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국제학석사학위논문

Policy Implication of Products from Gaeseong Industrial Complex to Korea-China FTA

개성공단 제품에 관한 한-중 FTA에의 정책적 함의

2014년 2월

서울대학교 국제대학원

국제학과 국제통상학전공

정승연

개성공단 제품에 관한

한-중 FTA에의 정책적 함의

지도교수 안덕근

이 논문을 국제석사학위논문으로 제출함

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서울대학교 국제대학원

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Policy Implication of Products from Gaeseong Industrial Complex to Korea-China FTA

A thesis presented

by

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to

Graduate Program in International Commerce

For the Degree of Master of International Studies

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Graduate School of International Studies

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ABSTRACT

In an era of remarkable development in FTAs, products manufactured from Gaeseong Industrial Complex (GIC) on Korea's side, carry positive implications that could lead to deeper progress in economic cooperation and relations between the two Koreas. However, given Korea's arranged FTA status, Gaeseong-products suffer from different arrangements under Korea's FTA schemes with other countries when it becomes a subject of export. At the core of the issue lie rules of origin factor. By analyzing special rules of origin cases of Korea, Israel-Egypt QIZ, and Singapore, this paper observes how the scheme is addressed differently across trade agreements. Through textual analysis, the paper has found that (1) classification of special rules of origin can be made into (1) outward processing (2) qualifying industrial zone and (3) integrated sourcing initiative. The findings lead to implications to upcoming Korea-China FTA in its outward processing scheme coverage on four levels: regulatory, economic, technical, and political.

This paper first provides research on FTA rules of origin. The second section regards worldly cases of special rules of origin, including that of Korea's FTA outward processing schemes on Gaesong-products. Then, the research attempts to explore consistent pattern, if any, across FTA special rules of origin based on its characteristics. Finally, the paper concludes by providing suggestions to upcoming Korea-China FTA on this issue.

Keywords: Free Trade Agreement (FTA), Gaeseong Industrial Complex, Korea-China FTA, Outward Processing Scheme, Rules of Origin (RoO)

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TABLE OF CONTENTS

ABSTRACT……………………………………………………………………………………..i

Table of Contents……………………..…………………………………………………..ii

Chapter I. Introduction………………………………………………………….…..……1

1. Motivation………………………………………………………………………….1
2. Case Selection…………………………………………………………..………….2
3. Research Question………………………………………………………………….2

Chapter II. Literature Review ………………………………………………………….…..3

1. Rules of Origin for FTA……………………………………………………………3
2. Importance of Rules of Origin in FTAs……………………………………………4

Chapter III. Special Rules of Origin in FTAs by Classification……………………………….5

1. Outward Processing Scheme under FTAs……………………………………………5

   A. Rationale of the Outward Processing…………………………………………5

   B. Legal Issues of Outward Processing…………………………………………..6

2. Qualifying Industrial Zones (QIZ) under FTAs……………………………………7

   A. Rationale of QIZ……………………………………………………………7

   B. Legal Issues of QIZ……………………………………………………...8

3. Integrated Sourcing Initiative (ISI) under FTAs………………………………...8

   A. Rationale of ISI…………………………………………………………...8

   B. Legal Issues of ISI…………………………………………………………10

Chapter IV. Gaeseong Industrial Complex (GIC) ……………………………………………11

1. History of GIC…………………………………………………………………….11
2. GIC in Korea's FTAs……………………………………………………………..12

Chapter V. Conclusion……………………………………………………………………18

1. Summary……………………………………………………………………………18
2. Policy Implication to Korea-China FTA ……………………………………………18

References……………………………………...…………………………………...20

ABSTRACT (KOREAN) ………………………………...…………………………..22

CHAPTER I. INTRODUCTION

1. Motivation

Market integration based on Free Trade Agreements (FTA) is another distinctive trend in world trade order. Under this FTA era, South Korea (hereafter Korea) has initiated a simultaneous arrangement of FTAs in accordance with its FTA roadmap settlement in 2003. Korea's key trading partners include Chile, Singapore, EFTA, ASEAN, India and Peru, EU and US, all of which entered into force. Currently negotiating partners include GCC, Australia, New Zealand, Colombia, Canada, Turkey, Mexico and China. Not only that, negotiation preparatory steps as of now is underway with Japan, MERCOSUR, Israel, Vietnam, Central-America, Malaysia and Indonesia.

