KOREA

TRADE SUMMARY

The U.S. goods trade deficit with Korea was $13.1 billion in 2011, up $3.1 billion from 2010. U.S. goods exports in 2011 were $43.5 billion, up 12.0 percent from the previous year. Corresponding U.S. imports from Korea were $56.6 billion, up 15.9 percent. Korea is currently the 7th largest export market for U.S. goods.

U.S. exports of private commercial services (*i.e.*, excluding military and government) to Korea were $15.1 billion in 2010 (latest data available), and U.S. imports were $7.8 billion. Sales of services in Korea by majority U.S.-owned affiliates were $10.2 billion in 2009 (latest data available), while sales of services in the United States by majority Korea-owned firms were $6.8 billion.

The stock of U.S. foreign direct investment (FDI) in Korea was $30.2 billion in 2010 (latest data available), up from $26.8 billion in 2009. U.S. FDI in Korea is led by the manufacturing and banking sectors.

UNITED STATES-KOREA TRADE AGREEMENT

In 2011, following an agreement in December 2010 that resolved outstanding issues related to automobiles and other matters, the Administration continued to build on extensive consultations with Members of Congress and other stakeholders to produce strong bipartisan support for the United States-Korea trade agreement (KORUS). On October 12, 2011, Congress passed, and on October 21, 2011, President Obama signed into law, legislation approving KORUS. Shortly thereafter, on November 22, 2011, Korea's National Assembly also approved the agreement. On March 15, 2012, KORUS entered into force, providing preferential access for U.S. businesses, farmers, ranchers, services providers, and workers to what is now the United States' seventh largest export market, while helping to solidify the two countries' long-standing alliance, and underscore the U.S. commitment to and engagement in the Asia-Pacific region. KORUS will strengthen and expand ties with an important strategic partner in Asia, and is expected to increase annual exports of American goods by up to $11 billion, supporting 70,000 jobs from goods exports alone.

The agreement provides for the elimination of tariffs on over 95 percent of U.S. exports of industrial and consumer goods within 5 years and on nearly two-thirds of U.S. agricultural exports immediately, and will level the playing field and enhance market access for U.S. exporters, including those in the automotive sector. KORUS will provide meaningful market access commitments across virtually all major service sectors, including improved access for telecommunications and express delivery services, and the opening up of the Korean market for foreign legal consulting services. The agreement will increase access to the Korean market and ensure greater transparency and fair treatment for U.S. suppliers of insurance and other financial services. KORUS will also address nontariff barriers in a wide range of sectors and includes strong provisions on intellectual property rights, competition policy, labor, environment, and regulatory transparency.

In December 2011, the United States and Korea began to review each country's respective laws and regulations to ensure their consistency with the provisions of the agreement. This review process has successfully concluded and the agreement entered into force on March 15, 2012. USTR will monitor Korea's compliance with its obligations.

IMPORT POLICIES

Tariffs and Taxes

Korea's average most favored nation applied tariff rate in 2010 was 12.1 percent for all products (48.5 percent for agricultural products and 6.6 percent for non-agricultural products) and Korea has bound 94.6 percent of its tariff lines.

Korea maintains particularly high tariffs on a number of high value agricultural and fishery products. Korea imposes tariff rates of up to 30 percent on nuts and 35 percent and higher on most dairy products. Pears, table grapes, juices, starches, and peanut butter are subject to tariffs ranging from 45 percent to 54 percent. Tea and peanuts, with some exceptions, are subject to some of the highest tariffs, ranging from 754 percent and 513 percent, respectively, for red ginseng tea and green tea to 230 percent for peanuts. Korea also imposes high tariffs on other products of interest to U.S. industry, despite having little or no domestic production, including cherries, certain distilled spirits, frozen corn, frozen french fries, pepperoni, and prepared or mashed potatoes.

