

Compensation Law are highlights of the legal reform toward a market-oriented economy. In addition, for the first time in the legal history of the DPRK, an official collection of laws and regulations for the public was published (2004). These changes will definitely contribute to the establishment of market institutions.

There are still many risks associated with investment in North Korea, some of which could be alleviated by more legislation or the revision or abolition of other legislation. There are several areas of investment in which it is unnecessarily vague which set of laws takes precedence, or under what circumstances this could change. Continued cooperation and increasing investment will bring these items more to the forefront where it will fall on the collective shoulders of the Supreme People's Assembly to continue to improve the legal framework that provides an environment conducive to foreign investment.

It is, of course, important to enact more sophisticated laws in order to reduce the contradictions and loopholes in this area. However, what is more important is to implement already existing laws and agreements to command the trust of the international community as well as South Korean investors.

The Legal Framework of the Gaesung Industrial Complex

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Abstract

Since the 2000 inter-Korean Summit, the two Koreas have continuously carried out the Gaesung Project while overcoming some challenges. At the outset of the Gaesung Project, North Korea's military objected to opening the Gaesung by reason of the military defense line. North Korea made the decision to open the Gaesung toward South Korea to revitalize its economy by persuading its military to tolerate the Gaesung Project. Meanwhile, in the summer of 2002, when the two Koreas began to move ahead with the Gaesung Project by re-connecting the inter-Korean expressway and railroad crossing the DMZ, the United States strongly resisted the two Koreas' attempts. Immediately afterwards, the two Koreas agreed on a detailed schedule for the reconnection of the inter-Korean expressway and railroad and North Korea designated Shinuiju, Kungangsan and Gaesung as special economic zones. To date, the two Koreas have established, through painstaking negotiations, the foundational work for the Gaesung ICZ's legal system.

This article attempts to investigate the legal framework of the Gaesung Industrial Complex, focusing on the Gaesung Industrial Complex Zone Law enacted in 2002. After conducting a detailed discussion on the various aspects of the law such as the administrative structure, foreign currency control and taxation, the author looks into the factors that are necessary for the successful development of the Zone.

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I. Introduction

From the early 1990's to the present, the Democratic People's Republic of Korea ("North Korea") has faced substantial economic hardships. During that time, due to a prolonged shortage of energy and raw materials, many factories were forced to shut down and the production of fertilizers was reduced substantially. In addition to such structural problems, a series of droughts and massive floods triggered numerous food crises throughout 1995 to 1997, resulting in the reported deaths of at least one million North Koreans.¹⁾ The conditions were so severe that immediately following the massive flood in the summer of 1995, on August 23, 1995, North Korea was forced to seek emergency relief from the United Nations. Since 1996 to the spring of 2004, North Korea has received approximately US\$ 219,541,000 in international aid of which 91% was in the form of foodstuffs.²⁾ According to the United Nations, an additional US\$ 208,928,930 for the years 2004-2005 was required to meet the assessed humanitarian needs in North Korea.³⁾

North Korea's dire economic state has been attributed to many structural factors such as the inefficiency in its centrally planned economy, the distorted allocation of resources with an excessive focus on the military or heavy industries, and the steep decline of petroleum and high-tech equipment imported from the U.S.S.R and other communist countries after their collapse. In this regard, some analysts attribute

1) See Daniel A. Pinkston and Phillip C. Saunders, "Seeing North Korea Clearly," (Center For Nonproliferation Studies: August 26, 2003), pp. 84-5. (Available at <http://cns.miis.edu/research/korea/450079.pdf>; last visited May 3, 2005). In this regard, Andrew Natsios asserted that two or three million people died of starvation and hunger-related illness. See Andrew Natsios, "The Politics of Famine in North Korea, Special Report" (United States Institute of Peace: August 2, 1999). (Available at <http://www.usip.org/pubs/specialreports/sr990802.html>; last visited May 3, 2005). Meanwhile, as Pinkston and Saunders explained as to the food crisis in North Korea, "the Korean Peninsula has experienced periodic spring famines for centuries due to mountainous terrain, limited arable land, and a relatively short growing season." "[South Korea] now avoids food shortages by exporting products that earn sufficient exchange to import food", but "[North Korea]'s failure to produce exportable goods has made this option difficult" to implement in practice.

2) See Tae-Jin, Kwon, "Kuk-je Sa-hoe-ui Dae-buk Ji-won Tong-hyang-kwa Wu-ri-ui Dae-eung Jeon-ryak [Trend of International Society's Aid to North Korea; and Our Strategy]", *Buk-han Nong-eop Tong-hyang [Agricultural Trend of North Korea]*, Volume 6-3, (October, 2004), p. 94. (Available at <http://www.krei.re.kr/issue/index.php?vKey=NK00023&vDown=read&vTop=1&vPage=1&vBid=:> last visited May 3, 2005)

3) See Consolidated Appeal Process (CAP), Democratic People's Republic of Korea 2004 (Revision), (United Nations: June 9, 2004), p. 1. (Available at [http://ochadms.unog.ch/quickplace/cap/main.nsf/h_Index/MYR_2004_DPRK/\\$FILE/MYR_2004_DPRK_SCREEN.PDF?OpenElement](http://ochadms.unog.ch/quickplace/cap/main.nsf/h_Index/MYR_2004_DPRK/$FILE/MYR_2004_DPRK_SCREEN.PDF?OpenElement); last visited May 3, 2005)

North Korea's economic difficulties to its current regime or political system, concluding that any meaningful improvement in North Korea will only be brought by a change in the current regime.⁴⁾ While such an assertion may hold some persuasive weight, a sudden collapse of the current North Korea regime will not address North Korea's fundamental economic problems. Rather, such a collapse may lead to a national disaster for the Republic of Korea ("South Korea"), caused by millions of North Koreans flooding into South Korea to seek refuge and jobs.⁵⁾ China and Vietnam have, to some extent, been successful in pursuing their open door policies under the title of a "socialist market economy," normalizing their diplomatic relationship with the United States. North Korea might also follow the same path toward a market economy. From South Korea's perspective, the following are more desirable options to pursue: (i) for North Korea to reform its economic structure steadily and successfully; (ii) for South Korea to assist North Korea in its transition toward a market economy; and (iii) for South and North Korea to jointly pursue policies that will steadily and continuously strengthen inter-Korean economic cooperation.

For the past fifteen years, North Korea has tried to expand its contacts by seeking economic and political cooperation with the Western countries, especially the United States, Japan, and South Korea in order to revitalize its economy and stabilize its regime by taking a number of critical measures that would put it on the road toward a market economy.⁶⁾ Most of the measures taken by North Korea seem to have been modeled after China's open door policy. While many projects with respect to North Korea's open door policy failed due to North Korea's half-hearted implementations

4) See Nicholas Eberstadt, "Tear Down This Tyranny: A Korea strategy for Bush's second term," *The Weekly Standard*, November 29, 2004. (Available at <http://www.weeklystandard.com/Content/Public/Articles/000/000/004/951szxxd.asp>; last visited May 3, 2005); Jim Lobe, "Hawks Push Regime Change in North Korea," *ANTIWAR.COM*, November 23, 2004. (Available at <http://www.antiwar.com/lobe/?articleid=4036>; last visited May 3, 2005)

5) Seung Park, the Governor of the Bank of Korea, expressed this opinion in his speech at the Asia Society meeting in New York, held on June 3, 2004. (This speech is available at http://www.bok.or.kr/template/main/default/introduction/view.jsp?id=IN0000032987&tbl=tbl_FM0000000066_CA000000383&SearchKeyWord=&page=1; last visited May 3, 2005) Seung Park's opinion constitutes the predominant view held by South Korean officials.

6) Hak-Soon Paik, "Continuity or Change? The New U.S. Policy Toward North Korea," *East Asian Review*, The Institute for East Asian Studies, Vol.13, No.2, (Summer 2001), pp. 24-26.

and military confrontation with the United States, some projects focusing on inter-Korean transactions and cooperation are in progress. Among the ongoing inter-Korean projects relating to North Korea's special economic zones is the development of the Gaesung Industrial Complex (the "Gaesung Project"), which is mainly targeted at the South Korean market. The Gaesung Industrial Complex Zone (the "Gaesung ICZ") is located at the southwestern area of North Korea, bordering on the Demilitarization Zone (the "DMZ").⁷⁾ The North Korean military initially objected to the Gaesung Project because a South Korean company was entrusted with the management of the Gaesung ICZ, which would result in the retreat of North Korea's line of defense from the DMZ to the northern part of the Gaesung ICZ. North Korea's eventual participation in the Gaesung Project shows its serious, almost desperate, attitude toward inter-Korean economic cooperation. Furthermore, the Gaesung Project has contributed to easing the military tension between the two Koreas, and it is seen as a symbol of inter-Korean economic cooperation based on the combination of South Korea's capital and technology and North Korea's labor. The Gaesung ICZ's success will further a peaceful reunification of the two Koreas based on the principles of democracy and market economy.

This paper will offer a general overview of the legal framework for the Gaesung ICZ. Since the Gaesung ICZ's legal framework has been based on North Korea's past economic reform experiments, Part II will briefly review North Korea's previous open door policy and its legal reform. This review will suggest that North Korea has been steadily progressing, despite some setbacks, toward a market economy by continuously improving its open door policy. In Part III, this paper will introduce the Gaesung ICZ's legal framework consisting of inter-Korean agreements and North Korea's law and regulations. More specifically, Part III.C will suggest that inter-Korean agreements provide investors with, to some extent, protection for their rights and assets. Part III.D will introduce North Korea's existing law and implementing regulations for the Gaesung ICZ. Finally, Parts IV and V will evaluate the Gaesung ICZ's legal system.

7) The Demilitarized Zone or the DMZ is the buffer zone established under the Armistice Agreement dated July 27, 1953, ceasing the Korean War. The parties to the Armistice Agreement are the commander of United Nations Forces, the commander of North Korea Forces and the commander of China's People's Forces. Each party retreated two kilometers immediately thereafter. The DMZ is the area in which it was promised that it would be prohibited to station an army, deploy arms, and install military facilities.