In this expanding trade structure, it is critical to include Korea's outward processing zone into FTA negotiations. Gaeseong Industrial Complex (GIC) is a representative case of such to this point. GIC, a special economic zone located just within 10 km away from Seoul, and 8 km away from Demilitarized Zone (DMZ), serves as a symbolic product of inter-Korean cooperation between the South and the North. Basically, GIC utilizes capital and technology from the South while incorporating labor and land elements from the North in order to build mutual prosperity that serve as a founding step for inter-Korean economic cooperation, ultimately leading to a peaceful reunification of the two Koreas (Choi, 2006). Therefore, the founding philosophy beneath establishment of GIC itself serves more than an economic purpose. Rather, GIC is closely related to establishing peace and prosperity on Korean peninsula, on reaching Korea's reunification goal and on also alleviating Asian security concerns. Not only that, successful operation of GIC may expand into further establishment of facilities sharing similar mechanism. In this sense, Korean government is committed to inserting outward processing scheme or GIC provision to its FTA agreements.

This paper seeks to verify the type of pattern that is acknowledged across different special rules of origin schemes in worldly FTAs. Although there are numerous literatures that study international trade law-related issues with special rules of origin schemes, most of them are focused on explaining individual country's case of special rules of origin in their FTAs. By studying cases of Korea, Israel, and Singapore, this paper seeks to expand the horizon of how special types of rules of origin schemes are addressed across different FTAs, exploring the

similarities and differences, so that the results can be applied for expansion of GIC and/or any other upcoming OPZs that Korea may pursue in the future.

2. Case Selection

Korea, Israel, and Singapore are three countries that have some common aspects that make each of entities to regard them to observe as major groups. These countries institute special rules of origin scheme that serve as an exception to the territoriality principle. The scheme is based on the concept where the exporting party is allowed to assemble goods using a non-party's labor in the midst of the manufacturing process and claim preferences for the final goods to the importing party. Following this scheme, final goods exported to the importing party need not be manufactured without interruption in the exporting party's territory. Rather, certain parts and components are exported from the exporting party to a non-party for processing, and non-party-made semi-products are then re-imported to the exporting party for final operations (Komuro, 2009).

3. Research Question

Korea's GIC case serves as an experimental facility of market economy located on North Korean land, geographically. In case the project reaps success, this can contribute to a facilitation of North Korea's transition to market economy, as many other GIC-replicating models will come to exist (Choi, 2009). Based on this idea, the paper is focused on to answer the research question of defining characteristics of major FTA special Rules of Origin schemes and its implications to upcoming Korea-China FTA. Due to data availability, the years are limited to past three decades. Chapter II explains literatures addressing similar topics. Chapter III explores special rules of origin cases by countries, and derives quantitative findings in order of Korea, Israel, and Singapore. Chapter IV covers GIC and explores GIC provisions in Korea's FTAs. Finally, Chapter V concludes the paper.

CHAPTER II. LITERATURE REVIEW

1. Rules of Origin for FTA

FTA rules of origin is a set of administrative guidelines of which goods shipped from an FTA Party must meet in order to enjoy preferential tariff treatment from an importing Party. Generally, origin refers to countries with its political identity. But non-independent state such as Hong Kong can be eligible for an origin. The controversy over rules of origin is deeply related to different natures across different countries. Moreover, its complicated and discriminatory nature serves as a trade barrier to many trade case (Bang, 2004). Therefore, as firms decides to go global sourcing their raw materials or expand their manufacturing operation overseas, judging a product's rules of origin grew in difficulty and in importance. Generally, the rules can be viewed from three levels: origin criteria, cumulation rules, territoriality and direct transport principles.

A. Origin Criteria

Origin criteria are utilized in ruling whether goods imported from an FTA Party has acquired an originating status under the FTA and are eligible for origin criteria: i) a value-added test, ii) a change-in-tariff-classification test; and iii) a processing test. Parties of an FTA may choose their own origin criteria, stemming from two approaches: the single test approach and product specific approach. The single test approach covers all goods by FTA preferences that passed a sole origin test. Examples include the former 40% value-added test under the ASEAN FTA and 50% value-added test under Australia-New Zealand Closer Economic Relations Agreements (ANZCERTA). The other approach is product specific in that origin test differ according to individual goods covered by FTA preferences. Examples are a variegated combination of value-added and change-in-tariff-classification tests in the NAFTA, MERCOSUR, and most FTAs.