Korea has established tariff-rate quotas (TRQs) intended to provide at least a minimum level of access to previously closed markets or to maintain pre-Uruguay Round access. In-quota tariff rates may be very low or zero. To help offset the increasing cost of food, in 2011 Korea announced emergency duty-free TRQs on a wide range of agricultural commodities including pineapples, malting barley, pork, frozen chicken, some frozen fish (including mackerel and Alaskan Pollack), powdered milk, frozen cream, processed milk and cream, butter, cheese and curd, egg powder, wheat, vegetable oils, some sugars, potato, soybeans, corn for feed and processing, frozen pork and pork belly. Nevertheless, the over-quota tariff rates are often prohibitive. For example, natural and artificial honey are subject to an over-quota tariff rate of 243 percent; skim and whole milk powder (176 percent); barley (324 percent); malting barley (513 percent); potatoes and potato preparations (more than 300 percent); and popcorn (630 percent). In addition, for some agricultural products, such as corn grits, popcorn, and soy flakes, Korea aggregates raw and value-added products under the same TRQ. Korean domestic industry groups, which administer the quotas, frequently allocate the more favorable in-quota tariff rate to their larger members that import raw ingredients.

Korea uses "adjustment tariffs" on some agricultural, fishery, and plywood products, which increase the applied tariff rates. Most of the adjustment tariffs are imposed on agricultural and seafood products, including frozen croaker, which are products of interest to U.S. exporters. Korea has eliminated tariffs on most or all products in the following sectors: paper; toys; steel; furniture; agricultural equipment; construction equipment; and information technology products (those included in the WTO Information Technology Agreement). Korea has harmonized its chemical tariffs to rates of zero percent, 5.5 percent, or 6.5 percent, depending on the product. Bound tariffs, *i.e.,* the level that generally cannot be exceeded under WTO rules, on textile and apparel products remain relatively high: 30 percent on several man-made fibers and yarns; 30 percent on many fabrics and most made-up and miscellaneous goods (*e.g.*, pillow cases and floor coverings); and 35 percent on most apparel items. KORUS will eliminate tariffs, including adjustment tariffs, on over 95 percent of originating industrial and consumer goods within five years. Almost two thirds of U.S. agricultural products became duty free on entry into force and virtually all tariffs on agricultural goods will be eliminated when KORUS is fully implemented.

Beef

Following a 2008 U.S.-Korean agreement to fully re-open Korea's market to U.S. beef and beef products, Korean beef importers and U.S. exporters have operated according to a voluntary, commercial understanding that limits imports to beef and beef products from animals less than 30 months of age, as a transitional measure, until Korean consumer confidence improves. Reopening fully Korea's beef market consistent with science and international standards as well as in a commercially viable manner remains an important priority. This issue is discussed in greater detail in USTR's 2012 Report on Sanitary and Phytosanitary Measures.

Rice

In the Uruguay Round, Korea negotiated a 10 year exception to "tariffication" of rice imports in return for establishing a Minimum Market Access (MMA) quota that was set to expire at the end of 2004. Korea subsequently negotiated a 10 year extension of the MMA arrangement in April 2005. The extension called for Korea to increase its total rice imports over the succeeding 10 years, from 225,575 metric tons in 2005 to 408,700 metric tons in 2014. Along with the country specific quota commitments to purchase minimum amounts of imports from China, Thailand, and Australia, Korea also agreed to purchase at least 50,076 metric tons annually from the United States until 2014.

Access to the Korean rice market for U.S. exports has improved significantly under this agreement. Under the 2011 MMA, the U.S. rice industry obtained 29 percent of Korea's total MMA imports by winning tenders for 101,490 metric tons of (milled) rice, valued at $87 million. In addition, the quality of access has improved as rice marketed to consumers as table rice was for the first time included as a portion of the MMA quota. In addition, nearly 32,062 of the 101,490 metric tons will be sold as table rice.

GOVERNMENT PROCUREMENT

Korea is a signatory to the WTO Agreement on Government Procurement (GPA). For procurement of construction services by sub-central and government enterprises covered under the GPA, Korea applies a threshold of over $23 million, which is three times the threshold applied by the United States. Under the KORUS, U.S. suppliers will have rights to bid on the procurements of more than 50 Korean central government entities, nine more than are covered under the GPA. The agreement also expands procurements to which U.S. suppliers will have access by reducing by nearly one-half the threshold applied under the GPA, from $203,000 to $100,000.

