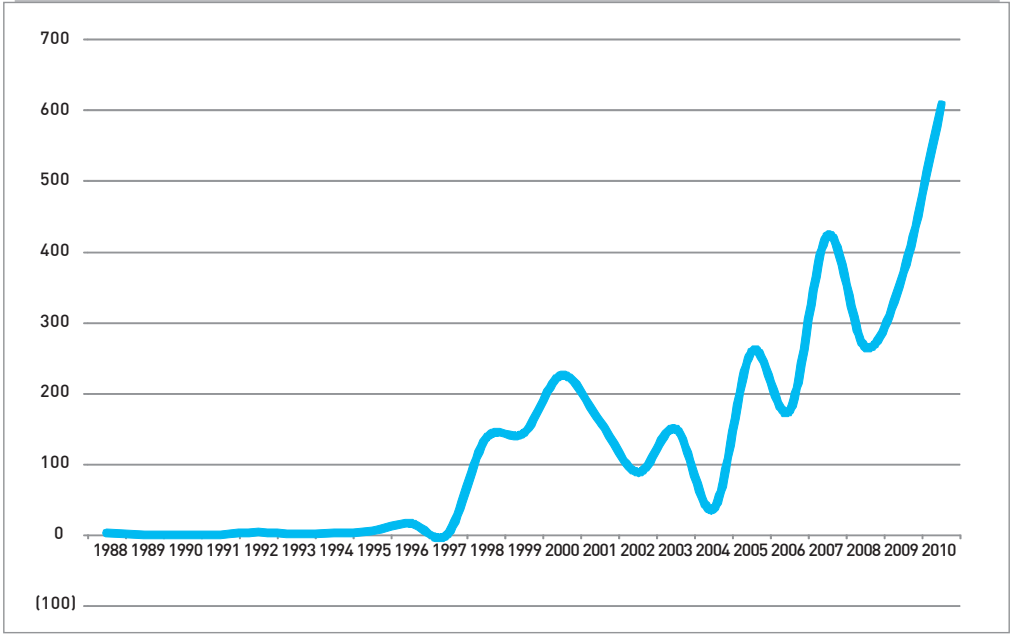
operators conformed to this in acknowledging their faults. They requested favorable punishment to authorities rather than claim their innocence.

Even for fair trade policymakers, it was difficult to strictly impose sanctions on violations because of low understanding by business operators of fair trade policy. Due to this, only light penalties were given in the 1980s to most violators. Under these circumstances, when a business operator was judged to have violated the law, he or she felt no need to actively defend his or herself.

Records on rectification of violations of the Fair Trade Act increased rapidly in the 1990s. This was not because anti-competitive practices had increased in the market, but more likely the result of stronger enforcement by authorities and increased professionalism in the execution of law. In 10 years of carrying out the Fair Trade Act, overall understanding of the fair trade system by society had grown and social criticism of violations had also increased, so authorities could respond to violations more actively than before.

Especially in 1994 as the penalty system was reinforced in accordance with the fourth amendment of the Fair Trade Act, the Fair Trade Commission had also changed the policy to punish violations, and the imposition of penalties increased greatly (Figure 1). For example, five oil refinery companies judged to have committed irregularities in joining a military bidding contract in 2000 were fined 190 billion won. The amount was considered astronomical at the time.

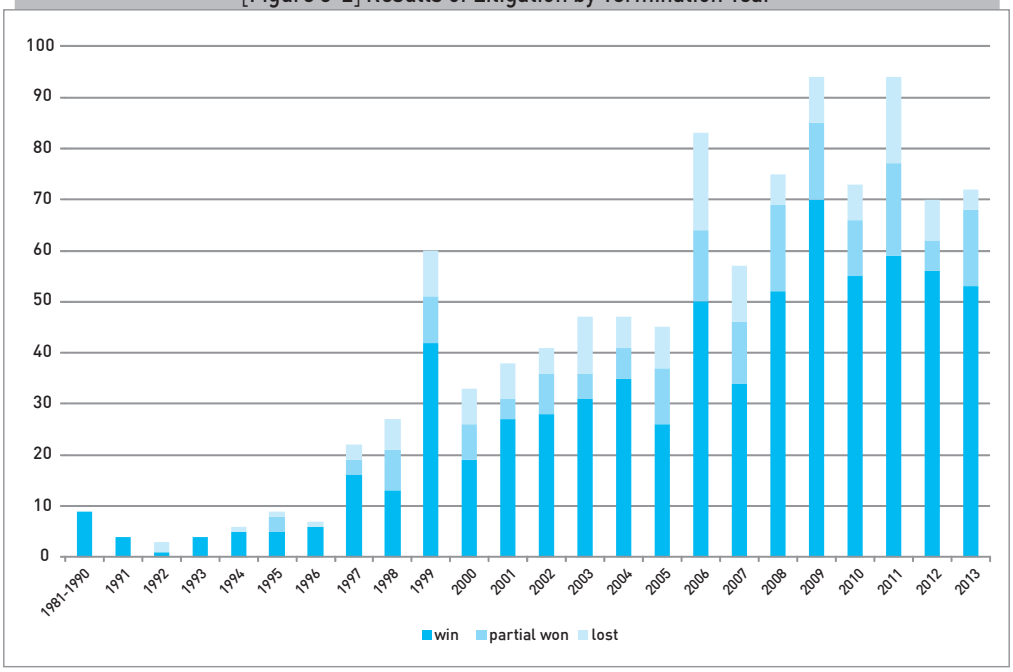
[Figure 3-1] Surge in Imposition of Penalties



Unit: 1 billion won

As restrictions on violations of the Fair Trade Act grew big enough to trouble corporations, companies began to pay more attention to the decisions of the Fair Trade Commission. More corporations denied violating fair trade law or claimed that their actions had no anti-competitive effects. Also, the number of appeals on commission decisions began to increase, and corporations actively used economic analysis in this process. They also utilized economists and legal experts in trials and lawsuits and claimed innocence through economic analysis, resulting in more cases of using the results of economic analysis for important information in the decisions of the commission and trials. As a result, the commission had more difficult fights in trials and lawsuits, and the importance of economic analysis in appealing decisions grew.

[Figure 3-2] Results of Litigation by Termination Year



Unit: case

In response to this changing situation, the commission reinforced the function of economic analysis. As a result, economic analysis greatly affects the results of trials while the commission's court and judicial courts are de facto arenas for economic analysis between corporations and the commission. Not in just trials but also in administrative litigation and civil suits (related to compensation), economic experts are serving as witnesses to testify and economic analysis reports are being submitted in court. So the role of economic analysis in the execution of competition law is expanding.

Hailed as an important development in Korean society and the competition law environment is the practice of corporations of denying the claims of the Fair Trade Commission by incorporating theoretical and practical evidence based on economic analysis and requesting formal trials to appeal to commission decisions. Corporations can file a protest to the government under social rules, and this could be an aspect of market economy development. It appears that corporations will continue to contest the commission's decisions, and the watchdog is also expected to reinforce its economic analysis capacity in preparation for this change in the political environment.

2.2. Reinforcement of Economic Analysis Capacity of Watchdog

As more problems emerged in enforcing the Fair Trade Act, the commission also took action amid the changing situation and focused on strengthening its economic analysis capacity.

2.2.1. Accumulation of Economic Minds: Features of Commission's Organizational Culture

Since its beginnings, the Fair Trade Commission has had a more flexible "economic mind" than any other government department due to its original feature. The Fair Trade Act, the main competition law in Korea, was enacted in April 1981, and the Fair Trade Office was established under the Economic Planning Board to enforce the act as a competition policy authority. The minister of the Economic Planning Board, who was concurrently minister of economic affairs, headed competition policy, and this structure continued until the commission was promoted as a leading administrative agency in 1990. Because of this organizational history, most commission staff were from the Economic Planning Board, and this was an important factor for the competition policy authority to recruit flexible economic minds.