B. Cumulation Rule

The cumulation rule applies to the rules of origin and is coupled with a value-added test. When calculating the value-added of an exporting Party, costs incurred in the exporting Party are cumulated with parts originating in other Parties to the FTA. Due to the cumulation rule under FTA, parts manufactured in the importing Party must be deemed originating in the exporting Party. Usually, the cumulation is largely divided into two types: partial or full cumulation. Under the partial, only materials from other Parties that acquire an originating status are deemed

originating in an exporting Party and are aggregated with local content in the exporting Party. In contrast, under full cumulation, even in cases where materials from other Parties to do not obtain the originating status, an originating input incorporated into such non-originating status, and originating input incorporated into such non-originating materials is rescued and cumulated with other regional contents. In this sense, full cumulation is more beneficial to producers of final goods that partial cumulation.

C. Territoriality and Direct Transport Principles

Despite an originating status for FTA preferences is met, goods from a Party do not always categorically qualify for preferences in an importing Party. First, the good must meet the territoriality principle, an additional requirement for preferences. This principle requires that the goods be manufactured without interruption in the exporting Party. Consequently, if semi-finished goods or intermediate goods are exported for further processing to a non-Party and is re-imported for finishing in the exporting Party, the final goods would lose preference eligibility. The outward processing is in principle prohibited under FTAs. Second, the final goods must be directly transported to an importing Party (Komuro, 2009).

2. Importance of Rules of Origin in FTAs

The economic implication that is brought by rules of origins in FTAs is related to the influence it can place on the flow of trade and investment. For this reason, determination on rules of origin is precisely more about defining qualification on preferential treatment on trade (Kim, 2004). Accordingly, the rationales for rules of origin determination can be set differently across different FTAs. Given today's broad scale of economic production over the globe, it is becoming more complicated to rule a product's origin. What makes this more challenging task is, when two partners' industrial policy orientation and individual interests collide. So it can be said that rules of origin subject matter itself requires both a professional and technical evaluation on its FTA negotiation process.

CHAPTER III. SPECIAL RULES OF ORIGIN IN FTAS BY CLASSIFICATION

As explained earlier, the basic objective of Rules of Origin is to determine whether or not a good originated in FTA partners and is therefore eligible to receive preferential treatment. With regards to GIC products on its rules of origin, there are three types of special rules of origin across the world to take note of: Outward Processing, Qualifying Industrial Zone, and Integrated Sourcing Initiative. This paper will address each of special rules of origin regimes by looking at four levels of rationales: regulatory, economic, technical and political. By doing so, the similarities and differences can be derived.

1. Outward Processing Scheme under FTAs

The first type of special rules of origin scheme to be inserted in FTA is Outward Processing. Outward processing provisions allow processing to be taken outside of the territory without originating status upon product changed. In Korea's case, Gaeseong clause serves as an example to an outward processing scheme to be inserted into its FTAs.

A. Rationale of the Outward Processing Scheme

As mentioned earlier, outward processing scheme is exceptionally accepted under any FTA. The rationale for acceptance is multifold, ranging from economic to political reasons.

1) Regulatory Rationale

The outward processing scheme is a tool devised to avoid FTA-specific dilemma in that it "softens" strict rules of origin, precisely the territoriality principle, and enables an offshore-oriented FTA Party to use FTA preferential regime to the utmost for specified foods.

2) Economic Rationale

Outward processing allows economic benefits in that the producers can reap profit from cheap labor in third countries. An FTA Party with outward-oriented producers thus can persuade other Parties to extend outward processing zone into a preferential area. Moreover, this scheme conforms to economist David Ricardo's "comparative advantage" theory, which supports efficiency through extraction of materials and labor from the cheapest and best source. Thus, with an FTA implementation, producers in a Party could benefit from using materials and labor from non-Parties given that the latter are priced lower that intra-FTA partners.

3) Technical Rationale

The outward processing scheme falls under only to products subject to value-added test. There are two types to consider: value-added test for the final product and outward processing value added test. In case of value-added test for the final product, the first stage value added (i.e. the value of the exporting Party-made materials) and the third stage are aggregated. If the sum of these territorial value added reaches the minimum percentage and the second extra-territorial value added does not exceed the maximum percentage, the final product is entitled to FTA preferences. In case of outward processing value added test, there lies a requirement that value of outward processing be capped by a specified percentage. Though it tolerates the extra-territorial process, the scheme limits its value added to a certain percentage. Cost calculation is, therefore, determinant for any outward processing schemes under FTAs.