In December 2010, the Ministry of Knowledge and Economy (MKE) issued a notification establishing new procurement procedures for public entities related to MKE. U.S. industry raised concerns over evaluation criteria that appeared to give a preference to Korean small businesses. U.S. officials discussed this issue with Korean officials and conveyed the importance of ensuring that Korea complies with its commitments under the GPA. Following U.S. engagement on this issue, MKE issued guidelines to its related agencies reiterating that preferences should not be given to domestic businesses in procurement subject to the GPA.

Encryption Technology for Public Procurement of VoIP Equipment

In July 2009, Korea implemented a new regulation stipulating that encrypted network equipment must be certified by Korea's National Intelligence Service (NIS) in order to be procured by public sector agencies, while NIS will only certify encryption modules based on the Korean ARIA and SEED encryption algorithms, not the AES algorithm that is in widespread use worldwide. Some U.S. suppliers have been unable to sell virtual private network and firewall systems to Korean public sector agencies due to this restriction. We will continue to urge Korea to ensure that equipment based on widely used international standards has full access to Korea's public sector market.

INDUSTRIAL SUBSIDY POLICY

Historically, the Korea Development Bank (KDB), which as a government-owned entity is not necessarily bound by the same constraints as commercial institutions, has been one of the government's main sources of policy-directed lending to favored industries. The Lee Myung-bak Administration plans to privatize a wide range of state-owned enterprises, including the KDB. As a first step, Korea adopted a holding company system in October 2009 and divided the Korean Development Bank (KDB) into two new companies: (1) KDB; and (2) the Korea Finance Corporation (KFC). While still government-owned, the KDB is to operate as a commercial bank under this restructuring plan, and the KFC is to operate as a policy lending bank. The Korean government plans to list the KDB on the Seoul stock exchange and overseas stock markets in 2012. The U.S. Government will continue to monitor the lending policies of the KDB and other government-owned or affiliated financial institutions.

INTELLECTUAL PROPERTY RIGHTS PROTECTION

Korea generally provides strong intellectual property rights (IPR) protection and enforcement. The United States recognizes the importance the Korean government places on IPR protection, a development that has accompanied Korea's shift to becoming a significant creator of intellectual property. The 2009 amendments to Korea's Copyright Law include measures to deter copyright infringement via file-sharing platforms on the Internet. In 2010, the Korean government imposed sanctions against serial infringers under the "three strikes" law, and in 2011 it passed a law requiring online high-volume storage lockers ("webhards") to register with the Korea Communications Commission to address technical challenges related to online copyright enforcement. However, concerns remain over new forms of online piracy, corporate end-user software piracy, book piracy in universities, and counterfeiting of consumer products.

On December 2, 2011, Korea's National Assembly passed an amendment to the Copyright Act closing a sound recording protection gap for works produced between July 1987 and June 1994. This change expanded copyright protection for these works from 20 to 50 years, the same level of protection afforded for all other works.

Korea is also a signatory to the Anti-Counterfeiting Trade Agreement, which establishes an international framework to more effectively combat the infringement of IPR, in particular the proliferation of counterfeiting and piracy, which undermines legitimate trade and the sustainable development of the world economy.

In addition, KORUS contains state-of-the-art protections for all types of intellectual property, requirements to join key multilateral IPR agreements, and strong enforcement provisions.

SERVICES BARRIERS

Screen and Broadcast Quotas

Korea maintains a screen quota for films requiring that any movie screen show domestic films at least 73 days per year. Overall, foreign programs may not exceed 20 percent of terrestrial television or radio broadcast time or 50 percent of cable or satellite broadcast time on a semi-annual basis. Within those overall quotas, Korea maintains annual quotas that further limit broadcast time for foreign films to 75 percent of all films for terrestrial, cable, and satellite broadcasts; foreign animation to 55 percent of all animation content for terrestrial broadcast and 65 percent of all animation content for cable and satellite broadcasts; and popular music to 40 percent of all music content. Another quota, on a quarterly basis, limits content from any one country to 60 percent of the quota available to foreign films, animation, or music. KORUS will protect against increases in the amount of domestic content required and ensure that new platforms, such as online video, are not subject to these legacy restrictions.

Restrictions on Voiceovers and Local Advertisements

The Korean Broadcasting Commission's guidelines for implementation of the Broadcasting Act contain restrictions on voiceovers (dubbing) and local advertising for foreign retransmission channels. These prohibitions continue to be of concern to U.S. industry, as they limit the profitability of such channels in the Korean market.

