

2012 Modularization of Korea's Development Experience: Korean Government Procurement Experience

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Preface

The study of Korea's economic and social transformation offers a unique opportunity to better understand the factors that drive development. Within one generation, Korea has transformed itself from a poor agrarian society to a modern industrial nation, a feat never seen before. What makes Korea's experience so unique is that its rapid economic development was relatively broad-based, meaning that the fruits of Korea's rapid growth were shared by many. The challenge of course is unlocking the secrets behind Korea's rapid and broad-based development, which can offer invaluable insights and lessons and knowledge that can be shared with the rest of the international community.

Recognizing this, the Korean Ministry of Strategy and Finance (MOSF) and the Korea Development Institute (KDI) launched the Knowledge Sharing Program (KSP) in 2004 to share Korea's development experience and to assist its developing country partners. The body of work presented in this volume is part of a greater initiative launched in 2010 to systematically research and document Korea's development experience and to deliver standardized content as case studies. The goal of this undertaking is to offer a deeper and wider understanding of Korea's development experience with the hope that Korea's past can offer lessons for developing countries in search of sustainable and broad-based development. This is a continuation of a multi-year undertaking to study and document Korea's development experience, and it builds on the 40 case studies completed in 2011. Here, we present 41 new studies that explore various development-oriented themes such as industrialization, energy, human resource development, government administration, Information and Communication Technology (ICT), agricultural development, land development, and environment.

In presenting these new studies, I would like to take this opportunity to express my gratitude to all those involved in this great undertaking. It was through their hard work and commitment that made this possible. Foremost, I would like to thank the Ministry of Strategy and Finance for their encouragement and full support of this project. I especially would like to thank the KSP Executive Committee, composed of related ministries/departments, and the various Korean research institutes, for their involvement and the invaluable role they played in bringing this project together. I would also like to thank all the former public officials and senior practitioners for lending their time, keen insights and expertise in preparation of the case studies.

Indeed, the successful completion of the case studies was made possible by the dedication of the researchers from the public sector and academia involved in conducting the studies, which I believe will go a long way in advancing knowledge on not only Korea's own development but also development in general. Lastly, I would like to express my gratitude to Professor Joon-Kyung Kim and Professor Dong-Young Kim for his stewardship of this enterprise, and to the Development Research Team for their hard work and dedication in successfully managing and completing this project.

As always, the views and opinions expressed by the authors in the body of work presented here do not necessary represent those of the KDI School of Public Policy and Management.

May 2013

Joohoon Kim

Acting President

KDI School of Public Policy and Management



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Abbreviation

A/S	After Sales service
ADR	Alternative Dispute Resolution
APEC	Asia-Pacific Economic Cooperation
ASEAN	Association of Southeast Asian Nations
BAA	Budget and Accounts Act
CRM	Customer Relationship Management
DoD	Department of Defence
EAIS	e-Audit Information System
EDI	Electronic Data Interchange
EFTA	European Free Trade Association
EU	European Union
FTA	Free Trade Area
FTC	Fair Trade Commission
GGM	Government Goods Management
GP	Government Procurement
ICT	Internet and Computer Technologies
IPIS	Intelligent Product Information System
KICA	Korea Information Certificate Authority
KONEPS	Korea Online E-Procurement System
KOSCOM	Korea Securities Computing Corporation
KRW	Korean Won
LFA	Local Finance Act
MAS	Multiple Award Schedule
MFN	Most Favored Nations

MSCS	Multiple Supplier Contract System
NAFIS	National Finance Information System
NATO	North Atlantic Treaty Organization
NCA	National Computerization Agency
OECD	Organization for Economic Co-operation and Development
PDA	Personal Digital Assistant
PKI	Public Key Infrastructure
POFS	Provisional Office of Foreign Supplies
PPS	Public Procurement Service
PQ	Prequalification System
PR	Public Relations
QCRAQ	Quality Certification Regime for Administrative Goods
SICE	Systeme d'Information sur le Commerce Exterieur (French), Foreign Trade Information System
SME	Small and Medium Enterprises
UAE	United Arab Emirates
UNSPSC	United Nations Standard Productions & Services Code
USA	Unites States of America
WTO GPA	World Trade Organization Government Procurement Agreement

Summary

This paper provides overview of South Korea's government procurement (GP) experience in the context of its fast economic development. Public procurement is considered to be one of the major factors that contributed to its economic success, making Korea a suitable benchmark case. In this respect, this paper hopes to provide inspiration and platform to share Korea's procurement experience with other (not only) developing countries facing similar difficulties that Korea did in their public procurement on the way towards economic advancement.

Literature provides many definitions of GP. In general, GP can be seen as a formal process of purchasing goods and services for government agencies. The principal objective of GP is to acquire goods and services under the most advantageous conditions. This can mean either low price or the best quality, or their combinations. GP also pursues a number of secondary goals such as promotion of selected economic operators or industries, protection of domestic market, social policy enforcement, etc. At the same time, GP also aspires to achieve societal Pareto-optimum, which puts more emphasis on political-economic aspects of GP.

Although in the past GP focused on procurement at the lowest price with the view of promoting economic efficiency, recent trend is to emphasize quality and the achievement of the best value for money. This means that the paradigm of purchasing at the lowest price is being substituted by the paradigm of purchasing at the highest value, and that other criteria than purchase price, e.g. customized service, perfect A/S, fast supply, etc., are gaining importance.

As a process, GP can be divided into several phases, which are: procurement request, selection of contracting method, tender notice, submission of bids, selection of successful bidder, contract conclusion, contract delivery, and *ex-post* management with their own

goals and tasks. GP process also entails controversies in the form of diversity of GP goals, centralization vs. decentralization tendency, the issues related to the relationship between public and private procurement and tension between domestic industrial policy needs and globalization. At the same time, GP also needs to solve the issues of corruption and the enhancement of transparency, as well as the issue of selection of suitable contracting methods and tendering procedures.

The development of South Korea's procurement system can be divided into four periods; early foundation period (1948-1961), period of industrialization (1961-1979), pro-democracy movement period (1980-1992), and globalization and localization period (1993-present), each of which needed to solve specific tasks reflecting Korea's overall economic and social development. Throughout its development, GP in Korea gradually shifted emphasis from economic efficiency to the enhancement of transparency, and, more recently, towards ethical behaviour. This development has been accompanied by growing decentralization and *changes in legal environment* caused by Korea's entry into the WTO and, later, GPA.

As a key issue in Korean GP, procurement transparency has been enhanced in several ways. In relation to legal transparency, major Korean GP laws (the State Contract Act and the Local Contract Act) implicitly describe three main GP principles – transparency in fair procurement opportunity, transparency in contract practice, and the principle of non-discrimination applied in international tenders as per the WTO GPA. In addition, other Korean GP related acts describe the principle of information disclosure and the principle of objective criteria. Transparency in organizational management has been mainly pursued by the promotion of disclosure and access to information, transparency of procurement methods and evaluation system, discretionary power control, systematic elimination of unfair practices, improved ex-post management, dispute settlement procedures, the establishment of procurement call centre supported by the development of e-procurement, and the creation of procurement ombudsman system and integrity culture.

One of the important aspects of Korea's GP improvement was the introduction of e-procurement system motivated by the need to manage increasing number of procured items and companies involved in GP, along with the effort to provide value for money and customer-oriented service. During the development of e-procurement system, Korea managed to implement a high quality monitoring system preventing information abuse, supported by strengthened security measures including e.g. the existence of electronic signature, reliable user's authentication, blocking multiple bids from the same IP address, etc. At the same time, Korea also developed appropriate legislative and regulative framework covering issues such as electronic tendering and bidding procedures, data backup procedures, management of security measures and situations of shutdowns. Korea's

effort resulted in a high level of e-procurement security and increased transparency and efficiency of the whole GP system. Becoming a major success story in e-procurement development and implementation, Korea has repeatedly received awards for the quality of its e-procurement system and it has been repeatedly cited as the best case to benchmark.

Throughout its existence, Korea's GP has experienced problems with the deterioration of the quality of procured items. This was partially due to the fact that its early procurement methods were largely based on the lowest price system. Quality enhancement and quality management have thus gradually become a major Korean GP trend. To promote quality and quality control, Korea has developed a comprehensive quality management system involving the whole procurement process including related services such as A/S, contract delivery, information support for purchasing decisions, etc. The quality management tools Korea has introduced are mainly represented by regular quality checks and inspections (including those conducted on site), quality certification regime, the existence of Sinmungo, Excellent Procured Goods system, and Excellent Product Accreditation. Overall quality management improvement has also been supported by the creation of new product classification system and the Korean Intelligent Product Information System, which has received high international recognition as the best practice.

In line with the change of focus from cost-efficiency towards value for money, Korean procurement methods have also developed and changed throughout time. Korean GP originally recognized open (competitive) tendering, selective (competitive) tendering, and direct contracting, with total amount contract as the basic contracting method. However, these methods were often connected with difficulties in the form of lower quality of procured items or poor contract delivery. As a result, new contracting methods such as expected quantity competitive tendering, third party unit price contract system, restrictive competitive tendering, and negotiated contract were gradually introduced. To support increasing focus on procurement of quality and to increase contract fulfilment reliability, in 1995 Korea also introduced qualification evaluation system using various types of criteria including bidder's contract fulfilment history, labour costs, technical capability, quality and price of previous supplies, etc.

A major step in the improvement and simplification of Korea GP was the introduction of the MAS (Multiple Award Schedule) supported by the establishment of a comprehensive online shopping mall leading to the reduction in procurement time and costs, significant boost of transparency, and the achievement of better quality for lower price. However, on their implementation, Korea needed to tackle some negative aspects connected with them such as unfair purchase practices and strong supplier lobby, which were solved by the adoption of two-stage competitive regime. After these initial difficulties, MAS yielded excellent results as stated above. Apart from that, the introduction of MAS also represents

a successful case of SME cultivation and support. As already mentioned, all these changes were happening with the shift from supplier-oriented to customer-service oriented procurement in the background.

Finally, Korean procurement has been strongly influenced by internationalization and liberalization of global economy. Korea's experience shows that it is important to consider all aspects of potential membership in international or global organizations and that it is necessary to prepare well for the entry negotiations including the type and scope of concessions the negotiating country is willing to offer. The desirable level of openness of local economy must also be carefully considered, as when facing increased competition in global markets, underdeveloped domestic industries and inexperienced economic operators may be disadvantaged, which is especially the case for developing countries.

To facilitate the transition for domestic economic agents when Korea entered the WTO GPA, Korea used a number of measures including provision of information on international GP practices and standards, active promotion of participation in international tenders, and information sharing. To further protect domestic GP market, Korea also insisted on strict application of the rule of the country of origin and on basing prices in tender proposals on all relevant costs including shipping, tariffs, VAT, and others. Korea equally required that foreign companies participating at tenders be able to provide the A/S service level equivalent to the level provided by domestic companies and that foreign contractors must be paid in Korean Won. Apart from that, various forms of screening tests and prequalification evaluation have also been in use.

Last but not least, GP internationalization also raises the issue of compliance with international procurement procedures and law. This requires the answer to the question whether and to what extent domestic and international procurement procedures should differ and careful consideration of preparation of domestic legal environment for membership in international organizations.



Introduction

Representing on average 15% of GDP, government procurement has a strong impact on the economy as a whole. Successful economic development requires a significant amount of public works financed from the state budget, and state financed projects along with the operation of administrative institutions require a substantial amount of public funds to be spent on goods or services, in which public procurement plays a major role. Without a well-developed public procurement system, efficient purchase of goods and services would be problematic and the performance of the public sector functions as well as successful completion of state financed projects would be more difficult. As a result, increasing amount of attention is paid to the government procurement (henceforth GP) efficiency and achieving value for money. Furthermore, strengthened emphasis is also put on transparency, fairness, culture of integrity, and personal ethics in GP, as GP is prone to corruption and various types of unfair practices due to the large amount of funds involved. Along with that, liberalization and globalization of GP market also places strong demands on well-developed procurement system and GP management.

Implied by the above, this study focuses on government procurement in South Korea. As a country, which has followed a successful developmental path and which is often cited as an example of fast economic development, Korea represents a good case to benchmark. Moreover, as public procurement was one of the key aspects of the Korean economic success, study of the Korean government procurement system may offer important lessons and inspirations to other countries trying to follow their own developmental path. With such implications, this paper is motivated by the aim to share Korea's GP experience with developing countries, with the hope that Korea's successes as well as failures can offer developing countries some inspiration on their way towards becoming developed economies with advanced procurement system.

The whole paper is divided into two main parts - theoretical and practical. The main objective of the theoretical part, which is further subdivided into two chapters, is to provide theoretical background of this study. To do so, the first chapter focuses on the definition of the term of government procurement, its scope, and content, with brief description of GP process. After that, it explains four inherent GP controversies, and shortly discusses the relationship between GP, corruption, and transparency. The second chapter then provides brief overview of selected procurement methods. The list of the methods mentioned in this study is not exhaustive, as this paper only focuses on methods with direct relevance to the Korean experience.

The second, practical part of this paper, discusses the Korean GP experience. It consists of six chapters, the first one of which deals with the Korean procurement development and GP history. The second chapter then focuses on the Korean GP transparency and its characteristics, and transparency enhancement tools. In the third chapter, the Korean e-procurement system is discussed, followed by a chapter dedicated to GP quality management. The fifth chapter contains brief overview of development of the Korean procurement methods, and the six chapters dealing with internationalization of the Korean GP market closes this part of the paper. Apart from the mentioned topics, each chapter is concluded by a short summary including Korea's experience and lessons to be drawn in relation to the topic discussed in the respective chapter.

The authors of the study hope that its readers will find it useful and that it will meet its purpose of sharing Korea's vast developmental experience in relation to public procurement market and its methods with other countries. The authors further express their hope that the information provided by this study may help other countries avoid the mistakes Korea has made, as well as provide some inspiration as to how to solve particular issues to achieve the desired results.

In the whole text, Korea refers to South Korea and the terms government procurement and public procurement are used interchangeably.

2012 Modularization of Korea's Development Experience
Korean Government Procurement Experience

Chapter 1

GP – General Theory

1. Definition and Content of GP
2. GP Process
3. GP Controversies
4. GP, Corruption, and Transparency

GP – General Theory

Government procurement (public procurement) is a topic which deserves considerable amount of attention by policy makers and public organizations as well as private businesses. Representing the volume of funds typically corresponding to about 10 – 15% of the GDP, GP has a strong influence on the country's economy. Furthermore, with the recent liberalization and globalization drive, it also represents a powerful tool for the enforcement of domestic as well as international policies and a way to facilitate the entry of local companies in foreign markets. Related to this, transparency, fairness, and corruption in GP have become important aspects of the procurement process, accompanied by the development of corresponding regulative and legal framework and the existence of international GP related agreements.

This chapter focuses on the definition of the content and scope of GP, and the provision of basic GP related theories. The main purpose of this part of the paper is to make the reader familiar with the topic of GP and provide an introduction to the rest of the paper. In view of that, the theory and information provided here are not exhaustive. Rather, the chapter aims at a brief characterisation of topics bearing direct relevance to the practical part of the paper, where the Korean GP experience is described.

The chapter first discusses the definition and content of the term of GP procurement, after which GP process is described in the second subsection. The third sub-chapter is then dedicated to inherent controversies of GP, followed by the discussion on the relationship between GP, transparency, and corruption. After that, short overview of GP methods relevant to this paper concludes the chapter.

1. Definition and Content of GP

GP can be defined in various ways. For example, according to SICE (Système d'Information sur le Commerce Extérieur¹), GP is “the formal process through which official government agencies obtain goods and services, including construction services or public works” and GP also “includes all functions that pertain to the obtaining of any goods, service, or construction, including description of requirements, selection and solicitation of sources, evaluation of offers, preparation and award of contract, dispute and claim resolution and all phases of contract administration.” Similarly, Kim et al. (2010) states that, “government purchases are concerned with purchasing goods with suitable quality for supply from suitable suppliers in suitable quantities at the right time and at reasonable prices when a public agency such as the government procures goods needed for performing public service,” and United Nations Conference of Trade and Development materials provide the following definition of GP: “The generic definition of government procurement relates to the process by which a state agency procures a product or service for its own use.”

The principle objective of GP can be stated as the procurement of quality goods and services required by the nation under the most advantageous conditions. The most advantageous conditions can be understood in terms of the lowest price or the best quality, or the combination thereof. GP may also pursue a number of secondary goals, such as the promotion of selected economic operators, promotion of national industries, protection of domestic market, enforcement of government social policy, etc., and GP can also be efficiently used as a government policy tool. The most common examples of such use of GP policies are the support of SMEs, which can be given priority in the procurement process, or preferential treatment of companies possessing unique know-how or patents, or green procurement policy emphasizing environmentally friendly approach.

Another important aspiration of the whole GP system is the achievement of societal Pareto optimum, which also involves relationships and political-economic aspects of public procurement. The importance of relationships is implied by the fact that GP process includes in minimum two parties - the procuring authority (awarding organization) and the supplier (contractor), who enter in a mutual interaction. Political-economic considerations are related to the impact of GP on the whole economy, which is rather significant, as the volume of GP typically represents between 10 and 15% of the GDP of the economy.

Although until not long ago, the prevailing paradigm emphasized economic efficiency, essentially meaning procurement at the lowest price, limiting the understanding of GP to cost efficiency would mean neglecting its other major aspects. On an increasing scale, GP

1. <http://www.sice.oas.org/>

is concerned with diversified best value oriented criteria, rather than a uniform set of price (cost) driven factors. The concept of economic efficiency in GP can be also characterised as the avoidance of unnecessary fiscal expenditure while obtaining high value goods, implying that cost-benefit analysis to evaluate different projects or tender proposals can be conducted. In this respect, economic efficiency is value more strongly associated with the results or the content of GP (tendering process), rather than the process itself. The decision of a procurement agency is thus formed after the consideration of both, the price and the value that can be obtained, and related costs.

As already mentioned, the recent trend in GP is to emphasize other criteria such as the variety of procured goods, the design, the support of disadvantaged economic operators, government policy goals, achieving the best value for money, etc. The paradigm of purchasing at the lowest price is being gradually substituted by the paradigm of purchasing with the highest value. Such a change is accompanied by the shift from supplier-oriented to customer-oriented procurement administration. In GP, the term customer covers the procuring entity (e.g. public agency, government department, local government, etc.) as the first GP customer, and a supplier company as the second customer. The focus on maximizing customer satisfaction level results in the adoption of new approaches with broader range of procurement methods available to use. On an increasing scale, procuring entities require improved quality of procured goods, fast supply, customized services, perfect A/S, and more information for qualified purchase decisions. It is possible to say that these changes are market-friendly and as such, they are bringing procurement administration closer to the entrepreneurial mind-set.

2. GP Process

To be able to understand the following parts of the paper, it is important to become familiar with GP process and its phases, most of which are common to all procurement cases. Government procurement process can be divided into the following stages. First, a procurement request is placed by a procuring entity and a suitable contracting method is selected. At this stage, depending on the choice of the contracting regime, procuring entity either contacts a procurement agency which takes charge of the whole procurement process or, usually based on previous experience and the reliability of contract performance, it can directly approach a contractor. If the tendering methods is such that it requires selection of a contractor through a given procedure, tender notice is published and participating companies submit their bids. After the bid opening, a successful bidder is selected and the contract is concluded. During the delivery phase, the content of the previously concluded contract is performed, or, in relation to the contracting methods and circumstances, the terms of the contract may be adjusted. In parallel, inspection checks and tests are done to ensure

quality performance of the contract. After the contract is fulfilled, *ex-post* management of the contract, such as claims or A/S requests, is carried out. Although most of these stages are common to all procurement processes, some phases may be shortened or completely omitted, in relation to the selected contracting regime.

3. GP Controversies

Each government's procurement regime needs to overcome several inherent controversies, the most important of which are diverse GP goals, centralization vs. decentralization trend, relationship between public and private procurement, and the potential tension between domestic industrial policy needs and globalization trend of the current world economy.

Diversity of GP goals places high demands on policy makers to keep the goals in a mutual balance. For example, on one hand, it is important to consider the use of GP as an industrial policy tool, through which the government can foster specific groups or industries, such as SMEs or companies possessing special know-how.² On the other hand, this use of GP is in conflict with liberalization and internationalization of GP market and regulations of some international agreements such as the WTO GPA (World Trade Organization Government Procurement Agreement), and can be also viewed as a violation of GP principle of fairness. Another example of conflicting goals is the support of disadvantageous economic operators with the consideration of social aspects of GP, which may be in conflict with the goal of economic efficiency.

With regards to (de)centralization, it is obvious that both centralized and decentralized GP system have both advantages and disadvantages. In a centralized procurement system, which is usually found in countries with centralized administration, purchases of goods are conducted through one central procurement organization supplying the contracted items to the end-user organizations. Generally recognized advantages of such a system are economies of scale and scope, professional manpower and specialized organizational structures with sufficient know-how, easier coordination, process standardization, and more efficient use of GP for macroeconomic policy goals. At the same time, bureaucratization, rigidity, excessive emphasis put on the procurement process and regulations, delays caused by redistribution, high communication demands, and the impossibility of the use of local suppliers fall among the most commonly cited disadvantages. The advantages of decentralized procurement are higher level of flexibility, the possibility of engaging local contractors resulting in lower logistics costs, better knowledge of procuring entities' needs

2. One example can be the support of SME via the modification of regulations related to the participation at tenders throughout Korean history, or the support of specific industries during the times of economic crises.

allowing for more accurate targeting of procured items, lower level of stocks carried in central warehouses, etc. The major disadvantages of decentralized systems are exemplified by potentially lower level of qualification of local officers related to lower specialization, lack of experience and professionalism of procurement officers who usually carry out more responsibilities, and higher level of discretion for procurement officers creating a space of corruption and unethical behaviour. Whichever system a particular country chooses to use, it is important to keep the system well aligned with the whole political economy structure, as hybrid systems are likely to increase economic inefficiency and cause additional systemic difficulties.

Another important consideration of GP is the relationship between private and public procurement. If both sectors complement each other, supported by well-developed regulative framework, their overall functioning is smoother and more efficient and the synergy effect from mutual cooperation between private and public organizations can be achieved. However, significantly different systems usually entail potential disputes caused by for e.g., accounting differences or different remedial measures, which can be interpreted as injustice or favouritism of certain groups. Nevertheless, it is not desirable that private and public procurement systems and regulations be exactly the same, as private and public procurement are essentially different. Unlike private procurement, which is mainly driven by economic efficiency, public procurement also pursues other goals such as social justice, fairness, industrial policy enforcement, etc., even though economic efficiency may thus be impeded.³ Another major difference is that as private procurement places priority on procurement of best quality at lowest price, transparency is not a severe consideration. However, transparency is currently one of the most important issues in GP. This dissimilarity is caused by different level of information asymmetry, which is higher in government procurement than private procurement. Furthermore, GP regulatory bodies also need to take into account the political aspects of procurement and the need to ethically justify their decision in the eyes of the majority.

Finally, GP reflects development and conditions not only in domestic, but also in international environment. However, domestic industry needs may be in conflict with international economy trends. Especially now, in the era of international trade liberalization and globalization of the world economy, GP must respond to internationalization trends more strongly than ever. The membership in various international organizations, such as the EU (European Union), or the WTO, requires compliance with their GP regulations, which can differ from domestic regulations and legislation. The impact of external influences can be significant. For example, while the accommodation of the non-discrimination clause of the WTO in domestic legal

3. For example, higher level of fairness is usually achieved through stronger regulations resulting in more administrative processes and longer procurement time.

framework may require legal adjustments, easier access of foreign companies to the local procurement market may hinder the position of domestic firms. However, the increased competition may also result in the boost of economic efficiency in GP. In an effort to avoid negative impacts of GP globalization, countries are trying to protect their home economic operators and industries by restricting liberalization of the local GP market. However, at the same time, countries are aspiring to become members of international organizations and agreements promoting liberalization of GP market, with the view of expanding their export markets and creation of more opportunities for local firms. Related to that, it often happens that tendering procedures and the degree of transparency in domestic and international tenders are different, including different treatment of domestic and foreign firms.