4) Political Rationale

As in the case of Korea and Israel, some FTA outward processing schemes were proposed in a view to invite political and policy goals. Political motivations include the promotion of peace between former belligerents. Korea's FTA policy is closely related to reunification policy and Asia security goals that is aimed at bringing peace and prosperity in the region.

B. Legal Issues of Outward Processing

In the process of including outward processing scheme into FTAs, there lies a major concern. This problem relates to violation on WTO rules. According to Article I:1 of General Agreement on Tariffs and Trade (GATT), which later was absorbed as a part of WTO, discrimination between like products originating in, or destined for, different countries, with exceptions including preferential treatments through regional agreements in accordance with Article XXIV is prohibited. Nonetheless, this FTA exception only applies to intra-trade between the FTA partners involved. That is, the exception cannot expand its benefit coverage to goods originating in third countries by the FTA, as in the case of GIC.

As a matter of fact, there has been no ruling decision deriving from disputes on outward processing schemes thus far. However, since outward processing schemes within FTAs have potentiality to bring controversy in WTO MFN obligation and with its violation, defining the scope of the outward processing zone in its incorporation requires much attention. For this reason, there are not so many FTA cases worldwide in which outward processing schemes are inserted.

2. Qualifying Industrial Zones under FTAs

The second type of special rules of origin is the Qualifying Industrial Zone (QIZ). The QIZ program was designed by the United States as a unilateral act in order to offer products from designated QIZs (Kim, 2008). The Israel-U.S. FTA was signed on April 22, 1985 and entered into force on September 1, 1985. The U.S. enacted "The United States-Israel Free Trade Area Implementation Act of 1985" in order to implement the U.S.-Israel FTA. In November 1996, Section 9 of the Act was amended for Presidential authorization. Under Section 9, a QIZ was termed as an area that "(i) encompasses portions of the territory of Israel and Jordan or Israel and Egypt; (ii) has been designated by local authorities as an enclave where merchandise may enter without payment of duty or exercise taxes."

A. Rationale of Qualifying Industrial Zone

1) Regulatory Rationale

The QIZ program allows equal tariff treatment as what is offered to U.S.-Israel FTA: any product manufactured in designated area of QIZ, after meeting certain conditions, can enter the U.S. market tariff-free.

2) Economic Rationale

The QIZ regime allows Israeli producers to resort to offshore processing in QIZs of Egypt and Jordan, so that a duty-free entry to qualifying articles from West Bank, Gaza Strip, or QIZ can be made to the United States. Upon request from Egypt and Israel, in August 2005, the United States Trade Representative (USTR) additionally designated the Central Delta zone and expanded Greater Cairo and Suez Canal as QIZs (U.S. Federal Register, 2005).

3) Technical Rationale

Under U.S.-Israel FTA, several provisions stood out as U.S. Generalized System of Preferences (GSP)-type rules of origin and a limited cumulation test. However, an outward processing scheme was excluded from the agreement. Instead, the U.S. unilaterally stipulated the third country's content cumulation more than the outward processing (Komuro, 2009), via its legislation: a product manufactured in QIZ can have access to the U.S. market without paying

tariff if the sum of the cost of materials and the direct costs of processing operations attributable to Israel or the QIZ is not less than thirty-five percent of the value of the final product.

4) Political Rationale

The QIZ was unilaterally instituted by the United States with the main objective of reaching security goals in the Middle East. Where outward processing scheme embodied in reciprocal FTAs are mostly designed for economic reasons, the QIZ regime differs in its nature. Following this sense, the QIZ can be said to have successfully consolidated good neighborly relations between former enemies (Singer, 2002).

B. Legal Issues of Qualifying Industrial Zone

The QIZ derogates from the territoriality principle under many FTAs. "FTA territory" relates to areas under the customs control of Parties to an FTA. This means that, when any eligible goods are considered to have obtained an FTA-wide origin, only FTA-origin goods are preference-eligible. However, under the QIZ, eligible goods, whether produced in an FTA Party following outward processing in a QIZ or finished in a QIZ by utilizing materials from Parties to an FTA, are considered to be originating in an expanded area comprising the FTA territory and a QIZ in a non-party. Thus, the QIZ is founded on an "FTA-plus territory concept" (Komuro, 2009).

