Using Competition Policy to Promote "Shared Growth" in Korea

Seonghoon Jeon

Sogang University

Korea Fair Trade Commission

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"Shared Growth," a principle that both large and small companies should grow together, is among the top priorities on the political agenda of all Korean parties. There are many policy instruments to promote shared or mutual growth of large companies and small-medium enterprises ("SMEs"), but the Korea Fair Trade Commission ("KFTC") has played a pivotal role.

In this column, I would like to address the issue of using competition policies to promote shared growth in Korea, with an emphasis on innovation. Even though the recent drive of shared growth by KFTC covers issues larger than innovation, a main focus is to encourage cooperation in research and development ("R&D") between large companies and small-medium enterprises.

I. THE RECENT EMPHASIS ON SHARED GROWTH IN KOREA

Korea's competition law, the Monopoly Regulation and Fair Trade Act, explicitly mandates the balanced development of the national economy and the enhancement of consumer welfare as its two main purposes. Moreover, KFTC enforces a special statute, the Fair Subcontract Transactions Act, to protect SME sellers from large company buyers' abuses. However, shared growth has gained more emphasis recently in Korea, mainly due to the deepened gap between large companies and SMEs in terms of profitability, employment, and R&D.[1]

The Korean government declared that it would drive shared growth policies in September 2010, and KFTC cited improving relationships between large and small companies for shared growth as its top enforcement priority. In addition, the Shared Growth Commission was launched in December of that year. The Commission is a private institution that is formally independent from, but actually supported by, the government.

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* Dean, School of Economics at Sogang University in Seoul; Commissioner, Korea Fair Trade Commission. This work was supported by the National Research Foundation of Korea Grant funded by the Korean Government (NRF-2010-330-B00091). The preliminary version was presented at the ICC (International Chamber of Commerce) Round Table on Competition and Innovation, The Hague, May 21, 2011.

1 For example, according to the Korea Institute of Industrial Economics and Trade, the mobile division of Samsung Electronics earned operating profits of almost 9 percent of sales, while its 20 parts-suppliers earned less than 2 percent in 2009.

II. REINFORCEMENT OF FAIR SUBCONTRACT TRANSACTIONS ACT

The Fair Subcontract Transactions Act has been the main tool used by KFTC to promote shared growth, by which large-company contractors are required to make proper contracts with, and make proper payments to, SME subcontractors, and are prohibited from exploiting SME subcontractors in various ways. Recently the Act has been reinforced significantly.[2]

The main revisions are (1) expanding the applicable subcontract transactions; (2) making it easier for SMEs to ask for price adjustments reflecting the increase of material costs, and making it more difficult for large companies to reduce prices unreasonably; (3) taking more strict enforcement measures against large companies that steal technology, including treble damages recovery where it is stolen from small subcontractors,[3] and; (4) KFTC may suggest and encourage contractors and subcontractors to make mutual agreements of support and cooperation, which will be the legal basis of the recent drive of shared growth, especially in evaluation of the index of shared growth.

III. THE INDEX OF SHARED GROWTH

The Shared Growth Commission, which is a private institution in appearance but a government-supported one in substance, selected 56 large companies in various industries (including Samsung Electronics and Hyundai Motors) as objects to be evaluated for an index of shared growth.[4]

The index of shared growth will combine two kinds of evaluations: quantitative and qualitative. The quantitative evaluation will examine large companies' efforts for shared growth in terms of the contents and implementations of mutual agreements with subcontractors for shared growth. This evaluation will be conducted by KFTC as its inherited project. The qualitative evaluation, undertaken by the Shared Growth Commission as a newly launched project, reviews SME satisfaction with large companies' efforts for shared growth in terms of fair trade and cooperative subsistence.

The results of index evaluation in terms of grade or ranking will be announced in early 2012. The government will provide those large companies receiving the best evaluations with incentives, such as prizes, tax benefits, R&D projects, procurements, and exemptions.[5]

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2 The revision was declared on March 29, 2011; implementation began on June 20, 2011.

3 This particular revision is remarkable in that punitive damages to such an extent are exceptional in Korean civil law.

4 Samsung and Hyundai's sales accounted for 56 percent of GDP in 2009.

5 Details on the government incentives are yet to be fixed.

IV. KEY INGREDIENTS OF MUTUAL AGREEMENTS FOR FAIR TRADE AND SHARED GROWTH

Many large enterprises have recently reached mutual agreements with subcontracting SMEs for fair trade and shared growth, which were usually mediated by KFTC. Two prominent examples of such arrangements are Samsung and Hyundai's agreements with their respective subcontractors.

Nine Samsung group affiliates, including Samsung Electronics, made cooperative agreements for shared growth with 5,200 subcontractors in April 2011. The package of financial assistance amounted to $5.7 billion, among which R&D support comprised $1.7 billion. Samsung agreed to induce its subcontractors to make cooperative agreements with lower-level sub-subcontractors, and provide them with incentives. Moreover, Samsung promised to allow free licenses of its patents, and commit to protecting subcontractors' technologies.

Similarly, six Hyundai group affiliates, including Hyundai Motors, made cooperative agreements for shared growth with roughly 1,600 subcontractors in March 2011. The package of financial assistance amounted to $3.9 billion, with R&D and capacity investments making up $2.3 billion. Hyundai promised to provide 300 R&D support man-powers for its subcontractors.

V. CONCLUSION

I will conclude by remarking on both positive and negative sides of KFTC's recent drive of shared growth. No one objects to the necessity of "shared" growth for sustainable growth as well as stability. At the moment, even large companies regard the drive of mutual agreements for fair trade and shared growth as inevitable, and cooperate with KFTC.

However, there are concerns that too much emphasis on shared growth might distract KFTC from its main tasks of promoting competition such as regulating cartels, mergers and abuses of dominance. Moreover, the drive for shared growth may be transient. It may fade out if economic circumstances improve, or if the next government changes its policy priorities.