The Economic Planning Board had been the control tower of economic policy since the nation's economic development began. It was not bound to benefit specific industries because it controlled and commanded the Korean economy in general, regardless of industry or field. Because the board was discerning in looking at the overall economy, it had more understanding of the national economy than any other economic department. It also had free-thinking minds and a wide breadth of understanding on market economics. Because the Fair Trade Commission was derived from the Economic Planning Board, commission staff had more knowledge and expertise in economy than those at any other department, as well as deep understanding of market economics.

The commission prepared a high degree of knowledge in economic analysis because of this feature of organizational culture. Its organizational atmosphere had discussions about economic subjects in groups, a horizontal debate culture and research activities on economic theories and analysis methods, things that were hard to find in other governmental organizations. This characteristic can be considered the soil of organizational culture that enhanced the competence of economic analysis. In this kind of organizational environment, the use of economic analysis in enforcing the Fair Trade Act grew stable without any resistance.

2.2.2. Close Cooperation with National Project Think Tanks

The role of think tanks cannot be ignored in the development of Korea's competition policy. Korea Development Institute (KDI) is the country's leading state-run economic research institute, and has contributed greatly to the development of competition policy. Established in 1971, the institute helped to establish the Five-Year Economic Development Plan of Korea, and supported government policy development both directly and indirectly. Especially as Korea's economy saw major transitions, KDI took the lead and designed a paradigm for overall economy operation and proposed this to policy authorities, who embraced this heartily and considered KDI a partner of policy development.

KDI began to emphasize the introduction of competition policy from the mid-1970s. It explained the meaning of competition policy in the market economy system, benchmarked similar policies in advanced economies and rationally explained the reason for improving the monopolistic and oligopolistic market structure, which was dominant in Korea at that time. As a part of this research, KDI developed, created and analyzed market structure statistics in all Korean industries, something which was only possible in a few advanced economies at that time.

The Korean government accepted the KDI's suggestions, and the institute helped to devise the Fair Trade Act. Even after the fair trade system was introduced, close cooperation between competition policy authorities and KDI continued. In the beginning stage of competition policy, lots of demands poured in for research in the development and execution of policy. In meeting these demands for research on behalf of competition policy authorities, KDI not only carried out direct research requests but also took part in competition advocate activities jointly with the Fair Trade Commission. The regulatory reform policy that started in the late 1980s was a major task propelled by cooperation between the Fair Trade Commission and KDI.

The cooperative relationship between competition policy authorities and KDI continues to this day. KDI conducts research on competition policy that the commission forwards and continues advisory on enforcement of competition

law. Previously, most high-quality research personnel for competition policy were clustered in KDI, so the Fair Trade Commission maintained a close relationship with KDI. Recently, however, the basis of research on competition policy has been widely expanded and researchers are located at labs and educational facilities. So the commission has also expanded networking with think tanks and utilizing research resources.

2.2.3. Installation of Economic Analysis Team and Reinforcement of Expertise

The Fair Trade Commission has kept a team exclusively for economic analysis to strengthen that capacity. Under the Market Structure Improvement Policy Department, the Economic Analysis Team and Market Structure Improvement Team are in charge of economic analysis. The former team conducts economic analysis related to enforcement of the Fair Trade Act, and the latter analyzes and assesses the overall economic environment of competition law.

The Economic Analysis Team directly participates in rulings and trials of related events by supporting economic analyses for cases on competition law. Along with that, the team conducts tasks such as analysis of the economic effects of competition restrictive systems, analysis and improvement of monopolistic and oligopolistic factors by item, and developing indicators for factors that affect competition. The team recruits holders of a Ph.D. in economics to enhance expertise on economic analysis.

As a result of such efforts, the Fair Trade Commission has won trials against corporations using evidence from economic analysis, with the help of well-known economists in and out of the country by developing logic against defendants' analyses. When the Economic Analysis Team was established, defendants requested economic analysis to show that they did nothing wrong to well-known economics professors at renowned universities in Korea. The defendants submitted this report to the commission, which conducted economic analysis in defensive and critical aspects. But the commission now conducts more economic analyses preemptively to prove illegal actions deemed to have great effect on the market.

The Market Structure Improvement Team does not directly participate in legal procedures such as trials and rulings, and usually forms an overall information infrastructure for establishment and execution of competition policy. Along with setting general policies for market structure improvement, the team is also in charge of improvement and management of systems related to monopolistic and oligopolistic market structure and conducting research, investigation, statistical assessment and analysis on the overall economy.

The Fair Trade Commission has also been strengthening the economic analysis capacity of its employees by forming teams to that end. Holders of doctorates in economics are highly sought after, and even for general public officials, the commission is seeking to retain people with outstanding talents. Also, it is reinforcing its economic analysis expertise by increasing opportunities for training in and out of the country, reinforcement in task training and deploying competition policy authorities to other countries or international organizations.

2.2.4. Fair Trade Commission's Program for Enhancing Expertise

The Fair Trade Commission is introducing programs to enhance the economic analysis capacity of its employees. To grasp international trends of economic analysis in competition policy, the watchdog publishes the bimonthly <Anti-Trust Economic Analysis Trend Report> so that employees can study those methods. Also published are <An Easy Fair Trade Economic Analysis> and <Economic Analysis Manual> as guidelines for economic analysis methods that employees can refer to. Training programs such as online lectures on economic analysis are also available.

The commission has educational programs in and out of Korea for employee development. One program allows an employee to study at a renowned graduate school overseas for two to three years, and there are also opportunities to study at a Korean graduate school. Besides these degree courses, employees can attend economic analysis classes if related classes are offered at Korean universities.

Commission staff can also enhance their abilities in economics and economic analysis through study groups among employees such as one for econometrics and another for anti-trust economic analysis. The latter group invites outside experts and discusses their lectures.

The commission is also trying to understand the international flow of competition policy and communicate data on competition policies through exchanges with international organizations and competition policy authorities of other countries. The watchdog participates in discussion of competition policy in international organizations such as the OECD, ICN (International Competition Network), WTO, UNCTAD and APEC, and dispatches employees when necessary to contribute to these organizations as well as achieving close information exchanges with them. Cooperation with other countries is being sought for competition policy, and conferences are being held with fair trade authorities of the U.S., EU, Japan, China, France, Germany, Russia, Australia, Canada, Italy, Mexico, Romania, Chile, Singapore and members nations of the EFTA. The commission is also trying to help develop global competition policy. It regularly hosts the Seoul Competition Forum and International Competition Policy Workshop, and runs a competition

policy training program for less developed countries at the OECD Asia Regional Competition Center.

2.2.5. Reinforcement of Network Between Outside Expert Groups

The Fair Trade Commission is promoting extensional expansion of its economic analysis function through close ties with academia and expert groups in two ways.

First, the commission detects what could be problematic to competition policy and uses outside scholars to build an institutional base to stimulate competition. This is usually achieved by commissioned research by outside scholars, and though this is not directly related to fair trade events, it plays an important role in building the base for competition policy by expanding industrial data overall and understanding and dealing with the factors that could pose problems to competition policy in the early stage.

As for preliminary decisions on important cases, the commission fully utilizes consultation from outside specialists. Through this, it retains logical grounds that counter the economic analysis of defendants as well as verify and inspect its analysis for trial.

2.3. Institutional Base for Economic Analysis

As the importance of economic analysis has expanded in cases of fair trade violations, the commission prepares contextual and procedural regulations so that economic analysis can be used in verdicts systematically. <Guidelines on Submission of Evidence in Economic Analysis>, which were set in 2010 and amended in 2012, define the requirements and procedures if a defendant or investigator submits economic analysis evidence. In 2013, the commission established <Regulations on Submission of Written Opinions on Economic Analysis> for comprehensive matters on economic analysis including the contents of the 2010 guideline. This regulation defines the general principles, standards and submission procedures of the written opinions of economic analysis when an investigator or defendant submits forms like written opinions on economic analysis about the operation and case procedures of the commission.