II. North Korea's Open Door Policy and Legal Reform

A. First Experiment: Equity Joint Venture Law of 1984

Originally, North Korea pursued a self-reliant and centrally planned economy but, from the 1950's through the 1970's, it received approximately US\$ 3.5 billion of grants and loans from the U.S.S.R and other socialist countries. In 1975, due to its trade deficits, North Korea was forced to default on its international debts. Thereafter, it could not obtain any loans from international financial institutions, and its inability to export made it impossible to collect foreign currency from the Western countries. Under these circumstances, North Korea adopted a policy⁸⁾ to acquire foreign currency by enacting the Equity Joint Venture Law of 1984⁹⁾ which permitted foreign investors and Koreans residing abroad (excluding South Korean citizens living in South Korea) to establish an equity joint venture or a limited liability company in North Korea through contracts with various North Korean institutions, enterprises, or organizations. Under the Equity Joint Venture Law of 1984, foreign investors were officially allowed to directly invest in North Korea.¹⁰⁾

Ten years after the law went into effect, around 140 contracts worth approximately US\$ 150 million in investments were executed, with most of the amount originating from Koreans residing in Japan.¹¹⁾ However, most of the investments eventually failed, and only a few additional investments under the law were procured mostly from Koreans residing in Japan. Ultimately, the Equity Joint

8) This policy was announced in the resolution on "strengthening the South-the South cooperation and external economic activities and further developing foreign trade" adopted at the third session of the 7th Supreme People's Congress in 1984. This shift in North Korea's policy regarding foreign direct investment was caused not only by the shortage of foreign currency but was also prompted by the success of the Chinese Joint Venture Law promulgated on August 1979.

9) For more details on the Equity Joint Venture Law of 1984, see Eric Yong-Joong Lee, "Development of North Korea's Legal Regime Governing Foreign Business Cooperation: A Revisit under the New Socialist Constitution of 1998," 21 *NW. J. INT'L L. & BUS.* 199. (Fall 2000) ("Eric Yong-Joong Lee 2000"), pp. 201-203. (Available at LexisNexis.).

10) Subsequently, North Korea promulgated the Equity Joint Venture Taxation Law and the Foreigner Income Taxation Law in 1985.

11) See Hong-Taek Cheon, "Buk-han Kyeong-je Gae-bal: 1945-95 [Economic Development of North Korea: 1945-95]," *Buk-han Kyeong-je Yeon-gu [Research on North Korea's Economy]*, Vol.1. Korean Development Economics Association (1995), ("Hong-Taek Cheon"), p. 96.

Venture Law of 1984 failed due to North Korea's poor credit worthiness and rigid social structure. Even though the Equity Joint Venture Law of 1984 provided foreign investors with the right to manage their company in proportion to their investments, they were not allowed to exercise such rights because the North Korean counterparties did not understand the corporate governance of a joint venture company and insisted on their own style of management.¹²⁾ Moreover, if North Korean counterparties breached the joint venture agreement, the foreign investors had no appropriate dispute resolution procedure available to them in practice. Subsequently, of the joint venture companies invested in by Koreans residing in Japan, no less than 48% shut down their factories by 1996.¹³⁾

Nonetheless, the Equity Joint Venture Law of 1984 was noteworthy in that North Korea, for the first time, legalized economic collaboration with capitalist countries, even though the Equity Joint Venture Law of 1984 lacked a constitutional ground.¹⁴⁾

B. Limited Open Door Policy: the Rajin-Sonbong Free Economic and Trade Zone

In 1988, North Korea's trade volume totaled US\$ 5.240 billion¹⁵⁾, comprising mostly of trades with the U.S.S.R, China and other Eastern European communist countries that were typically settled by barter or on a subsidized basis. However, following the collapse of the Soviet Bloc (the U.S.S.R and Eastern European communist regimes) and China's economic reform, these countries began insisting on settling their trades on a hard currency basis. Since North Korea did not possess sufficient foreign currency to pay for the imports, its trade with these countries dropped off significantly. North Korea's trades with the U.S.S.R/Russia, in particular, decreased substantially from US\$ 2.223 billion (53.3%)¹⁶⁾ in 1990 to US\$

12) See Korea Institute of International Economy Policy, 2002 Buk-han Kyeong-je Baek-seo [2002 White Paper on North Korea's Economy] (February 27, 2003), ("White Paper on NK Economy"), p. 500.

13) *Ibid.*, p. 501.

14) See Dae-Kyu Yoon, "The Constitution of North Korea: It's Changes and Implication," 27 *Fordham Int'l L.J.* 1289 (April, 2004) ("Dae-Kyu Yoon, 2004"), p. 1300 (Available at LexisNexis).

15) Korea Institute of International Economy Policy, *supra* note 12, p. 55.

16) The figures in the parenthesis refer to North Korea's trade volume with the U.S.S.R/Russia as a percentage of North Korea's total trade volume for the respective year.

364 million (13.4%) in 1991 and to US\$ 46 million (3%) in 2000.¹⁷⁾ Since the U.S.S.R/Russia had been North Korea's primary source for energy and machinery needs, the steep decline in imports from the U.S.S.R./Russia triggered a severe shortage of energy, and in turn led to a sharp decrease in the operating rate of its industrial facilities.¹⁸⁾ Moreover, the U.S.S.R/Russia established a diplomatic relationship with South Korea in 1990, and other Eastern European countries followed from 1988 to 1993. As a result, North Korea was isolated economically and politically from the international community, which prompted it to devise its own survival strategy.

As a strategy to survive as a state and revitalize its economy, North Korea sought economic cooperation from South Korea, Japan, the United States and other Western countries, especially trying to normalize diplomatic relations with the United States and Japan. In response to South Korea's active measures toward inter-Korean cooperation¹⁹⁾, North Korea announced its coexistence policy by executing with South Korea the "Agreement on Reconciliation, Non-aggression, and Exchanges and Cooperation between South and North Korea" on December 13, 1991 (the "Basic Inter-Korean Agreement").²⁰⁾ North Korea adopted its revised constitution of 1992 (the "NK Constitution of 1992") providing for a peaceful unification of the two

17) Korea Institute of International Economy Policy, *supra* note 12, p.507.

18) According to Bank of Korea estimates, the operating rates of North Korea's industrial facilities in 1996 were as follows: 20% for iron facilities, 25% for auto plants, 31% for cement plants, 27% for chemical fertilizer facilities, and 22% for textile industries. (See Korea Institute of International Economy Policy, *supra* note 12, p. 509.)

19) It is noteworthy that South Korea's policy toward North Korea influenced North Korea's policy regarding the inter-Korean relationship. The South Korean government announced the "July 7, 1988 Declaration", a new inter-Korean economy policy permitting South Korean companies to invest in North Korea in 1988, and subsequently promulgated "the Guide for the Inter-Korean Exchange and Cooperation of 1990" and "the Law regarding the Inter-Korean Exchange and Cooperation of 1990" in order to legalize inter-Korean transactions.

20) The Basic Inter-Korea Agreement came into effect on February 19, 1992 and provides that the relationship between the two Koreas is not one between two different countries, but a special one constituted temporarily toward reunification. Both South and North Korea have officially recognized each other not as a foreign country but a *de facto* government under the Basic Inter-Korean Agreement. Reflecting such changes, the Constitutional Court of South Korea held that North Korea should be recognized as the partner for reconciliation and cooperation in the process of peaceful reunification of the two Koreas as well as the anti-state organization having the intent to scheme the overthrow of South Korea's government from South Korea's point of view. (See the Korean Constitutional Court Decision No. 92henn-ba48 dated July 27, 1993). Notwithstanding the above, unlike the Four Inter-Korean Agreements discussed below, the Supreme Court of South Korea held that the Basic Inter-Korea Agreement was not

Koreas²¹⁾, which has been the constitutional ground for North Korea's policy regarding inter-Korean cooperation.²²⁾

Since 1988, North Korea has tried to normalize its relationship with the United States. To this end, at the request of the United States, it signed the "South-North Korea's Joint Declaration on the Denuclearization of the Korean Peninsula" with South Korea on January 20, 1992²³⁾ and the safeguards agreement necessary for implementing the statute of the International Atomic Energy Agency (the "IAEA") on January 30, 1992. On April 10, 1992, North Korea's legislature consecutively ratified the safeguards agreement.²⁴⁾ Even though there were arguments regarding the transparency of North Korea's nuclear facilities, the first round of the North Korea nuclear crisis triggered by North Korea's 1993 declaration of withdrawal from the Treaty of Non-Proliferation of Nuclear Weapons concluded with the signing of the Geneva Agreed Framework (the "Agreed Framework") between the United States

legally binding between South and North Korea due to the lack of the ratification by the National Assembly of South Korea. (See the Supreme Court Decision No. 98du 14525 dated July 23, 1999).

21) See the NK Constitution of 1992, Article 9.

22) In 1992, both South and North Korea regularly discussed many issues at the inter-Korean high-level talks to implement the Basic Inter-Korean Agreement. Especially, the South Korean government and Daewoo Group tried to establish an industrial complex in Nampo, a port located at the southwest part of Pyongyang, North Korea. For this end, a joint survey group consisting of Daewoo Group and South Korean government officials visited Nampo, in October 1992. See Ministry of Unification website/Library/Chronicles available at <http://www.unikorea.go.kr/> (last visited September 6, 2005). At that time, the inter-Korean relationship was substantially developed compared to the past hostile confrontation period. However, according to Se-hyun Cheong, a former Minister of Unification, who played a key role in the inter-Korean relationship during the period from 1990 to 2003, the amicable mood between the two Koreas had abruptly been suspended due to the first round of the North Korea nuclear crisis initiated by the United States. See Sang-Hyun Eom, "Cheong Se-hyun ui Taek-gang: Mi-guk-eun Nam-buk-Kwan-kye Ho-jeon Doel Ddea-ma-da Buk-haek Ui-hok Je-gi [Se-hyun Cheong's Special Lecture; the United States raised North Korean Nuclear Issues when inter-Korean relationship improved considerably]," *Shindonga* (March 2005). This article is available at <http://shindonga.donga.com/> (last visited May 3, 2005).