Legal Services

The Foreign Legal Consultant Act of 2009 (FLCA) created a partial opening of domestic legal services. Under the FLCA, law firms from countries that have a free trade agreement with South Korea are able to start consultancy businesses in Korea. The law allows foreign attorneys with a minimum of three years of work experience to provide consulting services on the law of the jurisdiction in which they are licensed. Before the FLCA, only Korean-licensed lawyers could provide any form of legal advice in Korea, including advice on foreign law. In April 2011, the National Assembly amended the FLCA to allow a foreign legal consultant office to partner with Korean firms on cases with both foreign and domestic legal issues.

The Korean government plans to open its legal services market in several stages. The first step created a legal status for foreign legal consultants and allowed foreign law firms to open offices in Korea. The second stage allows cooperative agreements between foreign and domestic firms. Subsequent liberalization stages would address the ability of foreign-licensed lawyers and firms to establish joint ventures and hire Korean-licensed lawyers.

Over time, KORUS will permit free association of foreign legal consultants with Korean lawyers and allow U.S. law firms to offer a broader range of services.

Insurance and Banking

Korea is the second largest insurance market in Asia and the seventh largest in the world. Korea's laws and regulations permit foreign financial service providers to establish subsidiaries or branches in Korea.

Insurance suppliers remain concerned that Korea Post, the National Agricultural Cooperative Federation (NACF), and the National Federation of Fisheries Cooperative are not regulated by the Korean Financial Services Commission and therefore operate under different rules that may advantage these entities. The NACF Act, revised in March 2011, creates two holding companies: Nonghyup Economic Holding Company and Nonghyup Financial Holding Company. The Nonghyup Finanical Holding Company will include two new insurance subsidiaries, Nonghyup Life Insurance and Nonghyup Non-Life Insurance, which will be subject to the Insurance Business Act. USTR will closely monitor the implementation of the NACF Act to ensure that Korea complies with KORUS financial services provisions.

Lack of transparency in the adoption of financial regulations continues to adversely affect financial services suppliers. However, effective implementation of improvements in notice and comment periods and with respect to "administrative guidance" required under KORUS should enable financial services suppliers to play a greater role in the regulatory process.

Korea's strict data privacy rules require financial services providers to locate their servers physically in Korea, thus hampering foreign suppliers' ability to take advantage of economies of scale in the region to perform data processing in their daily business activity. Korea's implementation of commitments in KORUS will help address this concern.

Telecommunications

Korea currently prohibits foreign satellite service providers from selling services (*e.g.*, transmission capacity) directly to end users without going through a company established in Korea. Given the current investment restrictions in place (see below) and the fact that establishing a local presence may not be economically justified, this prohibition significantly restricts the ability of foreign satellite service suppliers to compete in the Korean market.

The National Assembly passed legislation in December 2007 to regulate the convergence technology Internet Protocol television (IPTV). In 2008, the newly formed Korea Communications Commission (KCC) began issuing implementing regulations and established the Framework Act on Broadcasting and Communications Development in 2010. The U.S. Government is closely monitoring this process with regard to transparency and due process. U.S. companies view some of the licensing requirements under discussion as market restricting (*e.g.*, applying content quotas to real time IPTV).

INVESTMENT BARRIERS

Capital market reforms have eliminated or raised ceilings on aggregate foreign equity ownership, individual foreign ownership, and foreign investment in the government, corporate, and special bond markets. These reforms have also liberalized foreign purchases of short-term financial instruments issued by corporate and financial institutions. Some U.S. investors have raised concerns, however, about a lack of transparency in investment-related regulatory decisions, including by tax authorities, highlighting concerns about possible discrimination.

Korea maintains a 49 percent limit on foreign shareholdings of facilities-based telecommunications operators. Foreign investment is not permitted in terrestrial broadcast television operations, and the Korean government also restricts foreign ownership of cable television-related system operators, network operators, and program providers to 49 percent. In March 2011, restrictions on previously closed areas were relaxed to 20 percent for program providers of channels that carry a range of programs and 10 percent for specialized news channels. For satellite broadcasts, foreign participation is limited to 33 percent. Foreign satellite retransmission channels are limited to 20 percent of the total number of operating channels. For Internet multimedia or news-focused broadcasting and retransmission cable networks, foreign investment is limited to 20 percent. Under KORUS, within two years from entry into force Korea will permit U.S. companies to own up to 100 percent of a telecommunications operator in Korea.