2.3.1. General Principles of Written Opinions of Economic Analysis

According to this regulation, a written opinion of economic analysis must follow the general principles below:

- Appropriateness: The hypothesis, sources, analysis method and conclusion

must be relevant to the corresponding case when doing a written opinion of economic analysis.

- Completion: Related materials must be sufficiently reviewed and complete to understand its contents when creating a written opinion of economic analysis. If the written opinion does not include materials and information that could be replicated after understanding the result, this means lack of completion.
- Clarity: A written opinion on economic analysis must be clear about related facts and assumptions, hypotheses, materials, analysis methods and conclusions on the corresponding case for third-party evaluation.
- Consistency: When different analysis methods are applied to a written opinion of economic analysis, the results of each method must not contradict another and maintain consistency.

2.3.2. Standards of Written Opinion on Economic Analysis

In creating a written opinion on economic analysis, the following standards must be followed:

- Establishment of hypothesis: The hypothesis must be clearly established and in accordance with the facts, characteristics of the relevant market and related economic theory of the case. It must also be objective, reliable and verifiable based on materials.
- Use of materials: Materials must be appropriate and reliable for verifying the hypothesis, and their sources, reason for selection, collection method, standards and procedure of cleaning, statistical population, sample selection procedure, sample period, measure unit and definition of each variable must be explained.
- Analysis method selection: The analysis method must be selected based on characteristics of the market, issue of the case and limitations of the analysis method, and should be what is generally acknowledged in the academic field.
- Derivation of conclusion: The economic analysis must be based on theoretical or practical models according to the economic theory related to the case, and its result must be reliable. At the same time, whether the economic analysis has been conducted irrespectively of the case or for the purpose of use for the case must be explained.

2.3.3. Materials to Submit When stating Written Opinion of Economic Analysis

This regulation prescribes to attach the following materials when submitting a written opinion of economic analysis

- Written opinion of economic analysis: The title, author, date of preparation, reference, summary and written opinion of economic analysis for nonprofessionals of economics must be included.
- Information on author of written opinion on economic analysis: Records of research in the corresponding field, list of written pieces on competition policy, activities as economic analysis expert over last five years
- Used materials: Raw data needed to verify written opinion on economic analysis, processed data used in analysis, electronic file for application program code used in data analysis

3. Economic Analysis in Major Judgments and Trials

3.1. Market Definition

3.1.1. Related Regulations

The market, defined as the place of competition per competition law, is called "relevant market" and expressed as a "certain line of commerce" in the Fair Trade Act. A certain line of commerce is defined as "the line in which commerce is at a competitive relation by object, level or region, or which has the potential of establishing competitive relation." Thus this is a concept that includes both the markets for products and geography. "Competitive relation of transaction by object" in the Fair Trade Act and "line of commerce" in U.S. antitrust law refer to the products market, and the key point here is what kinds of products should be included in the same market.

The Fair Trade Act says the following factors should be considered standards to decide the relevant market (certain line of commerce) (Merger Guideline, 2011):

- Similarity of function and utility of products
- Similarity of product price
- Consumer recognition of substitutability and related purchasing behavior
- Seller recognition of substitutability and related behavior of business decision-making
- Korea standard industrial classification noticed by head of Statistics Korea per regulations of Article 1, Section 1 of the Statistics Act
- Step of transaction (manufacture, wholesale, retail)
- Other party in transaction

As a method of market definition, the SSNIP Test developed in the U.S. is being used around the world. This methodology of market definition was introduced in the U.S. <Merger Guideline> in 1982, which "defines products which an assumed monopolist can attempt small but significant and non-transitory increase in price (SSNIP) or group of such products or geographic area as a relevant market." Even in Korea, the SSNIP Test is being adopted more as a method of defining the relevant market.

3.1.2. Major Judgments and Trials

3.1.2.1. Definition of Product Market

□ Hite Brewery's acquisition of Jinro

Hite Brewery Co., a beer company, took over Jinro Co., a maker of soju (Korean distilled liquor). Here, a critical loss analysis was accepted as the method of market definition because both the defendant and a competitor who opposed the corporate merger used critical loss analysis. The defendant's claim was accepted, confirming that the beer and soju markets are separate.

The major issue in this case was whether soju and beer should be classified in the same market in product market definition. In this ruling, the Fair Trade Commission judged that the two products are defined to be in separate markets considering the comprehensive econometric analysis of product features, consumption patterns and the effects of price change on corporate profit and other cases in and out of the country. As a metric analysis tool of economic analysis, critical loss analysis was adopted. Critical loss analysis is one of the analyzing methods developed to apply to the SSNIP (small but significant and non-transitory in price) Test that fair trade authorities of many countries generally use as the standard of market definition for the purpose of evaluating corporate mergers.

Critical loss analysis is a method of defining a market by comparing the sizes of actual and critical losses according to a price increase. If actual loss is greater than critical loss, the assumed monopolizing corporation cannot increase profit through SSNIP of relevant products so it needs to expand its market range. If actual loss is less than critical loss, the monopolizing corporation could increase profits through SSNIP in the relevant product (region), therefore it need not expand its market range. The appropriate market range defined by this method is called the "smallest market," which no longer needs to expand its product market.

Through critical loss analysis, Hite Brewery, as the corporation doing the merger, claimed that soju and beer do not belong to the same product market, whereas OB,

Hite's competitor, argued that the two products are members of the same market. The Fair Trade Commission sided with Hite, citing a problem in OB's sales data and saying OB erred by overestimating the margin rate by using the short period of one year when calculating.

□ Corporate merger of Lotte Shopping (2012)

Lotte Shopping, an operator of hypermarkets and supermarkets, in 2012 acquired the stock of CS Mart, a supermarket operations business. In this merger, the major issue in product market definition was whether the business line of an SSM (super supermarket) and similar business lines of hypermarkets and individual supermarkets form the same market. In this case, the SSNIP Test and consumer recognition of substitutability and related purchasing behavior were used to define the relevant product market.

In the SSNIP Test, analyses of critical loss and aggregate diversion ratio were adopted as specific methodologies. As a result of conducting both analyses, which are the general methods of the SSNIP Test on the survey results, the conclusion was that the relevant product market must be expanded to be bigger than the SSM market.

In a study on consumer recognition of substitutability, 28.2 percent of consumers said they would shop at a hypermarket if the SSM they go to raise prices 5 percent, and 47.9 percent said the same if the price hike was 10 percent. This shows that consumers recognize a hypermarket as substitute for an SSM. On the other hand, just 15.5 percent of consumers said they would rely on individual supermarkets if prices rose at the SSM they were using. Also, many differences were found in management and marketing between SSMs and individual supermarkets.

Based on these results, the Fair Trade Commission judged that hypermarkets and SSMs belonged to the same market, whereas individual supermarkets were part of a separate market.

3.1.2.2. Geographic Market Definition

□ Hite Brewery's acquisition of Jinro

In the Hite-Jinro merger, geographic market definition was also an important issue along with product market definition. As for the Korean soju market, the tendency was to separate markets according to region due to lingering government regulation of the soju industry. In this case, the geographic market of the liquor was defined as the whole country except for five regions including Busan, applying

regional consumption behavior vis-a-vis soju.

Hite Distillers, an affiliate of Hite Brewery, produces soju in North Jeolla Province and major sales were limited to the area, so whether the geographic market should be limited to the province had become the issue. While reviewing factors for geographic market definition and using critical loss analysis for the metric analysis model of geographic market definition, the Elzinger-Horgaty Test was conducted in the province. This test is a method proposed by Elzinger-Horgaty in a 1973 study and a theory of geographic market definition considering LIFO (Little In From Outside: regional production and consumption / total production of region) and LOFI (Little Out From Inside: regional production and consumption / total production of region) in production.