23) This joint declaration contains the following commitments: (i) not to test, manufacture, produce, receive, possess, store, deploy or use nuclear weapons, (ii) only to use nuclear energy solely for peaceful purposes, and (iii) not to possess nuclear reprocessing and uranium enrichment facilities. (This joint declaration is available at <http://www.unikorea.go.kr/>; last visited September 3, 2005)

24) North Korea became a member of the IAEA in 1977, and a party to the Treaty of Non-Proliferation of Nuclear Weapons (the "NPT") in 1985. However it was not until 1992 when North Korea signed the implementing agreement with the IAEA. (See, Eric Yong-Joong Lee, "The Six-Party Talks and the North Korean Nuclear Dispute Resolution Under the IAEA Safeguards Regime," *5 Asian-Pacific L. & Pol'y J.* 101, (2004) ("Eric Yong-Joong Lee 2004"), pp. 103-104.)

and North Korea on October 21, 1994.^{25) 26)}

As another strategy to revitalize its economy, North Korea pursued the development of the Rajin-Sonbong area located on the northeastern part of North Korea. Modeled after China's open door policy, the Rajin-Sonbong area was designated as a Free Economic and Trade Zone (the "Rajin-Sonbong FETZ") on December 28, 1991.^{27) 28)} The Rajin-Sonbong FETZ initially took up 671 km² in December 1991, and was extended to 746 km² in September 1993. The Committee

25) The Agreement Framework consists of three documents: (a) the Main Agreement dated October 21, 1994, (b) the Memorandum of Understanding dated October 21, 1994, and (c) President Clinton's Letter to Kim Jong Il dated October 20, 1994. The Agreed Framework was a result of the package deal resolving two key concerns of both parties: freezing and dismantling North Korea's suspected nuclear weapon program from the United States' perspective, and normalizing the relationship between the United States and North Korea from North Korea's perspective. The Agreed Framework provides for the following resolutions: (i) the United States shall replace North Korea's graphite-moderated reactors and related facilities with two Light-Water Reactor ("LWR") power plants with a total generating capacity of approximately 2000 MW(e); (ii) the United States shall supply 500,000 tons of heavy oil annually to North Korea by the completion date of construction of the first LWR unit to offset the energy foregone due to the freeze of North Korea's graphite-moderated reactors; (iii) North Korea shall freeze its graphite moderated reactors and related facilities during the LWR project and, upon completion of the LWR project, to dismantle these reactors; (iv) both parties to move toward full normalization of political and economical relations (including reduction of trade barriers, opening a liaison office in the other party's capital, upgrading bilateral relations to the Ambassadorial level, within three months of the execution date); and (v) North Korea to remain under the regime of the NPT, and keep the safeguard agreements with the IAEA. Immediately after execution of the Agreed Framework, the United States reviewed the normalization process with North Korea. See Zachary S. Davis, Larry A. Nikshe, Larry Q. Nowels, Vladimir N. Pregelj, Rinn-Sup Shinn and Robert G. Sutter, "Korea: Procedural and Jurisdictional Questions Regarding Possible Normalization of Relations With North Korea," Congressional Research Service: Report for Congress 94-933 S, November 29, 1994. (Available at <http://www.globalsecurity.org/wmd/library/report/crs/94-933s.htm>; last visited May 3, 2005)

26) For communist countries seeking economic and political cooperation with the Western countries, normalization with the United States played an important role in easing or ending the United States' economic sanctions against them. In case of Vietnam, the United States put an end to its trade embargo on Vietnam in February 1994, and established the normal diplomatic relationship with Vietnam in 1997, signed the bilateral trade agreement with Vietnam in 2001. (See Mark E. Manyin, "The Vietnam-U.S. Normalization Process," CRS Issue Brief for Congress, November 28, 2001.) In the case of China, even though it normalized the relationship with the United States at the outset of its economic reform, it had to negotiate with the United States on economic sanctions or trade embargo by the 2000s.

27) According to James Cotton, an Australian researcher, North Korea explained its policy shift in 1996 as follows: "the sudden collapse of the socialist market, which had accounted for 70-80% of the total volume of [North Korea]'s foreign trade, necessitated [North Korea] to take a new approach in [adopting] the form, method and subject of [North Korea's] external economic exchange. On the other hand, the end of the East-West cold war provided favorable conditions for developing economic exchanges on a wider scale of the countries in the region

on the Promotion of External Economic Cooperation (the “CPEEC”) of North Korea and its Chairman Jeong-U Kim took charge of the development of the Rajin-Sonbong FETZ. By 2012, North Korea originally planned to develop the Rajin-Sonbong FETZ into (i) an international freight terminal for Northeast Asia, (ii) an export processing center, and (iii) a tourist and financial service center.²⁹⁾ Reportedly, this development plan was originally based on, and closely related to, the Tumen River Area Development Programme (the “TRADP”)³⁰⁾, the regional cooperation project for Northeast Asia that had been supported by the United Nations Development Programme (“UNDP”) and the United Nations Industrial Development Organization (“UNIDO”). Under the TRADP, North Korea, China, Japan, Russia, Mongolia and South Korea attempted to create a free-trade zone in

and the rest of the world.” (See James Cotton, “The Rajin-Sonbong Free Economic and Trade Zone Experiment: North Korea in Pursuit of New International Linkages,” Working Paper No. 1996/9 (“James Cotton”), p. 9.) (Available at <http://rspas.anu.edu.au/ir/working%20papers/96-9.pdf>; last visited May 3, 2005).

28) According to Young Namkoong, “the establishment of a special economic zone is a way to minimize the risk of change in political system accompanying an all-out opening, witnessed in the Eastern Europe. [S]ince late 1993, North Korea built a fence of 3.6m in height and 80km in length around the 746 km² meter free economic and trade zone to cut it off from the domestic economy.” (See Young Namkoong, “North Korean External Economic Policies and Inter-Korean Economic Cooperation” (“Young Namkoong”), p. 6. This paper was presented at the Annual Conference organized by the Political Science Association, England, held on March 23-25, 1999, University of Nottingham, England.)

29) Jong-U Kim, Chairman of CPEEC, explained this plan in his speech at the Rajin-Sonbong Investment Promotion Seminar held in Tokyo on July 15, 1996. The full text of his speech in the title of ‘DPRK’ Policy on Development of Rajin-Sonbong Area’ (“Jong-U Kim 1996 Speech”) is available at http://210.145.168.243/pk/009th_issue/97091703.htm (last visited September 6, 2005).

30) The Tumen River is located in Northeast Asia and acts as a border between North Korea and China in its upper reaches, and between North Korea and Russia near the mouth thereof. The Tumen River area covers the Rajin-Sonbong area in North Korea, the Hunchun area in China and the Nakhoka area in Russia. James Cotton explained that the TRADP was suggested at the conference in 1991, where the Northeast Asian Economic Forum was established. (See James Cotton, *supra* note 27, p. 1.) However, according to the West-East Center, a U.S. research center based in Honolulu, Hawaii, “the idea of a Northeast Economic sphere was suggested at the 1988 Niigata Conference in Japan organized by [Dr. Okita Sabur, former Japanese Minister of Foreign Affairs] and Dr. Lee-Jay Cho of the East-West Center. Around the same time, [Dr. Jian Song], Chairman of the State Science and Technology Commission of China, was considering the possibilities of developing the Tumen River Basin. Dr. Song and Dr. Cho organized the 1990 Changchun Conference on Northeast Asian Development. The UNDP subsequently undertook the implementation of the TRADP.” (See its website http://www.eastwestcenter.org/resources-detail.asp?masthead=sem-header.asp&mastgraph=mast-sem-ld.gif&resource_ID=268; last visited September 6, 2005) For more information regarding TRADP, see the TumenNet website (<http://www.tumennet.org/tumenriver/tumenriver.html>; last visited September 6, 2005)

the Tumen River area. The Tumen River area was envisioned as the transportation and trading hub for Northeast Asia.

Meanwhile, to provide a legal framework for the development of the Rajin-Sonbong FETZ, North Korea enacted a series of laws and regulations. North Korea adopted the NK Constitution of 1992 as the basis for attracting foreign investment.³¹⁾ Immediately following the adoption of the NK Constitution of 1992, North Korea promulgated a series of laws and regulations on foreign investments. Key laws among them are as follows: (i) the Foreigner’s Investment Law of 1992 (later revised in 1999) which permitted three types of foreign-invested companies in North Korea, equity and contractual joint venture companies and wholly foreign-owned companies³²⁾; (ii) the Contractual Joint Venture Law of 1992; (iii) the Foreigner’s Enterprise Law of 1992; (iv) the Revised Equity Joint Venture Law of 1994 (later revised again in 1999); (v) the Law on the Free Economic and Trade Zone of 1993 (later revised in 1999); (vi) the Law on Taxes on Foreign-Invested Enterprise and Foreigners of 1993 (later revised in 1999); (vii) the Land Lease Law; (viii) the Foreign Exchange Control Law of 1993; (ix) the Foreign Invested Bank Law of 1993; (x) the Customs Law of 1993; (xi) the Civil Procedure Law of 1994; (xii) the External Economic Contract Law of 1995; (xiii) the Insurance Law of 1995; (xiv) the Regulations on Free Trade Ports; and (xv) the Labor Regulations for Foreign

31) The NK Constitution of 1992, Article 37 provides that “the State shall encourage institutions, enterprises or associations to establish and operate equity and contractual joint venture enterprises with corporations or individuals of foreign countries”. This provision was understood as the initial constitutional ground for the State to adopt an open-door policy to attract foreign investment.

32) First, an equity joint venture refers to a limited liability corporation where investors from foreign countries invest jointly, operate the business jointly, and enjoy profits in proportion to their investment shares. See the Foreigner’s Investment Law of 1999, Article 2. For more details, see the Equity Joint Venture Law of 1984 (revised in 1999) and its implementing regulations. Second, a contractual joint venture refers to a limited corporation where North Korean and foreign investors invest jointly and share the profits in accordance with the terms of the contract, but only the North Korean party may manage the operation of the joint venture. See the Foreigner’s Investment Law of 1999, Article 2. For more details, see the Contractual Joint Venture Law of 1992 (revised in 1999) and its implementing regulations. Third, the wholly foreign-owned enterprise refers to a corporation owned and operated exclusively by a foreign investor, but which is subject to various restrictions and regulations. See the Foreigner’s Investment Law of 1999, Article 2. For more details, see the Foreigner’s Enterprise Law of 1992 (revised in 1999) and its implementing regulations. Further, wholly foreign-owned enterprises may be established only in the Rajin-Sonbong FETZ, while equity joint ventures and contractual joint ventures may be established anywhere in North Korea. See, the Foreign Enterprise Law of 1999, Article 6.