4. GP, Corruption, and Transparency

Two issues closely related to GP are corruption and transparency. Corruption can negatively influence the whole procurement process and translate into hindering of some GP goals, such as fairness, justice, and efficiency. Along with suitable regulative framework and its enforcement, transparency is one of the most important ways to prevent corruption from happening.

4.1. Corruption

According to Transparency International's working definition, corruption is "the abuse of entrusted power for private gain."⁴ Due to its negative impact on organizations as well as the whole society, significant effort is made towards corruption elimination. As Kim et al. (2010) points out, in GP sector, the chance of corruption is high. Public procurement sector is more prone to corruption than other administrative sectors due to high volumes of funds and resources, which provide the involved parties with strong incentives to influence the procurement process in their favour or take advantage of their position. As suggested by the nature of the procurement process, corruption may occur on the side of the procuring agency (entity) or on the side of the contractor. The examples of corruption on the side of the procurer include provision of advantageous conditions for a given supplier, lower availability of information on tender opportunities and details, declaration of emergency restricting competitiveness of procuring process, abuse of situations and criteria allowing for the use of non-competitive bidding methods, violation of confidentiality, prequalification assessments conducted in such a way that a potential supplier is left out, bribery, etc. On the supplier's side, corruption may occur in relation to differentiated technical standards, attempts to interfere with and influence the officers in charge of proposal assessment, rigged bids, bribery, etc.

4. http://www.transparency.org/cpi2011/in_detail#myAnchor3, accessed August, 31, 2012.

In many cases, the relationship between contractual parties involved in GP is unequal with the bidder in a less advantageous position. Especially in a situation of underdeveloped procurement legal framework or when specific contracting methods such as direct contracting or contract via negotiations are used, the procurement authority may exercise an undesirable amount of discretionary power, which is likely to lead to corruption. This often happens during the proposal assessment phase when the evaluation criteria are not prescribed in sufficient detail and the evaluation of bids along with the contractor selection are conducted at the discretion of the procurement agency. Another case of discretionary power abuse is unfairness in imposing sanctions during the post-delivery management phase of the procurement process. One of the ways to tackle this issue is securing stronger protection of bidders through appropriate legislation and remedial measures. The reduction of the discretion of the procurement officers is also possible through well-developed contracting methods with accurate specification of cases when to use them. The abuse of discretionary power can further be prevented by enhanced transparency accompanied by clear definition of unfair practices and the application of the principle of proportion. It is obvious that some situations will always require decisions to be made at the discretion of procurement authorities; however, to ensure that a reasonable amount of discretion is exercised within legal boundaries, a well-defined public procurement legal framework must exist.

Another issue related to corruption is cultural characteristics. Local culture may either facilitate or hinder favouritism, paternalistic attitudes, collectivist insider protection, particularistic attitudes to laws and regulations, or collusive behaviour, which are strongly related to the understanding and existence of corruption in a given culture. It can be said that some political-economic-cultural systems make it more difficult to eradicate corruption than others, and that the possibility of corruption elimination or its drastic reduction also depends on the country's level of development and the local form of democracy and system of economy including the period that they have been in existence. It has been repeatedly mentioned that corruption is one of the most serious problems related to public procurement systems in developing countries.

When talking about corruption, it is not possible to omit ethical considerations. The topic of business ethics has been receiving increased attention, especially in the last few decades. Many companies have started implementing enhanced business ethics measures, such as the introduction of ombudsmen, the existence of hotlines for reports on unethical/corrupt behaviour, etc. This development also has bearing on GP, where ethics and ethical behaviour are beginning to be systematically promoted.

As has already been mentioned, certain types of economic or procurement systems are rather conducive to the existence of corruption while others make its occurrence less likely. For example, at the OECD level, discussions on the utilization of centralized or decentralized

procurement system in relation to the prevention of corruption are going on. While a centralized procurement system makes it easier to monitor the measures and the effort that is being made towards corruption prevention, it is also prone to more serious corruption cases due to the centralization of funds and responsibilities, and a larger scale of procurement. On the other hand, decentralized system brings corruption prevention effort closer to the procurement end-user organization. However, high degree of decentralization may also make it more difficult to monitor the use of anti-corruption measures and places more demands on coordination and developing communication network between local and central organizations.

Similarly, the use of contracting methods also has a bearing on the prevalence of corruption. Most countries use the open (competitive) tendering method as the basic procurement regime, as it encourages competition and also allows for a better control of the whole procurement process including limiting procurement officers' discretionary power. Other contracting methods such as selective (competitive) tendering or direct contracting, which gives procurement agencies more decision making power, are only possible to use under strictly prescribed circumstances as stipulated by the law. The use of these contracting methods require well founded justification and is also subject to a higher degree of control and inspections.

Anti-corruption measures adopted by countries to solve corruption issues include the development of legal and regulative framework, measures taken to limit procurement agencies' discretionary power, frequent inspections, regular checks of the use of non-competitive procurement methods, the encouragement of ethical attitudes and the implementation of ethical enhancement tools, the enhancement of transparency and information disclosure, the use of electronic procurement systems facilitating access to information, measures increasing accountability of procurement officers, existence of remedial measures including administrative litigation, and many others.

4.2. Transparency

Unlike in the past when the public procurement sector was to a large extent dominated by the paradigm of economic efficiency, recent development puts increased emphasis on ethics and transparency. In general, transparency can be defined as “characteristic of governments, companies, organizations and individuals of being open in the clear disclosure of information, rules, plans, processes and actions.”⁵ Achieving transparency thus means that all users are able to access information about an entity in the same way regardless of their location. As such, transparency is a concept related to information systems. However, although information provision is the core of transparency, a high level of transparency does

5. <http://www.ti-israel.org/?CategoryID=130&ArticleID=275>, accessed August, 31, 2012.

not necessarily mean the provision of all information. Rather, transparency is a concept emphasizing the quality of information over its quantity.

To better grasp the content of the term, literature recognizes various types and dimensions of transparency. For example, Böhm distinguishes result transparency, procedural transparency, contents transparency, and responsibility transparency. In his view, result transparency refers to the method of disclosure of the result of a decision, procedural transparency is related to the transparency of the decision making process, transparency of formality and responsibility transparency means the clarity of who is responsible for given administrative acts. Böhm further divides procedural transparency into transparency of general procedure and transparency of an individual event. Unlike Böhm, Arrowsmith describes four dimensions of transparency in GP, which are: disclosure of information regarding contract opportunities, disclosure of contracting procedure rules, restriction of discretionary power of procurement officers, and the establishment of verification and enforcement regulations.

In line with the general notion of transparency, transparency in GP refers to “the principle of guaranteeing general accessibility regarding information on contract execution procedures and the results thereof in government procurement and clearly presenting the contents thereof and naming the responsible parties” (Kim et al. (2010)). Despite the absence of strict legal definition, the APEC Government Experts Group, which outlined general principles of transparency, stipulates that “sufficient and appropriate information may be easily accessed by all the interested parties consistently and at appropriate times, which may be usable free of charge or at a reasonable price by using widely available means,”⁶ bringing information disclosure to the center of attention. In some countries, laws and regulations stipulate procurement transparency principles. For example, the German legal system considers transparency one of the major GP principles and the French Procurement Code recognizes procedural transparency, free participation, and equal treatment of participants as the major principles of GP. To these principles, WTO GPA also adds the principle of non-discrimination. Using the above classification of Böhm, GP transparency mainly emphasizes result and procedural transparency, while contents and responsibility transparency are more closely related to the use of discretionary power and participation in tender procedure.

GP transparency relates to all aspects of GP process. For example, WTO recognizes twelve different cases that transparency is directly involved in GP: “(i) definition and scope of government procurement, (ii) procurement method, (iii) announcement of information on law and procedure of a member state, (iv) information on procurement opportunity, (v) tender and prequalification assessment procedure, (vi) procurement time, (vii) transparency

6. In relation to government procurement.

of decision on prequalification assessment of suppliers, (viii) domestic assessment procedure, (ix) other issues related to transparency (maintenance of record related to procedure, utilization of IT, language issues, and corruption measures), (x) type of information to be provided for other governments, (xi) WTO dispute settlement procedure, and (xii) technical cooperation with developing countries and government procurement related issues such as special and differential treatment of developing countries (WTO, 1999; 2003).”

Transparency in GP also bears some specific characteristics. Transparency in GP is a feature of government policy regulating the relationship of the procurement authority towards civil suppliers (bidders), and it often represents an obligation that must be fulfilled in accordance with public procurement legislation and regulative framework. In this respect, obligation of transparency applies not only to procurement authorities, but also to tenderers, who must comply with prescribed requirements. An important issue which may arise in procurement process is the issue of excessive transparency. Too much transparency may result in the disclosure of important transaction information or information related to the contents of the tender proposal that may lead to tacit collusion or intentional parallelism among bidders. If so, disproportional level of transparency could reduce competition among tender participants and impede their trust in the bidding process. For these reasons, it is important to find the balance between the obligation of transparency and its excessive level.

Broadly, GP transparency issues may be grouped into three different categories - those that relate to legal transparency, issues related to transparency in organizational management, and issues related to electronic procurement systems.

Issues related to legal transparency mostly concern the transparency of laws, court rulings, administrative decisions, policies, and regulations in GP. It often happens that there is a discrepancy in the extent of disclosure of higher and lower laws. Most countries in the world provide extensive information on higher laws, while the disclosure of lower laws, which are more important for tender participants to prepare their tender proposals, is often insufficient (OECD, 2002). In many countries, the provision of specific information on the terms and results of tenders exceeding a given financial amount constitutes a legal obligation. However, in situations that the disclosure of this kind of information may violate tender participants’ rights, impede fair competition, or do harm to the public good, this obligation is relieved. As already mentioned, procurement legislation is strongly influenced by membership in international organizations such as the OECD, WTO, or APEC, which require from their members compliance with their own regulations and legal provisions. In some cases, international regulations may also take the form of recommendations or non-binding regulations.

The second group of issues are those which occur in relation to transparency in organizational management. Essentially, this kind of transparency means that sufficient amount of information of adequate quality should be made available with regards to all stages of GP process. In this case, emphasis is put on the disclosure of information such as tender price, tender documentation including the date of tender notice and proposal submission, criteria for proposal evaluation, and specification of tender method. In addition, *ex post* management measures to be used in case of the failure of a contractor to fulfil contractual conditions or when objections against the tender procedure are raised must be made generally known. The existence and provision of information on standards for dispute settlement procedures including the existence of an ombudsman system allowing for the rectification of undesirable behaviour or unfair actions of contracting officers are important for interested parties to be able to monitor the overall procurement process. This kind of transparency is especially important to boost the trust of all parties involved in GP.

Finally, the introduction of an e-procurement system leads to specific types of transparency problems that occur mainly in relation to information protection, the right to access information, procurement monitoring system, etc. Based on vertical transparency, i.e. transparency between procurement entity and contractors, e-procurement system must enable suppliers to have access to information they need to provide quality proposals. However, at the same time, information access must be limited and conducted on a selective basis, so that leakage or hacking of sensitive information can be effectively prevented. Furthermore, to prevent the manipulation of tender documentation or tender participants' data, a monitoring system must be implemented. Due to the information asymmetry between contractors and procurement agencies, there have been cases of misuse of electronic procurement information system such as using the names of other contractors or the provision of false cost information by bidders. Lastly, technical limitations of IT systems leaving space for system abuse or manipulation must also be considered.

4.2.1. Transparency enhancement

There are several reasons why enforcement of transparency is at the center of attention of public procurement authorities and their supervisory institutions. First, transparency is considered one of the most important tools limiting the corruption in public procurement and improved transparency also helps to secure fairness of the procurement process. This translates into more accurate expectations and increased trust of potential suppliers, which increases the number of tender bidders and thus leads to higher competition. Through intensified competition, the efficiency of the procurement process can be increased. Hence, it is possible to say that transparency in public procurement is tied to public procurement efficiency. Furthermore, transparency also helps protect bidders' rights, which again

increases the number of potential tender participants. More transparent procurement process as required by international organizations such as the WTO also means easier access for foreign companies to domestic procurement market. However, although foreign operators' participation in domestic tenders is likely to boost the economic efficiency of GP as it makes the procurement process more competitive, expanded accessibility of domestic market to foreign companies may be in conflict with domestic industrial policy goals.⁷ In this respect, within the boundaries of international agreements they have signed, countries tend to restrict the access of foreign companies in the local procurement market.

There exists a number of methods used to boost and enforce transparency. Among them, those aimed at the enhancement of transparency of information access and disclosure are timely and sufficient notice, which are especially important in international tenders, the use of neutral criteria in the sense that international or generally recognized technical standards be required for the preparation of tender documentation, the use of objective criteria, public announcement of offers, and public opening of bids. While the application of standards is important to ensure that any qualified bidder can freely participate in the tender and that goods of the same quality are treated equally, the use of objective criteria allows for fair and objective assessment of tender proposals. Other methods, such as the presentation of clear contract execution principles (for example, awarding the contract to the bidder presenting the proposal with the lowest price or the highest value in accordance with objective standards), or the guarantee of intellectual property rights and confidentiality of technical details included in bidders' proposals are employed to ensure tender participants' trust and protection of their unique know-how. One internationally recognized way to ensure high level of transparency of procurement process is also the use of e-procurement and electronic information provision methods.

7. In many cases, countries tend to solve this controversy by the separation of domestic and international procurement markets and the application of different regulatory measures to both. However, it is not easy to decide to what degree public procurement in both markets should differ and whether such difference is desirable or not.

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Chapter 2

Overview of Selected Procurement Methods

1. Tendering Procedures
2. Contracting Methods

Overview of Selected Procurement Methods

This section contains a brief overview of contracting and bidding methods relevant to this paper and their basic characteristics. As the authors of the paper only focus their attention on tendering regimes bearing direct relevance to the Korean experience, the list is not exhaustive, and some commonly used methods may be left out.

The choice of a particular procurement method or strategy depends on a wide range of criteria, among which the specification of procurement entity's needs, contract performance time horizon, predictable costs, the character of procured goods, and the accountability can be cited as the major ones. In addition, procurement regime is also strongly influenced by domestic political economy, including contractual relationships, working culture, and legal framework. Contracting methods are also becoming significantly affected by globalization and world trade liberalization and the membership in international organizations such as the OECD, WTO (GPA), or the EU, which often require harmonization or compliance with their regulations. However, it is important to bear in mind that any attempt to adjust local procurement system to meet international standards requiring major systemic changes must be accompanied by an overall system modification, as procurement system and related policies are embedded in local political-economic reality as well as culture. The change of a single aspect of GP or direct adoption of another country's system without modifications might thus lead to the creation of a hybrid system resulting in difficulties in the operation of the whole system. An example could be the Korean experience with the implementation of the U.S. Multiple Award Schedule system, which originally caused numerous complaints and misunderstandings, to a large extent due to the differences in the U.S. and Korean economy arrangement and GP practices implied by local culture.

1. Tendering Procedures

Tendering methods can be broadly classified into competitive and non-competitive regimes. Among competitive bidding methods, this paper mentions open (competitive) tendering and methods based on its modifications. With regards to non-competitive methods, selective (competitive) tendering and direct contracting are detailed below. Stipulated in the National Finance Act, with further details provided by the Budget and Accounts Act and the Act on Contracts to Which the State is a Party, all these bidding methods are recognized by the Korean law.

Open (competitive) tendering is a system which allows any bidder meeting given criteria to participate in the tender. The tender is then awarded to the bidder offering the best procuring conditions. The advantage of this system is that as it does not restrict participation to specific groups, it encourages fairness and competition which translates into economic efficiency. However, in open (competitive) tendering, it is common that the contract is awarded to the bidder offering lowest price, which may result in insufficient quality of the procured goods or services, various problems occurring during the contract delivery, or general difficulties with contract fulfilment. Related issues are also possible lack of experience of the contract winner and subcontracting.

In selective (competitive) tendering, participants are to bid for the contract. Participants' nomination is usually based on previous experience of procuring agency with the contractor and the reliability of contract performance. Specific contractor may also be nominated in situations that the nominated contractor possesses special know-how or capability required to satisfy the procuring agency's needs. The advantages of selective (competitive) tendering are that, similar to open (competitive) tendering, selective (competitive) tendering secures economic efficiency and fairness. In addition, by using this method, procuring agency can ensure contract fulfilment capability of the contractor, as well as sufficient quality of goods and services. Lower competition due to restricted number of tenderers can be cited as the main disadvantage of this form of bidding.

Finally, direct contracting consists of direct selection of a contractor to conclude the contract. As this method belongs among the non-competitive ones, its use must be well justified and is usually only possible under strictly prescribed circumstances. As implied above, the main advantages of direct contracting are reliability and the assurance that the contractor will be able to perform the contract as required. The disadvantage is that as the process in non-competitive, it may be regarded as unfair and the price of the contract is likely to be higher. However, direct contracting allows for the efficient use of public procurement as government industrial policy implementation tool.

2. Contracting Methods

In general, contract (or payment) methods can be divided into fixed price and prime cost contracts. In a fixed price contract, the sum of money covering all the works needs to be completed to fulfil the contract, or the price of each component of the work (or goods) is set. Unlike that, in prime cost contracts the contractor 'is paid the cost of the work together with an additional amount for the use of contractor's services,' implying that this type of contract allows for the change of price in a situation that the cost of for e.g. inputs such as raw materials or labor change. This contracting form is suitable when it is difficult to determine the cost related to the contract performance (for example, because of raw material price fluctuation) or when the contract delivery is expected over a long period of time and the expenses the contractor incurs are likely to change.

Another type of classification divides procurement methods into two major groups depending on different pricing systems - lump sum contracts and unit price contracts, which are both examples of a fixed price regime.

Lump-sum contract is a type of contract where the contractor agrees to complete the awarded work (render service, deliver goods) for the agreed total amount without the procuring agency requiring the specification of price for each item or detailed cost breakdown. A specific subtype of lump-sum contract is a situation that similar items are grouped or the whole contract is divided into smaller lots according to different delivery locations or quantities demanded. In this case, the lump-sum is specified for each lot or package separately. This system is often employed when the total contract quantity is too large or the contract covers a broad range of commodity types which would be difficult to deliver by a single contractor and the requested work is well defined. Although lump sum contracting has the advantage of reducing contract administration costs, the main weakness of this regime is that if the same item is purchased repeatedly at different times, the whole tendering procedure must be performed again, incurring additional administrative costs.

In unit price contracts, the price of a particular item is fixed for a certain period of time in relation to the expected quantity needed. When a purchase request arises within the contracted time period, the procuring agency approaches the contractor with an order without the need for additional tendering or bidding procedure, thus reducing administrative costs. This procurement method is typically used for items with high procurement frequency. Apart from economic efficiency, the advantage of the system is reduced procurement period and quantity discount achieved by bulk purchase. Furthermore, the system is also beneficial for contractors, as it allows them to forecast expected annual demand and plan production more efficiently.

A modification of the unit price contract is the so-called third party unit price contract, under which the procuring entity directly approaches the contractor with a purchase request, without the need to engage an official procurement agency. However, the procurement agency still negotiates the original contractual terms and concludes the contract with the contractor. Through this method, procurement procedure is simplified as one stage of delivery procedure is omitted.

The Korean law also recognizes the so-called expected quantity competitive tendering system, according to which the contract is divided into smaller parts and the bidding is performed separately for different quantities of the same items. The reason for the application of this system is that in case of large quantities it may be difficult to produce or supply the same item with a single contractor's performance capacity (production or delivery). As the price is fixed for each unit of a given purchase lot, the system is essentially a fixed-price type and represents a special case of open (competitive) tendering.

Another type of competitive tendering methods is restricted competitive tendering, in which the procuring agency approaches a number of economic operators, in principle at least three, and asks them to submit a tender. As this method violates the free competition principle, it is essentially usually possible to use in a limited number of cases or under special circumstances. These can be for example the supply of goods or services of special nature which makes it possible to procure them only from a limited number of companies or the situation is such that the subject of the contract is a classified secret. The advantage of this system is that it secures the quality of procured items and reliable contract performance, the main disadvantage consists of restricted competition and thus potential increase in procurement costs.

Finally, in contract by negotiations (or competitive proposal) contract is concluded after negotiations with suppliers who have been invited by the procuring agency to submit their proposals for review. The system is only possible to use in special cases, such as the situation where contractual speciality is required or for the reasons of security purposes or urgency. Similar to the general case of open (competitive) tendering, the issue of the proposal with the lowest bidding price winning the contract appeared. In response, Korea attempted to prepare a comprehensive system of evaluation including criteria such as contract performance, delivery period, or contract fulfilment capability.

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Chapter 3

History

1. Early Foundation Period (1948-1961)
2. Period of Industrialization (1961-1979)
3. Pro-Democracy Movement Period (1980-1992)
4. Globalization and Localization Period (1993-Present)

History

This chapter of the paper deals with the development of the Korean procurement system. As the Korean GP system history closely follows overall economic and social development of Korea, its periodization corresponds to the Korean economic development. The whole chapter is divided into four parts – early foundation period covering the years 1948-1961, period of industrialization (1961-1979), pro-democracy movement period (1980-1992), and globalization and localization period (1993-present).

1. Early Foundation Period (1948-1961)

Foreign procurement first gained importance in Korea after the end of World War II in 1945, when the country was divided into a northern part administered by the Soviet Union and southern part administered by the USA. The devastated local economy, severely limited industry production and poor living conditions meant that foreign procurement along with foreign aid supply became major factors of Korea's post-war economic as well as social recovery.

Increased importance of foreign aid and foreign procurement led to the need for efficient management of the supplies resulting in the establishment of the Provisional Office of Foreign Supplies (POFS) under the authority of the Prime Minister in January 1949. While the main responsibilities of the POFS consisted of the management of foreign procurement and foreign aid supplies, the management of counterpart funds also represented one of its major functions (counterpart funds generated by the Office amounted to 30-50% of all counterpart funds).

Although the POFS was originally responsible for both the foreign procurement as well as the management of foreign aid supply, in December 1949 the Office of Foreign

Procurement was established and the foreign procurement function was transferred to the newly established institution. The economic significance of foreign economic aid along with the need for better coordination of Korea's foreign procurement with its international diplomatic activities were two main reasons for this change. At the same time, POFS was renamed Provisional Office of Foreign Supply Management and its responsibilities were reduced to the sole function of the management of foreign aid supplies. However, in February 1955 the management of foreign aid and foreign procurement were integrated again under the Office of Foreign Supply, resulting in the improved efficiency of foreign procurement.

1.1. Laws and Regulations

Two main regulations related to foreign procurement of this period are the Presidential Decree No. 65, which was introduced in December 1949 with the establishment of POFS, and the Finance Act issued in 1951. Articles 5-9 of the Presidential Decree regulated the work of levy officers, who were in charge of the collection, management, and documentation of counterpart funds. In accordance with the Finance Act, which imitated the public procurement regime of Japan, the public procurement methods available to use were open (competitive) tendering, selective (competitive) tendering, and direct contracting, and the main contracting methods were the total amount contract and unit price contract. The Finance Act remained the main source of legal framework related to Korea's national accounting until the Budget and Accounts Act of 1961.

2. Period of Industrialization (1961-1979)

The period of industrialization started with the military coup of 1961 led by Major General Park Chung-hee, who later became the Korean president. The new military government sought to support Korea's industrial development through five-year economic development plans and improve the efficiency of national finance. To that end, a centralized procurement system was introduced. Along with that, in October 1961, the Government Organization Act was revised and the Office of Supply was established under the Economic Planning Board. Unlike before, the responsibilities of the new Office of Supply also included domestic procurement and public construction contracts, to which the management of national reserves of construction and raw materials, and consumables was added in February 1967 through the Procurement Fund Act.

2.1. Laws and Regulations

Five different subjects are important to mention in relation to regulations within this period: regulatory structure and regulations related to government procurement, direct contracting system of SMEs, cost accounting, contract price adjustment system, and limited competitive tendering system.