In the Elzinger-Horgaty Test, LIFO measures the level of reliance on consumption in a certain region on production within the region; in other words, the proportion of inflow to the area. If consumers in an area buy a lot of products from outside the region (low LIFO), the relevant market must be expanded because profit is effectively applied as competition pressure to business operators in the relevant region. LOFI measures the level of goods consumption in a certain region produced within the region; in other words, the proportion of export to other regions. If many products are being sold in other regions (low LOFI), the relevant market must be expanded because it is difficult to raise prices in the relevant region due to competition outside of the region. Generally, the datum point is set at 75 percent for both LIFO and LOFI.

The Fair Trade Commission decided that Hite Distiller should expand its geographic market from North Jeolla Province on the grounds that it did not meet the Elzinger-Horgaty Test when the market was limited to the province.

□ Corporate merger of Home Plus & Home Ever

Samsung Tesco, the operator of the hypermarket Home Plus, merged with E-land Retail, which operated another hypermarket, Home Ever, through stock acquisition. In general, the headquarters of hypermarkets set general prices of sale products but also control prices by item in accordance to competition of each branch and region. Given this, the Fair Trade Commission decided that hypermarket branches undergo price competition, and introduced the concept of the SSNIP Test as the method for geographic market definition in this case. More specifically, the approach of "A Union of Overlapping Circle" was adopted.

This approach had been used in the case of Tesco-Carrefour (2005) by the EU and in the case of E-Mart-Walmart (2006) by the Fair Trade Commission. This method

draws a circle with a certain radius around the business operator in a relevant product market and draws another circle with the same radius around the other business operator in the same market. This is to consider the entire area as the same market to recognize the extent of competition pressure in defining the geographic market. Thus when drawing a circle around each market area of companies A and B that are subject to the merger and an overlapping part is between those two, A and B are considered part of the same market.

If the circle of A and B overlaps and increases their prices, then consumers who are in the overlapping area will shop at B and A's profits will decrease. So A's geographic market should be expanded to include B. An important thing to consider in the approach is deciding the initial size of the circle. The Fair Trade Commission defines a radius of 5km from each branch for hypermarkets (metropolitan area) and 1km for SSMs as a geographic market.

By using this method, the commission decided that the merger could result in restrictions on competition in five regions.

3.2. Abuse of Market-Dominant Position

3.2.1. Related Regulations

Article 4 of the Fair Trade Act prohibits the abuse of a market dominant position. The statute has two stages, the first being the requirement to set up a business operator holding a market-dominant position (=market-dominant business operator), and prohibition of certain acts by a market-dominant business operator.

The requirement for the establishment of a market-dominant business operator is defined by Article 2 (Definitions) and Article 4 (Presumption of market-dominant business operator). Article 2 says that "in deciding a market-dominant business operator, its market share, existence and extent of entry barrier and relative size of competitor must be considered comprehensively." In Article 4, the standard of market structure is indicated as the requirement for assumption of a market-dominant business operator. When putting these two articles together, the requirement of such an operator is a business operator with more than 4 billion won in annual sales or purchases, and it can be defined as a business operator with market dominant power considering that ① it has a market share of more than half ($CR_1 \geq 50$ percent), ② the market shares of the top three companies exceed 75 percent (business operator with under 10 percent of market share is excluded in this case), and ③ existence and extent of entry barrier. A business operator who satisfies this condition is acknowledged as market dominant and need not consider other factors. When a business operator has market dominant power though failing

to meet these conditions, he or she is considered a market-dominant business operator.

〈Table 3-1〉 Requirements of Setting Up Market-dominant Business Operator

Article	Contents
Article 2 (Definitions)	- A supplier or buyer in a certain line of commerce and in a position to decide, maintain or change the price, quantity, quality and other conditions of transactions of products or services with other business operators in the market - Market share, entry barriers and relative competitor size are comprehensively considered for the decisions of the market-dominant business operator (Article 2) - Business operator with annual sales or purchase of under 1 billion won is excluded
Article 4 (Presumption)	① Business operator with half of market share or more ② Business operator where the market shares of the three top businesses exceed 75 percent (business operator with under 10 percent of market share is excluded)

The five types of abusive acts of a market-dominant position are: ① act of unfairly deciding, maintaining or changing the price of a product or service (price abuse), ② act of unfairly controlling sales of a product or provision of services (restriction of release), ③ act of unfairly interrupting business activities of other business operators (interruption of other business operator), ④ act of unfairly interrupting the entry of another competing business operator (interruption of new entry) and ⑤ act of transaction to unfairly exclude competing business operator (exclusion of competitor) and act that could noticeably hinder consumer benefits (impediment of consumer benefit) (Clause 2 of Article 3). The types and standard of abuse of market-dominant position are specifically stated in Article 5 of the Fair Trade Act Enforcement Ordinance.

3.2.2. Major Judgments and Trials

3.2.2.1. Posco's Denial of Transaction

Hyundai-Kia Motor Group constructed a cold-rolled plate factory (Hyundai Hysco) to supply cold-rolled plate for cars, a material which the group used to procure from Posco. Thus Hyundai-Kia is now a competitor of Posco in the cold-rolled plate market. Around the time of the plant's completion, Hyundai Hysco made five requests to Posco for supply of heat refining coil for cold-rolled plates for cars in a trial production, but Posco refused. The Fair Trade Commission decided that

Posco's decline caused more than just discomfort in business or economic losses for Hyundai Hysco. The watchdog said Posco erected a barrier hindering competition in the cold-rolled plate market, and judged that this was a violation of the Fair Trade Act. The commission offered no additional analyses on competition restriction effects aside from this.

Posco sought a trial in objection to this judgment, denying any competition restriction effects through economic analysis on the grounds that Hyundai Hysco produced cold-rolled plates normally despite Posco's transaction denial and had been continuously earning profits from it. Posco also said the price of related products such as cold-rolled steel plate and cars in Korea had risen or their supply had decreased. The Supreme Court decided that it was difficult to acknowledge that Posco had suffered injustice in that occurrence or that such concerns were unproven. The court also ruled that to acknowledge injustice was difficult just because a business operator had suffered a disadvantage due to refusal to perform an transaction, and that the Fair Trade Commission must prove "the decline of transaction was an act of concern of competition restriction effects such as increase in product price, decline in supply, impediment to innovation, decline in the number of potential competitors and reduced diversity."

In this case, the Supreme Court explicitly demanded from the commission an economic analysis that proved Posco's act violated fair trade law, and this raised the importance of economic analysis in the enforcement of competition law.

3.2.2.2 Microsoft's Tie-in Sale

Microsoft and subsidiary Microsoft Korea caused a problem by combining a media server program, media player and messenger program while selling server and PC operating systems in Korea. The Fair Trade Commission ruled the bundling of items constituted an unfair tie-in sale and violation of "the act of interfering business activity," "the act of impeding consumer benefit" among abuse of market dominant position, and "tie-in sales" among unfair transactions.

In this case, the defendants said their PC operating system, Windows, and WMS (Windows Media Service) or WMP (Windows Media Player) were the same product, adding that the bundled sale of these systems reduced costs like those of distribution, promoted technological development and not only benefitted consumers but also spurred competition in the relevant market. On this, the commission ruled that the bundled sale was tantamount to abuse of market dominant position and unfair transactions on the grounds that they caused several negative effects. First, the bundled sale generated ubiquity in WMS and WMP consumption and provided a competitive advantage in the media server program

market, leading to interference in the business activities of other business operators. Second, the bundled sale was deemed to restrict competition in the media server program market and interfered in the business activities of competitors. Third, the bundled sale restricted competition in the media server program market and impeded consumer benefits or was highly likely to do so.

In this case, the commission rejected Microsoft's denial of violations one by one on the grounds of economic analysis. At the same time, the watchdog clearly proved through economic analysis that the bundled sale by Microsoft constituted abuse of market dominant position. The important contents of Microsoft's violation as verified by the commission's economic analysis can be summarized as follows.