3. Integrated Sourcing Initiative under FTAs

The third type of special rules or origin is the Integrated Sourcing Initiative (ISI), as presented by U.S.-Singapore FTA. The basic idea of ISI in this FTA is that certain goods not produced from Singapore, will be deemed as of Singapore origin if exported via Singaporean port (Rossman, 2004).

A. Rationale of Integrated Sourcing Initiative

1) Regulatory Rationale

The U.S.-Singapore FTA, signed in January 2003 and implemented in December 2003, introduced the outward processing scheme in the form of ISI. Although widely publicized, its definition remains unclear (Komuro, 2009). Nonetheless, according to Article 3.1.c of the FTA, ISI products manufactured based on the outward processing scheme is defined as “One or more processes of manufacture was or were performed in the territory of that Party, by, or on behalf of, the principal manufacturer; One or more processes was or were performed in the territory of that Party by, or on behalf of, the principal manufacturer immediately prior to the export of the goods to the territory of the other Party; and the principal manufacturer in that Party incurred all the costs associated with any process performed in the territory of a non-Party.”

2) Economic Rationale

According to Article 3.2 of the FTA, an outwardly processed end product “is originating goods when imported into its territory from the territory of the other Party.” It does not matter whether goods produced in Indonesian islands – the Bantam and the Bintan or the Riau islands, which are located within twenty kilometers from Singapore Strait – are exported through Singapore following testing operations there or from the Indonesian islands directly. These items will enjoy both tariff-free treatment and a waiver of the “merchandise processing fee” in the U.S., in accordance with Article 2.8. This fee is imposed on importers amounting to 0.21% of the product value by the U.S. customs (Komuro, 2009). Many U.S. multinationals with their headquarters in Singapore can take advantage of the cheap land and labor offered by offshore assembly bases across the Bantam and Bintan.

3) Technical Rationale

The product coverage of the ISI only scale to 266 finished items, mainly Information Technology (IT) and some medical and instrumentation equipment. The United States has already accorded tariff treatment to these products in the non-preferential field as part of its implementation of the WTO Information Technology Agreement (Komuro, 2009).

4) Political Rationale

The Indonesian assembly bases across the Batam and Bintan, could be used as a strategic tool to the United States, with its cheap cost of land and labor. According to Coyle’s evaluation, the United States sought to use the ISI to demonstrate the advantages of free trade to other Southeast Asian countries, to enhance the competitiveness of the U.S. firms by cutting red tape. Moreover, the U.S. was committed to provide economic aid to Indonesia as a policy tool of its

campaign against terrorism (Coyle, 2004), as the scheme was designed and proposed by the United States after September 11, 2001.

B. Legal Issues of Integrated Sourcing Initiative

The 266 ISI products eligible for MFN duty-free treatment need not meet the FTA's rules of origin for preferential purposes. This is similar to the mechanism under North American Free Trade Agreement (NAFTA). According to Article 308 of the NAFTA, each Party shall accord MFN treatment to certain duty-free items. Therefore, what is important to the U.S. is, not where and how the products were assembled, but the consignee is located in Singapore (Komuro, 2009).

CHAPTER IV. GAESEONG INDUSTRIAL COMPLEX (GIC)

1. History of the GIC

The idea to implement the GIC has been under discussion since 1989, as Chung Ju-Yung and Kim Jong-il first met (Kim, 2008). However, Chung Ju-Yung, Hyundai Group's Honorary Chairman initiated the GIC project in 1998. At that time, Chung's leadership of GIC coincided with South Korea's "sunshine policy" under President Kim Dae Jung, which attempted to ameliorate relations with North Korea. Thus the year 2000 became a turning point to inter-Korean relations. As Hyundai Asan attained the approval of Kim Jong-il, on exclusive development right over the GIC, the project was launched in August 22, 2000.

On November 27, 2002, North Korea finally adopted and announced the Gaesong Industrial District Act, by the order of the Permanent Commission of the Supreme People's Assembly, of which appointed the GIC area as a special economic zone. On December 26, Hyundai Asan attained the necessary certificate for the rights to 50 years' use of 16,000 acres of land for the development of the GIC from the North Korean authority. On June 30, 2003, a groundbreaking ceremony took place at last, with the presence of both South and North Korean officials (Lim, 2007). According to Ministry of Unification of South Korea, as of 2012, 123 firms are under operation with output scale amounting to 197.5 million dollars. By 2012, 53,448 North Koreans were working in the industrial park (Ministry of Unification, 2013).