The basis of the government procurement regulatory structure was included in Cabinet Decree 279 providing a general framework for government procurement administration and procedures, with additional operational rules issued by the Economic Planning Board. Excluding those, the Budget and Accounts Act (BAA) legislated in 1961, along with its enforcement decree - Cabinet Decree 319, also provided some public procurement regulations. However, as the original BAA of 1961 only contained one provision related to government procurement, in 1975 it was revised to comprise more detailed provisions regarding for e.g. public procurement contracting methods, contract documentation, types of contracts, debarment provisions, etc. Furthermore, government procurement was also regulated by the Local Finance Act (LFA), which was enacted in November 1963 and later revised in December 1975. Both the BAA and LFA suggested that public procurement contracts and contracts under private law were not significantly different from each other. At the same time, the need to regulate government accounting and budgeting was met by the Procurement Special Accounting Act enacted in October 1961 and later abolished in November 1962, and Corporate Budget and Accounting Act, in which a double entry book-keeping system was introduced. Finally, the Procurement Fund Law of February 1967 regulated the management of procurement funds.

In line with the government goal to achieve fast economic development, the support of SME became one of the government's top priorities. In public procurement, this policy was reflected by the "Provisional Measure concerning Group Direct Contracting with Small & Medium Enterprise Cooperatives," which gave priority to SMEs cooperatives compliant to the Small & Medium Cooperatives Act in the procurement of goods, and under given conditions allowed for the use of direct contracting method.

One of the serious issues causing public procurement inefficiency was related to the cost accounting system. Regulated by the Enforcement Decree of the Budget and Accounts Act from 1961, cost accounting was composed of material, labor and service costs, and miscellaneous expenses. The same Act also stipulated that the accounting standards such as unit price, etc. shall be set by the Ministry of Finance. However, due to the fact that the Ministry did not provide such standards until 1978, government procurement organizations set their own unit prices, or operated without them. As a result, the system entailed cost inefficiencies and budgetary waste.

Another important feature of public procurement contract law was contract price adjustment system based on so-called “*clausula rebus sic stantibus*” (the concept of changed circumstances). Although public procurement contracts were fixed price in principle, this clause allowed for the change of the total amount of the contract when changes in circumstances that were never contemplated by the contract parties occurred. The system, which was incorporated in the Korean public procurement regulations on the recommendation of PPS, was also reflected in the revised accounting principles.

Finally, with the aim of securing high performance of procurement contracts, the “limited competitive tendering system” comprised of the advantages of both competitive tendering as well as selective (competitive) tendering was newly introduced in 1977 by the revision of the Enforcement Decree of the Budget and Accounts Act.

3. Pro-Democracy Movement Period (1980-1992)

Public procurement policy of pro-democracy period closely reflected the Korean social and economic development. Despite the fact that the Korean economy was growing at an average of 8.3% during the first four five-year economic plans, economic growth was imbalanced with unequal participation of different classes and regions. In response to the growing disparities in the distribution of income and resources and the increase in relative poverty, the fifth five-year economic plan was conceived as a five-year Economic and Social Development Plan. The increased emphasis on balanced development and social aspects of economic growth also served to emphasize the role of public procurement system as an economic and social policy tool. For example, through awardments of public project contracts earlier than originally planned, the Korean government was able to stimulate the national economy during the recession of the early 1980s. Similarly, the revision of public procurement contracting regulations enabled SMEs to participate at government projects in larger numbers than in the past.

3.1. Laws and Regulations

The most significant features of public procurement system of the pro-democracy movement period are direct contracting, a third party unit price contract system, the improvement of the cost system and the improvement of the contract price adjustment system.

Based on its last revision in 1975, BAA still remained the main act regulating public procurement during the period. However, in March 1989, public procurement legal framework was modified, as direct contracting became directly regulated by the BAA rather than by the Enforcement Decree and Enforcement Regulation of BAA. Furthermore, in 1985 the contracting method of 18 contracts worth 20.1 billion won in total was changed

from direct contracting to competitive contracting due to the growing need to ensure competitive and fair environment. In addition, 17 cases worth 14.4 billion won in total were excluded from tenders as tender prices were significantly lower than standard prices of the corresponding years and problems with the quality of construction works appeared.

The third party unit price contract system was first used in Korea in 1976 under the revision of the enforcement decree of the Procurement Fund Act. Originally, the system, in which the administrator of the PPS concluded a contract while the delivery was directly carried out between the contractor and the end-user organization, was too complicated. The most severe issues arose from the fact that, while the end-user organization was required to directly pay to the supplier, it was also obligated to separately pay a fee to the PPS. Moreover, although the terms of the contract were arranged by the PPS, the PPS could only monitor contract performance status by being notified by the end-user organization. As a result, it was not exceptional that the PPS encountered difficulties keeping track of contract performance, or that problems caused by different forms (e.g. invoices) or different administrative procedures of various end-user organizations appeared. In response to that, in 1988 the system was revised to simplify the management and improve the efficiency of the whole process. Under new procedures, end-user organizations only remained in direct communication with the PPS to which they also made all payments including the procurement fee, while the PPS dealt with the contractor directly including the contract delivery phase. Through that, the PPS was able to monitor the contract delivery more easily, and the efficiency as well as transparency of the system was enhanced.

The improvement of the cost system included the revision of government cost accounting system so that the government accounting reflected the conditions in the market more realistically. Under the new government accounting principles, the calculation of indirect labor costs did not require the use of ratios related to different business types, the expense account newly contained other expense categories such as waste or publishing expense, administrative expense ratio was brought up-to-date, and profit rate calculation was changed. Through the 1988 revision, government accounting principles became more similar to those used in corporate accounting, which made administration of procurement contracts easier. The revision also meant that public procurement contracts became less prone to entail disputes caused by the failure of government accounting principles to reflect real expenditures in the corporate sector.

Along with the changes in the cost system, the contract price adjustment system was also significantly revised. In line with the general democratization trend, the new system following the 1988 revision of the Enforcement Decree of BAA and Contract Administration Regulation was closer to the principles of market economy system with fluctuating prices. As a result, all expense items as well as all prices became adjustable.

4. Globalization and Localization Period (1993-Present)

The period from 1993 until present is characterized by the continuing democratization of Korea, vast domestic economy reforms following the 1997 Asian Crisis, and Korea's growing international recognition. Similarly, the Korean public procurement system also went through major changes. In 1995, public procurement became regulated by a separate act – “Act on the Contracts to Which a State is a Party,” rather than a single chapter of the BAA. In addition, when Korea signed World Trade Organization (WTO) Government Procurement Agreement (GPA) in 1997, public procurement legal framework was significantly transformed, mainly with the aim to enhance transparency and adopt market approach. Following the trend, in 2005, procurement contracts of local governments became subject to “Act on Contracts to Which a Local Government is a Party” (instead of the previous Local Finance Act).

4.1. Laws and Regulations

Four different areas need to be mentioned in relation to the Korean public procurement legal and regulative framework in the most recent period: remedies, local autonomy, a multiple supplier contract system, and transition in group direct contracting.

The existence of remedial measures⁸ in Korean public procurement system has been influenced by two factors - Korea's admission to the WTO GPA, and the recent trend putting emphasis on alternative dispute resolution (ADR) in the administration. In both cases, the central and the local government levels, the current system allows a person who suffered as a result of the act of a government official or a public servant of a relevant public organization during the tender process to raise an objection and have such an act rectified or cancelled. Furthermore, on the central level, a person objecting to measures taken by the head of a central government division has the right to appeal to the International Contract Dispute Resolution Committee, and, on the local level, such a person has the right to appeal to the “Local Government Contract Dispute Resolution Committee.” Disputes that include international aspect are subject to dispute resolution procedures of the GPA.

The relationship between public procurement and local autonomy represents one of the controversies in the current Korean public procurement. As generally known, both centralized and localized procurement systems have their own advantages and disadvantages resulting in tension. In Korea, local autonomy was initiated when provincial councils were established in 1991,⁹ and local governments gained the authority to realize their own procurement. The

8. Remedial measures were first introduced in GP in 1997 based on Enforcement Decree and Regulation on Special Cases of Act on the Contracts to Which the State is a Party.

9. Full autonomy was not created until 1995.

transition of procurement functions to local level was not smooth and various problems appeared during the process. Local public procurement later became regulated by the Local Contract Act (LCA), which contains various provisions that are different from those in the Government Contract Act.

Over the time of its existence, serious issues also appeared in relation to group direct contracting system. Although originally meant to enable SMEs to compete for government tenders, the system was often abused (for example, subcontracting, or illegal lending of company names were not rare practices). While the PPS continued to improve the system via a number of measures, such as those aimed at the improvement of the quality of supplied goods, or the improvement plan of group direct contracting implemented in September 1998, a survey conducted in 2003 by the joint effort of SME Administration, Board of Audit and Inspection, and Fair Trade Commission (FTC) showed that numerous problems still persisted. As a result, the group direct contracting system was abolished and by 2007 it gradually became completely eliminated. At the same time, to balance the disadvantage of SME participating at government tenders, a list of 226 items for which only SME were allowed to bid was created. In addition, a limit of 85% for the lowest acceptable bid for items subject to competition was introduced to prevent excessive price competition among competing SMEs.

Imitating a US Multiple Award Schedule, a multiple supplier contract system (MSCS) was introduced in Korea. The main reason for the introduction of the MSCS was the effort to tackle problems resulting from the lack of diversity of supplied products, long time needed for the tendering process, and poor quality of goods, entailed in lowest price competitive tendering system. The MSCS, based on the principle that the same product may be delivered by two or more contractors meeting given criteria, was fully implemented in 2004 by the Enforcement Decree of the Act Concerning Government Procurement.

Although by 2007 the system was widely used (the MSCS accounted for 68.7% of all contracts, 52.5% of the supply amount, and 89.3% of all items), controversies related to the system appeared. One of the most serious issues was the fact that operating *de facto* like direct contracting system, opinions that the system violates the Act on Contracts to Which the State is a Party existed. It also turned out that by weakening the competitiveness and violating the transparency of government procurement, the system was unable to ensure sufficient quality of procured goods and thus failed to achieve its main goal – improved efficiency in government procurement. As a result, the MSCS was modified to involve a two-stage competition system, in which a final contractor was selected from a group of two or more contractors pre-selected for the procurement of goods exceeding a given amount in the first stage. However, for the sake of reinforced competition and increased efficiency, the two-stage competition system was also later modified. Following the changes, the applicable

amount was doubled (100 million won instead of 50 million) and the final selection became conducted from three (instead of two) or more contractors.

2012 Modularization of Korea's Development Experience
Korean Government Procurement Experience

Chapter 4

Transparency in Korean GP System

1. Legal Transparency
2. Transparency in Organizational Management
3. Lessons and Implications for Developing Countries

Transparency in Korean GP System

The following section contains the Korean experience with the enhancement of legal transparency and transparency in organizational management (transparency in e-procurement is mentioned in the chapter dedicated to Korean e-procurement system). The authors of this paper hope that this part of the paper can provide readers with the inspiration to the solutions of specific GP problems or help them avoid repeating the mistakes that Korea made.

1. Legal Transparency

The Korean GP legislation has been continuously changing to respond to the needs of a particular period and stage of development. The focus has gradually shifted from economic efficiency to the enhancement of transparency and, more recently, ethical behaviour. The changes in major Korea laws also respond to increasing decentralization and changes in legal environment due to the entry into the WTO and later GPA. In the Korean GP legislation, the principle of transparency is applied via provisions regulating individual stages of GP process. Although transparency is specifically mentioned only in the Local Contract Act and Defence Acquisition Program Act, all GP related acts contain provisions pursuing transparency, suggesting that Korea is making strong effort towards GP transparency enforcement.

The basis of Korea's public procurement legislation is constituted by the National Finance Act from 1951 and Budget and Accounts Act. Korea's GP legal framework has also been strongly influenced by its membership in the WTO GPA. After Korea became a signatory party of the WTO GPA in 1994 during the Uruguay Round of the WTO negotiations, the Act on Contracts to Which the State Is a Party ("State Contract Act") was legislated in January 1995. This act provides regulative framework for contracts with domestic as well

as international aspects, mainly focusing on the procurement process and contracts of central national organizations. Rules and regulations dealing with the procurement of local governments¹⁰ are provided by the Act on Contracts to Which a Local Government Is a Party (“Local Contract Act”) from 2005. In addition, government procurement contracts are further regulated by the Government Procurement Act from January 1995, Defence Acquisition Program Act from January 2006, Framework Act on the Construction Industry from July 1997, and Fair Transactions in Subcontracting Act from April 1983. Regarding international tenders, the State Contract Act stipulates that international tenders also be regulated by the Special Regulations on the Enforcement of the Act on Contracts for Specific Procurement to Which the State is a Party (“Special Regulations on Specific Procurement”) and Special Rules on the Enforcement of the Act on Contracts for Specific Procurement to Which the State Is a Party (“Special Rules on Specific Procurement”). Korea’s tendency to establish separate policies for each government department is well manifested in the existence of independent GP laws and systems, reflecting local political culture.

The major Korean GP laws (the State Contract Act and the Local Contract Act) implicitly describe three major GP principles – transparency in fair procurement opportunity, transparency in contract practice, and the principle of non-discrimination applied in international tenders as prescribed by the WTO GPA. Both these acts specify their main purpose as securing smooth execution of contract business affairs and they stipulate that the conclusion of contracts shall be conducted in accordance with mutual agreement of the involved parties, that the position of the parties be mutually equal, and that the contract be performed in accordance with the principles of faith and trust. Furthermore, the enforcement decrees of both acts contain provisions preventing unfair limitation of contractual profit of the other party. Other acts dealing with GP¹¹ describe the principle of information disclosure and objective criteria. For example, the Defence Acquisition Act mentions transparency as one of the ways to strengthen the competitiveness of the defence industry, and Defence Acquisition Program Act contains provisions regulating information disclosure and ombudsman system.

Since the State Contract Act was introduced, it has been significantly revised six times. Among these revisions, five were made in response to the revision of other major acts¹² and one with the aim to secure more transparency and prevent the abuse of authority.¹³

10. Local autonomy was established in Korea in June, 1995, when elections for local government officers were held for the first time.

11. Government Procurement Act, Defence Acquisition Program Act, Framework Act on the Construction Industry, and Fair Transactions in Subcontracting Act.

12. Administrative Procedures Act, Government Organization Act, Management of the National Funds Act, and National Finance Act.

13. Based on this revision, which focused on the punishment of unfair practices, the provision related to punishment period changed from “a certain period” to “within two years”.

Similarly, the Local Contract Act has also been revised several times. Five revisions were due to the revision of other acts¹⁴ and two dealt with the punishments of unfair practices, bidder prequalification system and debarment, and the optimal value system. Based on the revision in 2009, the optimal value system was legally expanded to include not only price, but also quality, technology, and proposal and contract period. The objective of the 2009 revision was also to make awarding contracts through open (competitive) tendering quicker and more reliable. Overall, the main aim of the revisions was to allow local governments to conduct more thorough assessment of GP contracts. Furthermore, to bring laws closer to its actual user, the revision of the Local Contract Act in 2009 was also accompanied by rewriting the law in easier language.

Regarding other GP acts, the main content of the revisions of the Government Procurement Act was the implementation of three-procurement system, punishment of corruption, procurement training, financial loans expansion, “information requests to other organizations to operate G2B, government-private joint reserves, requirements for derivative transactions, mandatory procurement items and contracts requested by the local government in 2009; and consortium made of small and medium companies in the competitive tendering and punishment of consortium in case of unfair practices in 2010,”¹⁵ and the main content of the revisions of the Defence Acquisition Program Act related to GP was the specification of “R&D leading organizations, selection of small and medium companies in producing prototypes, introduction of the project coordination request system in 2009, requirements for ombudsmen, and limitation for foreign companies’ participation in national strategic weapon projects in 2010.”¹⁶

2. Transparency in Organizational Management

Transparency in organizational management involves various kinds of issues. The following text deals with those aspects of organizational management transparency that relate to disclosure and access to information, transparency of procurement methods and evaluation system, discretionary power control, unfair practices and *ex-post* management, dispute settlement procedures, procurement call center and e-procurement, and procurement ombudsman system and integrity culture.

14. The Act on Facilitation of Purchase of Small and Small and Medium Enterprise-Manufactured Products and Support for Development of Their Markets, Government Organization Act, and Local Autonomy Act.

15. Kim et al, 2010, p. 72.

16. Ibid.

2.1. Disclosure and Access to Information

Access to information and information disclosure in GP mainly concern the accessibility of information on GP legislation, tender conditions, and the announcement of successful bidder. As already mentioned, information disclosure and transparency often represent a legal obligation given by GP laws. However, when constituting legal obligation to disclose tender information, countries need to solve the issue of what degree of transparency is desirable and at what point transparency becomes excessive and starts doing harm to tender participants or public good. In Korea, these decisions are within the scope of responsibility of the PPS, which considers both aspects of disclosing information in every decision it makes and makes significant effort to keep them in balance.

The availability of information on procurement procedures in the law is mainly secured by the existence of online information provision system of the Ministry of Government Legislation and the PPS.¹⁷ The websites of both institutions enable their visitors to search and view GP relevant laws, including international tendering procedures.¹⁸ Furthermore, contracts officers or the heads of central government agencies are supposed to respond to bidders' information requests regarding tendering process, procedures, and practices, except the case of disclosure of information that may impede public good or law enforcement.

In case of domestic tenders, tender announcement is supposed to include information regarding tender conditions such as qualification criteria, bidder selection procurement, contract starting and ending date, etc. In addition, the announcement of an international tender is also supposed to provide information on any additional conditions, follow-up tendering announcement schedule in case of the recurring contract; tendering method (open (competitive) tendering or selective (competitive) tendering); negotiation procedure; procurement type (purchase, tendering or instalment plan); application for tendering qualification; tendering application; address to submit the proposal; due date; language to be used; and GPA applicable contract. Moreover, as per the Enforcement Decrees of both the State and the Local Contract Act, information concerning quarterly procurement plans (e.g. the amount of orders to place, changes or conclusions of contracts, etc.) should be published by the head of central government agencies or contract officers.

Finally, provisions regulating the announcement and notice of successful bidder are provided by the Enforcement Decree of the State Contract Act. It is stipulated that information regarding the contract awarding and modification, such as the contract purpose,

17. Main laws on GP in Korea, i. e. The State Contract Act, the Local Government Act, and their enforcement decrees, do not contain provisions concerning the disclosure of information on procurement procedure.

18. Korean online information provision system is considered to be among the best practices by the OECD.

tendering date and contract awarding date, estimated or expected price, contract awarding method, contractor's name, contract quantity or volume, contract amount, and reason for the selective (competitive) tendering or direct contracting, should be disclosed, and that the disclosure is to be made by the head of a central government agency or contracting officers through designated means. In an international tender, the information to be disclosed includes information on the procurement item, its quantity and the amount, successful bidder or contractor selection procedure (or the reason for the choice of a particular contracting methods),¹⁹ and other information regarding the selection of a contractor. As with domestic tender, the information should be provided by designated means, in compliance with the WTO GPA. It is also stipulated that any information request by bidder regarding tendering should be replied. In special cases, when such a request is declined, the reason for the request rejection must be made known. Similarly, when a bidder's application is rejected, the reason for the rejection (or suspension), the reason why the bidder is not qualified or selected, the name of successful bidder, and features of the successful proposal must be disclosed. However, in case of violation of the public good or when the execution of contract may be impeded, WTO GPA does not allow for information disclosure.

2.2. Transparency in Procurement Methods and Evaluation System

Transparency in procurement methods and evaluation system focuses on the clarity with which procurement methods, evaluation criteria and evaluation system are defined, and the extent to which proposal assessment is objectively conducted. This kind of transparency also deals with whether and how discretionary power of procurement officers is controlled. The following text first focuses on how transparency in procurement methods and evaluation system is fostered, followed by a part dedicated to the control of discretionary power in proposal evaluation system and contracting methods.

As already mentioned in the chapter dedicated to procurement methods, Korea uses various tendering methods. The main competitive tendering methods are open (competitive) tendering and its variations, and the non-competitive tendering methods include selective (competitive) tendering and direct contracting, while open (competitive) tendering is designated as the main contracting method. As the economic-political environment evolved, the Korean procurement system needed to respond to the changing situation. In line with that, tendering and contracting methods also changed, some became modified, some completely abolished and some refined to better reflect new conditions and needs. Since the Korean economy started opening-up to international trade in the second half of

¹⁹ In case of direct contracting. In case of open (competitive) tendering, the announcement procedure should be disclosed.

the 1980s, the Korean GP methods have also been strongly influenced by international environment and Korea's membership in international organizations. One example of such influence is limited competitive tendering, which, in compliance with the WTO GPA, is not used in international tendering.

To increase the level of transparency in procurement methods, Korea introduced a pre-qualification system (PQ) under which only bidders satisfying given criteria (for example, bidder's history, technical capability, financial status and credibility, the difficulty of construction, etc.) were allowed to compete for the contract. As per the Enforcement Decree of the State Contract Act, this kind of evaluation was conducted for projects with the estimated value exceeding 30 billion won, with the specification of evaluation criteria carried out by the Ministry of Strategy and Finance.

Upon its introduction, the PQ system suffered from some serious issues. First, as the PQ system was unable to effectively select the optimal bidder, problems related to efficiency appeared. It often happened that uncompetitive companies passed the pre-qualification assessment without difficulty and received high enough points to stand a good chance of winning the contract, although cost-competitive constructors using new technologies were supposed to receive higher evaluation scores. The reason was that inappropriate weights assigning more points for construction experience led to the distortion of proportions among criteria in use. Although this issue is more a matter of choice and definition of a contracting method, the cases that PQ criteria are violated directly concern transparency and transparency enforcement.

Violation of PQ criteria is regulated by the Enforcement Decree of the State Contract Act, which stipulates that potential bidders failing to meet any of the prescribed criteria should not pass the PQ stage. There have been cases that the Supreme Court ruled a tender invalid when a contractor that was not supposed to successfully pass the PQ assessment was awarded a contract and other tender participants raised objections.

To enhance transparency of the PQ system, it is necessary to clearly define each evaluation system and the criteria in use including their respective weight. In relation to that, it is also important that the criteria reflect procuring entities' needs; otherwise PQ assessment would fail to meet its purpose. Despite the need for clearly defined criteria and procedures, excessive rigidity of the system would be contra-productive. As each project is different, it is also important that the system allow for the consideration of each project's individual features, which should also be manifest in PQ criteria. Hence, it is important to find balance between transparency, in the sense of clear definition of PQ procedures and criteria, and efficiency, meaning the ability to flexibly react to the cases of non-standard projects requiring special treatment, so that optimal bidder is not ruled out during the PQ

phase. Another issue is also the amount of discretion procurement officers can exercise in PQ assessment; this topic is dealt with in more detail in the next subchapter.

2.3. Discretionary Power Control

In GP, discretionary power control mainly concerns regulation of contracting methods and contractual relationships. Among these, the issue with strongest bearing on transparency is the extent to which direct contracting (or, in general, other non-competitive tendering methods) is possible to use and the clarity with which the circumstances for its use are defined.

With regards to direct contracting, the Local Contract Act and the Enforcement Decree of the State Contract Act stipulate that the disclosure of the content of direct contracting is obligatory and that in case of small projects, the use of electronic open direct contracting system is encouraged. The State Contract Act further stipulates that proposals from more than two suppliers must be received.²⁰ This measure was introduced in order to avoid a situation that only proposals from regular suppliers usually engaged in direct contracting are received. In addition, it also serves to enhance transparency.