- Windows PC operating system and WMS or WMP are separate products.
- The defendants' act compels the purchase of WMP by other parties who do not want the program.
- The bundled sale puts the other party to the transaction at a disadvantage.
- The bundled sale restricts competition in the streaming media player market.
- Due to the ubiquity of WMP and competitive advantage from this ubiquity cause tipping effect to WMP.
- The bundled sale erects an entry barrier in the media player market.
- The bundled sale restricts competition and interferes in the business activity of competitors.
- The bundled sale infringes on consumers' right to choose for media server programs.
- The competition restriction effect due to the bundled sale reduces technological innovation and impedes consumer benefits.

3.2.2.3. Intel's Discriminative Rebate

Intel abused its dominant position in Korea's CPU market and provided rebates to PC manufacturers in Korea such as Samsung Electronics and Trigem Computer on the condition that they not buy CPUs from Intel competitor AMD (Advanced Micro Device). The Fair Trade Commission judged that Intel's act was unfair to a competing business in Korea's CPU market and constituted abuse of market dominant position.

In this case, the commission adopted as the method of economic analysis the cost-price test, which is often a standard for deciding the illegality of a royalty rebate. More specifically, this method decides whether a business can compete with a market-dominant business operator when the latter provides conditional rebates by calculating an effective price that applies to a commercially viable share and comparing it with average cost.

Through this test, the commission proved that Intel's competitor AMD found it impossible to compete with Intel's prices, taking Intel's rebate into account even when AMD gave its CPU free to PC manufacturers in Korea, and under this rebate system, AMD significantly reduced its price but offered no incentive for Samsung Electronics to purchase AMD's CPU unless the price was negative. The commission through an analysis of market conditions also found that markets affected by Intel's rebate had noticeably low shares of competitors compared to places unaffected. Based on this, the watchdog ruled that Intel's rebate system was abuse of its market dominant position.

3.3. Unfair Common Action

3.3.1. Related Regulations

Article 19 of the Fair Trade Act prohibits unfair restriction of competition jointly with other business operators by contract, agreement, resolution or any other way. Types of the unfair common actions are as below.

- Act of deciding, maintaining or changing price
- Act of deciding business terms and conditions and payment terms for price or cost
- Restriction on production, release, delivery or transaction of product or service
- Restrictions on trading area or other party to transaction
- Interference or restriction of establishment or extension of facilities or introduction of equipment
- Restriction on type and standard of product or service
- Establishment of company that jointly executes or manages major parts of sales
- Common actions in bidding and auctions
- Other acts that result in restricting competition

3.3.2. Characteristics of Economic Analysis in Common Action and Penalty

In enforcing competition law, common action has characteristics different from other types of violations. While the problems of abuse of market dominant position, corporate mergers and unfair transactions are the anti-competitive effects that such acts have, the major issue of unfair common actions is the existence of the acts themselves. Thus as for common actions, violations of competition law are decided based on their existence.

For this reason, there is a relatively low chance that economic analysis will be conducted for determining the illegality of an unfair common action. Because the

existence of the act determines whether there was a violation of law, it is common for the related business operator to deny the existence of such an act, and economic analysis is sometimes used to estimate the existence of the act as circumstantial evidence of the common action. Even in these cases, however, it is difficult to prove illegality with only circumstantial evidence and without direct evidence, and the competition policy authority focuses on the "investigational approach" to search for direct evidence in uncovering common action rather than using economic analysis.

In this respect, economic analysis is used more for calculating the amount of damages from common actions proven illegal in unfair common actions rather than providing evidence of illegality. Damage from unfair common actions affects consumers, competing businesses and market participants, and the amount of damage is calculated through economic analysis to estimate the corresponding penalty and decide the scale of civil compensation for damage.

3.3.3. Major Judgment Cases

3.3.3.1. Unfair Common Action of Five Oil Companies (2011)

Five oil companies in Korea agreed to restrict the transactions of other parties with gas stations by rejecting business with pole sign gas stations of competitors or gas stations of previous competitors, and restricted competition in the Korean market for light oil petroleum products such as gasoline, kerosene and diesel being provided through gas stations. The Fair Trade Commission decided that this corresponds to unfair common actions, imposed a fine of 432.6 billion won and reported the relevant companies to the Prosecutor General.

The commission defined the extent of relevant products to light oil petroleum products that the defendants provided to independent gas stations through economic analysis, and excluded those unlikely to be affected by common actions from relevant products. The five companies claimed that the extent of exclusion from relevant products must be expanded and that relevant sales should be controlled, but the commission dismissed this. The period of violations by the companies was assessed and relevant sales were calculated by each company.

The commission had considered that the solidity and continuity of this common action were weak, that there was no agreement on supply price or output, and that the effect on consumers was limited. It decided that this common action was part of "violations with low importance" and lowered the penalty standard to 1 percent. After deciding the general penalty by defendant, the commission modified the amount for each defendant by considering their histories of fair trade violations, activeness in participating in common action and the benefits earned from common

action. The state of the conditional period was considered again for the decided penalty, a random amount of penalty was modified again and a fine of 432.6 billion won was imposed.

3.3.3.2 Unfair Common Action of Four CRT Glass Businesses (2012)

Four CRT glass manufacturers in Korea and Japan including Samsung Corning and Nippon Electric Glass jointly set prices with competitors and allocated customer share, agreeing on production restrictions. Explicit types of agreements established in the cartel meeting were those on sale prices, allocation of customer share and information exchange for production reduction to prevent price decline.

The Fair Trade Commission judged this case as a severe violation of fair trade law, as the domestic market share of the cartel exceeded 90 percent, and only competition restriction effects were the result while efficiency rose very little. This common action was maintained to alleviate falling prices and deteriorating profitability from the continuous fall in CRT glass prices due to rapid changes in the market, and the association and execution structure among defendants were not strong in the common action. So the commission set the penalty standard rate at 3.5 percent. Then the extent of the cartel's calculated sales amount was decided through economic analysis, and a general penalty was calculated by applying the penalty standard rate.

The commission saw the need to raise the fine since this cartel was systematically run at the company level. But given that the relevant companies cooperated with the investigation and had difficulty in management due to falling profitability, while the CRT market as deemed a consumer-dominant one and the execution of the agreement on common action was only partially carried out, the commission halved the fines for each defendant. Through this process, a combined fine of 54.5 billion won was imposed on the four cartel companies in Korea and Japan.

4. Economic Analysis as Information Infrastructure for Competition Policy

4.1. Competition Policy and Market Information

For the effective forwarding and execution of competition law, comprehensive information on national industry, market conditions and corporations is important. An effective political maneuver is possible if competition policy authorities fully understand how the extent of competition is changing throughout the country, what features mega-corporations or business groups that hold absolute influence

in industrial organization and market structure have, how the overall industrial structure of the nation and market structure are changing with it, and what industries and markets need special attention in competition policy. If such data on industries and markets is fully understood, a preemptive response to select problems in competition policy are possible, and the political effect will be strengthened.

Securing information on industries and markets and subsequent analysis are important in establishing and executing competition policy as it provides the function of competition advocacy. The competition advocacy function includes activities that lead the economic society overall to become competition-friendly by improving the legal and institutional business environment in a market-friendly way, and enhancing social consensus on market economy and competition policy. This can be more important than exposing and punishing individual violations of competition law over the long term, as it creates a competitive market environment at the social base. Once the data on industries and markets is transparent, the question is if it is possible to grasp the institutional and artificial factors that hinder the smooth operation of market function beforehand and form a social consensus to improve them, as well as if market information can be a factor, solution and evidence to devise a competition policy response for a market with a highly monopolistic and oligopolistic structure.

In Korea, statistical infrastructure that can figure out the conditions of industries and markets are organized, and research and analyses on industries, markets and corporations using this infrastructure are being conducted. Three types of information on industries and markets exist today.