The GIC project allows mutual benefits for both Koreas. It is aimed at maximization of economic synergy between the South and the North as South Korean small to medium-sized firms can fully utilize low-cost supply of labor for product manufacturing from the North. This cycle not only offers jobs to North Koreas but also brings hard currency for Pyongyang. Moreover, the complex is expected to serve as a model for future economic cooperation between the two Koreas. As North Korean economy and the standard of living improve, it is likely that reform and opening of North Korea will be facilitated (Kim, 2008) by an exposure to market economy. Ultimately, GIC may contribute to reducing reunification cost on the Korean Peninsula, based on a balanced development of the both economies.

2. GIC in Korea's FTAs

Thus far, Korea's FTA umbrella includes 45 countries in its effect as of September 2012 (MOFAT, 2013). Among the trading partners are Chile, Singapore, EFTA, ASEAN, India, U.S. and the EU. While outward processing scheme in other countries is generally utilized to alleviate rigidness that is due to production specialization, Korea's FTA outward processing schemes carry more political significance that that, given the peculiar division status of the country. Needless to say, Korea benefits from low-cost Gaeseong processing from the North, attaining comparative advantage to China and South Korea. The main products from Gaeseong are textiles, chemical goods, metals and machinery, and electric and electronic goods. According to 2007 data from the Ministry of Unification, around 80 percent are consumed in South Korea and the balance is exported overseas. Aside from the economic gains anticipated to reap from Gaeseong, incorporating Gaeseong element into Korea's FTAs is crucial. Given the significance that the rules of origin determination from Gaeseong-products could lead to further contribution in building peace and prosperity in the Korean peninsula and even security issues in Asia as a whole, placing GIC as an outward processing zone to FTA negotiation is of a national interest to Korea.

A. Comparison of Gaeseong-Products under Korea's FTAs

To better grasp the status and nature where Korea FTAs stand with its outward processing scheme along GIC, a comparative examination of the negotiation text of 7 FTA partners was conducted. Under the textual arrangement lies the level in which Gaeseong-products are incorporated, as an exemption to rules of origin. However, the manner in which Gaeseong-products are managed differs in terms of scope and its detail. Specific details can be observed from the following figure.

Table 1. Comparison of Korea's FTAs in its Exemption to Rules of Origin

Name of FTA	Main Provision
Korea-Chile FTA	No Provision
	- (Article 4.4 Outward Processing) 134 goods listed in Annex 4C (10 digit HS code) provided that goods fall under the following conditions:

Korea-Singapore FTA	(a) the total value of non-originating inputs as set out in paragraph 2 does not exceed forty (40) per cent of the customs value of the final good for which originating status is claimed; (b) the value of originating materials is not less than forty- five (45) per cent of the customs value of the final good for which originating status is claimed; (c) the materials exported from a Party shall have been wholly obtained or produced in the Party or have undergone there processes of production or operation going beyond the non-qualifying operations in Article 4.16, prior to being exported outside the territory of the Party; (d) the producer of the exported material and the producer of the final good for which originating status is claimed are the same; (e) the re-imported good has been obtained through the processes of production or operation of the exported material; and (f) the last process of production or operation takes place in the territory of the Party. - (Article 4.3 Treatment of Certain Goods) The 4,625 goods (6 digit HS code) listed in Annex 4B shall be originating goods when the goods are imported into the territory of Singapore from the territory of Korea. The goods shall also be originating material for purposes of satisfying the requirements specified in this Chapter
	- (Appendix 4. Exemptions from the Principle of Territoriality to Annex 1)

Korea-EFTA FTA	(a) the total added value as set out in paragraph 5(a) does not exceed 10 per cent of the ex-works price of the final product for which originating status is claimed; (b) the materials exported from the Party concerned shall be wholly obtained in that Party or having undergone working or processing going beyond the insufficient operations listed in Article 6 prior to being exported outside the territory of that Party. - For 267 goods listed in Appendix (6 digit HS code) the acquisition of originating status shall not be affected by working or processing carried out in an area, for instance an industrial zone, outside the territory of a Party, on materials exported from the Party concerned and subsequently re-imported to that Party, provided that: (a) the total value of non-originating input as set out in paragraph 5(b) does not exceed 40 per cent of the ex-works price of the final product for which originating status is claimed; and (b) the value of originating materials exported from the Party concerned is not less than 60 per cent of the total value of materials in manufacturing the re-imported material or product.
Korea-ASEAN FTA	- (Article 6 Treatment of Certain Goods) Letters of Understanding among the parties include goods from outward processing zones to be given tariff benefits - FTA partners, upon mutual agreement limits each countries' number of goods to 100 (6 digit HS code) under the following conditions;