Invested Enterprise.³³⁾ The legal system for the Rajin-Sonbong FETZ was modeled after that of China and was more sophisticated and attractive than the Equity Joint Venture Law of 1984.³⁴⁾ For the first time, wholly foreign-owned companies were permitted in the Rajin-Sonbong FETZ. These laws and regulations also offered preferential treatment (including tax incentives) to foreign investors and guaranteed their right to freely remit profits. Of particular importance was Article 19 of the Foreign Investment Law of 1992, in which North Korea guaranteed to secure foreign investors' property by declaring that the "foreign invested enterprises, and the assets invested by foreign investors, shall not be subject to nationalization or seizure by North Korea. And, should unavoidable circumstances make it necessary to nationalize or seize such enterprises and assets invested by foreign investors, appropriate compensation shall be paid."³⁵⁾ In addition, these laws provided foreign investors with the right to file lawsuits in the North Korean courts or submit a claim to arbitration in North Korea or in another country to resolve disputes arising out of their investments in North Korea.³⁶⁾ However, although the allowance of a third country-based arbitration is a noteworthy development, its value remains unclear since North Korea is not a party to any relevant international convention on enforcement of foreign judgments and arbitrations. Thus it is dubious whether any

33) From 1992 to 2000, North Korea promulgated 57 laws and regulations related to foreign investment, especially the Rajin-Sonbong FETZ. For more details, see the following articles: (1) Greyson Bryan, Scott Horton & Robin Radin, "Foreign Investment Laws and Regulations of The Democratic People's Republic of Korea," 21 *Fordham Int'l L.J.* 1677 (June, 1998) (Available at LexisNexis.); (2) Haksoo Ko, "Foreign Investment In North Korea: An Assessment of Recent Laws and Regulations," 38 *Va. J. Int'l*, 221 (Winter 1998) (Available at LexisNexis.); and (3) Eric Yong-Joong Lee (Fall, 2000).

34) In this regard, Jong-U Kim remarked on the legal system of the Rajin-Sonbong FETZ as follows: "[North Korea] has directed considerable efforts to alleviating the inconvenience which may be caused by the difference in the legal system and institutional systems with regard to the investment and operational activities to be undertaken by foreign investors. Ours is a socialist country, in which the socialist system and law prevail throughout the social and economic life of the people. [North Korea] proclaimed [the Rajin-Sonbong FETZ] as a zone functioning under the unique economic regime instituted by the state and established in it a universally accepted system customary to other similar zones in the world." (See Jong-U Kim 1996 Speech, *supra* note 29). According to Jong-U Kim, North Korea seems to have implanted the legal system of capitalism into the Rajin-Sonbong FETZ for the first time.

35) However, the above law did not define the concept of "nationalization" and "appropriate compensation", therefore the issues as to (i) whether certain measures taken by North Korea constitute 'nationalization' and (ii) the amount to be compensated in case of nationalization remain arguable.

36) See the Foreign Investment Law of 1992, Article 22; the Law on the Free Economic and Trade Zone of 1993, Article 42.

arbitration award rendered under a foreign country's arbitral procedure can be enforced in North Korea. In this regard, Sang-Jick Yoon analyzed, in 1997, that North Korea's foreign investment laws had the following characteristics: (1) a passive policy toward foreign investment: its foreign investment laws are in fact applicable only to the Rajin-Sonbong FETZ for socialist system defense; (2) underdeveloped legal drafting: many laws and regulations contain undefined or ambiguous terms and there are inconsistencies among some laws and regulations; and (3) an incomplete legal structure: some laws and regulations are based on the basic laws such as civil code and corporation laws but no basic laws have been enacted, and some laws and regulations regulating other specific areas remained to be formed.³⁷⁾

North Korea's target for foreign investment in the Rajin-Sonbong FETZ was initially set at US\$ 4.73 billion. However, despite considerable publicity efforts to invite foreign investments in the mid-1990s, North Korea's contracted foreign investments stood at US\$ 750 million as of March 1999. Of that figure, only US\$ 140 million was actually exercised.³⁸⁾ Such failure was attributed to several reasons.

37) For more details, see Sang-Jick Yoon, "Critical Issues on the Foreign Investment Laws of North Korea for Foreign Investors," 15 *Wis. Int'l L.J.* 325, pp. 330-333, (Spring, 1997) (Available at LexisNexis.) The above characteristics seem to be due to the fact that the Rajin-Sonbong FETZ's legal system was modeled after China's foreign investment law. For reference, according to Peter Howard Corne, the legal drafting in China's foreign investment laws and regulations have the following characteristics: (i) principle-like pronouncements (some laws do "not specify who the authority is and whether there is more than one authority"); (ii) vagueness and ambiguity (these features "grant the implementing authority the power to determine the legal meaning itself through subservient enactments, formal legislative interpretation or ad hoc case-by-case interpretations"); (iii) undefined terms (i.e. "certain periods of time", "advanced technology", "especially serious case" etc.; such undefined terms "produces a great amount of discretion for implementing authorities to interpret [such] terms as it fits"); (iv) broadly worded discretions (since the administrative authority played a key role in initiating and drafting laws and regulations, many broadly worded terms were inserted so as to grant the implementing authority more discretionary power); (v) omissions (some laws refer only to the "relevant Chinese laws and regulations", even though no sets of regulations to be applied to the pertinent area exist); and (vi) general catch-all clauses (these clauses "serve to invest an implementing authority with the option of extending the scope of regulation without the necessity for legislative amending"). See Peter Howard Corne, "Lateral Movements: Legal Flexibility and Foreign Investment Regulation in China," 27 *Case W. Res. J. Int'l L.* 247 (Spring/Summer 1995), pp. 253-262.

38) Korea Institute of International Economy Policy, *supra* note 12, pp. 513-4. According to Young Namkoong, "compared to China and Vietnam, actual cases and the scale of foreign inducement into North Korea [were] disappointing." Because "[f]oreign capital inflow into China has been increasing since December 1978. As a result, during 1997, investment contracts equivalent to US\$ 61.7 billion were concluded and the amount of money actually invested was US\$ 64.0 billion." (See Young Namkoong, *supra* note 28, p. 7-8.)

First, the delay of the TRADP seemed to have had a negative influence on foreign investment in the Rajin-Sonbong FETZ.³⁹⁾ While the Agreed Framework promising comprehensive improvement of the United States-North Korea relationship induced 95% of foreign investment in the Rajin-Sonbong FETZ⁴⁰⁾, the United States' delay in lifting its economic sanctions against North Korea and the political and military tension between the United States and North Korea during the late 1990's caused foreign investors to hesitate to invest in the Rajin-Sonbong FETZ. More importantly, North Korea retreated from its open door policy worrying about its regime stability and the Rajin-Sonbong FETZ's negative influence on the other areas. For example, it built barbed-wire fences and entanglements around the Rajin-Sonbong FETZ in the mid-1990s, and twice (in 1996 and 1998) forbade South Korean delegations to attend the Rajin-Sonbong Zone International Business and Investment Forum there.⁴¹⁾ Also, in February 1998, Jeong-U Kim was stripped of his position as the Chairman of CPEEC and was placed under house arrest.⁴²⁾ In April 1998, the term "free" was officially removed from the name of the Rajin-Sonbong FETZ, changing the "Rajin-Sonbong Free Economic and Trade Zone" to the "Rajin-Sonbong Economic and Trade Zone".⁴³⁾ Such measures taken by the North Korean central government undermined its plan for development of the Rajin-Sonbong Area. In addition, poor infrastructure, high logistical costs and the lack of a consumer market further hindered North Korea from attracting sufficient investments from South Korea and other foreign countries.⁴⁴⁾

39) At the initial stage, the countries concerned agreed to establish a multi-lateral corporation to lease land for port and infrastructures, and signed the Memorandum of Understanding on Environmental Principles to govern any environmental issues arising out of future projects. However, North Korea objected to the Chinese proposal to establish the main port on Chinese territory and which called for upgrading links to the inland railway and warehouse hub located in Hunchun, China. Russia also delayed enactment of law supporting the TRADP.

40) See Young Namkoong, *supra* note 28, p. 8.

41) See Korea Institute of International Economy Policy, *supra* note 12, pp. 517 and 519.

42) See Ministry of Unification, "Nam-buk Kwan-kye Ju-yo Tong-hyang Il-il Bo-go [Daily Report regarding Major Inter-Korean Relationship]," September 25, 1998 (Available at http://www.unikorea.go.kr/kr/unitrend/unitrend_daily.php?cur_date=1998-09-25&type=0; last visited May 3, 2005)

43) See Ministry of Unification, Buk-han Kwan-ryeon Jeong-bo [North Korea-related Information], October 3, 2003 (Available at www.unikorea.go.kr; last visited September 6, 2005.)

44) Some analysts asserted that such failure was due to the following causes: (i) the primitive infrastructure in the Rajin-Sonbong area, (ii) no developed region adjacent to the Rajin-Sonbong area, (iii) North Korea's poor state credit worthiness, and (iv) the delay in North Korea's improving relations with the United States. See Korea Institute of International Economy Policy, *supra* note 12, p. 514.