First is statistical information on activities of industries and corporations. This data is geared toward industry and corporation policy to a large extent. Although not just for competition policy, the information is being used as basic market data in competition policy. Second is the creation and analysis of market structure statistics, or information that measures market structure throughout the economy through industrial statistics and analyzes them. This contributes to raising understanding of the extent of competition in the overall economy and grasping what the competition policy authority should focus on beforehand. Third is in-depth research and analysis on a specific industry. The Fair Trade Commission conducts comprehensive and in-depth research on industries that require special attention in competition policy internally or in connection with outside scholars, focusing on overall conditions of an industry and market, related policies and systems, and public and private restrictions that impede competition. The accumulated information from these studies are greatly utilized in the execution of competition policy.

4.2. Basic Information on Industrial and Corporate Activity

In Korea, statistics are being compiled and supplied that can provide understanding of industrial and corporate activities and information on individual businesses. A great deal of this data is compiled by the government but recently, data from the private sector is also increasing. Among the more important of such information is introduced here.

4.2.1. Industrial Structure Statistics

Industrial structure statistics are comprehensive numbers that cover the overall economy of industrial and corporate activities from Statistics Korea. Such statistics are recommended by the United Nations and other international organizations, and in addition to Korea, other countries such as the U.S., Japan, nations in Europe and others are compiling them. Industrial structure statistics comprise basic information for economic policies such as comprehension of an economy's overall size, features and extent of the development of national industries and industrial policies, but are also often used in competition policy. Such numbers help set a long-term direction for competition policy since they provide information on structural change, developmental forms of the overall economy, and general distribution of corporate scale.

As for industrial structure statistics in Korea, the Economic Census is a comprehensive statistical survey conducted every five years that targets every establishment and collects annual survey statistics by industry such as manufacturing and services. These statistics have the qualities of basic information on the national economy and industry, and are being widely used as basic data in policy development, academic research and corporate activities.

Industrial structure analysis of Korea is not only used as aggregated data but also microdata. Statistical data is important as aggregation, but its value as information goods become greater when statistical users can utilize individual information on studied corporations (or establishments). Statistics Korea has developed ways for users to utilize information on individual businesses and is implementing them on the assumption that it strictly protects the secrets of business operators. This has improved the value of statistical studies and enabled the use of more detailed and accurate information in policy developments, including that of competition. Expansion of statistical data use as microdata is a major development in the recent statistics policy of advanced countries.

4.2.2. Online Provision of Conglomerate Information

Conglomerates are significant players in Korea's competition policy. Because they take up a high proportion of the Korean economy, not only is the proportion overwhelmingly high but also affiliates of conglomerates hold a dominant position in individual industries or markets. Because of this, conglomerates are considered important political factors in Korea's competition policy.

For this reason, the Fair Trade Act of Korea implements a regulation system for conglomerates, unlike in other countries. A system to prevent economic power concentration in the act defines restrictions on conglomerates, and the major concerns are definition of conglomerate, public announcement and public system, mutual investment system, debt guarantee limit system, holding company system, and restrictions on voting rights of finance and insurance businesses and on illegal support.

The Fair Trade Commission is operating the Online Provision of Enterprises Information System (OPNI) as a database of conglomerate interrelated corporations. OPNI provides the corporate data reported from conglomerates that are subject to the preventive system after obtaining the database. This got information on conglomerates to become more transparent and provided understanding of competition policy to the people. The data was also used more broadly in the aspect of policy and academia.

Initially, OPNI focused on preliminary restrictions on conglomerates such as the restrictive system on total investment amount under the Fair Trade Act. As criticism increased over the way the preliminary restriction system was acting as an excessive restriction on conglomerates, competition policy authorities gradually converted the system to post-regulation. As restrictions on conglomerates changed to reinforcement of market surveillance instead of direct restriction, OPNI was created to expand the market surveillance base in 2007.

OPNI is a comprehensive public information database that contains the status of a company, stockholder, investment, debt guarantee and holding company submitted by each corporation and mutual investment limited conglomerates, debt guarantee limited conglomerates, and affiliate companies of a holding company as defined in the Fair Trade Act. Data provided in OPNI is being used as important basic information not only in competition policy but also government economic policy toward conglomerates and academic research on conglomerates.

4.2.3. Private Corporate Information Database

As corporate activities are being carried out in more complex and diverse ways, and especially as the effect of large corporations on the national economy is increasing, social demand for information on individual corporations for various purposes is growing. Such data is increasingly being used as investment information for the public, basic data for academic research, basic information for government policy development and essential information for enforcement of competition policy. A corporate information database is usually developed and provided by the private sector.

A stock exchange provides detailed information on the status of listed corporations. This is to help investors invest with a more transparent background for market information. The purpose of corporate information is to make the stock market more transparent, but is also being widely used as academic and political data.

Private credit evaluation agencies such as Korea Investors Service Inc. and National Information & Credit Evaluation Inc. are also operating corporate information databases independently. Their databases provide clients with multidimensional information on corporate activities such as ownership structure, business activity and the corporate performances of about 300,000 companies that do business in Korea. Direct demands of these databases are private, but large think tanks are also using this information as research data. While corporate finance data is generally insufficient, this corporate information database of private corporations is considered a comprehensive source of information on Korean companies.

4.3. Creation and Analysis of Market Structure Statistics

4.3.1. Importance and Roles of Market Structure in Competition Policy

The purpose of competition policy is to improve economic efficiency through competition stimulation and increase in consumer benefits. So under what conditions is stimulation of competition possible? Early in the history of industrial organization theory, a unilateral relationship was said to be established in the order of structure, behavior and performance. Thus monopolistic market structure was said to create monopolistic market behavior, and this is again connected to monopolistic market performance. So for competition to operate effectively in the market, creating a competitive market structure (=decentralization of market) is extremely important.

As economics developed, however, the structure - behavior - performance theory faced a lot of challenges. Even so, market structure is acknowledged as the most critical factor in determining the extent of market competition, and there are also times when the standard of illegality lies with market structure. In this respect, no better objective indicator generally describes the overall level of market competition than market structure, so market structure is deemed the most important among several factors that indicate competition level in the market in establishing and executing competition policy throughout the world.

Competitive market performance is expected not only in circumstances in which market structure is highly dispersed. Although market structure is monopolistic, if a monopolizing corporation is continuously aware of the possibility of the entry of new corporations and takes the same action as business operators in competing markets, effective distribution of resources can be expected. But if market structure is not competitive, market performance will depend on the behavior patterns of corporations, and the latter will be determined by market conditions. Therefore, evaluating the extent of competition beforehand is hard without in-depth analysis for a market with monopolistic structure. On the contrary, if market structure is competitive and there is no artificial restriction that could impede competition such as cartels, stimulation of competition will be guaranteed and effective resource distribution can be expected.

Measurement of market structure is crucial in this matter. In competition law, the general assumption is that sufficient competition is going on in a market if market structure is competitive, and if market structure is monopolistic, there is the probability of inefficient resource distribution due to the existence of monopolistic profit. In other words, market structure is an important standard that primarily filters a market's competition status.

Market structure refers to the number of corporations in a market and the relative scale distribution. Market structure becomes closer to a monopoly if fewer corporations are in the market and the scale distribution of companies is more unequal, and the closer the market is to a monopoly, the higher the possibility that market dominance (monopolistic strength) will be created. Market structure is an index that represents the degree of competition, which is becoming an important standard in the establishment and execution of competition policy. In the Fair Trade Act, market structure is the standard for estimating a market-dominant business operator and the primary standard for deciding competition restrictiveness of a corporate merger. Also, market structure is an important consideration in deciding the extent of illegality when enforcing regulations on unfair transactions. Not only in Korea, but also in the U.S., Japan, EU and most other countries, market structure is important as a standard measuring degree of competition and in deciding the

restrictiveness of competition.