In accordance with the Korean law, direct contracting can also be used in international tenders in a situation of urgency when open (competitive) tendering cannot be used. However, this provision does not fully correspond to the WTO GPA regulations. Although GPA also allows for the use of direct contracting in a situation of urgency when goods cannot be procured within due time, according to the Korean legislation, the scope of the use of direct contracting in international tenders is broader. Similar situation also exists in relation to domestic tenders, where direct contracting is used even more often. The cases where direct contracting can be used in domestic tenders but not in the international ones are confidentiality, the conclusion of a contract with a certain party, local resident, provider of the specific provider or equivalent party, and where the purpose and nature of the contract allows only direct contracting. Other cases also include natural disasters, troop mobilization, or similar situations requiring immediate action. As floods occur regularly in Korea, even though the legal conditions for the use of direct contracting are met, this contracting method maybe still used excessively. Moreover, the definition for the cases of “confidentiality” is vague, thus contracting officers or agencies can exercise their discretion is determining which procurement case are those that their details must be kept confidential. In this respect, clarification of conditions regulating the use of direct contracting is needed. Another related topic is the length of proposal submission period. In case of urgency, the period is five days, while some argue that in minimum seven days submission period in domestic tendering is

20. As per the State Contract Act revision from 2005.

desirable. The discrepancy between the Korean and WTO GPA regulations along with the difference in usage of direct contracting in domestic and international tenders receive a lot of objections and discussion is currently going on whether to modify the Korean legislature to comply better with international regulative framework or not.

A modification of direct contracting system is the so-called collective (group) direct contracting, the purpose of which is to facilitate tender participation to SMEs, which would otherwise not be able to meet PQ criteria. This method is receiving criticism as it actually represents positive discrimination and results in reverse discrimination against other SMEs. As the use of this method did not bring the desired result (SME support) due to the failure of SMEs to handle organization of group contracting, the method was abolished. Instead, SME support was secured via the issuance of the Small and Medium Enterprises Promotion Act and the Special Act on the Promotion of Business Conversion in Small and Medium Enterprises.

Other types of contracting methods where the risk of abuse of discretionary power is high are contract via negotiation and multiple supplier system. Contract via negotiation is a system where proposals are received from several suppliers based on specialty, technology, urgency, safety of public buildings, and national security, and the successful bidder is then selected through negotiations. In accordance with the Enactment Decree of the State Contract Act, this contracting method is to be used as the preferred method in knowledge-based projects. However, since the successful bidder is the one who offers the “best benefit” for the country or the local government and the definition of what is “beneficial” falls within the discretion of the procurement organization, the likelihood of non-transparent or unfair use of this form of contracting is relatively high. To tackle this issue, the Account Rules regulating (in case of contract via negotiation) tender announcement period, proposal technical evaluation, price evaluation method, and negotiation procedure, were issued by the Ministry of Strategy and Finance.

Another efficiency improvement measure, which also resulted in the increase of procurement transparency, was the implementation of a multiple-supplier system. In this system, multiple bidders submitted their proposals and more than one successful bidder could also be selected. An important feature of the system was that a number of criteria, among which quality played an important role, were used to evaluate the proposals. As especially quality assessment leaves a lot of space for the use of discretionary power by contracting officers, the Government Procurement Act and regulations of the PPS describe the system in great detail to prevent potential discretionary power abuse. Currently, discussion is going on in the Board of Audit and Inspection of Korea and the National Assembly as to whether the multiple-supplier system is actually a form of limited competition system or not. For this reason, the PPS is trying to refine requirements for supplier qualification. Apart from

providing balance against the lowest price system, this system also represents the PPS effort to build procurement environment based on market principle (provision of quality goods via fair competition).

2.4. Unfair Practices and Ex-Post Management

As procurement market represents a large portion of the Korean economy and contracting methods based on limited or non-existent competition are also used to conclude contracts, the likelihood of unfair practices or the suppliers' failure to fulfil a contract is high. Moreover, the high volume of funds spent by the government every year on procured goods and services creates incentive for companies to participate at tenders and potential tenderers have strong motivation to cheat in PQ assessment. Criteria manipulation, bribery, subcontracting, nepotism, provision of goods of inferior quality, the failure to fulfil contractual terms, unjustified price increase while contract is being performed, etc. are just a few examples of unfair practices the Korean procurement system is plagued with.

To increase transparency and improve situation, Korea uses various kinds of remedial measures. A contract execution letter of pledge is an example of a pre-measure, while sanctions imposed in case of unsatisfactory contract performance are examples of post-measures. The purpose of imposing sanctions and punishing suppliers who do not fulfil the contract or unfairly participate at tenders is to create more reliable, fair, and transparent procurement environment. To facilitate the process, definition of unfair practices should be provided by the law, so that false interpretations of legal provisions or abuse of discretionary power are not possible. In addition, to prevent the occurrence of situations that discretion is exercised unfairly, administrative litigation should exist. In relation to that, it is also important that any time sanctions are imposed they be accompanied by their proper justification.

The State Contract Act stipulates that tender participation of those who might hinder fair execution of competition or appropriate performance of a contract, or those who are not eligible for participation in the tender, should be limited from participating in the tender within the scope of two years under the conditions as prescribed by the Presidential Decree. Although the limitation period was not specified originally, the provisions were later revised to prevent their overly extensive interpretations.

The limitations on participation in tender, which are regulated by the Enactment Decree of the State Contract Act, can be divided into four categories – sanctions aiming at the prevention of future crime, procedural issues ensuring that procurement is carried out smoothly (both of these groups are not directly related to the capability of contract execution), sanctions imposed when a contractor fails to pay off liabilities (the main

purpose of these is to ensure contract completion by the contractor), and those concerning contractor's capability to perform contract in future.

Since limiting a potential contractor from participating in tenders for a given period of time may have a strong negative impact on the contractor's bottom line, the abuse of agency's discretionary power must be prevented. However, as the adequacy of the length and form of limitation on tender participation is a normative question, there is no consensus regarding the type and period of such limitations. Currently, four different opinions with bearing on limiting participation in tenders in Korean environment exist.

First, regarding sanctions preventing future crimes, there is an opinion that the limitation period of three to five years as originally stipulated by the Korean legislation is too long. As a consequence, it has recently been reduced to two years.

Second, in terms of the second group (procedural issues), an opinion that the supplier that violates prescribed procedures should be fined and banned from participating in the tender exists. However, some also argue that a supplier that intentionally makes an invalid proposal should also be punished in a different form (e.g. prohibition to participate at the GP market, etc.).

Third, with regards to the contractor's failure to pay off liabilities, there is an opinion that by limiting a supplier from tender participation regardless of the reason for the failure to perform contractual obligations, the principle of proportion may be violated. In a situation that the reason for unsatisfactory contract performance is gross negligence, insufficient capability, facilities, or expertise, or contractor's intention, punishment in compliance with the principle of proportion is well justified. Nevertheless, there is also an argument that the issue of whether the supplier has sufficient expertise and capability including the equipment and facilities necessary to satisfactorily perform the contract should be sufficiently addressed during the PQ assessment stage.

Finally, as far as the capability to perform future contracts is concerned, there is an argument that if Paragraph 1 Substandard Contract Execution is applied to a supplier, the principle of proportion may be violated. Hence, the opinion that the application of Paragraph 1 should be only applied in case of gross negligence exists.

2.5. Dispute Settlement Procedures

Dispute settlement is an important part of an *ex-post* phase of procurement process. In general, dispute settlement procedures can be divided into two categories – legal settlements and petitions. Dispute settlement can be further categorized into two groups – dispute settlement within administration and dispute settlement in court.

Dispute settlement in administration is regulated by the State Contract Act, which regulates the cases of disputes occurring in a contract conducted by the means of international trade. The Act stipulates that in a situation that any person suffers harm due to the procurement officer's action in an international tender, objections can be filed to the head of responsible central government agency. Moreover, if any person is not satisfied with the way the objection has been treated, it is possible to request re-examination by the International Contract Dispute Conciliation Committee. In compliance with the WTO GPA, by the order of the Committee, related tender procedures may be postponed, or the conclusion of the contract suspended, until the conciliation is completed.

Regarding domestic tenders, a dispute conciliation committee addressing issues concerning the selection of successful bidder, contract conclusion and performance, and follow-up management, exists under the PPS. The exceptions from the above are issues related to petitions, authoritative interpretation of the State Contract Act, matters decided in the contract evaluation committee, and constructing project disputes between a government agency and a constructor. Similarly, the Local Contract Act stipulates for projects with the amount higher than a given amount (decided by a presidential decree or a local government) that in relation to issues concerning tender participants' qualification, tender announcement, and successful bidder selection, objections can be filed. In case of an objection acceptance, the Local Contract Dispute Conciliation Committee can order a suspension of the tendering process or stop the conclusion of the contract until the conciliation is completed. Furthermore, re-examination of measures related to such objections can be requested from the Committee.

In terms of dispute settlement in court, legal evaluation is possible in domestic as well as international tenders. As a GP contract is recognized as a judicial contract, relief measures through civil actions are allowed by the Supreme Court. The ruling that GP contract is considered a judicial contract is based on the State Contract Act, according to which both parties in GP contract are in a mutually equal position.²¹ This means that in case of a dispute in tendering process, a civil action (for example, a civil action confirming the status of a successful or second successful bidder) accompanied by an injunction for the sake of quick settlement is filed.

However, in accordance with the Supreme Court rulings, revocation suit (a type of administrative litigation) is also permitted to use in a situation of punishment of unfair suppliers in relation to a GP contract where one involved party is central or local government. Dispute settlement concerning sanctions to unfair suppliers also follows a provisional relief

21. The State Contract Act stipulates that "a [GP] contract shall be concluded in accordance with the mutual agreement of the parties concerned in a mutually equal position and be performed in accordance with the principle of faith and trust".

system under the Administrative Litigation Act. Furthermore, as the supplier on whom legal sanctions are imposed suffers a loss whether he wins the suit or not if the sanctions stay effective,²² in many cases the sanctions are suspended. This is possible for as the objection against sanctions is not unreasonable and the suspension of sanctions is well justified. Apart from preventing suppliers from incurring unrecoverable losses, this provision also exists to prevent conclusion of GP contract with suppliers proposing the lowest price unreasonably.

2.6. Procurement Call Center and E-Procurement

Legal settlement is a time consuming and costly way to settle disputes, therefore many countries are now adopting systems allowing for interactive provision of opinions on tendering procedures and answers to inquiries regarding inappropriate practices. In line with this trend, since 2002, Korea has established and is running a Procurement Call Center. The center, which is integrated into the official G2B website, answers questions from civilians and also discloses already provided answers on the web. A separate call center to receive calls on petitions is operated by the PPS.

The introduction of a call center to receive questions on procurement process from civilians has been an important step to increase transparency of GP in Korea. The center, which can also be reached through the Internet, provides a call reservation system allowing clients to consult their questions with a government officer at a prearranged time. In addition, the establishment of a call center has the benefit of allowing procurement officers to concentrate on more complicated or important tasks, since routine questions can be answered by the call center staff. The quality of services provided by the center is constantly monitored and currently a Happy Call system²³ is in operation to deal with clients' complaints.

The operation of the call center is further supported by the existence of Korea Online E-Procurement System (KONEPS) and the PPS website, which are available twenty-four hours per day for online inquiries. An important feature of the information provision system is that it contains a search function to search through previously provided answers from government officers and makes a large amount of information readily available. In addition, the system provides automatic e-mails with information on changes in procurement laws, and reminder of certificate expiration service. As supplementary systems, the PPS also operates consulting knowledge system, e-procurement monitoring team, internal system collecting comments and suggestions from the staff, and other channels for the collection

22. If the sanctions are not suspended, the supplier is not permitted to participate at any GP tender. However, even if the supplier wins the suit, he is not able to participate at the tender that caused the suit. In both cases, the supplier suffers a loss that is not easily compensated.

23. Happy Call system is a hotline designed to solve urgent requests from customers.

of opinions from government officers and clients. Finally, a system for the provision of consulting service regarding inquiries about contracting systems and their legal regulations allowing clients to review legal issues before their contact government officers also exists.

The establishment and operation of the procurement call center brought up several issues that needed to be solved. First, the center was originally unable to deal with complaints regarding the whole procurement system. Another inconvenience was that when the call center responsibilities were expanded to cover all the aspects of GP, only telephone channels were available to reach the center. Hence, to make easier communication possible, a web-based center was later established.

2.7. Procurement Ombudsman System and Integrity Culture

The effort to increase transparency in organizational culture has also led to the establishment of procurement ombudsman system, which was the first ombudsman system established by a central government agency in Korea on legal grounds. The system has as its main objective the improvement of transparency in defence acquisition programs; hence, it is often employed by the Defence Acquisition Program Administration.²⁴ Another reason for the existence of the system is complexity and confidentiality of decision making in defence related projects, resulting in increased risk of power abuse and comparatively lower level of transparency. In such complex environment, ombudsman system is a relatively convenient tool for the enhancement of transparency even in projects related to national security.

Ombudsmen, who are appointed by the Commissioner of the Defence Acquisition Program Administration, must be individuals with personal integrity and experience in the field (associate professor or higher). In addition, to prevent conflict of interest, a person designated to perform an ombudsman or the person's family members must not have worked for a defence company or research institute for the last two years before the appointment as an ombudsman. Ombudsmen are appointed for two years and can serve for two consecutive terms. At one time, a maximum of three ombudsmen can perform their functions. In their work, procurement ombudsmen follow five principles, which are: "i) independence from their designators and government officers related to the program, ii) long-term, continuous activity, iii) encouraging people's participation and monitoring, iv) transparency for the maximum disclosure within the range of limitations, v) neutrality from petitioners or government agency."

24. Defence Acquisition Program Administration is a government agency responsible for the development of defence capability and defence industry, and the improvement of defence material procurement in Korea.

Ombudsman system has the authority to examine petitions filed in relation to defence acquisition program and ombudsmen can also request the Commissioner of the Defence Acquisition Program Administration for audits or corrections of issues raised by clients, with the exception of those where administrative litigation is in progress or which are being audited by a government agency or is under investigation.

During its existence, several problems related to the ombudsman system have appeared. First, due to the fact that the decisions made by ombudsmen take the form of recommendations, there is no legal way to enforce them, and their application is thus problematic. Second, as ombudsmen work without assistance and they are not full-time employees, the time necessary for the review of petitions is longer than three months. This results in the decrease in the number of petitions, which undermines the reason for the existence of the ombudsman system. Third, there is only a little room for petitions, as re-examination is only permitted for those petitions filed within the defence acquisition program. Finally, another issue is that there is no reliable way to secure ombudsmen fairness.

As a solution to tackle these problems the Defence Acquisition Program Administration is contemplating are revision of relevant laws, ombudsmen's independence enhancement, designation of assistants for ombudsmen, external screening for ombudsmen, information disclosure related to petition investigation, creation of obligation to cooperate with ombudsmen, automatic reporting of petition treatment to the National Assembly Standing Committee and the Board of Audit and Inspection of Korea, and the creation of possibility to attend the defence program committee and participate in it.

Despite the aforementioned issues, the ombudsman system of the Defence Acquisition Program Administration is recognized as the best practice in the field. As such, it is part of the training materials in the Anti-Corruption & Civil Rights Commission and it also has a high international standing. For example, in 2007, the system was selected as the best case in the field of defence procurement within OECD countries, the best case in the 13th International Anti-Corruption Conference held in Greece in 2008, and the best case in the 60th Anniversary of NATO held in the USA in 2009.

Integrity culture refers to the Korean government's effort towards instilling personal ethics and tenets in the management and organizational culture of the Korean institutions. The most common integrity culture tool worldwide is an integrity pact originally developed by the Transparency International. Integrity pact is also used in Korea, where its introduction was recommended to the Ministry of Strategy and Finance and the Ministry of Public Administration by the Anti-Corruption & Civil Rights Commission. Currently, in compliance with the pact, sanctions such as contract cancellation or ban from tender participation can be imposed if a tender participant violates the provisions by offering a

bribe. The 2010 recommendation of the pact stipulates that a supplier should be obligated to sign the integrity pact so that in a situation that the pact is violated, the tender participant may be sanctioned in accordance with the pact. When deciding about sanctions, government agencies also consider the public good or the impact on the country. Furthermore, there is also a recommendation that integrity pact fulfilment by the bidder should be taken into consideration in tender qualification.

To enhance integrity of GP officers as well as suppliers, the Defence Acquisition Program Administration distributes an integrity enhancement video every month and makes it obligatory for its employees to attend integrity classes. Integrity pact is also an integral part of widespread fight against corruption (so-called zero-corruption movement) in Korea. Another anti-corruption measure Korea has implemented is the code of conduct developed by the PPS for high ranking officers and petition committee members, and the integrity pledge PPS officers and GP suppliers must sign. Despite these attempts at corruption reduction or complete eradication, 246 cases of inappropriate practices were discovered between 2006 and 2008. Nevertheless, due to its continuous effort in making integrity one of its employees' core values and systematic fight against corruption, the PPS was evaluated as the best anti-corruption government agency by the Anti-Corruption & Civil Rights Commission Corruption Prevention Evaluation in 2009.

3. Lessons and Implications for Developing Countries

The Korean experience with transparency enhancement may offer some inspiration for other countries in their effort to build reliable a transparent public procurement system. With regards to legal transparency, Korea is a good example of a country where procurement legislation development reflected well the country's developmental path. Beginning with a few lines dedicated to GP in the National Finance Act up to the enactment of the State Contract Act and the Local Contract Act, it is obvious that GP legal framework responded to the changing domestic and international situation. Furthermore, it is also possible to see that the emphasis gradually shifted from management of foreign aid to economic efficiency, and finally provision of the best value. The important lesson here is that the legal framework and legal transparency must be consistent with the country's economic system and its needs, otherwise various problems may arise. Moreover, transparency enforcement must have solid legal grounds, whether stated explicitly, or implicitly, as in the Korean case. Legal provisions must also provide objective criteria according to which cases are assessed, and the principles of information disclosure and non-discrimination also need to be legally grounded. Apart from that, the system should ensure that sufficient and valid information about GP legislature is provided, along with the provision of information regarding remedial measures. To this end, Korea serves as an example of successful case of a well developed

e-procurement information system, through which transparency has been significantly boosted. Important part of information provision and transparency enhancement is also the disclosure of lower laws, as typically sufficient information on higher laws is provided, but detailed and reliable information on lower laws is difficult to obtain. Here again, the Korean e-procurement system supported by various services such as call centers, etc., can provide a good case to benchmark. Another interesting example of effort towards higher degree of legal transparency is also the 2009 revision of the Local Contract Act, during which the Act was rewritten in an easier language to bring it closer to its actual users. Finally, when developing their GP legal framework, countries should also take into consideration international trends and international influences, such as membership in international organizations or globalization of GP market.

As far as transparency in organizational management is concerned, an important consideration is the level of transparency to enforce. On the one hand, insufficient degree of transparency may undermine the trust of tender participants in the procedure leading to negative effects such exemplified by decreased efficiency. On the other hand, too much transparency is not desirable either, as it may hinder competition among tender participants, hurt tender participants themselves (e.g. through disclosure of information related to patents, etc.), or hurt national interests in case of procurement of goods related to national defence, situation requiring confidentiality, situation that disclosure of specific information may impede the public good, etc. With regards to information access and disclosure, it is also important that not only information on tendering procedures be disclosed, but *ex-post* measures and their legal justification must also be made available, which is especially important in case of sanctions and remedial measures. The Korean experience also shows that transparent evaluation system must be based on clearly defined objective criteria; otherwise too much discretion on part of the procurement officers would exist. Furthermore, any PQ system must be able to meet its main purpose – selection of the optimal bidder. To achieve this, it is not sufficient that the criteria and their content be clearly defined, but they must also be well selected, including careful choice of their weights. However, the system should also keep a certain degree of flexibility allowing for efficient handling of special procurement cases.

In terms of discretionary power, the Korean case shows that particular care should be paid to direct contracting and the conditions when it is allowed to use. For example, although the method is legally justified in a situation of urgency or disaster, regular occurrence of floods in Korea, which falls in the category of disasters, resulted in an excessive use of the method. Thus, in preparation of procurement method regulations and of measures limiting discretionary power, local conditions must be considered.

The establishment of an ombudsmen system also calls for careful consideration. In Korea, ombudsmen's decisions take the form of recommendation and their legal enforcement is not possible. The question of whether to create a legal obligation to follow their decisions or not is thus very legitimate and any country trying to establish their own ombudsmen system should pay sufficient attention to it. Another issue is securing ombudsmen fairness and sufficient amount of time for them to dedicate to their function, otherwise the time needed for decisions to be made might be too long, as was the case in Korea. Nevertheless, being repeatedly recognized as the best practice in the field, Korea's ombudsmen system can serve as a case to benchmark. Finally, Korea's experience also proves that promotion of integrity values and the culture of ethics bring positive results. The evaluation of the PPS, which has been making continuous effort towards the enhancement of personal integrity of its employees, as the best anti-corruption government agency in 2009 can make a good example.

2012 Modularization of Korea's Development Experience
Korean Government Procurement Experience

Chapter 5

Korean E-procurement System

1. Information Access and Protection
2. Procurement Monitoring System
3. E-Procurement Legal Framework
4. Lessons and Implications for Developing Countries



Korean E-procurement System

Informatization of public procurement and the introduction of an e-procurement system was part of Korea's effort towards the enhancement of transparency and efficiency of public procurement administration as well as provision of customer friendly service. The establishment of an e-procurement system was also influenced by the development in international environment such as the market opening, international trade liberalization including procurement market, worldwide introduction of e-procurement systems, and increased amount of attention paid to transparency and fairness in public administration. Several international events including the announcement of public procurement principles by the OECD and APEC and Korea's signing of the WTO GPA in 1994 also contributed to Korea's focus on e-procurement implementation. When Korean e-procurement system was built, Korea was experiencing a general paradigm shift towards customer-oriented GP administration. In line with the trend, provision of diversity and customized solutions gained more importance than before. For efficient management of more complex public procurement demands, e-procurement system became necessary.

The establishment of an e-procurement system that would be flexible, transparent, and fair was not an easy task and several important issues needed to be considered. First, the system needed to be able to successfully address the issue of the right to access information provided by the system, as not all files or information are necessarily desirable to be open to the public without restrictions. Related to that are the issues of implementation of a well-developed monitoring system to detect any attempt at the system abuse and information protection, which must be secured so that system users are able to develop trust in the system. This is especially important in procurement market, where the disclosure of proposals of competing bidders might for example do harm to the tender participants or lead to tacit collusion among bidders, resulting in the decrease of efficiency. In Korea,

the e-procurement introduction was even more difficult owing to the fact that in the 1990s, Korea was in the process of transition from economy oriented development-first policy period to a democratic administrative model.

E-procurement system development was a gradual process, which started in 1999 with the introduction of procurement Electronic Data Interchange (EDI). After that, in 2000, an electronic bidding system was built, and electronic payments became possible in 2001. In 2002, a national e-procurement system (also referred to as G2B or Nara Marketplace, which was part of eleven electronic government projects under development, was started. Later, in 2004, Customer Relationship Management (CRM) was gradually implemented, and PDA (Personal Digital Assistant) bidding started being used in 2005. In 2006, an electronic commerce shopping mall for procurement services was built. Since 2008, the electronic shopping mall has provided the service of bidding via cellular phone devices and since 2010 bidding has been conducted by the means of fingerprint recognition registration.

This chapter further discusses three topics related to Korean e-procurement system. First, information access right and information protection is discussed in the first subsection. Brief description of the procurement monitoring system follows and the chapter is concluded by a subsection dedicated to the e-procurement legal framework.

1. Information Access and Protection

Information access and protection is an important aspect of all elements of the Korean electronic procurement system. This subsection focuses on how Korea solved the issue of information access and protection in its public procurement EDI project, electronic bidding system, national e-procurement system, and so-called ‘ubiquitous electronic public procurement sophistication project.’

When first conceived, public procurement EDI project was receiving high priority as it represented a convenient means to provide private sector with information from public and administrative sectors. The project, which started full operation in 2001, had as its main objective the adoption of electronic data interchange (EDI) in procurement, construction contracts, and accounting. To provide information security and prevent system abuse, the PPS took charge of issues related to electronic tender, and document and user authentication along with supportive security systems were implemented by the Information Clearing Center. As electronic tendering system was the one with the highest likelihood of potential abuse, when a tender was being conducted, enhanced staff and tendering security measures were applied. While user authentication was secured by the use of authentication key management system, the EDI system also allowed for the use of electronic signature in case

of standard documents. Helping to improve public procurement efficiency, the EDI project was an important step towards transparent and reliable electronic procurement environment.