For now, the Rajin-Sonbong project lies dormant.⁴⁵⁾ The Loxley Group of Thailand completed the construction of Ra-Son International Communication Center in August 2001. And, on September 20, 2003, Suyul Kim, the Chairman of People's Committee of Ra-son City (former Rajin-Sonbong area), expressed that North Korea would continue with the development of the Rajin-Sonbong FETZ.⁴⁶⁾

C. Dormant Project: Shinuiju Special Administrative Region

During the mid-1990s, North Korea's centralized distribution system failed to supply food, energy, and raw materials to its people. It is within this context that many informal, farmers' black markets almost spontaneously sprouted up all over the North Korean countryside. While the North Korean central government initially tried to suppress these markets, it gradually began to shut its eyes to these markets as it realized that most urban residents purchased their foods and other necessities through these black markets.⁴⁷⁾ These markets eventually became the so-called the

45) In this regard, James Cotton's analysis regarding the Rajin-Sonbong FETZ is noteworthy even though his paper was prepared in 1996. James Cotton discussed in his paper the characteristics of North Korea's open door policy by reviewing three possible interpretations. According to the first interpretation, Jong-U Kim, the Chairman of CPEEC, proceeded to develop the Rajin-Sonbong city "without the consistent and comprehensive support of the whole system and North Korea's leadership, his achievements may be nullified or disowned or they may have a major impact on the overall system, depending upon its complex operations." A second view would view North Korea's "reform as, at best, a tactical measure." And on the second view, "Jong-U Kim and his associates are in charge of what is essentially a propaganda mission." Third, North Korea's opening policies may be the first step in a learning exercise. According to James Cotton's analysis, (i) the third view would appear to be supported by the fact that the debate about additional free economic zones has become moot for other localities, pending further progress and experience in the Rajin-Sonbong FETZ and (ii) the changes made in foreign economic policy in North Korea go beyond mere matters of style. (See James Cotton, *supra* note 27, pp. 14-19) Considering the facts that, as will be discussed below, North Korea designated Shinuiju, Gaesung and Kumgangsan as special economic zones in 2002, and the development of these special economic zones are undergoing, James Cotton's above analysis seems to have been basically correct.

46) See The Chosun Sinbo, Interview Ra-son-si In-min-wi-won-hoe Kim Su-yeol Wi-won-jang [Interview with Suyeol Kim, the Chairman of People's Committee of Ra-son city], September 20, 2003. (Available at <http://www.korea-np.co.jp/news/ViewArticle.aspx?ArticleID=2136>; last visited May 3, 2005)

47) According to Myoung-Chul Cho and Hyoung-Soo Zang, North Korea's urban residents obtained approximately 70% of foods from farmers' market or their relatives in rural areas. As of the summer of 1999, "more than 80% of North Korea's working population purchase some of their goods in the farmers' markets and black markets, and 50% of the population are daily customers in these unauthorized markets."

“market economy” or the secondary economy, growing on the fringes of the centrally planned economy (the primary economy) and became an important component of the North Korean economy as a whole.⁴⁸⁾ Reflecting the formation of private economic sectors and its past experience with its open door policy, North Korea adopted a revised constitution (the “NK Constitution of 1998”) on September 5, 1998 providing for a constitutional ground for more market-oriented policies as discussed below.⁴⁹⁾ After the stabilization of its regime, North Korea more actively carried out not only its internal economic reform policy but also its open door policy.⁵⁰⁾ In respect to its domestic economy reform, it took the so-called “7.1 Measures” in 2002, which contained a number of comprehensive economic reforms including the implementation of (i) a substantial increase in both prices and wages, (ii) a shift in the price-fixing mechanism, (iii) changes in the distribution system, (iv) decentralization of its nationally planned economy, (v) an increase in the autonomy of corporate management, (vi) the opening of the distribution market for the means of production, (vii) the differentiation of the distribution network, and (viii) a social security system reform.⁵¹⁾ In respect to its open door policy, North Korea opened

(See Myoung-Chul Cho & Hyoungsoo Zang, “The Present and Future Prospects of the North Korean Economy,” Korean Institute for International Economy Policy, working paper 99-7 (1999) at 28-29. (Available at [http://www.kiep.go.kr/Project/publish.nsf/webview1/77A752FCA3CD312B49256EB7001D77ED/\\$file/WP99-07.pdf](http://www.kiep.go.kr/Project/publish.nsf/webview1/77A752FCA3CD312B49256EB7001D77ED/$file/WP99-07.pdf); last visited May 3, 2005).

48) Ministry of Unification of South Korea estimates that, as of March 2004, there were approximately 300 general markets (or formerly called as farmers’ markets) in North Korea, 40 of them existing in Pyongyang. (See Ministry of Unification, *Buk-han Kwan-ryeon Jeong-bo [North Korea-related Information]*, September 13, 2004. Available at www.unikorea.go.kr; last visited September 6, 2005.)

49) See the NK Constitution of 1998, Article 37.

50) During the period of 1998 to 2001, approximately 850 North Korean government officials, economic experts and students participated in overseas training programs to learn about the market economy. See Jong-Woon Lee, “Economic Opening of the Hermit Kingdom: Current Status and Future Tasks of the New SEZs in North Korea,” *Journal of International Economic Studies*, Vol. 8, No.2, (December 2004), p. 130. According to the Ministry of Unification of South Korea, in 2002, about 450 North Koreans were sent to Southeast Asia alone to study the market economy. See Ministry of Unification, “Frequently Asked Question. Q.9 Do you think that North Korea has changed as a result of the Sunshine Policy?” (available at http://www.unikorea.go.kr/en/faq/faq.php?mode=view&cfa_num=9; last visited May 3, 2005)

51) See Ihk-Pyo Hong, “A Shift Toward Capitalism? Recent Economic Reforms in North Korea,” *East Asian Review*, The Institute for East Asian Studies, Vol.14 No.4 (Winter 2002) (“Ihk-Pyo Hong”) at 94. The core feature of the 7.1 Measures was the huge hike in prices and wages to reduce the price gap between the farmers’ markets and the State-owned stores. For example, the purchase price of rice increased from 0.8won/kg to 40won/kg. And, the

three areas toward South Korea and other countries: (a) Shinuiju in September 2002, (b) Kumgangsan in October 2002, and (c) Gaesung in November 2002 (Part III).

Shinuiju is a city located in the northwestern part of North Korea, bordering China. North Korea designated Shiuiju City, together with 132 km² in the adjacent county, as the Shinuiju Special Administrative Region (the “Shinuiju SAR”). North Korea also enacted the Basic Law of Shinuiju Special Administrative Region (the “Shinuiju Law”) on September 12, 2002⁵²⁾ and appointed Bin Yang, a Dutch national, as the Chief Administrator of the Shinuiju SAR. Bin Yang took office on September 25, 2002.⁵³⁾ The Shinuiju Law is modeled after the Basic Law of the Hong Kong Special Administrative Region of the People’s Republic of China (the “Hong Kong Law”) that established the so-called “one country-two system.”⁵⁴⁾ And,

wages increased in proportion to the increase in prices. But, the characteristics of 7.1 Measures still remain arguable. While North Korea’s official position is that the economic reform will be carried out within the framework of socialism, Il-Chon Kang, a scholar who is a proponent of North Korea and resides in Japan, asserts that “the 7.1 Measures is a bold policy having transitional aspect even though carried out within the frame of socialism,” and the policies “should be carried out fully”, warning that “suspending [the implementation of 7.1 Measures] might in effect cause even more drastic results. (See The Chosun Sinbo News, *Tae-dam-ha-go Hyeok-sin-jeok-in Gae-seon-chaek: Ro-im Mit Cheon-ban-jeok-in Ka-gyeok In-sang [Bold and Reformative Policy, Increase in Wages and Overall Prices]*, July 26, 2002. (Available at <http://www.korea-np.co.jp/news/ViewArticle.aspx?ArticleID=3243>; last visited May 3, 2005) ; See The Chosun Sinbo News, *Cho-sun-ui Kyeon-je Kwan-li Gae-seon Cho-chi (Ha): Tae-dam-han Cho-chi, Pyeon-hyang-eul Je-ttae Si-jeong-ha-yeo-ya [The Reform Measures for the Economic Management of North Korea: Bold Measures, if there are biased measures, they should be corrected timely]*, February 3, 2003. (Available at <http://www.korea-np.co.jp/news/ViewArticle.aspx?ArticleID=616>; last visited May 3, 2005) Regardless of the North Korean government’s intent, no one knows where such economic reform will eventually lead. (See Ihk-Pyo Hong, *Ibid*, p. 94.)

52) See The Chosun Sinbo News, “Shin-ui-ju Haeng-jeong Teuk-gu Jeong-ryeong Bal-pyo Doe-yeo Du-dal [Two months after Designation of Shinuiju Special Administrative Region],” November 18, 2002 (Available at <http://www.korea-np.co.jp/news/ViewArticle.aspx?ArticleID=3000>; last visited May 3, 2005); The Chosun Sinbo News, “Gae-seong Gong-up Ji-gu-reul Bo-neun Si-gak: Min-jok Gong-dong-che Keon-seol-ui Keo-dae-han Sil-hum-jang [Viewpoint on Gaesung Industrial Complex: A Huge Experimental Site for Constructing National Economy],” December 20, 2002 (Available at <http://www.korea-np.co.jp/news/ViewArticle.aspx?ArticleID=2809>; last visited May 3, 2005) For reference, North Korea had planned to entrust Hyundai Group with the development of Shinuiju as an industrial complex in 1999. However, after surveying the Shinuiju area in October 1999, Hyundai refused such a suggestion due to the possibility of land subsidence and high maritime transport cost. Instead, the Hyundai Group chose Gaesung area for the industrial complex as reviewed below.

53) See Yonhap News, “Yang Bin Pledges to Fulfill Agreements on [Shinuiju] Development,” September 24, 2002. (Available at http://crm.kotra.or.kr/main/common_bbs/notice_read.php3?board_id=20&pnum=899581&cnum=0; last visited May 3, 2005)

54) According to the analysis of Sung-wook Nam, a professor at Korea University and North Korea specialist,

like the Hong Kong Law,⁵⁵⁾ the Shinuiju Law governs the politics, organizations (including the Legislative Council, etc.), economy and culture of the Shinuiju SAR, as well as setting forth the fundamental rights and duties of residents, and specifies even the flag and emblem of the Shinuiju SAR. Politically, even though the Shinuiju SAR is an administrative unit under North Korea's sovereignty,⁵⁶⁾ it is to have its own Legislative Council,⁵⁷⁾ its own Chief Administrator,⁵⁸⁾ and even its own courts whose decisions shall be deemed conclusive and final.⁵⁹⁾ According to Shinuiju Law, the North Korean central government is committed to maintaining the legal system of the Shinuiju SAR for 50 years, and it also guarantees that no cabinet ministers, state commissions, or other institutions may interfere in the Shinuiju SAR's affairs.⁶⁰⁾ In regard to property rights, the Shinuiju Law allows residents (not only citizens) (i) to lease land from the State; (ii) to own or transfer to third parties buildings, facilities and the right to use land; and (iii) to establish mortgages on buildings, facilities, and the right to use land.⁶¹⁾ Nationalization or expropriation can only be carried out for the purpose of national security, and in case of expropriation, compensation is

“[one country-two system] strategy aims to open up to the world in only limited areas, while blocking any unwanted outside influence on the regime. For this type of opening, four requirements must be met. First, the areas to be opened must be far away from Pyongyang and must not be located close to any military base. Second, it must be a coastal city with a port nearby which can serve as a gateway for international trade. Third, it must be equipped with industrial infrastructure. Lastly, it must have an easy access to a labor force.” See, Sung-wook Nam, “Theory and Practice: Kaesung and Inter-Korean Economic Cooperation,” *East Asian Review*, The Institute for East Asian Studies, Vol. 13, No.1 (Spring 2001) (“Sung-wook Nam”) at 80.)