Dozens of indexes that represent market structure (market structure index) have been developed, but the indexes generally being used in competition policy are CR_k and HHI (Herfindahl-Hirschman Index). The concentration ratio of the top k corporations equals the sum of market shares (S_i) of the top k corporations in a market, and its definitional identity is as follows.

$$CR_k = \sum_{i=1}^{k} S_i$$

HHI is the sum of the square amount of the market shares (S_i) of all corporations, and defined as follows.

$$HHI = \sum_{i=1}^{N} S_i^2$$

N = No. of corporations in the relevant market

Although CR_k has previously been used a lot in competition policy, use of HHI has increased recently because of its excellent attributes as a structure index. The U.S. in the past used CR_4 as the standard for judging anti-competitive corporate merger, but converted to HHI since the enactment of the Merger Guideline in 1982. In Korea, the Fair Trade Act has also adopted CR_1 and CR_3 as standards for estimating a market-dominant business operator and anti-competitive corporate merger, and HHI is used as the standard for deciding the degree of competition restriction in the Merger Guideline. The same goes for Japan.

〈Table 3-2〉 HHI as Competition Restriction Standard in Corporate Merger Evaluation

Country	HHI Reference point	Political meaning	No. of same scale corporations1)
Korea	1,200	Boundary of existence of competition restriction	8.3
	2,500	Boundary of judgment of competition restriction	4
U. S.	1,000	Boundary of existence of competition restriction	10
	1,800	Boundary of judgment of competition restriction	5.6
Japan	1,500	Boundary of existence of competition restriction	6.7
	2,500	Boundary of judgment of competition restriction	4

Note: 1) Inverse number of HHI (1/HHI) that indicates the number of corporations when the relevant market is constituted of hypothetical corporations of same scale

As shown above, market structure is the most important factor in measuring degree of competition and the critical standard for judging restrictiveness of competition in competition laws in Korea and other countries. So market structure is the most important factor in measuring the degree of competition in a specific market, and can be a potential surrogate variable as well. In this aspect, creation and analysis of market structure statistics for the overall industry can be significant information that shows the overall degree of competition in the national economy.

4.3.2. Creation and Analysis of Market Structure Statistics

4.3.2.1. Creation

The Fair Trade Commission compiles market structure statistics every year (CR3 and HHI) as basic information for the establishment and execution of competition policy, and announces analysis reports on the results. In the U.S., industrial concentration statistics according to the North American Industry Classification System (NAICS) are based on the Economic Census conducted every five years by the Census Bureau of the Commerce Department. Japan Fair Trade Commission also announces statistics on overall market structure focusing on products with high concentration or major products that are important in daily life every two years.

The compilation and analysis of market structure statistics in Korea were first conducted in 1977 by KDI researchers. This was before the Fair Trade Act was enacted in Korea, and this research was frequently used as theoretical and practical evidence that supported the introduction of a fair trade system. Afterwards, KDI researchers compiled statistics on industrial concentration and market structure and published analysis reports on the statistics every four to five years. These studies were extensively used as basic information for the development and execution of fair trade policy. Furthermore, KDI researchers completed statistics on industrial concentration and market structure per request from the Fair Trade Commission and provided them to the watchdog. These statistics, however, were unofficial and not authorized by the government.

In the 1999 amendment to the Fair Trade Act, the compilation and announcement of structure statistics were carried into court. Article 3- of the act said, "The Fair Trade Commission must establish and implement solutions to promote competition in the supply or demand market of products or services that the monopolistic and oligopolistic market structure has maintained for a long time." In Article 3- , the compilation of market structure statistics was indicated in the line "The Fair Trade Commission shall investigate and announce market structure to establish and carry forward the policy of regulation in Article 1." In accordance to this, the government has approved market structure statistics as official statistics

since 2000, and compilation of the statistics went from being done every other year to every year in 2010.

4.3.2.2. System, Method & Scope of Creation

The Fair Trade Commission is the main agent for compiling market structure statistics. For the compilation and announcement of market structure statistics, related tasks can be commissioned to government-funded institutes. Under this regulation, KDI is assigned by the commission to collect market structure statistics each year, and receives microdata of industry structure statistics from Statistics Korea to do this. KDI compiles statistics and analysis reports and submits them to the commission, which then makes public the market structure statistics and analysis reports through its website and Korea's national statistics portal.

KDI also conducts independent research on market structure analysis, apart from commission from the Fair Trade Commission. As opposed to studies contracted by the commission with a usually standardized format, the independent studies of KDI are undeterred by format and research and analysis can be done more freely. And what is considered significant here is again applied to the contract study assigned by the commission.

To compile statistics in industrial concentration and market structure, complete enumeration data on sales by individual corporations by industry (or product) is needed. Statistics targeting the activities of corporations (or establishments) are being collected in Korea, and as for complete enumeration, statistics like 「Report on the Mining and Manufacturing Survey」 (1 year cycle) target mining and manufacturing businesses and 「Economic Census」 (five-year cycle) targets the entire industry. Statistics similar to 「Report on the Mining and Manufacturing Survey」 are being collected in many countries including China, Japan and the U.S., and although 「Economic Census」 was started in the U.S., China has had one since 2000 followed by Korea and Japan.

To collect statistics on industrial concentration and market structure based on the microdata of 「Report on the Mining and Manufacturing Survey」and 「Economic Census」, which are the most basic statistics on national industry, two problems must be solved. First, industry structure statistics are being studied using the unit of establishments, and changing the unit to corporations is required. Second, the use of individual information on the subject of a study is strictly restricted in the statistical systems of many countries, and statistics of industrial concentration and market structure are possible only when the statistical authority provides information on individual corporations.

Statistics Korea has made many efforts so that statistics using establishment as a unit can be changed to using a corporation as the unit. As the result of developing 「Establishment Corporation Population DB」, which connects establishments and corporations, the establishment-corporation connection has been made possible for the industry since the mid-2000s. The problem of using individual corporations (or establishments) as units was solved without difficulty by the efforts and persuasion of the Fair Trade Commission, which urgently needed market structure statistics, the active cooperation of Statistics Korea, and the proper adjustments and accumulated research experience of KDI.

4.3.3. Contents of Market Structure Analysis

The 『Market Structure Analysis』 KDI produces and submits under contract with the Fair Trade Commission is largely composed of three parts: ① basic information analysis for compiling statistics on industrial concentration and market structure, ② compilation and analysis of statistics on industrial concentration and market structure, and ③ compilation and analysis of statistics on conglomerates.

① explains basic information and statistics standard related to compilation of statistics on industrial concentration and market structure such as the meaning of market structure in competition policy, definition, attributes and the meaning of market structure measurement index, and the basic attributes of industry structure statistics, which are the basic data for compiling market structure statistics, and the process of converting establishment-oriented statistics into corporate statistics. Along with this, the report analyzes overall industry trends, features of sector structure and changes shown during the analysis period.

② is the major content of market structure analysis. Here, general concentration statistics targeting the entire industry are compiled and trends are analyzed. Then market structure statistics (CR3 and HHI) by industry and item are used in the five unit classifications of KSIC and product classification levels. Based on the collected statistics on industrial concentration and market structure, market structure analysis by features of industry and item, time-series analysis of market structure and analysis of rooted monopolistic and oligopolistic industries are conducted.

③ is the creation and analysis of statistics on chaebol (Korean conglomerates), the distinctive corporate organizations in Korean business. Chaebol occupies an important part in Korean industry, and this analysis report collects and analyzes statistics on the proportion of chaebol in Korean industry, chaebol's monopolistic and oligopolistic position in specific sectors and product market, and business diversification activities (inter-market activities).

4.3.4. Limitations and Significance of Market Structure Analysis

To properly understand market structure, in-depth analysis on an individual market is needed. To understand market structure, the extent of the market must be delineated first and this requires complex and meticulous analysis. For example, for regulation of limiting a corporate merger, market delineation itself is directly linked to a judgment of illegality because market structure is applied as the absolute standard of judging violations of law. So most economic analyses for judging illegality of corporate mergers can be said to be market delineation tasks.