	(a) non-originating good's price is not less than FOB 40 per cent value of the good (b) value of materials before export is more than 60 per cent of total value of the material - In case where ASEAN member countries' domestic market is harmed or subject to be negatively affected, special restrictive measure can be made, which stops application of Article 6 - After 5 years in effect, when ASEAN member countries decide Article 6 brings negative effect to domestic industry, Letter of Understanding can be withdrawn.
Korea-India FTA	- (Article 3.14 Exemption from the Principle of Territoriality) Notwithstanding the provisions of Article 3.13, the acquisition of originating status in accordance with the conditions set out in Articles 3.2 through 3.12 shall not be affected by working or processing carried out in the area agreed by both Parties (9.9 km2 North Korea's Gaeseong Industrial Zone) in the Exchange of Notes on materials exported from the Party concerned and subsequently re-imported there, provided that the conditions set out in Annex 3-B are fulfilled. - Under Annex 3-B-1 Product List Subject to Exemption from the Principle of Territoriality, are listed 108 goods (6 digit HS code); condition to be conferred rules of

	origin, special import restrictive measure, and the right to withdraw is stipulated the same with Korea-ASEAN FTA
Korea-U.S. FTA	- (Annex 22-B Committee on Outward Processing Zones on the Korean Peninsula of Chapter 22. Institutional Provisions and Dispute Settlement) The Parties shall establish a Committee on Outward Processing Zones on the Korean Peninsula. The Committee shall review whether conditions on the Korean Peninsula are appropriate for further economic development through the establishment and development of outward processing zones. - The Committee, comprising of officials of each Party shall meet on the first anniversary of the entry into force of the Agreement and at least once annually thereafter, or at anytime as mutually agreed. - The Committee shall identify geographic areas that may be designated outward processing zones, establish criteria that must be met before goods from any outward processing zone may be considered originating goods for the purpose of this Agreement, including but not limited to: progress toward the denuclearization of the Korean Peninsula; the impact of the outward processing zones on intra-Korean relations; and the environmental standards, labor standards and practices, wage practices and business and management practices prevailing in the outward processing zone, with due reference to the situation prevailing elsewhere in the local economy and the relevant international norms. The Committee shall determine whether any such outward processing zone has met the criteria established by the Committee. The

	Committee shall also establish a maximum threshold for the value of the total input of the originating final good that may be added within the geographic area of the outward processing zone.
Korea-EU FTA	- Stipulated in the identical manner as with the Korea-U.S. FTA

Source: Korea Customs (2013), Office of US Trade Representative (2013)

Korea's first meaningful adoption of outward processing into its FTA was from Korea-Singapore FTA, which was followed by Korea-EFTA FTA and Korea-ASEAN FTA. As what can be observed from the table above, Korea's outward processing scheme is applied and addressed differently depending on geological factors and defining industrial characteristics of individual trade partners. Under these FTAs, there are two types to consider. The first type is a general outward processing scheme without restrictions placed on products. The other type is a restrictive form of outward processing where product listed under 6 digit HS code and 10 digit HS code are allowed under limitation. In Korea-EFTA FTA, both schemes are accepted where as Korea-Singapore FTA and Korea-ASEAN FTA adopts the restrictive type of scheme. However, in case of Korea-EFTA FTA, outward processing is only allowed when its outward processing ratio is below 10%. In case of Korea-Singapore FTA, Korea-EFTA FTA and Korea-ASEAN FTA's restrictive outward processing, the details on product and location, rationales differ respectively. Meanwhile, Korea-U.S. FTA stipulates reasons to establish Committee on Outward Processing Zone on the Korean Peninsula, instead of adopting a restrictive outward processing scheme on GIC. This is due to there being no diplomatic ties established between North Korea and United States. Later, Korea-EU FTA followed suit with the United States.

While Korea continues to pursue a strategy of having outward processing scheme incorporated as part of Korea's FTAs with partners, it could be argued that GIC clause does not perfectly fall under equal status: the agreement varies in its details depending on individual FTAs. Also, it could be easily said that negotiations on outward processing schemes have been too reliant on past cases of concluded FTAs, without placing much effort to unifying the scheme as a 'model template' insert to the FTA text. These observations lead to several policy recommendations to the upcoming Korea-China FTA.