Electronic bidding system (GoBIMS) started its full operation in 2001 with the revision of the Enforcement Decree of the State Contract Act, which contained provisions regulating electronic bids. In order to make the operation of GoBIMS possible, several existing laws needed to be modified and new laws needed to be enacted. One of the main reasons for the modifications of GP legal framework was the necessity to provide provisions for information access and protection measures. Some of the newly regulated areas related to e-procurement were procedures allowing for the confirmation of time that electronic documents were sent or received, the use of electronic signature, the situation of system shutdown, awarding a contract in electronic tendering, etc. The operation of electronic bidding system was accompanied by the introduction of terms of agreements for electronic bidding participants and bid executors, and special regulations for electronic bids. The activation of electronic tendering services also required electronic signature certification from accredited certification authorities, which were the Korea Securities Computing Corporation (KOSCOM), Korea Information Certificate Authority (KICA), and National Computerization Agency (NCA). Similarly, any bid offering was also accompanied by validity check by accredited certification authorities. Other security measures included the use of an encrypted public certificate used in each bid or debarment from a tender when participation fees were not paid for.

The expansion of the EDI project included an online shopping mall as its integral part. Public Procurement e-Mall was environment where government departments were able to electronically purchase office supplies and other goods. The establishment of the mall was accompanied by the introduction of electronic payment systems, electronic warranty issuance and reception system, and security measures using public certificates.

After the implementation of electronic bidding system, the PPS found out that a comprehensive portal involving the whole public procurement process was needed. Furthermore, the central as well as the local governments along with the public corporations wished for a single system incorporating all GP functions to avoid redundancies and unnecessary expenses caused by the existence of a number of parallel systems operated by individual institutions. Consequently, the national e-procurement system was built with the use of GPB project as its foundation.

As e-security measures, the system used technology for document security to secure information protection and safe access to information, and electronic signature based on Public Key Infrastructure (PKI).²⁵ Other security measures included the use of nationally-

²⁵. [An official national encryption method.](#)

certified encryption algorithm based on the PKI, EDI-based security system for safe communication among computers using web XML standard, and, similarly to electronic bidding, publicly certified electronic signature.

The implementation of the system also required a revision of GP laws as already mentioned. Namely, they were the Enforcement Decree and Enforcement Regulations of the Government Contract Act, Enforcement Decree of the Government Procurement Act, and Enforcement Decree of the Local Finance Act. The resulting e-procurement system and website represented an important step in efficiency and transparency enhancement, as it effectively became the single GP channel. This was also possible due to the fact that its electronic solutions promoted open technical standards and the system was compatible with the systems of GP relevant organizations.

In the process of the creation of the Ubiquitous Electronic Public Procurement Sophistication Project, strengthened security measures along with measures to tackle unexpected events such as unplanned system shutdown, etc., received a high priority. The system security was ensured by the use of double firewalls, intrusion detection system to monitor unauthorized access, the PKI, measures to control information access and prevent unauthorized program modifications, and data backup system allowing for the data restoration within four hours after system failure. As security measures in use were numerous and their use complex, operating guidelines for their systematic management were created.²⁶ The whole system was operated by an integrated computer center. As a result of the security effort, between the years 2003 and 2005, the occurrence of system failure dramatically declined and in 2006, the system operated without any failures.

To boost customer satisfaction and increase the reliability and transparency of the system, public procurement web-call center, information notice service, mobile electronic bidding system, mobile inspection of procured goods, and mobile office gradually started to operate. The most recent development includes the establishment of Nara Marketplace shopping mall, intelligent merchandise information service, and fingerprint recognition based bidding.

However, as e-procurement systems developed, difficulties related to incomplete legal regulations and security measures along with conflicting interests with regards to electronic bidding appeared. Although significant amount of effort was made to solve them, a lot of systems and functions that were developed were never used, a problem, which partially prevails until today.

Despite its undeniable success, Korean e-procurement is also receiving some criticism. There are opinions that as procurement process is complex, the system is too complicated

26. [Personal Information Protection Guideline](#), [Outsourcing Security Management Guideline](#), [Human Security Management Guideline](#), and [Emergency Disaster Procedures](#).

and covers too much information. It is thus difficult to easily reach the information the client is looking for. Moreover, e-procurement system clients are repeatedly required to install a security program every time they visit the website, causing an abundance of inconveniences. Furthermore, as authentication for various channels is not integrated, different pre-registration procedures are required and system users thus need to go through different registration process several times. Finally, the efficiency of the system operation is still hindered by the existence of some tacit factors influencing the system utilization, such as cultural practices. In a number of cases, personal communication and contact is preferred over electronic monitoring, online as well offline processes are used in procurement for goods.

2. Procurement Monitoring System

In the operation of e-systems, issues related to system users' true identity and distribution of false information may also arise. In the Korean e-procurement project, there have been cases of illegal bidding caused by information infringement or illegal price collusion due to sharing of public certificates. These cases were revealed in an audit conducted in 2009 by the Board of Audit and Inspection of Korea. The audit also found cases of 697 companies that won constructing contracts despite the fact that administrative measures or business suspension was imposed on them (in total, this represented 1,740 cases worth 285.3 billion won). These cases have only served to highlight the importance of monitoring and auditing systems.

To tackle the issue of more bids submitted from one computer for the same contract, in 2005, the PPS introduced measures electronically blocking multiple bids from the same IP address. In 2007, a reward program was introduced. Under the program, a person who reported an illegal electronic bid was rewarded two to ten million won if the court ruling confirmed illegality of the bid. By this, the system provided an additional incentive for companies to monitor each other's behaviour. Finally, bidder identifications using fingerprint recognition in combination with public certificates, and a system designed to automatically detect fraud or illegal behaviour through the analysis of information such as log-in record, IP address, bidding history, etc. (so-called illegal electronic bidding sign analysis system) were introduced.

Strengthened monitoring measures were also applied to companies with a higher likelihood of illegal bids. To prevent fraudulent behaviour of such companies, the PPS conducts regular screening (every three months) and signs of illegal electronic bids are given priority checks by the sign analysis system. Furthermore, if a company is found or is suspected of illegal bids as a result of system analysis, the Fair Trade Commission is asked

to examine it, or, if the suspicion is confirmed, strong punitive measures are taken.²⁷ Another issue is the existence of cases that unqualified companies were awarded a contract.²⁸ To prevent recurrence of such situations, the PPS decided to implement an automated blocking system against unqualified bidders, supported by regular monitoring of administrative information on companies involved in e-procurement system.

Apart from the above monitoring measures, e-Audit Information System (EAIS) is also a result of the effort to monitor the behaviour of companies using electronic procurement and electronic bidding systems to prevent the system abuse. EAIS, which covers the whole procurement process, was implemented by the Defence Acquisition Program Administration in 2008.

3. E-Procurement Legal Framework

To build electronic procurement system that is able to efficiently provide high level of e-services, corresponding legal and regulative framework must be prepared in advance with sufficient. In preparation of e-procurement legislative framework, it is not only important to consider existing legislature, but also the governance style and administrative culture of a particular country. To achieve legal stability of e-procurement including online bidding characterized by sharp conflict of interesting among its participants, certificate authentication services must exist and the system must incorporate measures securing authentication, integrity, confidentiality, and non-repudiation. Authentication and non-repudiation are especially important in e-Bidding, as they have the same effect as seals on abid.

Preparation of relevant legislation usually means amendments of existing laws as well as preparation of new ones. New laws and regulations are often needed because of specific features of e-commerce and electronic transactions, such as impersonality, impossibility of personal identity verification, difficulties in verification of validity of exchanged information, forgery, falsification, prohibition of access to transaction information, etc.

In Korea, the launch of the Korea Online E-procurement System (KONEPS) required the amendment of the State Contract Act along with its Enforcement Decree and Enforcement Regulations, amendment of the Enforcement Decree of the Government Procurement Act, and the Enforcement Decree of Local Finance Act (for detailed information on the amendments, refer to <Table 5-1>), which were completed prior to the launch of the system.

27. For example, in 2006, signs of illegal bids were detected in one percent of cases (i.e. 21,000 out of the total of 21,000,000 bids).

28. For example, there have been cases of companies winning contracts despite their business being suspended.

The law amendments contained provisions regulating general terms and conditions of the use of e-procurement service, user guidelines, and any necessary special provisions.

Table 5-1 | Amendments of Laws & Regulations Relevant to e-Procurement

Law (Regulation)	Content of Amendments
Enforcement Decree of Act on Contracts to which the State is a Party (Amended: July 2002 Effective: September 2002)	<ul style="list-style-type: none"> • Publish all invitations for bidders in KONEPS instead of official gazettes and newspapers, realizing a single procurement window (article 33) • Replace off-line bidding with online bidding through uplifting the legal status of KONEPS (article 39) • Publish notice of fraudulent bidders online (article 76), systemizing bidders' information via designated system • Report total contract record online via designated system (article 94) • Provision of more grounds on the use of designated system (KONEPS)(article 96)
Enforcement Decree of Government Procurement Act (Amended: July 2002 Effective : September 2002)	<ul style="list-style-type: none"> • Introducing more competition in price and quality allowing MAS (clause 2, article 7) • Requiring organizations make payment on their purchase however, on request, PPS may reimburse on their behalf (article 12)
Enforcement Rules on Act on Contracts to which the State is a Party (Amended: August 2002 Effective : September 2002)	<ul style="list-style-type: none"> • Provision of more grounds on the sharing of information on registered suppliers (article 15)
Enforcement Decree of Local Finance Act (Amended and effective: November 2002)	<ul style="list-style-type: none"> • Publish all invitations for bidders in KONEPS (article 70) • Publish notice of fraudulent bidders online (article 76), systemizing bidders' information via designated system

A key feature enabling the use of e-procurement was the use of e-Signature, which was enabled by the enactment of the Framework Act on Electronic Commerce and Digital Signature Act enacted in 1999 by the Ministry of Information and Communication. As e-Signature plays a major role in securing validity of transaction information and verification of the identity of suppliers and system users, e-Signature must have legal validity. Legal validity of e-Signature is also essential so that the legal validity of a bid submitted online and a bid submitted by the supplier without the use of electronic means are the same. As per the Framework Act, legal validity of e-Signature is defined in Article 6 stipulating that “an e-Signature authenticated by a certificate authority under Article 16 shall be deemed to be a legally effective signature or seal” and that “An e-Document with an e-Signature under Paragraph 1 shall be presumed not

to have been altered since it was signed by the creator.” Apart from that, the Framework Act also regulated the situations of errors and contract awarding notices.

Finally, the operation of e-Bidding, which is another crucial subsystem of KONEPS, required the preparation of new regulations. Consequently, Terms & Conditions for e-Bidder focusing on the rights and responsibilities of the PPS and bidders related to the use of e-Bidding, Terms and Conditions for e-Bidding Officers regulating rights and responsibilities of system operators and officers from procuring organizations including the PPS, Special Guidelines for e-Bidding on Public Construction, and Special Guidelines for e-Bidding on Commodity Purchase were adopted in 2000.

4. Lessons and Implications for Developing Countries

The establishment of the Korean e-procurement system was motivated by the need to manage an increasing number of items and companies involved in GP, as well as an effort to provide customer-oriented service. Focusing on the provision of diversity to procuring entities, the system also aimed at the enhancement of efficiency and transparency of public procurement.

In relation to the development of the system, Korea needed to solve the issue of the right to access information and implementation of a high quality monitoring system. The system needed to be able to prevent information abuse, hacking, and unauthorized access, supported by strengthened security measures such as electronic signature, users’ authentication, confirmation of time when documents were sent, blocking multiple bids from the same IP address, etc.. Korea represents a successful case of maintaining a high level of e-procurement security. As a result of the measures implemented, between the years 2003 and 2006, the occurrence of system failures was significantly reduced, and in 2006 the system operated with no failure.

As the Korean experience shows, the introduction of an e-procurement system must also be accompanied by the development of appropriate legislative and regulative framework covering topics such as contract awarding when electronic tendering is used, electronic bidding procedures, preparation of terms of agreements for electronic bidding participants, data backup procedures, guidelines for the situation of shutdown, etc.. As satisfactory level of security required complex measures, the need for operating guidelines to manage security measures also arose.

With regards to monitoring system, Korea has experienced cases of illegal bidding, information infringement, and illegal price collusion through the sharing of public certificates. To avoid such cases in the future, a system electronically blocking multiple

bids from the same computer and a reward program under which a person who reported an illegal bid was rewarded 2-10 million won were introduced. Furthermore, fingerprint recognition system for bidder identification and automatic fraud detection system were also implemented. Korea also experienced cases that non-qualified companies won bids although, for example, their business was suspended. This was possible as information among various organizations was not shared. Apart from the development of automated blocking system against unqualified bidders, an important lesson is that a good information system must be able to link and analyze information from various resources. It is not sufficient that information exists and is stored, it must also be processed and used otherwise cases like those in Korea will happen.

As already mentioned several times, Korea was very successful in the preparation and implementation of its e-procurement system. Korea e-procurement system has been repeatedly receiving awards for its quality and is often cited as the best case to benchmark domestically as well as internationally. One of the reasons for its success was that so-called Ubiquitous Electronic Public Procurement Project provided a common platform enabling communication and data sharing among all major e-information systems used in the public and private sectors. Through that, significant costs could be saved and efficiency was enhanced. Another important point was that the Korean e-procurement system was comprehensive and also involved other supplementary services such as web-call center, electronic notices, mobile electronic bidding system, mobile inspection of procured goods, mobile office, etc., making the system user-friendly. The Korean e-procurement success was also facilitated by the local culture of widespread use of modern technologies, high level of computer and ICT literacy (often referred to as “technologically savvy Koreans”), and well-developed Internet services (Korea has the highest penetration of high-speed Internet in the world) and IT infrastructure. Hence, for successful e-procurement implementation, developing countries should also take into consideration the level of infrastructure needed to actively operate the system, such as the penetration of Internet and usual speed of internet service, existence of electronic payment systems, the possibility to issue and receive electronic warranty, computer literacy of local inhabitants, or local culture which may give preference to personal contact in doing business over electronic form.

Implementation of the Korean e-procurement system was also accompanied by some difficulties. The major one was incomplete legal framework and underdeveloped security measures. Any country wishing to implement an e-procurement system should thus carefully consider what laws and regulations will be needed for the system operation, and prepare well-developed legislature sufficient amount of time in advance so that the new laws and regulations become effective when the e-procurement system starts operation. Another issue Korea experienced was that the system also included a number of systems

and functions which were developed but never used, leading to unnecessary expenses and waste of resources. Hence, in preparation of an e-procurement system, it is also important to consider what functions are really needed and will actually be used. The system design may thus for example incorporate information from future system user surveys. Related to that is the criticism of the Korean e-procurement system that it is too complex and contains too much information, so when particular information is needed, it is difficult to access. E-procurement system thus should be designed in a user-friendly way, with well-developed logical structure that is easy to understand for the common people. Critics also complain about the inconvenience caused by the necessity to repeatedly install security programs and go through a separate registration procedure each time that a new website is visited. Hence, e-procurement system should be designed in such a way that these redundancies and repetition are avoided or minimized. There is also criticism that the efficiency of the system is hindered by tacit factors such as local cultural practices, under which preference may still be given to personal contact.

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Chapter 6

GP Quality Management

1. GP Quality Management Tasks
2. Korean GP Quality Management Tools
3. Government Goods Management System
4. Lessons and Implications for Developing Countries

GP Quality Management

As the Korean economy developed and domestic as well as international environment started changing, the Korean public procurement practices could no longer fit without modifications. The beginning of the era of openness and increased competition meant a paradigm change that also affected GP field. Increasing demands were registered from the side of GP customers (i.e., procurement entities) in terms of the quality of procured goods or services, improved design, and a larger variety of procured items. However, procurement organizations' demands also increased in relation to the whole procurement process, as they started to require customized solutions, high quality of A/S service, supplementary information to facilitate purchasing decisions, consulting services, etc. As a result, shift from supplier-oriented procurement system towards customer-oriented system was necessary to satisfy procuring entities increasing needs.

This development was also accompanied by an increased demand on quality. Quality in this respect does not refer only to the quality of the procured items, but also to all supplementary services and purchasing values including e.g. timely delivery, swift reaction to changed needs, or supply procedures. In this chapter, the term 'quality' thus has a broader meaning, as it includes the whole procuring process. With quality defined in this manner, quality management involves a large variety of topics and its operation becomes a complex task. Bearing this in mind, the following text focuses on the most important aspects of the Korean experience during the drive for GP quality control and improvement, which are quality management tasks, quality management tools, and government goods management system.

1. GP Quality Management Tasks

Quality management tasks are implied by the main goal of the government procurement policy, which is timely and smooth procurement of goods or services with sufficient quality under the most advantageous conditions. The evaluation of the government procurement system and policy is closely related to the ability of the system to meet these goals. The role of quality management in GP is to ensure that procured goods and services are of desired quality and that the supply and after sales services and procurement systems meet the procuring entities' needs.

There are four main objectives that procurement quality management must meet to fulfil its role. First, the system must ensure that companies participating in GP have sufficient resources and capabilities to fulfil the contract. This can be done through PQ assessment, in site inspection, etc., and is closely related to tendering and contracting methods. Second, procured goods and services must be regularly checked and delivery inspection must be conducted by a specialized agency so that quality can be constantly monitored and swift correction can be carried out when deteriorating quality is registered. Third, the system must be able to efficiently analyze information regarding quality checks and the companies' performance including their ability to meet the required quality control criteria. Through these measures, recurrence of supply of lower quality goods and participation of companies who registered repeated problems with quality management or delivered goods of unsatisfactory quality in the past can be prevented. Finally, the system must be able to efficiently cooperate with testing and certification institutions so that independent quality assessment can be conducted and tests requiring special expertise (e.g. chemical laboratory testing) can be carried out.

2. Korean GP Quality Management Tools

A number of methods and tools used for quality management in procurement exist. This text focuses on the methods falling within Korea's experience, which are the establishment of the Quality Management Office, Total Service for Administrative Supplies, quality certification regime, company qualification checks and subcontracting prevention, quality inspection, special checks, contract fulfilment plan, procurement quality Sinmungo, education and PR, and Excellent Procured Goods accreditation regime.

2.1. Quality Management Office

Quality-oriented customer satisfaction survey conducted in 2006 revealed that procuring entities were on average more satisfied with the quality of procurement service provided by the PPS than with the quality of the procured items. While the satisfaction with procedural service was not significantly different from international level, satisfaction with the quality of procured goods was lower. Furthermore, as the inspections of delivered items were conducted by the procuring entities themselves, their objectivity and efficiency could not be fully secured. In addition, since feedback on quality control was often missing, the results of these inspections were not always reflected in the contractors' ability to participate at tenders and win contracts in the future, even in cases that the quality of items provided by the same contractor was low. The introduction of Multiple Award Schedule (MAS), under which SMEs with relatively weak quality management were also able to participate in the procurement market, even emphasized the need for systematic quality control.

This development led to the implementation of quality control system supervised by a central agency. The Quality Management Office, which was established in 2007, set the following three strategic goals: the establishment of a system for *ex-ante* quality control, the establishment of a system for *ex-post* quality control, and the enhancement of quality control capabilities. These goals were to be achieved by the fulfilment of ten implementation tasks (See <Table 6-1>). In relation to quality control *ex-ante*, the tasks involved direct operation of production confirmation regime, internal inspections of the PPS, introduction of a specialized agency inspection regime, and quality control in relation to the contract fulfilment. *Ex-post* quality control tasks included strengthened special quality checks of procured goods and the operation of *Sinmungo* (more information provided below). Finally, in terms of control capability enhancement, the Office set out to acquire KOLAS international accreditation, build a comprehensive quality certification network, and provide PR and training related to the quality control regime. The vision of the Quality Management Office to become “the Best Quality Control Specialty Agency Providing the Best Value Quality Service to Customers” is in line with these goals and also corresponds to the changes in the procurement market caused by the shift from supplier-oriented to customer-oriented system, where diverse best value criteria play an important role.

Table 6-1 | Mission, Vision, and Goals of Quality Management Office

Mission	Providing the best quality service by building a systematic quality control system		
Vision	"The best quality control specialty agency" providing the best value quality service for customers		
Strategic Goals	Building an <i>ex-ante</i> quality control system	Building an <i>ex-post</i> quality control system	Strengthening quality control capabilities
Implementation Tasks	<ul style="list-style-type: none"> • Directly operating a production confirmation regime • Advancing internal inspections of the Public Procurement Service • Introducing a specialty agency inspection regime • Quality control on the basis of the contract fulfillment plan 	<ul style="list-style-type: none"> • Strengthening special quality checks on procurement goods • Operating the procurement quality control Sinmungo 	<ul style="list-style-type: none"> • Acquiring international accreditation (KOLAS accreditation) fa test agency • Building a comprehensive quality certification network • Education and PR of the quality control regime

2.2. Total Service for Administrative Supplies

An important step in GP quality improvement was the implementation of the Total Service for Administration Supplies, the main reason for the introduction of which was growing dissatisfaction of procuring organizations with customer service. To respond to the changing needs, the Service had as its objective to increase procuring organizations' level of satisfaction with procurement of administrative goods and related services. The Service, which was implemented in 2004, involved issues such as A/S of office supplies, public opinion survey, survey of service satisfaction level, supply warehouse system, etc.

The operation of the Service resulted in procurement system changes, among which the replacement of procured goods, A/S, and quality opinion survey introduction were the major ones. Although the selection of target organizations for the new system was originally limited to organizations under the central supply warehouse system, it was later expanded to cover the organizations in the whole country.

To improve quality control and A/S service for office equipment (e.g. furniture, filings, etc.), an A/S group was formed. The group's main responsibility was performance of A/S according to prearranged schedule. To facilitate its operation, the group consisted of six people representing the central warehouse system, the Korea Metal Furniture Industry Cooperative, and the Korea Wood Furniture Industry Cooperative.

With regards to supply replacement, the Service brought several changes. Under the new system, office supplies in bad condition and expired goods could be replaced with new ones free of charge, items owned in excess could be replaced with different types of goods, and low quality goods could be replaced with goods of better quality. Any existing price difference was reconciled by the modification of quantity of the newly provided items.

Finally, other types of services, such as quality opinion surveys, special quick service for the procurement of goods in the situation of urgency, mobile office and help desk, and satisfaction surveys were also implemented.

2.3. Quality Certification Regime

The Quality Certification Regime for Administrative Goods (QCRA) was introduced to provide an incentive for suppliers to voluntarily improve the quality of supplied goods, as quality improvement is difficult to achieve without suppliers' participation. The implementation of the Regime was accompanied by the enactment of the Enforcement Regulations on the Procurement Goods Quality Certification in 2001.

Under the Regime, goods from companies that passed comprehensive quality evaluation were exempt from delivery inspection for a given period of time (one year from the date the quality certification was issued). The evaluation is conducted based on quality evaluation criteria involving the company's financial status, factory (plant) assessment, quality inspection of the PPS, technology, etc. To be eligible to obtain a quality certification, a company must receive on average a minimum of 75 points. After the end of certification period, a company can re-apply for certification and the effective period is extended by one year, unless reasons for the company's disqualification exist. As quality certification involves expenses related to consulting, PR, training, etc., the certification service is provided for a fee of one to five million won based on the annual contract amount of the commodity to be certified.

Quality certificates are issued by the Quality Certification Evaluation Committee consisting of four subcommittees for different types of supplies (stationery and paper; equipment and furniture; electric and electronic communication devices; others). In total, the Committee has nine members, three of whom are appointed from internal committees; the remaining six members are appointed from the outside. One of the Committee members is the chief of the central supply warehouse system, who also acts as the Committee chairman.