In addition to the investment restrictions in telecommunications and key services sectors described above, Korea maintains other important restrictions on foreign investment. Specifically, Korea prohibits foreign investment in rice and barley farming and imposes a 50 percent foreign equity limitation on meat wholesaling. Moreover, Korea limits foreign investment in electric power generation, distribution, and sales to 50 percent. It also restricts foreign investment in the areas of news agency services and publishing and printing, where it has foreign equity limitations of 30 percent for enterprises publishing newspapers and 50 percent for enterprises publishing other types of periodicals.

In July 2009, the Finance Ministry announced plans to sell a number of state-owned companies, including Korea Real Estate (KOREIT), Grand Korea Leisure Corporation, Farmland Improvement & Modernization, Korea Asset Investment Trust Co. Ltd., Korea District Heating Corp., and Korea Power Engineering Co. Since then, the Korea Stock Exchange listed the Korea District Heating Corporation in

January 2010 while other privatizations are still in process. The government continues to postpone its separate plans to privatize Woori and KDB financial holding companies due to global financial conditions. (*See the Industrial Subsidies section for detail on developments related to the Korea Development Bank.)*

The Korean government also operates several Free Economic Zones (FEZs) and has provided a range of investment incentives including tax breaks, tariff-free importation, relaxed labor rules (primarily exemptions from workforce quotas for disabled and older workers, and mandatory paid leave), and improved living conditions for expatriates in areas such as housing, education, and medical services. The Korean government has promoted these zones as an important step in making Korea's business environment more open, liberal, and responsive to economic needs.

ANTICOMPETITIVE PRACTICES

The Korea Fair Trade Commission (KFTC) has played an increasingly active role in enforcing Korea's competition law and in advocating for regulatory reform and corporate restructuring. In addition to its authority to conduct investigations and to impose penalties, including broad authority over corporate and financial restructuring, the KFTC can levy heavy administrative fines for violations or for failure to cooperate with investigations.

A number of U.S. companies have expressed concerns that respondents in KFTC investigations have not been afforded a sufficient opportunity to review and respond to the evidence against them, including an opportunity to cross examine those who testify in KFTC investigatory hearings. Concerns have also been raised that procedural rules for KFTC hearings have not been sufficiently transparent and that the KFTC lacked authority to enter into settlement agreements with respondents by mutual agreement.

The KFTC has taken some steps to address these concerns. In September 2011, procedural rules were modified to extend from two weeks to three weeks the deadline by which respondents can submit a formal rebuttal to the KFTC staff's report recommending enforcement action. Additionally, new procedures and criteria for closed hearings and decision-making were added. Under an amendment to the Monopoly Regulation and Fair Trade Act passed in December 2012 to implement provisions of the KORUS FTA, the KFTC has been given authority to enter into settlement agreements with respondents, as of March 15, 2012 when KORUS entered into force. In an attempt to curb illegal abuse of investigative power on the ground, the KFTC also introduced an Ombudsman to respond to problems experienced by businesses during investigations. In March 2009, the KFTC amended its regulations to expand the rights of respondents by allowing respondents to request a resumption of hearings to submit new evidentiary material or if the complexity of the case warrants additional hearings. Furthermore, the examiner's recommended sanction (including details of the surcharge calculation) is now provided in most cases to the respondent along with the examiner's report. The KFTC also amended regulations to increase its operational transparency, requiring examiners to inform claimants promptly of its conclusions and the grounds for those conclusions.

OTHER BARRIERS

Regulatory Reform and Transparency

Korea has improved its rulemaking and regulatory system in recent years. However, inconsistent implementation and a lack of transparency cut across various issues affecting U.S. firms in many different sectors. This continues to be one of the principal problems cited by U.S. businesses seeking to compete in the Korean market.