55) For comparison of the Shinuiju Law with the Hong Kong Law, see Joongi Kim, “North Korea: Legal Perspectives and Analysis: Essay: The Challenges of Attracting Foreign Investment into North Korea: The Legal Regimes of Sinuiju and [Gaesung],” 27 *Fordham Int'l L.J.* 1306 (April, 2004). Available at LexisNexis.

56) See the Shinuiju Law, Article 1.

57) The Legislative Council consists of 15 members elected by residents. Any residents may be elected as a member of the Legislative Council regardless of his or her citizenship. (See the Shinuiju Law, Article 2, 61 and 62). It should be noted that residents under the Shinuiju Law include residents having North Korean citizenship and some foreign nationalities. (See the Shinuiju Law, Article 42).

58) The Chief Administrator shall be appointed or dismissed by the Supreme People's Assembly of North Korea, and major actions by the Chief Administrator shall be subject to the approval or deliberation of the Legislative Council of the Shinuiju SAR. (See the Shinuiju Law, Articles 2, 64, 76 and 79)

59) See the Shinuiju Law, Articles 2 and 98.

60) See the Shinuiju Law, Articles 3 and 6.

61) See the Shinuiju Law, Articles 15 and 16. The longest lease term for the land located in Shinuiju SAR is 50 years. Thereafter, the enterprise concerned may renew the lease agreement upon the approval of the North Korean central government.

required.⁶²⁾ The Legislative Council, the Chief Administrator or both, will be in charge of most of the economic policies (including tax incentives, tariff system, foreign exchange, visa, procedure for residents' travel to foreign countries, etc.).⁶³⁾ The residents are entitled to political, economical, social and fundamental human rights like the citizens of other countries.⁶⁴⁾ The basic picture of the Shinuiju SAR, as Bin Yang unveiled in his press interview on September 25, 2002, consists of the following: (i) a legal system that would be controlled by Westerners; (ii) a Legislative Council that would comprise a majority of members appointed by Westerners; (iii) an investment environment that would be more investor-favorable than any found in the Chinese special economic zones; (iv) a totally capitalist region that would hold financial, industrial, commercial and tourism centers; and (v) the Shinuiju SAR existing apart from the rest of North Korea and having a physical barrier to isolate the area.⁶⁵⁾ Since the legal system of the Shinuiju SAR is much more reformative than that of the Rajin-Sonbong FETZ, the designation of the Shinuiju SAR could be understood as another bold experiment to attract direct foreign investment.

However, on October 4, 2002, the Chinese government subpoenaed Bin Yang in connection with alleged economic crimes⁶⁶⁾ and has detained him thereafter. By its actions, China demonstrated its concerns about the potential negative impact of the Shinuiju development project on the Chinese economy, especially on Dandong, a Chinese city that borders North Korea near the Shinuiju SAR and has impeded the advancement of North Korea's Shinuiju development project.⁶⁷⁾ North Korea seems

62) See the Shinuiju Law, Article 17.

63) See the Shinuiju Law, Articles 23, 24 and 25.

64) See the Shinuiju Law, Chapter 4.

65) See Digital Chosun News, “[Shinuiju] Follows Hong Kong Approach,” September 24, 2002. (Available at <http://english.chosun.com/w21data/html/news/200209/200209240030.html>; last visited May 3, 2005);

CNN News, “N. Korea creates special economic zone,” September 25, 2002. (Available at <http://archives.cnn.com/2002/WORLD/asiapcf/east/09/23/nkorea.economic/index.html>; last visited May 3, 2005).

66) See Kyodo News, “China subpoenas head of N. Korean economic zone,” October 4, 2002. (Available at - <http://home.kyodo.co.jp/all/display.jsp?an=20021004171>; last visited May 3, 2005)

67) In 2001, Sung-wook Nam, in his paper, indicated that the development of Shinuiju might have failed without the cooperation of China because it would have been “for economic cooperation with China and for the development of Dandong [in China bordering Shinuiju].” China favored a “plan to develop Dandong and turn it into an economic center, as well as a bridge linking China and North Korea.” See Sung-wook Nam, *supra* note 54, p. 81.

to have been negotiating with China with respect to the Shinuiju development project and China's concerns about Dandong. However, it has failed to make any substantial progress so far.

D. Ongoing Projects: Kumgangsan and Gaesung

Unlike North Korea's Rajin-Sonbong FETZ and Shinuiju SAR, aimed mainly at foreign investors, the Kumgangsan Tourism Region (the "Kumgangsan TR") and the Gaesung ICZ are aimed at South Koreans. The development projects of the Gaesung ICZ (the "Gaesung Project") and the Kumgangsan Tourism Region (the "Kumgangsan Project") are current symbols of inter-Korean economic cooperation. Originally Hyundai Group, a South Korean conglomerate, initiated these projects. With respect to the Kumgangsan Project, Ju-yung Chung, the founder of Hyundai Group, in 1989, agreed with North Korea on two projects: (i) the development of the Kumgangsan area located on the southeastern part of North Korea to attract tourists from South Korea and elsewhere and (ii) the establishment of the Joint Venture to invest in Siberian energy business. However, it was not until 1998, when the South Korean government adopted the so-called "sunshine policy" or "engagement policy," which actively encouraged South Korean companies to engage in inter-Korean transactions, that Hyundai Group launched the Kumgangsan Project. Having maintained the Kumgangsan Project⁶⁸⁾ in accordance with the Agreement on Kumgangsan Tours ("Hyundai Kumgangsan Agreement")⁶⁹⁾ dated June 28, 1998, Hyundai Group suffered a considerable loss by 2004.⁷⁰⁾ To secure the profitability of the Kumgangsan Project, on August 22, 2000, North Korea granted a subsidiary of

68) From 1998 to November 2004, about 840,000 people have toured the Kumgangsan area, spending a total of \$ 500 per person. It has been a source of hard currency for North Korea. The Kumgangsan Project has played an important role in easing tension and facilitating inter-Korean exchange. See The Korea Times News, "Kumgangsan Tours Celebrate 6th Anniversary," November 29, 2004. Available at <http://times.hankooki.com/page/nation/200411/kt2004111921273311990.htm> (last visited May 3, 2005). As inter-Korean exchanges increased dramatically, business communities pushed the authorities of the two Koreas to provide a predictable and transparent legal system to secure their economic activities. Under these circumstances, the Four Inter-Korean Agreements, as discussed below, were executed by the two Koreas, and ratified by the National Assembly.

69) The counter party in this agreement is North Korea's Asian-Pacific Peace Committee.

70) Reportedly Hyundai Asan suffered a considerable loss due to the Kumgangsan Project from 1998 to March 2004. However, the Kumgangsan Project turned profitable thereafter.

the Hyundai Group, Hyundai Asan, the exclusive right to develop several areas in North Korea (including the Kumgangsan area) by executing the Agreement on the Construction and Operation of Industrial Parks in North Korea (the "2000 SEZ Agreement").⁷¹⁾

In 1998, the Hyundai Group suggested to North Korea a development project regarding the west coast area of North Korea, and agreed to pursue that project with North Korea's Association of National Economic Cooperation. In 1999, after having conducted the preliminary survey of some proposed sites in North Korea (including Shinuiju, Gaesung, Nampo etc.), the Hyundai Group chose Gaesung⁷²⁾ as the first site to be developed. It should be noted that North Korea preferred Shinuiju to Gaesung because Gaesung borders on the DMZ. If North Korea allows a South Korean company to develop Gaesung, it, subsequently, should tolerate continual traffic between Gaesung and Seoul, which means that, from the view point of North Korea, the defense line against South Korea and the United States' Armed Forces in South Korea is to be retreated to the northern part of Gaesung. For this reason, North Korea was reluctant to open Gaesung toward South Korea.⁷³⁾ Nevertheless, concessions on the Gaesung Project were granted to the Hyundai Group because Hyundai earned North Korea's trust by both performing its payment obligations under the Hyundai Kumgangsan Agreement and contributing to the 2000 inter-Korean summit. Subsequently, Hyundai Asan executed the 2000 SEZ Agreement. Under the 2000 SEZ Agreement, Hyundai Asan obtained not only the exclusive

71) The counter parties in this agreement are North Korea's Asian-Pacific Peace Committee and Association of National Economic Cooperation.

72) According to the analysis of Sung-wook Nam, "the most ideal and realistic form of economic cooperation for both South and North Korea would be to construct a special industrial complex in which goods would be jointly produced by the two sides. To ensure the success of such economic cooperation, the industrial complex should be located in an area where an efficient distribution system could be put in place within a short period of time. What distinguishes Gaesung from Rajin-Sonbong or Shijuiju are its proximity to capitalist regions and other diverse favorable economic special zones, comparable to Shanghai or Shenzhen." See, Sung-wook Nam, *supra* note 54, p. 68-69. For reference, Gaesung is about 60 km distant from Seoul, the capital of South Korea, and about 160 km from Pyongyang, the capital of North Korea.