2.4. Company Qualification Checks and Subcontracting

Another issue the quality improvement system needed to solve was subcontracting and tender participation of so-called “paper companies.” As until 2008, it was possible to register as an eligible bidder a small company without a factory registration certificate, companies without their own production facilities submitted their bids. If such companies were awarded a contract, the goods they supplied were either imported (in many cases from developing countries) or delivered by subcontractors. Since this practice prevented other, better qualified companies from winning the contracts and resulted in poor quality of procured goods, the Quality Management Office introduced the Regime of Checking the Direct Production of Small Manufacturers. The Regime meant that registration of a manufacturer was only possible after a site visit verifying production facilities’ existence. At the same time, all companies already registered as procurement manufacturers were checked. As a result of the strengthened measures, 46% of companies checked by the end of October 2008 were found unqualified, 50 companies needed to change their status from registered manufacturer to a supplier, the registration was cancelled in 24 cases, and in another 18 cases adjustments needed to be made. There were also 25 cases of registration or renewal application rejection.

2.5. Quality Inspection

One of the ways to secure satisfactory quality of procured goods is frequent quality inspections. These can be either conducted internally by the procuring entity or the PPS, or the inspection service can be provided by specialized agencies. This happens especially in cases that special equipment or expertise is needed to test the product quality.

The PPS operates its own Product Quality Test Laboratory, which originally focused on the inspection of garments and office supplies. Since available manpower and equipment are limited, the PPS concentrates on the inspection of goods where problems with quality are likely to occur or have frequently occurred in the past. At the same time, specialized agencies are hired in cases that the inspection cannot be done by internal means.

In 2008, the list of items for inspection was expanded from 54 to 210 products, the suppliers of which were small companies. After quality inspection was conducted, companies that were able to keep high quality standard of their supply in 12 deliveries without failure were exempt from further inspection checks. As a result of exemptions, by the end of September 2008 procurement companies’ cost reduction amounted to 808.288 million won.

About 70% of goods needed to undergo quality tests were conducted by a specialized agency. Since 2005, the PPS was using a certified test agency in accordance with The Inspection

Agency Regime. Under the Regime, the PPS was in charge of target goods selection, tender notice, the disclosure of inspection fee on the contract, etc., while the inspection agency collected samples to test. As when the system is organized like this, it is not certain whether the samples submitted by a supplier are representative of the actual delivered goods or not, the Regime was later abolished and since 2009 Specialized Inspection Agency Regime has been in operation. Under the new system, the standard procedure is that quality inspections are conducted by a specialized agency and inspection by procuring agency is only permitted in special cases. Furthermore, unlike before, samples are newly collected by the inspection agency straight from a manufacturing plant or delivery site. To minimize financial effect on procuring entity, quality inspection expenses are born by the supplier.

2.6. Special Checks

With the expansion of MAS regime, increased diversity of procured goods, and higher number of supplier companies, quality control has become more demanding. In response to this development special checks, as a quality management tool, have been expanded. Currently, special checks are performed in relation to 100 products including basic construction materials, multiple supply items, and good procured goods. Apart from special checks, good procured goods also undergo planned inspections.

The sanctions for failing a special check are restriction on the contractors' allocation in relation to the number of failures, and the exclusion from the contract for one term. In addition, a company that fails a special check is obligated to submit The Plan on the Annual Comprehensive Quality Management along with three or more random checks. If the failure to pass special checks repeats, the company is sanctioned by reporting the failure on the G2B website and dissemination of the quality check results among companies within the industry. At the same time, positive incentives are also offered. For example, ten selected companies with outstanding quality management are awarded good quality management awards.

2.7. Contract Fulfilment Plan

Special conditions of GP contracts prescribe submission of a Plan to Fulfil the Contract on Manufactured Commodities, without which procurement contract cannot be concluded. The submission of the Plan makes it possible to check whether the manufacturing process is conducted according to the Plan and whether the quality management corresponds to the content of the Plan or not. Typically, major manufacturing processes, lead time, raw material origin, the proportion of outsourcing, etc. are checked. Nevertheless, as the Quality Management Agency, which conducts quality inspections, possess limited manpower and resources, it is not possible to perform site checks for all manufacturing contracts.

Consequently, the companies whose quality management should be checked are selected and prioritized based on the contract importance, contractor's reliability and previous supply history, etc.

2.8. Procurement Quality Sinmungo

Procurement Quality Sinmungo is a system enabling anonymous reporting of low quality products, the quality of which differs from the original contract. The main objective of the system is to facilitate prompt and convenient handling of supplies of defective products. The procedures and regulations related to delivery of defective goods are specified in the Regulations on the Post Quality Management of Procured Goods, which also include defect recurrence prevention plans and follow-up measures.

The introduction of Procurement Quality Sinmungo had immediate positive effects. For example, simple A/S requests that had not been dealt with for a significant period of time were promptly processed, after similar cases were reported to Sinmungo. Sinmungo also plays an important role in prevention of defect recurrence, since it receives quality improvement proposals and information on the types of defects that occur. These are later analyzed and the results of the analyses are communicated to the purchasing department. Furthermore, procuring agencies and the PPS departments receive the reports on cases related to defect occurrence and their follow-up.

2.9. Education

Efficient quality management system in GP must involve both the procuring entities and procurement agencies, as well as supplier companies. Mutual cooperation and understanding are necessary prerequisites to quality improvement of supplied items. To secure desirable quality of procured goods, the procurer uses various kinds of procurement methods and regimes, including inspections and special checks. At the same time, contractor is responsible for the delivery of non-defective items in accordance with the contract. Optimal operation of quality management thus requires constant effort of all involved parties.

Education plays an important role in facilitation of mutual cooperation between GP suppliers and procuring entities (agencies). On one hand, suppliers must be aware of and understand well the procurer's policies in quality management methods to be able to secure supply of quality goods meeting procurer's requirements. On the other hand, procuring entities' staff must undergo constant education and training so that they can implement quality management policies and procedures with the desired effect. To that end, the Quality Management Agency provides quality management education within professional

procurement education, and quality management related policies are part of each education course of all public procurement officials.

2.10. Excellent Procured Goods

First introduced in 1996, Excellent Government Procured Product Regime had as its main objective the enhancement of the quality of procured goods. Apart from that, the system also sought to provide sales support to SMEs and venture companies possessing special technology and to help enforce various government policies (e.g. environment, technology, energy, resource recycling, etc.) via GP services. In 2000, the operation of the Regime was facilitated by the amendment of Article 18 of the Enforcement Decree of the Government Procurement Act, and the enactment of Regulations of Designating and Managing Excellent Procured Goods.

Excellent Government Procured Product is an accreditation system, which provides excellent product designation to SMEs or venture companies (large companies are not eligible to apply for the accreditation). Through the excellent product accreditation, companies with new technology or quality certified products, or companies utilizing patents and utility models, can gain advantage against their competitors. The excellent procured product designation was accompanied by the operation of price calculation and disclosure regime helping to correctly price newly developed products. In addition, to expand the sales opportunities of good procurement companies and provide them with marketing support, the Exclusive Excellent Product Shopping Mall was established within comprehensive shopping malls.

The effective period of excellent procured commodity designation is three years, with the possibility of extension by another year if given criteria are met. Through registration in a comprehensive shopping mall and the Exclusive Excellent Product Shopping Mall, excellent product receives a significant PR benefit, including the opportunity of overseas sales, as product catalogues in English are distributed to companies and embassies.

The Excellent Government Procured Product designation is another example of procurement measures putting increased emphasis on quality and design against price. In line with the government policy, the system mainly focuses on finding products using new or environmentally-friendly technologies. The effect of the excellent procured product system was enormous, as between 1996, when the system was introduced, and 2007, the revenue earned due to the system operation increased by 11,700%.

3. Government Goods Management System

An issue strongly related to GP quality management is the method which goods in possession of the government are managed. If the system is well developed, public procurement can better reflect the procuring entities' needs and respond to their requirements more efficiently. On the other hand, if the government goods management is neglected, a number of negative effects such as the procurement of unnecessary items, storage of items that are never used, procurement of items with different characteristics that needed, excessive logistics expenses, etc., appear.

Regarding the content of the term, management of government goods refers to “the control technology through which the nation acquires and owns the items needed for the nation to provide administrative services, execute projects, and enhance the productivity of administration as a result of efficient processing.” Specifically, government goods management (GGM) consists of acquisition, storage, usage, disposal, and accounting for items within the responsibility of the Control Conversion Department. The principles of government goods management are formulated in the Government Goods Management Act, which was enacted in 1962 and substantially amended in 1972.²⁹ Based on the Act, GGM relates to movable items either possessed by the country or kept for the country's use, with cash, securities, and national property excluded. GGM is conducted by the Department of Government Goods Management, which is in charge of the overall coordination of government goods management related functions, including the management of the disposal of disused items, GG recycling, promotion of RFID service, inventory investigation and item supply management, inspections system, and other systems related to the management of items in possession of government agencies.

3.1. Basic Elements of GGM

The following text discusses basic elements of GGM, which are full number control, longevity, unused article disposal, and special case items. GGM also includes management of objects of art, leased items, and computer software; however, due to the limited scope of this paper, for more detailed information we refer the reader to the reference list provided at the end of the paper.

29. Before the enactment of the Government Goods Management Act in 1962, the principles of government goods management were included in The Commodity Accounting Rules from 1889 and The Commodity Accounting Regulations from 1907.

3.1.1. Full Number Control

When an organization possesses a given item in the quantity needed for the organization to efficiently perform its goal, the organization possesses the full number of the item. Until 1999, the full number of items managed by the Supply Administration (8 types of items such as electronic copiers, air conditioners, motorcycles, refrigerators, fan heaters, air cleaners, washers, etc.) and the full number of items managed by central government agencies (30 types) were controlled separately. In t, each government agency also performed autonomous full number control, with the exception of the above mentioned items within the responsibility of the Supply Administration.

In 2000, full number standards were specified for selected types of items with the value exceeding one million won (since 2005, no less than two million won). Full numbers standards were based on the conditions such as capacity, function, work characteristics, number of departments, workspace area, etc. of each organization. Furthermore, in accordance with the Full Number Appropriation Standards of Major Commodities, the full number of each item was autonomously determined by each agency. However, in a situation wherethe government goods management officer finds that the full number is in conflict with Government Goods Management Act provisions, it is reviewed by the head of a governing agency.

3.1.2. Longevity

Longevity refers to the period of economic use of an item, over which the function of the item can be maintained without significant repair expenses. For selected items, the value of which exceeds a given amount,³⁰ longevity is set centrally by the PPS. However, if an agency wishes to apply its own longevity periods, after discussion with the PPS, the agency can internally set its own standards. Due to the general drive for efficiency, if an item can continue to be used without excessive maintenance or repair cost even after the expiry of its longevity period, the item is not replaced. Similarly, there is a general effort towards the reduction of the storage of unused items.

3.1.3. Unused Article Disposal

Disposal of unused articles has been regulated since 1982, when the guideline for the management of recyclable items, unused articles, and non-recyclable item salvage value was enacted. Based on the guideline, parts of unused articles that can be still utilized are to be recycled, and non-recyclable items are to be disposed of without unnecessary delay

30. The number of items for which longevity is defined keeps increasing. In 1981, when longevity was first defined, it was specified for 180 items. By 1999, the number had risen to 244, and in 2007 longevity was defined for 1,044 items.

with the collection of their salvage-value. An additional provision from 2000 also allows the heads of central government agencies to declare that an item is of no further use, after the consideration of the longevity of the item and its potential repair expense. Furthermore, if an item with the acquisition value higher than one million won is classified as waste, the attachment of relevant material is necessary. In 2005, the guideline on the disposal of articles was amended with stronger emphasis put on recycling and waste reduction.

3.1.4. Special Case Items

Each government is also in possession of items that cannot be managed by the use of standardized methods. Typically, such items involve computer software or leased items. In Korea, efficient management of software used by national organizations is regulated by the Software Government Goods Management Operation Instructions enacted in 2001. Furthermore, in order to secure systematic control including the possession status, Regulations on Software Control and Regulations on the Control of Leased Items were introduced by the PPS in 2007. As a result of systematized approach and more thorough control including follow-up measures (e.g. software collection when computers are disposed of, etc.), budget reduction was achieved.

3.2. GGM Efficiency Enhancement

To secure optimal operation of the system and to keep up with the changes in economic environment, GGM system is repeatedly modified and brought up-to date. The system also employs a number of measures aimed at the increase in the system efficiency and improvement of managerial techniques is in use. In this part of the paper, comprehensive evaluation program, GGM inspections, staff training, digitalization and product information system, and the development of new commodity classification system are going to be discussed.

3.2.1 Comprehensive GGM Evaluation Program

The comprehensive GGM evaluation program (full name “Comprehensive Individual Agency Evaluation on Government Goods Management”) was introduced by the PPS to prevent the occurrence of government goods mismanagement and to help better target GGM system inspections. The evaluation program was implemented in 2005 through the National Finance Information System (NFIS) after discussions of the PPS with the Ministry of Public Administration and Security and the Ministry of Strategy and Finance. Through the system, government goods management performance of central government agencies and of over 2,000 public entities is regularly evaluated. The evaluation focuses on seven categories including 18 evaluation indices involving for example inventory inspection, plan

of government management goods, annual government goods management closing, etc. Based on the evaluation results, outstanding public entities and officials are awarded, while underperforming agencies are subject to strengthened inspections and control.

3.2.2. GGM Inspections

Although the efficiency of GGM has been increasing, the cases of inefficient GGM such as the use of inappropriate management plans, inadequate inventory inspections, delayed disposal, and disuse of procured items, etc. repeatedly occur. Consequently, in relation to their type, size, the value of items in their possession, and the result of last inspection, GGMS agencies undergo two types of regular inspections - periodic inspections and theme inspections. While periodic inspections are performed in essentially the same way for all agencies, theme inspections focus on each agency's specific service area. Although documentary inspections have been conducted since 1996, in 2006 online inspections targeted at agencies with unsatisfactory performances and the value of items in possession not exceeding five billion won were also introduced. Government goods management inspections fall within the area of responsibility of the Department of Government Goods Management, which also performs other GGM related functions.

Agencies to be inspected are selected based on the above mentioned criteria, along with the results of comprehensive evaluation. If an agency passes comprehensive evaluation with good results, the agency is exempt from inspection for a given period of time. Recently, the nature of the inspection has changed from comment-oriented to the provision of guidance and consulting with main emphasis put on guidance to provide agencies with motivation to actively pursue efficient GGM and properly conduct tasks related to the registration, utilization, and disuse of the items they possess.

As any inspection is costly, the benefits of an inspection must outweigh the costs incurred in relation to it. Since their introduction, GGM system inspections have brought considerable results. For example, when five local governments were inspected in 2000, 117 cases of inappropriate management of GG were discovered.

3.2.3. GGM Training

Training on good management of government goods, which is provided by the PPS as the central training body for GGM in the public sector, covers various areas related to good management, such as managerial techniques, related laws and regulations, budgeting, selected accounting topics true, etc. Reference material containing experience of other countries and cases to benchmark was provided by a comparative analysis of government goods management systems in the USA, Canada, GB, Germany, Japan, and Korea published in 2003. Later, the PPS also published several training materials and provided trainings on

the changes in GGM system pursuant to the introduction of the National Accounting and Financial Information System. In addition, in 2008 an electronic manual on GGM processes was published on the PPS website.

3.2.4. Digitalization and Intelligent Product Information System

To facilitate efficient and smooth operation of GGMS, an electronic system for management of government assets, which was distributed to all public agencies, was developed. The system, which comprised of a variety of functions such as asset management accounting techniques, multiple communication systems, etc., also allowed for online reporting of GGM status to the Board of Audit and Inspection in electronic form. Currently, Comprehensive Government Goods Management System operating under NAFIS (National Finance Information System) is in operation. Since 2006, the functions of Fiscal Information Management System and NAFIS have been integrated under Digital Budgeting and Accounting System, also called “dBrain.” As a comprehensive system, dBrain currently involves all government finance processes, such as budgeting, accounting, performance assessment, etc. This development has also been accompanied by the shift from accounting-oriented to project-oriented asset management style.

An important aspect of the digitalization drive was also the introduction of the Radio Frequency Identification (RFID) technology in 2004. The technology significantly facilitated logistics processes via the reduction of simple and repetitive work and a decrease in processing time. It also made it possible to monitor inventory movement more accurately, and enabled provision of more accurate statistical data regarding government assets. As a result, the RFID led to cost reduction and improved the accuracy of GGM. For example, due to the RFID technology, work productivity of inventory inspections increased up to 6.5 times, and the work time needed to perform certain tasks was reduced by up to 86%. In 2007, the time reduction for 23 agencies using the system was 1,373 days in total.

3.2.5. Intelligent Product Information System

The development of intelligent product information system (IPIS) was brought only by the need to design a system that would be able to link all other major information systems, including those used by public agencies and supplier companies. While electronic information exchange based on mutually linkable electronic catalogues among various public e-systems exists, a number of different electronic catalogues are in use in B2B in the private sector, making it difficult to smoothly perform e-commerce functions involving both sectors. Furthermore, flexible computerized system allowing for sharing of commodity related information also turned out to be necessary to fully realize improved efficiency benefits of e-commerce and new commodity listing system.

Intelligent product information system meant the addition to the development of uniform commodity classification system described below and was closely related to the digitalization of government goods management along with the creation of comprehensive e-procurement system. Following the policy according to which electronic catalogues used in the private sector should be used in their current form, the PPS decided to develop an ontology-based intelligent product information system allowing for mutual linkages of existing catalogues, rather than devise another standardized information sharing system that would exist in parallel to others.

The development of a basic form of the system was finalized at the end of 2004, with the service operation beginning in February 2005. In 2005, the system was also patented. In its initial form, the system included a standard ontology model, a standard database, an ontology control system, and an ontology reference system, to which an ontology-based commodity list generation support system, an ontology-based system supporting the mapping and cataloguing of product information between B2B and G2B, and a system establishing the link between product information system and G2B shopping mall were added in December 2005. In the third stage, ontology-based system for the search of product information in the comprehensive shopping mall, system allowing for automatic registration of product property information, and product image registration system were built in December 2006.

As apparent, the system placed emphasis on the provision of a unified platform allowing for convenient information sharing among various existing electronic catalogues and systems. As a result of the system implementation, the reliability and efficiency of procurement administration improved significantly. Tasks, which have been previously handled manually, were automated, leading to reduction of mistakes and processing time. The system introduction also meant reduction of the costs of private and public sectors related to the redundancy of product code systems, reduction of transaction costs, and realization of synergy effect due to efficient use of existing electronic GGM and e-procurement systems. The unified system also made it possible to develop various procurement services based on swift information exchange requiring one information cataloguing and information sharing platform. Finally, IPIS increased Korea's international recognition, as it has been repeatedly cited as a successful example of procurement computerization and the best practice to benchmark.

3.2.6. Commodity Classification System

The main aim of commodity list is the classification and identification of commodities according to selected standards. Based on the list and classification criteria, commodities are assigned a unique code facilitating their cataloguing, purchase, management, budgeting, statistical control, etc. From the viewpoint of procurement system, commodity list is essential to provide a common platform and content to perform procuring service including

its procedural aspects such as tendering notices, bidding, contract conclusion, delivery, payment, etc.

In Korea, the new commodity list was created in response to the growing variety of government assets, and their increasing scale and volume of transactions in which they were involved, resulting in difficulties and inefficiencies of GGM. Furthermore, as the existing regime was based on the framework suitable for military purposes (the framework of the Military Supply Division of the Ministry of National Defence), it was necessary to devise a system better suited for the needs of public sector and privately possessed commodities.

The development and introduction of a new commodity list was based on a study of needs of government entities along with the examination of the US federal government and Department of Defence (DoD) classification regimes. In the development of a single commodity classification, the main goal of the PPS was the implementation of electronic commerce; with less emphasis put on GGM. The new commodity list, which was gradually developed between 1988 and 1995, with implementation in 2001, was based on the United Nations Standard Productions & Services Code (UNSPSC code) along with the US FSC classification system. The advantage of the use of FSC system was its compatibility with international classifications (e.g. NATO, etc.) and suitability to electronic commerce. While the UNSPSC provided the unified classification standard effective since 2006, the FSC was only used as reference classification. Providing a uniform classification platform, the new classification system allowed for easy information flow among the information systems of the Ministry of Finance and Economy, the city and province administration organizations, digital budget and accounting of the Ministry of Strategy and Finance, and other education, administration and finance related systems (for details on the system functioning see <Table 6-2>).

Table 6-2 | Organizational System of Commodity List Numbers

Category	Commodity Classification Number				Commodity Identification Number
	Large Classification	Middle Classification	Small Classification	Detailed Classification	
Classification Name	Transport devices	Automobiles	Passenger cars and buses	Regular passenger cars	Unmeaningful serial number
Classification Number	25	10	15	03	

The catalog is organized into 58 large classifications, 327 middle classifications, 1,466 small classifications, and 10,263 detailed classifications

4. Lessons and Implications for Developing Countries

As Korea has been repeatedly experiencing problems with deterioration of the quality of procured items to a large extent due to the use of procurement methods based on the selection of the proposal with the lowest price, significant amount of effort has been recently made to promote quality in GP. Similarly to Korea, any country attempting to develop GP quality management system is likely to follow the same developmental path from low cost procurement towards procurement of quality accompanied by increased complexity of procurement process. It can be expected that such a country is going to face the same question as Korea – how to secure quality in GP with increasing number of procured items and supplier companies. Some lessons or implications that can be drawn from Korean experience as detailed in previous text are briefly summarized below.

The Korean experience has shown that to practice efficient GP quality control, a comprehensive quality management system involving the whole procurement process must exist. That means that quality should also be defined in terms of the related services, such as A/S, delivery, provision of information for purchase decisions, etc. An integral part of quality management system is also government goods management, without which it is difficult to target items to procure and inefficiencies such as excessive amount of items in stock, procurement of items that are not needed, procurement of items in unsuitable quantity, or unnecessary logistics expense are likely to occur.

Among quality management tools in use in Korea, check, inspections, quality certification regime, and existence of Sinnungo play an important role. When quality checks and inspections are conducted, the system must make sure that any samples are representative of the delivered goods. This can be done through sample collection directly from manufacturing plants or delivery sites. If situation requires, checks and inspections should be conducted by specialized agencies that possess necessary equipment and expertise to secure inspection and testing objectivity as well as reliability. However, mere operation of checks and inspection system cannot reliably secure quality improvement. The existence of such system must be accompanied by information analyses and feedback, so that recurrence of defects and repeated tender participation of non-qualified companies with problematic record can be prevented. In principle, results of all quality checks and inspections should be reflected in future processes in some form. For example, if quality problems in deliveries from the same supplier are repeatedly registered, the supplier should not be able to easily participate at tender in future and checks on the goods of the same supplier should be strengthened. On one hand, exemptions from inspections for a given period of time in case of companies with excellent record of uninterrupted delivery of high quality goods can serve as an important incentive towards quality management enhancement on the supplier's

side. On the other hand, disincentive for supplier companies to neglect quality management can be public dissemination of the inspection results among companies within the industry and procurement agencies. However, through public dissemination of positive results, good quality management companies can obtain significant marketing and advertising benefit. In this respect, procurement quality Sinnungo plays an important role in the Korean quality management system, as through its existence, procuring entities can be easily and swiftly informed of problematic suppliers. At the same time, Sinnungo also collects quality management enhancement ideas, thus promoting further system development. The fact that after Sinnungo was introduced an immediate positive effect was registered proves effectiveness of its use.

An interesting quality promotion tool is the existence of Excellent Procured Goods system, providing SMEs or venture companies with Excellent Product Accreditation. When obtained, this accreditation gives companies marketing and advertising benefit over their competitors and also enables them to register their goods in Exclusive Excellent Shopping Mall, by which they can gain access to overseas markets. For SMEs and venture companies these are major benefits, as smaller sized companies often suffer from low capitalization and underdeveloped selling channels.

Korea also needed to solve the issue of outsourcing and paper companies without own production facilities participating at tenders. On site check and inspections showed to be an efficient tool to prevent occurrence of such practices. Korea has also issued regulations to handle the cases of special items, such as leased goods or computer software. Here, practice that is often not remembered is the removal of usable software in case of computer disposal.