Extremely difficult and complex analysis is required in market delineation, so to delineate all markets in the overall industry through analytic methods is impossible. To comprehend the general degree of competition in the overall industry, a general measure is to gauge market structure by hypothesizing statistical classification standards as the market boundary. The use of market structure statistics is limited because they are not a market index in an economic sense but rather an index on abstract market structure according to the statistical classification system. These statistics are difficult to use as data for judging illegality in specific cases of Fair Trade Act violations.

Despite the limitations of market structure statistics, they hold great significance in competition policy. They can be used as potential basic information for grasping the overall degree of competition and changes in the entire economy, or understanding industries or market groups that the competition policy authority should pay special attention to. In this regard, market structure statistics are important as political infrastructure in that they suggest the reference point for fair trade policy despite its limitation.

Market structure study statistics largely contribute to the establishment and execution of fair trade policy by objectively showing the status and features of industrial concentration and market structure in Korean industry. The U.S. and Japan have long had market structure statistics as basic data for the forwarding of competition policy, and although Korea was late to start this, its preparation of official market structure study statistics on a national level led to faster development of competition policy. Market structure statistics are being widely used not only in competition policy but also in related academic studies.

4.4. In-depth Study on Industry and System

The Fair Trade Commission conducts in-depth studies on specific industries and systems as basic information for efficient development and enforcement of competition policy each year. These studies are mostly commissioned through

contracts with outside scholars or experts. The study results are used in competition policy, and besides the direct effect, they give the subsidiary effect of reinforcement of network between the commission and outside experts as well as enhancing academic interest in competition policy. The study area of such commissioned studies can be largely divided into three categories.

The first is a study on improvement of laws and regulations related to competition policy. The competition law system of Korea consists of many laws and regulations, with the Fair Trade Act at the center. Extensive research, study and analysis of the evaluation of policy and system and trends and legislation of foreign policies are required for the enactment and amendment of laws and legislation related to competition law and their improvement. In-depth studies on this are commissioned to outside experts. The study results obtained are applied to the improvement of laws and regulations related to competition law. Many statues in Korea's competition law system have been established and improved on based on such study results.

Second is a study on related laws and regulations that affect competition policy. The Korean economy has many cases of restriction on market competition due to laws and regulations, and this study has discovered the effects of related laws and regulations on competition, political objectives that the related law system seeks and the validity of measures, balance of related policies and competition policy, and methods to improve related policies. On the improvement of policy and law tasks and regulations generated from this, the Fair Trade Commission consults related political authorities to draw conclusions on improvement methods. This study also enhances understanding by other policy authorities of competition policy along with improving related systems. This is an important part of the competition advocacy function that the competition policy authority conducts.

Third is an in-depth study on a specific industry or market. This study aims to find competition policy measures to an industry that might have problems in competition policy through extensive and in-depth analysis on basic status of the industry and market, state of the market and competition, and laws, regulations and restriction systems around related sectors and markets. The results of this study enable a preemptive response by competition policy authority to a problematic industry and market in competition policy, and helps enhance the effect of competition policy.

Major studies commissioned by the Fair Trade Commission in recent years are summarized in <Table 3-3>.

〈Table 3-3〉 Major Studies Commissioned by Fair Trade Commission

Research area	Major research cases
Improvement of competition law-related system	Study on complete revision of Electric Commerce Consumer Protection Act
	Economic analysis on effects of competition law enforcement
	Study of types of unjust indication and advertising and revision of standard
	study on method to improve non-horizontal merger examination standard
	Performance assessment of Fair Trade Act after 30 years of implementation and future political directions
	Methods to improve compliance program (CP)
	Study on leniency program of EC
	Study on estimation of consumer damage from unfair common action
	Study on method to improve common action examination standard
	Comparative study on corrective measures on common action
	Manual on competition effect assessment
	Review of corporate merger simulation model
Study on laws and regulations affecting competition policy	Study on revision method of Product Liability Act
	Study on improvement of cooling off system to respond to changes in e-commerce environment
	Revision plan for Public Notice of Critical Information System for reinforcement of green information provision
	Study on procurement of fair competition related to standard patent selection and reasonable licensing method
	Study on consumer orientation of policies and regulations by government departments
	Policies toward competition and environment
In-depth study on industry and market	Analysis of use of terms and conditions in private education market and consumer protection methods
	Pre-assessment of competition among major monopolistic and oligopolistic industries
	Study on method of procurement of soundness of consumer cooperatives such as mutual aid project
	Market analysis on online education industry
	Market analysis on multi-channel broadcast service industry
	Unfair transactions in open market and improvement methods
	Study on anti-competitive actions related to intellectual property of pharmaceuticals
	Analysis of charging system of mobile communication field and competition status
	Method of activation of competition in Web browser market
	Analysis of restrictiveness of competition in public procurement area and measures
	Sales commission of large retailers and political measures
	Competition law on co-marketing in pharmaceutical market

5. Assessment and Tasks

Competition policy in Korea has been quickly developed over the last 30 years despite a history shorter than in other advanced economies, and Korea's competition policy is being executed at a similar level of advanced countries. Korea's economy has gone from a situation in which various forms of economic regulation was generalized under a government development strategy to a genuine market economy, and is considered a competition policy success hard to find elsewhere in the world.

Several factors helped the development of market economy in Korea where market functions and competition are respected, with competition policy playing a great role. Korea in 1908 privatized the basis of economic management, which used to be driven by the government, and the most symbolic policy marking this change was the implementation of competition policy. The Monopoly Regulation and Fair Trade Act, Korea's top law on fair trade, was promulgated over this time period and competition policy was developed as basic regulation in Korea. Competition policy in Korea has not just remained as enforcement, but it established its function of "competition advocate" such as development of market function throughout the economy and promotion of competition, reestablishment of government-market relations and higher understanding of market economy.

The development of Korea's competition policy has a lot to do with continued research and analysis of fair trade authorities. They developed logic to persuade other policy officials or people by using economy analysis to get the Korean economy to be more competitive, and the growth of economic reforms and market economy was based on this theoretical and practical logic. Korea's competition policy authority has been hailed as performing better than any other government ministry in related policies and research and analysis.

Competition policy in Korea has been assessed to have developed rapidly after economic analysis was implemented in the execution process. The notion of competition policy, something which was implemented under the government-planned economy era, was unfamiliar to the private sector. As the competition policy authority reinforced the execution, however, private corporations could not help but respond to the policy and used economic analysis as a means to respond. As such, logical confrontation based on the economic analysis of private corporations and competition policy authority was an important factor in developing competition policy in Korea.

The Fair Trade Commission should be lauded for its achievements, having accepted the claims of private corporations as their exercise of rights in a horizontal

structure and displaying corresponding logic. In the past, relations between the Korean government and corporations were unequal and were more of a vertical structure. It took courage for the competition policy authority to acknowledge corporations equally and fight for legitimacy with logic rather than pressure, and this should be rated as huge progress in Korea's economy.

As such, economic analysis has greatly contributed to the development of Korean competition policy, but tasks remain. The importance of economic analysis in establishment and execution of competition policy is expected to grow, and the Fair Trade Commission must actively respond to this.

The enforcement of the Fair Trade Act will be reinforced and the weight of sanctions for violations will be strengthened, so corporations will respond to the commission's decisions and reinforce economic analysis. Fair trade authorities must also strengthen their capacity to analyze the economy and network with external experts. As industrial development is moving from manufacturing to IT and the service industry, where the importance of competition policy is relatively weak, the commission must expand and intensify economic analysis of more industries and markets.

Korea's great task at hand is economic reform and all economy authorities are contemplating changing the direction of Korea's economy. Whatever the details of economic reform are, however, the entire flow will apparently focus on market function and move toward promoting competition. In this situation, the commission has the responsibility to demonstrate active leadership. To lead change in economic management and reform, thorough preparation of theory and logic is required and economic analysis is the most important tool to support this.

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