CHAPTER V. CONCLUSION

1. Summary

Under an era of FTA proliferation, Korea avidly initiated series of FTAs according to its FTA roadmap. Korea's key trading partners include Chile, Singapore, EFTA, ASEAN, India and Peru, EU and US, all of which entered into force. Currently negotiating partners include GCC, Australia, New Zealand, Colombia, Canada, Turkey, Mexico and China. Not only that, negotiation preparatory steps as of now is underway with Japan, MERCOSUR, Israel, Vietnam, Central-America, Malaysia and Indonesia.

In this expanding trade structure, Korea's FTA continues to negotiate its trading partners for inclusion of GIC clause into its FTA texts. This is due to the symbolic implication that inter-Korean economic and cultural cooperation of GIC carries and the potential development that is expected in reaching security goals in the Korean Peninsula and in Asia. Though there are numerous literatures that studied different schemes on special rules of origin, many of the existing literatures focused on individual FTA case of special rules of origin. By analyzing three different schemes across the world examined through regulatory, economic, technical, and political rationales, this paper seeks to provide answer to establishing a 'model template' of GIC clause into Korea's future FTAs.

2. Policy Recommendations to Korea-China FTA

An exploration on world's major special rules of origin schemes under FTAs – Outward Processing, Qualifying Industrial Zone, and Integrated Sourcing Initiative – uncovered the similarities and differences across one another. Given the peculiar state of division on Korean Peninsula, it is hard to deny outward processing scheme is largely driven by its political rationale. However, this holds true to not only to GIC but also to upcoming joint economic projects between North Korea and China. According to a state announcement in 2011, North Korea declared China will be participating in joint economic plans over Naseon and Hwanggeumpyong. Though it is hard to estimate when and how the project will be realized, the project is meaningful

in itself because another commitment to engage North Korea in market economy from an isolated state, in a large sense, is being made.

Based on four levels of analysis on special rules of origin regimes, this paper concludes by offering four recommendations to upcoming Korea-China FTA on Korea's dimension. First, on regulatory rationale, Korea-China FTA will need to come up with a 'model template' on GIC so that future outward processing complex from either side can enjoy full benefits of the FTA. Second, on economic rationale, since China is also expected to establish special economic zones based on outward processing, it is important to make more efforts to secure more elements of low cost labor and land from North Korea for opening of new outward processing facilities of similar nature. Third, on technical rationale, origin determination on GIC products may lead to possible violation of WTO rules. In order to avoid this problem, designing the GIC clause without referring to specific area, can be an option as in the case of Korea-EFTA FTA. Last but not the least, on political rationale, it is crucial to continuously persuade China on importance and the influence of joint economic cooperation on positive outcomes on security concerns.

According to Korean government, China has agreed to Korea's request to incorporate the Gaeseong clause into its FTA text (Money Today, 2012). Thus, the same should be addressed in case China requests the recognition of outward processing zones in North Korea. Under an optimistic scenario, North Korea can enjoy expanded economic gains from its trade between Korea and China. In a long term, the outward processing zones of the Koreas may bring stability based on economic cooperation, which ultimately leads to attaining security goals such as peace and prosperity in the region.

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개성공단 물품에 대한 한-중 FTA에의 정책적 함의

국문초록

FTA가 범람하는 현재, 한국에서는 추진하는 FTA에 개성공단 조항을 포함하는 것이 매우 중요하다. 그것은 개성공단의 발전이 향후 남북한 경제 및 협력 관계에 기여할 수 있는 발전 가능성을 내포하기 때문이다. 그러나, 현재 한국의 체결된 FTA를 살펴보면, 개성공단 관련 조항이 FTA별로 상이한 것을 찾아볼 수 있다. 그 문제의 중앙에는 원산지 규정이 있다. 본 논문에서는 한국, 이스라엘, 싱가포르의 원산지 규정에 관한 특례를 분석하였으며 살펴본 결과, 특징별로 (1) 역외가공 (2) QIZ (3) ISI 로 구분지을 수 있다는 결과를 도출하였다. 이러한 결과를 바탕으로, 다가오는 한-중 FTA에 개성공단 조항과 관련하여 법률적, 경제적, 기술적, 그리고 정치적인 측면에서 정책적 함의를 도출하였다.

주요어: 자유무역협정(FTA), 개성공단, 한-중 FTA, 역외가공조항, 원산지규정

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