73) Originally, North Korea was, by December 2000, expected to enact the Law on the International Free and Economic Zone for the Gaesung ICZ and to announce the detailed conditions regarding the land use right and labor issues. However, no substantial results had been made by early 2001. The Gaesung Law was enacted only on November 27, 2002. Such delay seems to have been influenced by the North Korean military's objection. See Dong-ho Cho, "Gae-seong Gong-dan Geon-seol Sa-eop-ui Chu-jin Bang-hyang [The Direction in the construction of the Gaesung Industrial Complex]," *Tong-il Kyeong-je [Unification Economy]*, (11-12, 2001), p. 16.

right to develop the Gaesung ICZ and the Kumgangsan TR but also concessions regarding large-scale social overhead capital projects in North Korea.⁷⁴⁾ In December 2000, Hyundai Asan completed the land survey of the Gaesung area in conjunction with Korean Land Corporation (“KLC”), a South Korean government invested corporation, and prepared the detailed master plan for the development of the Gaesung ICZ in 2001. According to Hyundai Asan and the Ministry of Unification of South Korea,⁷⁵⁾ the Gaesung Project is a three-stage project for developing a total of 20 million pyongs⁷⁶⁾ (approximately 66 million m²) consisting of 8 million pyongs for an industrial park and another 12 million pyongs for commercial housing and apartments. The 8 million-pyong industrial park will be constructed in following three stages: (i) at the first stage, one million pyongs, or 3.3 million m², for labor-intensive industries or general light industries (including 28,000 pyongs for the pilot site), (ii) at the second stage, two million pyongs, or 6.6 million m², for a worldwide export base and IT industries, (iii) at the third stage, five million pyongs, or 17 million m², for a compound industrial complex.⁷⁷⁾

The Gaesung Project is expected to benefit the two Koreas economically by combining South Korea’s capital and technology with North Korea’s land and labor. From South Korea’s view point, an abrupt collapse of the North Korean system could lead to a national disaster because millions of North Korean might be forced to flood into South Korea seeking refuge and jobs, and in such a case the reunification cost might be a chronic burden to a reunified Korean economy.⁷⁸⁾ Therefore, it is

74) The businesses to which Hyundai Asan obtained rights under the 2000 SEZ Agreement are as follows: electric power business, telecommunication business, road and railroad business, Tongchon airport business, Imjin river dam business, business for utilization of water reservoir in Kumgangsan, tourism business for major tourist attractions. See Gaesung Forum website at <http://www.kaesong.org/park.htm> (last visited May 3, 2005). It is said that Hyundai invested approximately US\$ 1 billion in North Korea in the last several years.

75) Hyundai Asan made public its plan to develop Gaesung as an industrial complex in 2002. This development plan (in Korean) is available at www.hyundai-asan.com (last visited May 3, 2005). This plan was partially changed when Hyundai Asan obtained South Korea government’s approval regarding its investment in North Korea. See Ministry of Unification, “Bo-do Mit Hae-sul Ja-ryo [Press Release and attached Commentary]”, April 23, 2004. (Available at <http://www.unikorea.go.kr/>; last visited September 6, 2005.)

76) 1 pyong is approximately equal to 3.3058 m².

77) Inter-Korean Exchange & Cooperation Bureau, Ministry of Unification, “Summary of the Approval of the Cooperative Project: Gaesung Industrial Complex First-Stage Development,” April 23, 2004. This paper is available at <http://www.unikorea.go.kr/> (last visited May 3, 2005).

78) Reportedly, Germany has experienced considerable depression due to the unification cost during the last 10

most desirable for South Korea to encourage North Korea to become accustomed to market economy practices and to help revitalize the North Korean economy by implementing inter-Korean economic cooperation projects like the Gaesung Project. In addition, considering that since the 1990s many South Korean labor intensive companies have relocated their plants to China, Vietnam or other countries, and as a result the South Korean manufacturing sector has been hollowed out, the Gaesung Project could be an alternative to decelerating such trends of hollowing out because small-medium sized enterprises (“SMEs”) doing business in labor intensive industries can take advantage of low wages and low land cost in the Gaesung ICZ by relocating their plants to the Gaesung ICZ.⁷⁹⁾ The Gaesung Project would be the model of peacefully utilizing the nearby areas of the DMZ and thereby contributing to easing military tension on the Korean peninsula. From the viewpoint of North Korea, the Gaesung ICZ, if constructed and operated as scheduled, would offer approximately two hundred thousand jobs to North Korea. North Korea could sell not only raw and supplementary materials, but also impose transportation fees, taxes and collect foreign currency as well.⁸⁰⁾ The Gaesung Project is now understood to be integral in the process toward the unification of the two Koreas. For these reasons, both South and North Koreas have been continuously discussing the issues related to the development of the Gaesung ICZ in the inter-Korean Minister Talks on a regular basis from 2000 to the present in order to support the stable and predictable investment environment.

years after the collapse of the Berlin Wall. Given that the economic structure of North Korea is more problematic than that of East Germany, it is not difficult to expect that abrupt reunification of the two Koreas could have a considerable negative impact on the South Korean economy. For this reason, South Korea has pursued the gradual and peaceful reunification of the two Koreas and, has tried to increase the economic interdependency between the two Koreas through economic cooperation with North Korea so as to make a de facto unification.

79) Many of South Korean SMEs have faced difficulties in their business due to weakened price competitiveness, and thus have been increasingly relocating their domestic production lines overseas. See Seung Park’s speech, *supra* notes 5. Thus, when Hyundai Asan and KLC announced the bidding process for the first stage 1st stage in 2004, approximately 1,500 to 1,600 SMEs expressed their interests in moving into the Gaesung ICZ. With respect to development of the pilot site, a part for the first stage, Hyundai and KLC selected, among 136 SMEs, 15 SMEs as the companies to be located into the pilot site. See Ministry of Unification, “Issues in Focus (Gaesung Industrial Complex Development Project)”, April 20, 2004, p. 2.

80) The economic effect of the Gaesung Project on North Korea’s economy varies depending on the analyst’s assumption. According to Suhk-sam, Park, the money to be paid as wages and enterprise income taxes to North Korea is predicted to be at least (i) in the ninth year when the first, second and third stage projects are to begin operation, US\$ 600 million (with 725,000 new jobs) and (ii) in the 17th year US\$ 2.28 billion, and US\$ 2.28 billion

In this regard, North Korea designated the Kumgangsan area as Kumgangsan TR, and enacted the Kumgangsan Tourism Region Law (the “Kumgangsan Law”) on November 13, 2002. Likewise, North Korea designated Gaesung city and its adjacent counties as the Gaesung ICZ and enacted the Gaesung Industrial Complex Zone Law (the “Gaesung Law”) on November 20, 2002. Under the Kumgangsan Law and the Gaesung Law, North Korea designated Hyundai Asan as the developer for both regions. In addition, North Korea has since promulgated a series of regulations for implementation of the Kumgangsan Law and the Gaesung Law.

Today, the Kumgangsan Project and the Gaesung Project are ongoing. Every day hundreds of South Koreans tour the Kumgangsan area by passing through the DMZ. As of July 20, 2005, 13 South Korean SMEs established or are establishing their plants in the pilot site of the Gaesung ICZ and approximately 4,400 South and North Korean employees are working at the Gaesung ICZ.⁸¹⁾ A department store in Seoul sells set of kettles produced in the Gaesung ICZ by Living Art, a kitchen utensil producer in 2005.

corresponds to 12.4 percent of North Korea’s 2003 gross national income. See Suhk-sam Park, “Creating a Visible Bridge: The Economic Impact of Kaesung Industrial Complex Construction,” *East Asian Review*, The Institute for East Asian Studies, Vol. 16, No. 3 (Autumn 2004), p. 99-102. (“Suhk-sam Park”). Meanwhile, according to Sun-Jick Hong, the economic effects on North Korea are estimated to be, in the ninth year, US\$ 4.65 billion (as for only the direct economic effects) and US\$ 9.6 billion (including direct and indirect economic effects). Considering that North Korea’s total budget for the fiscal year 2002 was approximately 9.6 billion, and its total trade amount for 2002 was US\$ 2.26 billion, the Gaesung Project is expected to contribute substantially to revitalizing North Korea’s economy. See Sun-Jick Hong, “Gae-seong Gong-dan Gae-bal-ui Kyeong-je-jeok Hyo-kwa-wa Seong-kong Kwa-je” [The Economic Effect of Gaesung ICZ and Some Tasks for Its Success], August 24, 2004. (“Sun-Jick Hong”) (Available at http://www.hri.co.kr/file_pds/pub02/200204/UEB200204_08.pdf; last visited May 3, 2005.)

81) See Ministry of Unification, Gaesung Gong-dan Sa-eop Cham-go Ja-ryo [Reference concerning the Gaesung Project], July 22, 2005. Meanwhile, according to Hyundai Asan’s Newsletter in March 2005, notwithstanding North Korea’s February 10, 2005 announcement that it would suspend participation in the Six-Party talks acknowledging its nuclear arsenal, more than 16,500 tourists visited Kumgangsan area crossing the DMZ in February 2005 and thousands of South and North Korean employees are regularly working in March 2005 at the Gaesung ICZ. See Hyundai Asan News Update, March 2005.

III. Legal Framework for the Gaesung Industrial Complex

A. Legal Framework Overview

The legal frameworks of both the Gaesung ICZ and the Kumgangsan TR are substantially identical because the regulations⁸²⁾ for the Kumgangsan TR were modeled after those of the Gaesung ICZ. The following discussion will focus on the legal framework of the Gaesung ICZ consisting of (i) the NK Constitution of 1998, which is in effect, (ii) the Gaesung Law, (iii) its implementing regulations and (iv) inter-Korean agreements. First, the NK Constitution of 1998 provides the constitutional ground for special economic zones. Details of economic provisions thereof will be reviewed in Part III.B. Second, unlike the Shinuiju Law that governs its own politics, organizations, economy and culture of the Shinuiju SAR, the Gaesung Law and its implementing regulations only govern matters regarding economic activities in the Gaesung ICZ. Matters regarding economic activities that are not provided for in the Gaesung Law and its implementing regulations shall be dealt with based on consultations between the North Korean central government (the Central Guidance Agency as defined below) and the local administrative agency under South Korean control (the Administrative Agency as defined below).⁸³⁾

82) The enacted regulations for the Kumgangsan TR as of March 22, 2005 are as follows:

- (1) The Regulations on the Development of the Kumgangsan Tourism Region (May 12, 2003);
- (2) The Regulations on the Establishment and Operation of Enterprises in the Kumgangsan Tourism Region (May 12, 2003);
- (3) The Regulations on the Establishment and Operations of the Administrative Agency for the Kumgangsan Tourism Region (April 29, 2004);
- (4) The Customs Regulations in the Kumgangsan Tourism Region (April 29, 2004);
- (5) The Regulations on Entrance and Exit, Sojourn and Residence in the Kumgangsan Tourism Region (April 29, 2004);
- (6) The Regulations on Foreign Exchange in the Kumgangsan Tourism Region (May 6, 2004);
- (7) The Regulations on Advertisement in the Kumgangsan Tourism Region (May 6, 2004);
- (8) The Labor Regulations in the Kumgangsan Tourism Region (May 6, 2004);
- (9) The Regulations on Real Property in the Kumgangsan Tourism Region (September 21, 2004);

The above regulations are available at www.uniKorea.co.kr (last visited September 6, 2005) and www.korea-np.co.jp (last visited May 3, 2005).