It is obvious, that due to increasing complexity of GP processes, GP quality management must be supported by the use of new technologies such as RFID and e-procurement systems. Korea's major achievement has been the development of a uniform computerized procurement platform that is able to link all major public and private procurement systems. Through that, costs related to the operation of different systems and their redundancies could be saved in the public as well as private sector. Korea has also learnt that the introduction of such a system must be supported by uniform commodity classification system if the synergy effect of information sharing is to be achieved. However, commodity classification system must be suitable for its purpose, which essentially means that such a system must be developed after careful consideration of the needs of economic operators that will be using it, rather than blindly adopting already existing system from a different field or country. In addition, it is also important that the classification system can be used for e-commerce. In this respect, the Korean Intelligent Product Information System has received high international recognition and is often cited as the best case to benchmark.

2012 Modularization of Korea's Development Experience
Korean Government Procurement Experience

Chapter 7

Development of Korean Procurement Methods

1. Contracting Regimes
2. Multiple Award Schedule
3. Paradigm Shift towards Customer-Oriented Service
4. Lessons and Implications for Developing Countries

Development of Korean Procurement Methods

Procurement methods are one of the key elements of a country's procurement system. It is often the case that the choice of appropriate procurement method and the quality with which the method is defined play decisive role in the achievement of GP goals. It is thus essential that procurement methods are thoroughly legally grounded and well aligned with the overall economic-political environment of the country. Furthermore, the methods available to the procuring agencies should reflect the procuring entities' needs, and they should also respond to the changes in domestic as well as the international environment.

This chapter focuses on the development of procurement and contracting methods in Korea. As such, it is closely related to Chapter 2 of this paper which provided a brief overview of procurement methods relevant to this paper. The whole chapter is divided into three main parts. The first one focuses on the development of the Korean contracting systems, also mentioning some tendering and contracting regimes characterized in Chapter 2. The second part provides detailed description of Multiple Award Schedule and its basic elements, while in the last part key aspects of customer-oriented procurement service are described.

1. Contracting Regimes

This subchapter deals with development of the Korean contracting regimes along with the qualification evaluation system. As such, it mainly focuses on the development of contracting methods in time along with the reasons for their implementation or abolishing, without repeating the analysis of their advantages and disadvantages already provided in Chapter 2. In cases that such details were already provided, they are only mentioned again if it is essential for the understanding of the text.

1.1. Development of Korean Contracting Regimes

In accordance with the National Finance Act, the bidding methods possible to use in GP were open (competitive) tendering, selective (competitive) tendering, and direct contracting. At the same time, total amount contract was stipulated as the basic contracting methods, with unit price contract possible to use under specific circumstances. Later, to simplify the delivery procedure and increase convenience for procuring entities, the Third Party Unit Price Contract System was introduced in 1976.

The enactment of the Budget and Accounts Act expanded the scope of available contracting methods. It newly introduced the Expected Quantity Competitive Tendering Regime, under which the contract is divided into several parts delivered by different suppliers. This method is often used in situations that the scope, variety or large volume of procured goods make it difficult for the procured items to be delivered by one contractor. Although the regime represents a special case of open (competitive) tendering, qualification review is not conducted. Regarding the pricing method, based on the quantity procured, expected unit price is determined. The regime specifically targeted situations that a large volume of the same item which would be difficult to produce with one supplier's capacity needed to be procured, or the case that a large quantity of the same items impossible or difficult to buy with one person's capability needed to be sold. Consequently, the regime was typically used for the procurement of goods such as iron bars, asphalt, cement, or concrete, etc.

As a result of the effort towards continuous contracting methods improvement, Restricted Competitive Tendering Regime was introduced by the amendment of the Enforcement Decree of the Budget and Accounts Act in 1977. The reason for the introduction of the regime was the attempt to develop a contracting method combining the advantages of open (competitive) tendering and selective (competitive) tendering such as the contract performance stability, quality of procured items, and the possibility to receive special treatment (customization).

The Enforcement Decree of the Act on Contracts to Which the State Is a Party allowed for the use of the Negotiated Contract Regime. The Enforcement Decree of the Act stipulated that the method of contract via negotiation can be used in situations of urgency, contractual specialty, or for national security purposes, while the procedures and standards of contract conclusion were to be determined by the head of a central government agency. The introduction of the regime was accompanied by the adoption of The Negotiated Contract Conclusion Procedure prescribing comprehensive evaluation of a bidder based on the price, performance, delivery time, and contract fulfilment capability. The purpose of the existence of different criteria was to solve the problem of procured items quality deterioration related to the lowest price regime.

However, despite the existence of regulations regarding contract conclusion procedures, detailed execution standards and procedure descriptions were missing. This led to excessive discretion exercised in the application of this contracting method by procurement officers or to its abuse. In order to correct the situation, studies on domestic and overseas cases related to the use of negotiated contract method were conducted and the PPS Directive on the Negotiated Contract Conclusion Standard was enacted 2000. Based on the Standard, contract proposals and bidding forms including the project specification and price were to be separately prepared by the person in charge of the negotiating process. In accordance with the Standard, negotiated tendering targeted expensive advanced precision system equipment, software development, and the ICT (Internet and Computer Technologies) related projects.

In accordance with legal provisions, in contract via negotiations proposal evaluation was to be conducted. Evaluation methods differed for services and equipment. For example, in evaluation of software development, the weight of price was 30% and technology 70%. However, when equipment was evaluated, price as well as technology evaluation were both assigned 50%. The bidder with the highest amount of points was awarded the contract. Modification of weights of different criteria meant that by the use of the method, not only low price, but also quality could be achieved. Furthermore, negotiating with individual companies also represented a relatively reliable means to prevent collusion among them.

1.2. Qualification Evaluation System

A crucial aspect of many tendering methods is qualification evaluation system. By the choice of criteria and assignment of weights the result of the tender can be effectively manipulated, or if the criteria and their assessment are vague, tendering methods cannot secure the selection of the best proposal (bidder). Qualification evaluation system is a relatively new element of the Korean GP system, as it was only introduced in 1995 (effective since January, 1997) in response to Korea's signing of the WTO GPA, according to which the use of qualification evaluation is obligatory.

There are several reasons that qualification evaluation exists. The system was originally conceived to provide counter-balance against the lowest price system, in which low pricing made it possible that the contract was awarded to a contractor lacking fulfilment capability, excessive price competition resulted in quality deterioration to such an extent that fatal incident occurred due to poor construction quality, or cases of subcontracting often happened. Apart from securing quality and increasing contract fulfilment reliability, the system provides tenderers with incentives to improve their management and operations, thus also strengthening their external competitiveness. However, the method has recently

received criticism that despite qualification evaluation the best bidder is not selected due to the ease of qualification evaluation standards.³¹

When evaluating contract fulfilment capability, detailed evaluation criteria are determined in compliance with standards issued by the Ministry of Strategy and Finance. If a special nature of procured goods requires, evaluation criteria can be directly determined by the head of a central government agency via discussion with the Minister of Strategy and Finance. After that, successful bidder is selected in accordance with “The Public Procurement Service Detailed Standards for Evaluating the Qualifications of Commodity Procurement” separately prepared for that particular bidding case. In qualification evaluation, various criteria such as bidder’s contract fulfilment history, technical capability, financial status, suitability of material, labour costs, quality and price of previous supplies, etc. are considered.

Based on Korean legal framework, qualification evaluation is prescribed for the procurement of commodities with the estimated price equal to or exceeding a notified amount when the tender is conducted via competitive tendering. However, the National Contract Decree also specifies cases that a bidder can win a commodity or service contract the value of which is no lower than the notified amount without qualification evaluation.³²

2. Multiple Award Schedule

The Multiple Award Schedule (MAS) is an advanced procurement method operated in the USA, Canada, Britain, and other countries in the world, typically used to procure items with high procurement frequency. In Korea, the MAS was introduced to overcome difficulties such as low product diversity or procured items quality deterioration, usually connected with contracting regimes putting emphasis on price. The MAS was also implemented to facilitate procurement of local organizations after decentralization of the Korean governance structures was initiated. Furthermore, as the demands of procuring entities increased, the existing system of “One Contractor for One Item” was no more suitable to meet their needs and the shift towards “Multiple Contractors for One Item” regime became necessary.

Before the introduction of a new purchasing regime, studies on procurement methods of the USA MAS, British Framework Contract Regime, and Canada Standing Offer were conducted. Based on the studies, the USA MAS and the PPS multiple item supply contract were modified to prepare the MAS system to be suitable for the Korean environment. However, despite the efforts to adjust the system to local conditions, a number of difficulties

31. The system is often referred to as “The Bidding by Luck” or “The Bidding of Fortune”.

32. These cases include for example the use of second stage competitive tendering, expected quantity competitive tendering, multiple competitive tendering, negotiated contracts, direct contracting, qualification evaluation notice, etc.

caused by the fact that Korea and U.S.' political-economic environments are different appeared. Local as well as central agencies expressed their concerns with regards to the possibility of negative effect on civil market, the nonexistence of protection measures for the disadvantaged when group direct contracting regime was applied, and the existence of lobby when procuring entity was conducting commodity selection. Furthermore, they were also worried that the regime seemed to facilitate collusion and made procuring agencies look like direct contracting agencies.

In response to these concerns, the PPS and the Korean Association of Procurement and Supply Management conducted a joint research and collected opinions of relevant agencies, after which four months' discussions with the Ministry of Finance and Economy about the introduction of the new regime were held. In preparation of the regime, the PPS mainly focused on satisfying diversified consumer needs. It was also expected that the introduction of the MAS would make it possible to procure better quality products at lower prices. The regime was finally introduced in 2005, when the relevant regulations were enacted.

The main aim of the MAS is to provide procuring entities with more procurement options and diverse products, and to facilitate suppliers' entrance in procurement market. The MAS consists of the conclusion of a contract with two or more contractors producing commodities that are similar or equivalent in performance, quality, and efficiency. The offered commodities are registered in a shopping mall, where various procurement entities can comfortably choose from the registered items. The items can be mutually compared and the procuring entities can choose the optimal procurement options to meet their budget. As only qualified companies with quality items are registered within the system, a complex bidding procedure is not needed and delivery requests can be made directly to a supplier.

2.1. Electronic Shopping Mall

The existence of a comprehensive shopping mall is an important aspect of the system. To make sure that the system is user-friendly, it offers ontology-based fast product search function. It is thus possible to search products even when incomplete information is input. In addition, procuring entities' purchase decisions are facilitated by the product comparison management and operation system. This way, processing time as well as manpower necessary to perform procurement functions can be reduced. For example, when artificial turf was procured via total amount contract as prescribed, more than 40 days were needed to conduct the whole process from bidding to delivery. However, under the MAS, the deliveries could be made concurrently with the order, and the contract procedure could be left out, reducing the amount of time for the request administration to days. Furthermore, due to prequalification criteria and convenience of product comparison, the system also enhances competition and makes it possible to obtain value for lower price.

From the viewpoint of procurement methods, all items registered in the comprehensive shopping mall are by nature unit price contract³³ falling in three different categories – regular unit price, third party unit price, and the MAS items (See <Table 7-1>). However, even the MAS, which applies to a vast majority of items and suppliers, can be viewed as a specific category of a third party unit price contract system.

Table 7-1 | Status of Registration for Each Registration in the Shopping Mall in 2009

Category	MAS	Direct Contracting			Competitive Tendering			Total
	3 rd Party	3 rd Party	Regular	Total	3 rd Party	Regular	Total	
Number of Contracts (Cases)	5,891 (82.9%)	706 (9.9%)	33 (0.5%)	739 (10.4%)	319 (4.5%)	153 (2.2%)	472 (6.6%)	7,102 (100%)
Supply Amount (100 million won)	60,706 (53.9%)	10,780 (9.6%)	11,779 (10.5%)	22,559 (20.0%)	544 (0.5%)	28,743 (25.5%)	29,288 (26.0%)	112,553 (100%)
Number of Items (Units)	297,585 (92.7%)	20,040 (6.2%)	298 (0.1%)	20,338 (6.3%)	1,005 (0.3%)	2,107 (0.7%)	3,112 (1.0%)	321,035 (100%)

With regards to scope and size, 297,585 items and 3,732 companies were registered in the system in 2009 (see <Table 7-2>). Furthermore, in 2009, almost 83% of procurement contracts were awarded through the MAS, representing slightly less than 54% of the total supply amount.

33. In a unit price contract system, the unit price of a given commodity is predetermined for a given period on the conclusion of the contract. The commodity is then delivered upon request over the agreed period at the price that had been set. This system is typically used for items procured frequently and in large quantities.

Table 7-2 | Status of the Number of MAS Companies, Number of MAS Products, Number of MAS Items in the Comprehensive Shopping Mall

Category	2007			2008			2009		
	Number of Companies	Number of Products	Number of Items	Number of Companies	Number of Products	Number of Items	Number of Companies	Number of Products	Number of Items
MAS*	2,078 (68.1%)	1,057 (57.9%)	185,235 (89.3%)	2,938 (76.5%)	966 (54.6%)	240,764 (90.9%)	3,732 (84.2%)	1,032 (60.6%)	297,585 (92.7%)
Non-MAS	972 (31.9%)	768 (42.1%)	22,274 (10.7%)	902 (23.5%)	802 (45.4%)	24,113 (9.1%)	702 (15.8%)	670 (39.4%)	23,450 (7.3%)
Total	3,050 (100%)	1,825 (100%)	207,509 (100%)	3,840 (100%)	1,768 (100%)	264,877 (100%)	4,434 (100%)	1,702 (100%)	321,035 (100%)

2.2. MAS Difficulties

Similarly to other procurement methods, the operation of the MAS has also been connected with some difficulties. One of the most common problems related to the MAS has been unfair purchase practices occurring during the delivery stage. As the MAS regime made it possible to award a contract worth several billion won with one click on the Internet, in attempts to win such contracts supplier companies used strong lobby. Consequently, the adoption of measures to enhance transparency and fairness turned out to be necessary. Among them, the Two-Stage Competition Regime plays an important role.

The Two-Stage Competition Regime, which is applied when the total contracted amount is equal to or exceeds a given amount,³⁴ consists of a selection of two or more tender participants for the submission of proposal. After the proposal evaluation, one successful bidder is selected to perform the contract. The introduction of the system in 2008 provoked complaints from both the procuring entities as well as the supplying companies. While the procuring entities mainly complained about the necessity to follow new procedures in relation to the introduction of a new system and the fact that the new system limited their choices, making it difficult to fully exercise their preferences, the supplier companies lobbied for the abolition of the system claiming that increased competition will lead to excessive price competition. Nevertheless, the regime stayed in operation and positive results connected with its existence were achieved. The operation of the regime enabled procuring entities to reduce their purchase budget, and excellent results were achieved with regards to the purchase of value for money and enhancement of culture of fair competition and transparency.

34. Here, Korean Two-Stage Competition Regime was again inspired by the USMAS, in which two-stage competition is also used in a situation that the total price of procured goods is no less than prescribed amount.

2.3. SME Cultivation

Apart from economic benefits, the MAS also provide opportunities to SMEs offering quality products. Through participation in the MAS, SMEs that are weak in advertising and marketing can gain access to new selling channels and their potential market can be significantly expanded. Registration in the shopping mall also provides them with the chance to enter foreign markets, as the service is also available to foreign embassies. In this respect, the MAS can be effectively used for SME support. Furthermore, as advertising benefit is only achieved for companies that have passed given criteria and are registered in the shopping mall, only high-performing companies are promoted through it. In addition, a specialty mall focused on good technology, environmentally-friendly products, and energy-efficient products is separately operated, providing incentives for SMEs to focus their effort in this direction and also offering the opportunity to use the MAS as government policy tool. Statistical data on the MAS operation show that the purchases of SME manufactured products through the MAS are steadily increasing, proving SME support through the MAS is efficient.

3. Paradigm Shift towards Customer-Oriented Service

Development of procurement methods reflected changes in domestic as well as international environment including a major shift from supplier-oriented to customer oriented paradigm. Similarly, one of the major changes in procurement market was the shift from procurement of a commodity to procurement of a complete service, requiring systemic changes and a vast ICT support. In line with that, when digitalization of GP was started and the MAS was introduced, provision of customer-oriented services and customers' convenience in their use represented major concerns. In the effort towards provision of customer-friendly services, the establishment of the Comprehensive Shopping Mall, changes in the method of administrative goods supply, implementation of the Network Loan Service, and the provision of additional contract-related services played an important role.

As suggested by the above, the establishment of the Comprehensive Shopping Mall in 2006 represented extension of the services offered by the MAS. The main aim of the creation of the shopping mall was the provision of a convenient and customer friendly environment and services for comfortable procurement of goods. As part of the national comprehensive procurement system (G2B), the shopping mall is the largest public agency-operated electronic shopping mall.

3.1. Change in System of Administrative Goods Supply

Another part of customer-orientation drive was the change in the system of administrative goods supply. Originally, to procure administration consumables, unit price contract based on the quantity of a given item expected to be needed within one year was concluded, and the items were stored in the central supply warehouse system or central warehouse of each provincial office. Procurement request was then made to the supplying company when the quantity in the warehouse fell under a given level (the quantity needed for three months). Procured items were delivered either via external parcel service company or by a truck possessed by the PPS. The advantage of this system, which was in operation from 1962 to 2005, was the delivery of commodities from different vendors at one time; however, it also entailed problems with excessive logistics expense, inefficient inventory management, and lower quality of supply service.

Due to these issues, in 2006 the system was changed to the so-called “Direct Delivery by Contractor” regime. The new system was also based on a unit price contract concluded with each vendor, however, unlike before, deliveries were made directly to procuring entities. This made it possible to promptly supply required items immediately after procurement request was received. Nevertheless, complaints related to a complicated goods receipt and payment procedure. In response, “Collective Supply by a Logistics Specialty Company” system was implemented. In this system, the purchase, storing, transport, and delivery functions were performed by a specialized company (so-called MRO company³⁵) working as the PPS agency. To secure better quality and lower price, more MRO companies were selected to provide the service while competing against each other. Since 2007, both systems, direct delivery by contractor as well as MRO company delivery, used concurrently.

3.2. Network Loan Service

To provide additional support for SMEs, which are usually financially weaker than large companies, Network Loan Service was implemented in June 2006. The Service consists in the provision of a loan worth 80% of the value of the contract to SMEs that have concluded a total amount procurement contract with the PPS. The money is to be utilized for the contract performance and paid back including the interest after the contract is fulfilled. The loan interest is in minimum one percent lower than that of a regular credit, providing SMEs with additional financial benefit. Furthermore, the fact that provision of the Network Loan does not require a separate guarantee also represents another form of support.

35. MRO: A type of procurement service under which the office supplies and materials (excluding raw materials) needed for maintenance, repair, operations, maintenance and repair of facilities, and management and production activities of a company, can be promptly procured via a specialized logistics company.

To provide the service, which is fundamentally different from the usual type of loan offered after the evaluation of company's financial indicators, the PPS made agreements with Woori Bank and the Industrial Bank of Korea. Upon the conclusion of a contract, the PPS provides the bank with information necessary to execute the network loan. At the same time, bank account for payments from the PPS is opened with the same bank. After the contract is delivered, the money the supplier company receives is deposited on the same account. When the loan is paid off, any other financial issues between the bank and the supplier follow their separate agreement.

The Network Loan is the first loan of this type that was introduced in the public sector in Korea. As for the results of its introduction, within the first eight months of the Network Loan existence, over 1,330 loans worth 139.5 billion won were provided.

The Network Loan is similar to two other types of loans provided for GP supplier companies – advance payment and public procurement loan. However, their targets are different. Advance payment is provided to a supplier in case of a manufacturing contract worth in minimum 30 million won or a service contract worth no less than 5 million won. For a supplier company, it is more advantageous to obtain advance payment, as unlike in the case of the Network Loan, it does not involve interest. On the other hand, the Network Loan allows for the extension of payment period by up to two months, which can be a significant benefit for companies with short-term liquidity problem. Finally, in case of contracts with public agencies, SMEs may also be able to obtain a public procurement loan offered by the Small and Medium Business Administration. Although this type of a loan is somewhat similar to the Network Loan, its scope and target is broader (For more details, see <Table 7-3>).

Table 7-3 | Comparison of Advance Payment, Network Loan, and Public Procurement Loan

Category	Advance Payment	Network Loan	Public Procurement Loan
Main Operating Agent	-	Public Procurement Service	Small and Medium Business Administration (Commissioned management of the Korean Company Data)
Target	The construction or commodity manufacturing contract with the amount of 30 million won or the service contract with the amount of no less than 5 million won	Exclusive contract out of the total amount contract of the Public Procurement Service (Excluding the facility construction)	The contracts with public agencies (115 public agencies) (Including the unit price contract)

Category	Advance Payment	Network Loan	Public Procurement Loan
Contract Confirmation	Public Procurement Service	Public Procurement Service	Public agency
System	EDI	G2B	Public agency procurement loan gateway
Security Conditions	Cash or guarantee	Guarantee not required	Evaluated with the credit evaluation rank
Maximum Payment Rate	70% of the contract amount	80% of the contract amount	80% of the contract amount (Excluding the amount paid in advance)
Money Collection	Making an adjustment when the contract is expired	Collecting the money with the money for delivery	Complying with separate agreement
Participating Agency	-	Public Procurement Service	115 public agencies
Enforcement	-	August 2006	September 2006
Application Procedure	-	3 stages Public Procurement Service → Public Procurement Service → {bank ↔ company}	4 stages Company → credit evaluation agency → public agency → {bank ↔ company}
Participating Bank	-	IBK, Woori, and Hana	IBK, Woori, Hana, Busan, and Kyongnam
Operation Results	1,835 cases, 306.9 billion won, and 167 million won for each case in average in 2007	757 cases, 110.9 billion won, and 146 million won for each case in average in 2007	443 cases, 66.6 billion won, and 150 million won for each case in average in 2007

4. Lessons and Implications for Developing Countries

Procurement methods are one of the key aspects of a country's procurement system. In preparation of a procurement regime framework, the main GP goal and needs of procurement entities in a country needs to be considered. Furthermore, it is essential that procurement methods complement well the local environment to secure smooth functioning of GP within local economy context. In many tendering methods, qualification evaluation system also plays an important role.

Development of the Korean procurement methods has been marked by constant quality improvement accompanied by the fight against negative side effects of procurement methods based on the lowest price. Common problems related to these regimes were poor quality of procured goods, unsatisfactory services, problematic delivery and maintenance, accompanied by the issue of subcontracting and unfair practices.

One of the ways Korea attempted to secure better quality of procured items was the introduction of restricted competitive tendering, which combined the advantages of open (competitive) tendering (competition) and selective (competitive) tendering (contract performance stability, quality, and customization). With a view to ensure better quality of procured items, Korea also implemented negotiated contract regime, which could be used under strictly prescribed circumstances. However, the method was connected with too much discretion on part of procurement officers, as detailed procedural regulations were missing, although the regime was legally grounded. In response, detailed regulations related to the use of the method were later introduced. Another quality improvement tool was qualification evaluation system, which was later criticised for overly lenient criteria making it easy to pass qualification evaluation even for companies with poor quality management.

As the Korean case shows, it is important that procurement methods and qualification system be defined in sufficient detail, so that the amount of procurement officers' discretion and the methods' abuse are limited. Qualification evaluation must be based on well selected criteria, including the prescription of cases when such criteria are to be used and what their weight is. Here, it may be considered that different procurement cases may require different weights of the same criteria. For example, in the Korean system, procurement of services and equipment is treated differently. While in case of procurement of software, the weights of price and technology are 30% and 70% respectively, in procurement of equipment the respective weights are 50% and 50%.