Korea's Administrative Procedures Act (APA) stipulates that the public comment period for draft regulations subject to the APA shall be no less than 20 days. However, in many cases, the 20 day minimum is insufficient. In addition, in many instances the final versions of regulations do not reflect the comments provided and often offer no explanation for why they were rejected. Under KORUS, the minimum comment period will be increased to 40 days, and other transparency-related obligations will take effect, including the obligation to address significant, substantive comments received and to explain substantive revisions made in any final regulation.

Motor Vehicles

Increased access to Korea's automotive market for U.S. automakers remains a key priority for the U.S. Government. Korea maintains an eight percent tariff and a range of nontariff barriers, such as taxes based on engine size, unique standards, inadequate regulatory transparency, and an inadequate ability of stakeholders to provide input at an early stage into the development of regulations and standards. KORUS, together with a February 10, 2011 Exchange of Letters between the United States and Korea, contains provisions designed to address many of these nontariff barriers and will contribute greatly to leveling the playing field for U.S. automobiles in the Korean market.

Korea enacted regulations for motor vehicle average fuel economy standards and greenhouse gas emission standards in June 2011. These regulations contain small-volume manufacture provisions that permit standards 19 percent more lenient than the regular standard from 2012 to 2015 for manufacturers with sales of no more than 4,500 units in 2009. Korea also allows emissions credit sharing between passenger cars and SUVs, credit carryover, and offset purchases.

Motorcycles

Although progress has been made over the past several years to resolve U.S. concerns over Korea's noise standard on motorcycles, several market access issues remain including a highway ban on motorcycles, high tariff and tax levels, and the inability of motorcycle owners to obtain ownership titles and financing for a motorcycle purchase that uses the motorcycle as collateral. A 2011 study on the safety of motorcycles on highways commissioned by the Korean National Police highlighted inadequacies in Korea's regulatory and safety practices surrounding the licensing of motorcycle drivers and the proliferation of young, untrained motorcycle riders driving dangerously on city streets. The U.S. Government maintains that heavy motorcycles riding on highways do not pose the same safety concerns as do riders of smaller, lighter motorcycles, and continues to urge Korea to eliminate the ban on riding large motorcycles on highways.

Pharmaceuticals

Cost containment measures under the Drug Expenditure Rationalization Plan (DERP), enacted in December 2006, continue to subject pharmaceutical products to downward price revisions. This affects not only drugs that have entered the market since DERP was adopted, but also products that were approved for reimbursement prior to DERP's adoption. The U.S. Government continues to urge Korea to refrain from implementing reimbursement policies that discourage companies from efficiently introducing advanced medical products to the Korean market and that serve as a disincentive to investment in research and development.

In November 2011, Korea's Ministry of Health and Welfare (MOHW) announced a new drug pricing reduction plan, which will impose significant price cuts on off-patented and generic drugs. U.S. industry expressed its concerns with this policy. The U.S. Government has urged Korea to seriously consider stakeholders' concerns and ensure that pharmaceutical pricing is conducted in a fair, transparent, and non-discriminatory manner, and MOHW has shown willingness to consider some stakeholder comments. The U.S. Government will continue to monitor the situation closely in 2012.

Under KORUS, any new Korean regulations related to pricing and reimbursement of pharmaceuticals will be published in advance for notice and comment, and the Korean government will be required to respond to public comments in writing and explain any substantial changes it makes when the regulation becomes final.

Medical Devices

U.S. companies have continued to express concern that the lack of full transparency in the regulation of pricing and reimbursements has impeded efficient introduction of medical devices to the Korean market.

In February 2011, MOHW published a pricing plan for medical devices based on import price (for imported products) or manufacturing cost (for domestic products) and began phasing in its implementation in May. U.S. industry has raised concerns regarding this new pricing plan, in particular the concern that an import price is not an accurate reflection of the value of a product. The U.S. Government has also expressed its concern that the pricing of medical devices should be determined in a fair, non-discriminatory, and transparent manner and urged MOHW to engage directly with concerned stakeholders to address their concerns.

KORUS includes, among other things, provisions to ensure that Korea's pricing and reimbursement decisions for pharmaceutical products and medical devices appropriately recognize the value of innovation. The agreement's provisions call for that the processes for making these decisions to be conducted in a transparent manner and include sufficient notice and comment periods for legal and regulatory changes.