Major step in the improvement and simplification of the Korean GP was the introduction of the MAS supported by the establishment of a comprehensive online shopping mall. Through their implementation, procurement time was reduced from over one month to mere days, transparency was significantly boosted, costs of procurement system were reduced as no separate bidding procedure was needed for each procurement case, and better quality for lower price was achieved. Nevertheless, on its introduction, the system was also connected with unfair purchase practices and strong lobby on the suppliers' side. These were solved by the adoption of two-stage competitive regime, which originally received strong opposition from procurement entities as well as suppliers. However, as this opposition was partially caused by the novelty of the system (on the side of procuring organizations) and partially by increased competition (inconvenient for suppliers), the system stayed in operation. Furthermore, it later yielded excellent results, as, due to the regime, value for money resulting in budget reduction was achieved, and higher degree of fairness, competition, and transparency was secured.

The MAS also represents a successful case of SME cultivation and support. Through registration in the shopping mall, SMEs can achieve significant PR and marketing benefits and profit from expanded sales channels including the opportunity of overseas sales. In

Korea, since the MAS introduction, the proportion of SME goods among all items registered in the shopping mall has been constantly increasing. Another benefit of the use of the MAS for SME support is that due to the need to pass prequalification, only quality companies enjoy the support. It is also possible to use the MAS to provide support for companies offering products using new technologies, engaging environmentally friendly production, or using own patents, etc.

Korea's development and introduction of the so-called Network Loan Service can also offer inspiration to countries wishing to provide support for SMEs. The Loan, which is fundamentally different from classical bank loans based on financial and other indicators of companies' performance, may cover up to 80% of the procurement contract amount. The fact that 1,330 loans worth 139.5 billion won were provided within the first eight months of the system existence suggests that the Loan seems to be an efficient SME support tool.

Finally, Korea has also experienced the shift from supplier to customer-service orientation. Apart from the change of procurement methods and processes, such a shift also requires changes in the system of supply of administrative goods. Here, the result of Korea's attempts to find the optimum system was parallel operation of the system of direct delivery by contractor and the system under which specialized companies carry out the transport and delivery functions.

2012 Modularization of Korea's Development Experience
Korean Government Procurement Experience

Chapter 8

Internationalization of Korean GP Market

1. WTO GPA
2. Legislative Changes
3. Current and Future Trends
4. FTA Negotiations and Government Procurement
5. Lessons and Implications for Developing Countries

Internationalization of Korean GP Market

Internationalization of the Korean GP market started with continuing liberalization of its economy, democratization of political life, and intensification of international trade in the early 1990s. Before then, Korea made three attempts to join the WTO GPA to expand its export territories between 1979 and 1982. However, the negotiations failed as Korea was not willing to accept the level of liberalization required by developed countries. Korea finally opened part of its GP market (communication equipment) for the first time as a result of Korea-US telecommunication negotiations initiated in 1988. After that, Special Case Regulation on the Enforcement Decree on Contracts to Which the State is a Party to regulate the opening of GP market with communication equipment was enacted in 1992.

1. WTO GPA

In 1990, after Korea's proposal regarding the opening of its GP market was finalized, Korea started negotiations with GPA member countries to enter the WTO GPA. In the original version of the proposal, Korea offered to open 35 central government agencies, Korea Housing Corporation, KT, and the PPS to foreign companies. However, when Korea submitted its first proposal, discussions among the WTO countries on abandoning GATT system focused on trade in goods in favour of multilateral trade organizations covering new trade areas were going on. As these discussions also involved GP, Korea was recommended to modify and expand its proposal. In the modified material submitted in December, 1993, Korea offered concessions to open 42 central government agencies, 15 metropolitan governments, and 23 government invested agencies. After the successful conclusion of the negotiations and approval of the negotiated agreement by the National Assembly in December, 1994, Korea became a member of the WTO GPA in December, 1995, effective from January, 1997. The agreement, which involved procurement of goods, services, and

construction services, was enforced by the enactment of the Act of Contracts to Which the State Is a Party and its Enforcement Decree, Special Regulations on the Enforcement Decree, and Enforcement Rule. Furthermore, in 2011, an amended Agreement (GPA) reflecting technology development (e.g. e-procurement) and eliminating ambiguities by the clarification of obligations and provision of definitions was concluded.

By becoming a signatory party of the WTO GPA, Korea was able to realize various positive effects. Through the GPA, Korean companies were able to expand their markets and gain more export opportunities. Exposure to increased international competition also meant that only good companies managed to survive under the more difficult conditions. To help domestic companies realize benefits from global procurement market, the Practical Understanding and Application of WTO GPA and Concession Table of Other Countries were published by the PPS. The PPS also focused on the increase of awareness of global procurement practices via various materials including detailed studies on the procurement systems in other countries such as Canada and the USA, weekly publishing of Public Agency Bidding Information in Other Countries, and provision of other international procurement related information on the PPS website. This PPS effort also includes provision of information to foreign companies wishing to participate in the Korean market. In addition, “Plan to Support Korean Companies Entering the Global Procurement Market” aiming at the facilitation of Korean companies’ entry in global procurement market was prepared in 2005, accompanied by the creation of International Cooperation Team in charge of the plan implementation. Furthermore, the International Buyer Program and the International Buyer Corner were created in 2006.

While the WTO GPA meant an important step in liberalization and globalization of the Korean GP market, it also brought a number of challenges, such as increased competition for domestic companies, or the possibility of entry of unqualified foreign companies in the local GP market. To cope with these challenges and prepare Korea for GP market opening, the Government Procurement Market Opening Response Team (later transformed into the WTO Response Team) was formed in 1993. The team, which operated until 1996, was responsible for surveys and analyses of procurement systems in other countries and preparation of suggestions regarding adjustments of regulative and legal framework in relation to procurement of goods and facility constructions. Apart from that, the Government Procurement Policy Internationalization Planning Group was responsible for decisions regarding new regulations and legislation with regards to procurement of goods and facility constructions was also operated between March and June 1996.

2. Legislative Changes

The opening of the Korean procurement market also required changes to the Korean regulative and legal framework. To provide a legal basis for GPA application in domestic environment, the State Contract Act was enacted in 1995,³⁶ followed by the Enforcement Decree and Regulation on Special Cases of the same act and adjustments in accounting regulations. The new elements in Korean contractual procedures were a screening test, international bidding, work performance bonds³⁷ and International Contract Arbitration Committee.

Excluding the preparation of legal basis of GP market opening, Korea also needed to strengthen the competitiveness of local companies domestically as well as internationally and prevent the entry of foreign companies with insufficient qualification. To this end, several types of measures were implemented. During the preparation phase to enter the GPA, Korea was able to negotiate that SME business products would not be opened to international competition. This provision meant that around 55% of contracts for the procurement of goods were excluded from. Other measures that focused on the boost of international competitiveness of domestic companies included strict application of the rule of the country of origin (so that non-GPA member countries were not able to place their bids), calculation of prices for foreign goods including all related expenses (e.g., transport cost, VAT, tariffs, etc.), the necessity to operate A/S network with quality corresponding to that provided by domestic companies, etc. In addition, pre-qualification and screening tests to secure high quality procured items from foreign companies were conducted and foreign companies were required to receive their payment in KRW (Korean Won).

3. Current and Future Trends

After the adoption of new GPA in 1994, issues such as excessive rigidity or inaccuracy of terms appeared. It also became necessary to modify the system to embrace the development of ICT leading to the boost of e-commerce and the emergence of new procurement methods. Furthermore, EU countries raised the issue of GPA simplification by changing the current system of positive list of concessions into negative list and suggested classifying public-private partnership projects as projects falling in the GP category. While some issues such as the negative list of concessions and a broad range of contradictory opinions exists, there is a general consensus about others (e.g., simplification of statistical reports). It is thus

36. The Act provided a basis for the establishment of the International Contract Arbitration Committee, introduction of qualification evaluation system, and application of international bidding practices.

37. A performance bond is a surety bond issued by an insurance company or a bank to guarantee satisfactory completion of a project by a contractor.

likely that GPA may be amended in some form. In this respect, Korea must prepare for the eventuality that the exception regarding SME products may be abolished, as some countries object to any kind of exceptions and wishes to eliminate all special clauses obstructing market opening.

It is expected that in response to the adoption of the WTO GPA, the Korean procurement environment will continue changing. Apart from the revision of the whole regulative framework and verification of compliance of domestic GP procedures with those of the Agreement, it can be expected that the role of the PPS will also change over time. An important issue which is also likely to change is the existence of different procurement procedures for domestic and international market. Some argue that the separation of markets is necessary, as they differ in objectives (domestic procurement aims at procurement of domestic products within the country while the objective of international procurement is to procure foreign products overseas), procurement procedures, and practices. In the international market, customers are separated by nationality and language, and overseas procurement also involves more complicated shipping and customs procedures. Furthermore, international procurement practices may bear special features that must be taken into consideration. It is thus argued that separating both markets by different procedures increases efficiency, has positive effect on procurement administration expertise, and boost professionalism of procurement staff.

Despite that, there is also a counter-opinion that procedural and operational separation of domestic and international procurement markets is not appropriate. The arguments are such that even domestic products often contain foreign parts and price analysis may thus require thorough knowledge of overseas procurement procedures and foreign products may already be available domestically. If so, contractual terms and procedure would have to comply with domestic laws and regulations and the knowledge of such procedures would thus lead to more efficient procurement administration. Furthermore, the liberalization of domestic market means that the differences between domestic and international procurement environment are becoming smaller, as part of domestic procurement already must comply with the GPA and thus reflects international practices. It is also often the case that catalogues from foreign tender participants are issued in foreign languages. Finally, even domestic product market surveys may contain an international aspect, as in some cases, to obtain market data related to foreign products it may be necessary to conduct thorough analysis of domestic market. In such a situation, rigid separation of domestic and international procurement procedures might make it difficult to collect necessary information and make the whole process more complicated.

4. FTA Negotiations and Government Procurement

Another significant factor influencing GP market in Korea is the existence of FTAs (Free Trade Agreements) with other countries. Depending on the definition and scope of a particular FTA, the effect on GP can be strong. Since the period of liberalization, Korea has been actively pursuing the conclusion of FTAs with its major trading partners to secure international markets and enhance the competitiveness of its economy.

Currently, Korea has FTAs with a number of countries and regional integrations. The first FTA agreement was concluded with Chile in 2004, after which FTAs with Singapore and EFTA³⁸ were signed in 2006. In 2007, FTAs were signed with ASEAN, the USA, and the EU in 2009.

While all signed FTAs contain a chapter on GP, they differ in their specifics (For the overview of FTAs with the participation of Korea see <Table 8-1>). For example, as Chile is not a member of the WTO GPA, compliance with the GPA regulations was not required by the Korea-Chile FTA. Despite this fact, excepting that the provisions related to the exclusion of concessions regarding privatized government agencies provided without compensation and provision of bidding information in electronic form, in GP the Agreement follows the GPA. Similarly, the Korea-Singapore FTA also follows GPA provisions except those related to the provision of bidding information in electronic form and exclusion of concessions related to privatized government agencies provided without compensation, and Korea-EFTA FTA is compliant with the GPA with the exception of the MFN (Most-Favoured-Nations) clause and exclusion of concessions related to privatized government agencies provided without compensations.

Table 8-1 | FTA Government Procurement Minimum Concession

(unit: SDR 10,000)

FTA	Concession Agency	Goods	Service	Construction
Korea-Chile	Central Government	5	5	500
	Local Government	20	20	1.500
	Public Agency	45	-	1.500
Korea-Singapore	Central Government	10	10	500
	Local Government	20	20	1.500
	Public Agency	40	-	1.500

38. European Free Trade Association. Member countries: Switzerland, Norway, Island, and Lichtenstein.

FTA	Concession Agency	Goods	Service	Construction
Korea-EFTA	Central Government	13	13	500
	Local Government	20	20	1.500
	Public Agency	45	-	1.500
Korea-US	Central Government	7	7	500
	Local Government	20	20	1.500
	Public Agency	45	-	1.500
Korea-EU	Central Government	13	13	500
	Local Government	20	20	1.500
	Public Agency	45	-	1.500

Unlike in the above mentioned agreements, in the Korea-USA FTA, GP is regulated in more detail. While the Agreement requires compliance with the GPA, it also contains separate agenda on the opening of GP market. The FTA also stipulates that the evaluation of a supplier participating at tender should be based on commercial activities of the supplier in all countries where the supplier operates (not only on the operations in concerned countries). Furthermore, an FTA party and its procuring entities may prepare, adopt, or apply technical specifications with the aim to promote conservation of natural resources and protect the environment or to require a supplier to comply with generally applicable laws related to fundamental principles and rights at work as well work conditions (e.g. minimum wage, occupational safety, etc.). The FTA also provides regulations regarding a government procurement team for information exchange or discussion of a given issue, which is to be formed upon request or by mutual agreement.

Finally, Korea-EU FTA provisions do not impose the condition to disclose information regarding prior experience with procurement contracts or prior work experience in the territory of the FTA party of tender participants. In addition, according to the Agreement, private sector invested projects may be defined based on domestic law.³⁹ Similarly, contractor selection procedures as well as the project executions are also subject to domestic law; however, the Agreement stipulates that they must be conducted in a non-discriminatory way. Finally, the Agreement also involves some provisions related to GP transparency.

39. Similar provision is also part of the US-Korea FTA.

5. Lessons and Implications for Developing Countries

In the internationalization of GP market, countries should give thorough consideration to the positives as well as the negatives that higher level of internationalization and liberalization might bring. For example, in negotiations to become members of the WTO GPA, countries must take into considerations the type and scope of concessions they are willing to offer, as well as the fact that the required level of liberalization might be higher than the level optimal for that particular country, such as in the Korean case during the early GPA negotiations. Careful consideration of the level of openness is especially important for developing countries, which may need to protect underdeveloped domestic industries that might be hurt when suddenly exposed to tough international competition. On the other hand, high level of internationalization usually brings a number of positive effects, such as market expansion, increased export opportunities, facilitation of know-how exchange, the chance for domestic companies to gain international experience, etc.

To realize these benefits, local economic operators may need some help. To this end, Korea has used a number of measures, such as provision of information of international GP practices and standards, or information sharing and active promotion of participation in international tenders. At the same time, in relation to the level of a particular country's development, certain degree of protectionism may be needed. Some measures helping protect the Korean environment against negative aspect of GP market opening are e.g. strict application of the rule of the country of origin, the requirement to base prices in tender proposal on all relevant costs including shipping, tariffs, VAT, etc., the requirement that foreign companies participating at tenders be able to provide the A/S service level equivalent to the level provided by domestic companies, the requirement of foreign contractors being paid in KRW, etc. To prevent the entry of low qualified companies in domestic market, Korea used various forms of prequalification evaluation and screening tests. Korea also paid special attention to the protection of domestic SME companies, for which Korea managed to negotiate an exception in the WTO GPA negotiations and SME market was thus not required to be opened to international competition. In this respect, countries should also be aware that the situation is likely to change in the future, so any exceptions or protectionist measures are rather temporary and their abolishing may be required. It is thus desirable to gradually prepare domestic economic operators for the increased competition and other effects related to the opening of GP market.

GP market internationalization may also require corresponding changes in domestic law. Here, discussion is currently going on regarding the degree to which domestic and international procurement procedures should differ. Some arguments for separation of both markets are different languages used in different countries (territories) and the fact

that international procurement involves complicated shipping and customs procedures, differences in administrative and cultural practices, etc. On the other hand, the argument against separation of domestic and international procurement are that clear dividing line between the two does not exist anymore, as foreign products are typically easily available domestically, preparation of domestic price calculations, marketing plans, etc. must involve international aspects and vice versa, domestic GP must to a certain degree already comply with international regulations due to the membership in the WTO GPA or other international organizations, etc.

2012 Modularization of Korea's Development Experience
Korean Government Procurement Experience

Chapter 9

Conclusion

Conclusion

It is undeniable that economic development depends to a large extent on the role of the state in the economy. Apart from other aspects of administration, a factor that significantly influences state and public sector operation is government procurement. The last century has shown that GP system has played a major role in the development of many fast growing economies, thus pointing at the importance of studying procurement systems of those countries that have been successful in their effort to become economically advanced internationally recognised economies.

In view of that, this paper focuses on the experience with development and refinement of GP system in South Korea, which is one of the most often-cited examples of remarkable economic development. In eight major chapters, this study covers theoretical basis of GP, development of the Korean procurement system and procurement methods, transparency in GP, the Korean e-procurement system, GP quality management, and internationalization of GP market. The first part of this study provides general theoretical background for its second, practical part that focuses on the Korean experience with GP. Korea's GP experience as presented in this study can be summarised as follows.

The Korean development shows that transparency of GP law is closely tied to economic development and that legal transparency must be consistent with a country's economic system. Furthermore, transparency must be based on solid legal grounds and it is important that principles of information disclosure and non-discrimination be legally grounded, too. In relation to that, countries should be careful to transparently provide information on lower laws, which are often neglected in favour of transparency of higher laws. When trying to constitute a legal obligation of transparency, desirable level of transparency must be considered, as too much transparency may also be harmful. In particular, in tendering process, disclosure of certain information, such as prices or patents, may hurt

the tender participant or lead to various negative effects such as collusion among tender participants. Moreover, sufficient attention should also be paid to the transparency of ex-post measures and especially cases when sanctions are imposed or remedial measures are taken. Closely related to that is the issue of potential abuse of discretionary power. A high risk of discretionary power abuse is especially related to direct contracting; it is thus mandatory that the use of this method be regulated in sufficient detail. The Korean case of frequent occurrence of floods also shows that in preparation of direct contracting or other non-competitive tendering methods regulative framework, local conditions must be considered. Although in the Korean law floods are considered a situation of natural disaster in which direct contracting is possible to use, direct contracting was used excessively as in certain parts of Korea floods happen every year. An example of important tools Korea has used for transparency enforcement is the ombudsman system and integrity culture. While the operation of the ombudsman is still connected with some issues such as securing ombudsmen's fairness or problematic application of ombudsmen's decisions as no legal obligation to follow ombudsmen's decisions exists, integrity culture promotion has brought positive transparency enhancement results.

In Korea, transparency was also successfully enhanced via the development of an e-procurement system, which also served to improve GP efficiency and the quality of procurement service. The Korean e-procurement system was originally established to satisfy the increasing need to manage growing number of items and companies involved in GP and to help provide better customer-oriented service. During the e-procurement implementation, the issues of right to access information, implementation of reliable monitoring system, and protection of information along with prevention of information abuse needed to be solved. To that end, Korea introduced a number of measures such as electronic signature, users' authentication, confirmation of time when documents were sent, blocking multiple bids from the same IP address, fingerprint recognition system, automated blocking system against unqualified companies, etc. E-procurement implementation was accompanied by the development of legislative and regulative framework, in which major issues were constituted by regulating electronic contract awarding, electronic bidding procedure, data backup procedures, situations of shutdown etc. Korea's e-procurement success was also enabled by the fact that the Korean e-procurement system provided a uniform platform that was able to link all major existing electronic systems used by the public as well as private sector. Furthermore, the system operation was also supported by supplementary services such as web-call center, mobile electronic bidding system, mobile inspection of procured goods, mobile office, etc., making the system user-friendly. In the e-procurement implementation, Korea also needed to overcome a number of difficulties, such as incomplete legal framework and underdeveloped security measures, or the fact that a number of functions were developed but never used. The e-procurement system is also

receiving criticism for being overly complex and inconveniences caused by the necessity to repeatedly install security program when accessing different websites and the need to go through a separate registration procedure each time a new website is visited. Finally, there is also criticism that the efficiency of the system is hindered by tacit factors such as local cultural practices, under which preference may still be given to personal contact. Despite that, the Korean e-procurement system has been repeatedly awarded as the best practice and the best case to benchmark domestically as well as internationally. However, it is important to bear in mind that the Korean e-procurement success was also facilitated by the local culture of widespread use of modern technologies, high level of computer and ICT literacy, and well-developed Internet services. For successful e-procurement implementation, developing countries should thus take into consideration the level of infrastructure needed to actively operate the system along with the level of computer literacy of local citizens.

The growing effort to improve GP efficiency and transparency was accompanied by the shift towards the provision of customer-oriented service. As procuring entities started demanding better quality, better design, more choices, and better supplementary services including A/S as well as more information to facilitate their purchase decisions, systematic quality control turned out to be necessary. To practice efficient quality control, Korea introduced a comprehensive quality management system. The quality management tools Korea employed are mainly constituted of quality checks, inspections, quality certification regime, Sinmungo, and Excellent Procured Goods system. Furthermore, the use of these tools was supported by the creation of feedback on results of any inspections or checks, the use of modern technologies, the implementation of e-procurement system, along with the creation of a uniform commodity classification system. Finally, integral part of the Korean GP quality drive was also the adoption of well developed government goods management system, which is closely related to most GP functions. In its quality management effort, Korea needed to overcome difficulties related to low quality of procured goods caused by outsourcing and tender participation of paper companies, negative effect of the lowest price procurement methods, and solve the issue of special items requiring special regime such as leased goods or computer software, which became regulated separately.

Success or failure of GP system is to a large extent dependant on the procurement methods in use. The choice of procurement methods needs to be based on GP goals as well as the needs of procuring entities. Furthermore, to avoid implementation and operation difficulties, it is also necessary that procurement methods reflect local environment. Development of the Korean procurement methods has been marked by constant quality improvement accompanied by the fight against negative effects of procurement methods based on the lowest price exemplified by poor quality of procured goods, unsatisfactory level of services, problematic delivery and maintenance, and the issues of subcontracting and

unfair practices. To solve these problems, Korea introduced various tendering methods such as restricted competitive tendering or negotiated contract, which were often connected with excessive discretion of procurement officers. In response, the use of the methods became regulated in great detail. Another important step was also the introduction of qualification evaluation system, the development of which showed the importance of detailed definition of the system including careful selection of criteria and the specification of their weights. A very successful method in provision of diversity of procured goods and customer-oriented service was the Multiple-Award-Schedule (MAS), through which better quality for lower price was achieved. The system also provided the opportunity for SME cultivation and the support of companies using new or environmentally-friendly technologies, patents, etc. SMEs were also support through Network Loan, as an efficient SME promotion tool. Despite the fact that the MAS yielded excellent results, in its operation Korea needed to tackle the issues such as unfair purchase practices and strong lobby to a large extent solved by the introduction of two-stage competitive tendering regime.

In internationalization of GP market, countries should give thorough consideration to positives as well as negatives higher level of internationalization and liberalization might bring. Careful consideration of the level of openness is especially important for developing countries, which may need to protect underdeveloped domestic industries. On the other hand, high level of internationalization usually brings a number of positive effects, such as market expansion, increased export opportunities, facilitation of know-how exchange, etc. To help local economic operators realize these benefits, Korea used a number of measures such as provision of information on international GP practices and standards or information sharing and active promotion of participation in international tenders. Some measures helping protect the Korean environment against negative aspect of GP market opening are strict application of the rule of the country of origin, the requirement to base prices in tender proposal on all relevant costs, the requirement that foreign companies participating at tenders be able to provide the A/S service level equivalent to the level provided by domestic companies, the requirement of foreign contractors being paid in KRW, etc. To prevent the entry of low qualified companies in domestic market, Korea used various forms of prequalification evaluation and screening tests. Korea also paid a special attention to the protection of domestic SMEs, for which Korea managed to negotiate an exception in the WTO GPA negotiations. In this respect, countries should also be aware that the situation is likely to change, so any exceptions or protectionist measures should be viewed as temporary as their abolition may be required. It is thus desirable to gradually prepare domestic economic operators for the increased competition and other effects related to the opening of GP market.

The authors of this study hope that its content will be beneficial for any persons with interest in the Korean public procurement system. In the last six decades, Korea has gone

through a remarkably successful economic development, in which public procurement has played an increasingly important role. Due to Korea's condensed development, Korea has faced a number of issues and obstacles, and also achieved major victories on the way toward becoming an advanced economy with developed infrastructure, structure of international trade on an increasing scale favouring modern technology and IT products, and a number of internationally recognised industry brands. However, the "Miracle of the Han River" would not have been possible had the state and public sector dealt efficiently with any developmental challenges Korea faced. It is thus the hope of the authors that Korea's positive as well negative experience with the government procurement development and perfection will prove useful for developing countries on their way towards economic advancement supported by a well-developed public procurement system.

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