83) See the Gaesung Law, Article 9. For reference, in the Rajin-Sonbong FETZ any matters that are not addressed in the relevant laws and regulations for the Rajin-Sonbong FETZ are governed by other relevant laws of North Korea. See the Law on the Free Economic and Trade Zone of 1993, Article 6.

However, other laws of North Korea may regulate any activities other than economic matters in the Gaesung ICZ. For example, investors (including South Koreans, Koreans abroad, foreigners and their companies) in the Gaesung ICZ shall be, in principle, subject to North Korea's criminal jurisdiction unless inter-Korean agreement or other treaties exclude the application of North Korean laws.⁸⁴ Furthermore, North Korea has enacted 13 regulations to implement the Gaesung Law so far⁸⁵ based on consultation with Hyundai Asan and KLC, and, as reviewed

84) See the Gaesung Law, Article 8.

85) As of August 31, 2005, the following 13 regulations for the Gaesung ICZ are enacted:

- (1) The Regulations on the Development of the Gaesung Industrial Complex Zone (April 24, 2004) ("Development Regulation");
- (2) The Regulations on the Establishment and Operation of Enterprises in the Gaesung Industrial Complex Zone (April 24, 2003) ("Enterprise Regulation");
- (3) The Tax Regulations in the Gaesung Industrial Complex Zone (September 18, 2003) ("Tax Regulation");
- (4) The Labor Regulations in the Gaesung Industrial Complex Zone (September 18, 2003) ("Labor Regulation");
- (5) The Regulations on the Establishment and Operations of the Administrative Agency for the Gaesung Industrial Complex Zone (December 11, 2003), ("Administrative Agency Regulation");
- (6) The Regulations on Entrance and Exit, Sojourn and Residence in the Gaesung Industrial Complex Zone (December 11, 2003) ("EES Regulation");
- (7) The Customs Regulations in the Gaesung Industrial Complex Zone (December 11, 2003);
- (8) The Regulations on Foreign Exchange in the Gaesung Industrial Complex Zone (February 25, 2004) ("Foreign Exchange Regulation");
- (9) The Regulations on Advertisement in the Gaesung Industrial Complex Zone (February 25, 2004) ("Advertisement Regulation");
- (10) The Regulations on Real Property in the Gaesung Industrial Complex Zone (July 29, 2004), ("Real Property Regulation"); and
- (11) The Insurance Regulations in the Gaesung Industrial Complex Zone (September 21, 2004) ("Insurance Regulation").
- (12) The Account Regulations in the Gaesung Industrial Complex Zone (June 28, 2005) ("Account Regulation")
- (13) The Regulations on the Finance of Enterprises in the Gaesung Industrial Complex Zone (June 28, 2005) ("Finance Regulation")

The above regulations are available at www.uniKorea.co.kr (last visited September 6, 2005), www.kidmac.com (last visited September 6, 2005) and www.korea-np.co.jp (last visited May 3, 2005).

For reference, Bae, Kim & Lee, a Korean law firm, published Bae, Kim & Lee, *Gae-seong Gong-eop Ji-gu Beop-ryeong Hae-seol [Gaesung Industrial Complex Zone Law and Regulations Manual]*, Law and Business (December 2004). This book tried, for the first time in Korea, to offer analysis regarding the Gaesung Law and its 9 regulations (excluding Real Property Regulation, Insurance Regulation, Account Regulation and Finance Regulation). As far as the interpretation regarding the Gaesung ICZ's legal system is concerned, I do not put any footnote in this paper.

below, these regulations are basically of a market-friendly nature.⁸⁶ Basic issues under the Gaesung Law and its implementing regulations will be discussed in Part III.D as below. Third, under the Gaesung Law, any inter-Korean Agreements⁸⁷ executed with respect to the Gaesung ICZ have the same force and effect as the Gaesung Law.⁸⁸ From 2000 to the present, both South and North Korea have executed tens of inter-Korean agreements to enhance inter-Korean economic cooperation. More details regarding inter-Korean agreements will be discussed in Part III.C.

B. The NK Constitution of 1998: North Korea's Current Constitution

Experimenting with its open door policy, North Korea sometimes took measures beyond the written law. As mentioned above, North Korea adopted the Equity Joint Venture Law of 1984 allowing North Korea's institutions, enterprises or associations to establish and operate equity and contractual joint venture enterprises with foreign counterparts without a constitutional basis at the time. The Equity Joint Venture Law of 1984 received constitutional grounding by the NK Constitution of 1992. Also, North Korea established the Rajin-Sonbong FETZ even though the NK Constitution of 1992 did not expressly allow the State to establish a special economic zone. These incidents suggest that a constitutional or other legal ground was not necessarily required to implement the open door policy in North Korea.⁸⁹ However,

86) North Korea's legislative branch is the Supreme People's Assembly ("SPA") having the highest state power. During the period when SPA is not in session, the Standing Committee of SPA acts in place of SPC. Even though the Standing Committee of SPA promulgated both the Gaesung Law and its regulations, it is construed that the Gaesung Law is superior to its regulations from the viewpoint of systematic interpretation.

87) The inter-Korean Agreements mean the agreements executed by and between the two Koreas. As discussed below, the inter-Korean Agreements, if ratified by both South and North Korea's legislature, apply to the relevant inter-Korean relationship.

88) See the Gaesung Law, Supplementary Clause 2. The Kumgangsan Law has the same provision. With respect to the concept of inter-Korean Agreement under the Gaesung Law and the Kumgangsan Law, it is said, according to some South Korean government officials, that North Korea has a position that the inter-Korean Agreement covers the agreements executed not only between South and North Korea's governments, but also between the North Korean government and Hyundai Group. From the viewpoint of South Korea's legal system, since the inter-Korean Agreement under the Gaesung Law has the same force and effect as a law, it should be confined to the inter-Korean Agreement executed only between South and North Korea at a government level and ratified respectively by each party's legislature.

89) In my experience, the North Korean government allowed some foreigners to establish wholly foreign-

an alteration in the law is required to institutionalize the policy. In this context, the NK Constitution of 1998 contains North Korea's institutional achievements related to North Korea's economic changes and open door policy. Moreover the NK Constitution of 1998 is important in that it provides guidelines for laws and regulations to be enacted or revised.

The NK Constitution of 1998 adopted on September 5, 1998 legalized the following significant economy-related policies.⁹⁰⁾ First, the NK Constitution of 1998 changed the ownership structure in North Korea. For reference, the NK Constitution of 1992 recognized three types of ownership: (i) State ownership, (ii) cooperative-working organization ownership⁹¹⁾ and (iii) individual worker ownership. With respect to the State ownership, while under the NK Constitution of 1992 all natural resources, major factories and enterprises, ports, banks, and transportation and communication establishments were the objects of the State's exclusive ownership⁹²⁾, under the NK Constitution of 1998 "railway and airports" were added to the objects of the State's exclusive ownership.⁹³⁾ With respect to cooperative-working organization ownership, the NK Constitution of 1992 allowed these organizations to own land, livestock, agricultural machinery, ships, buildings, medium-sized factories and enterprises, and the properties of cooperative-working organizations belonged to the cooperative-working organization's members as a group.⁹⁴⁾ The NK Constitution of 1998 broadened the subject of such ownership by entitling "social organizations" to own the properties which cooperative-working organizations had been solely permitted to own.⁹⁵⁾ According to some analysts,⁹⁶⁾ social organizations

owned companies in Pyongyang (not in a special economic zone) in 2004, even though under the relevant law wholly foreign-owned companies are allowed only within the special economic zones (See *supra* note 31). Reportedly at the Pyongyang-Overseas Korean Trade Association business conference held on October 23-25, 2004 at Pyongyang, North Korea announced their policy that it would allow Koreans abroad to establish wholly foreign-owned enterprises through all the area of North Korea. This shows that the Korea Labor Party's policy still prevails over the written law and also suggests that the relevant law may be enacted based on its preceding experiment.

90) This paper does not address other parts of the NK Constitution of 1998.

91) Cooperative-working organization refers to socialistic economic organizations such as collective farms.

92) See the NK Constitution of 1992, Article 21.

93) See the NK Constitution of 1998, Article 21.

94) See the NK Constitution of 1992, Articles 20 and 22.

95) See the NK Constitution of 1998, Articles 20 and 22. The social organization refers to both economic and/or cultural organizations.

96) See Soo-Young Choi, Seung-Ryul Oh, Hyeong-Jung Park & Kang-Taek Lim, "Buk-han Heon-beop Gae-

including the Korea Labor Party or organizations affiliated with the Korea Labor Party (including the Democracy Woman Alliance and the Kim Il-Song Socialist Youth Alliance) had traditionally, and illegally, owned and/or operated enterprises or factories and engaged in illegal trade with foreign companies. With the adoption of the NK Constitution of 1998, such organizations are now permitted to own and operate enterprises, and to trade with foreign companies. With respect to individual private ownership, the NK Constitution of 1992 allowed only workers to enjoy the proprietary rights to (a) socialist distribution as consideration for labor, (b) additional benefits from the State and society, and (c) the products of individual sideline activities including those from his or her private garden. The State had guaranteed such private ownership rights and their inheritance.⁹⁷⁾ The NK Constitution of 1998 enlarged the individual private ownership by allowing *any citizen*, not only workers, to enjoy the ownership rights to items (a) to (c) above, as well as to "income [from] other legal economic activities."⁹⁸⁾ Thus, a citizen's ownership is not limited to the products of individual sideline activities but also includes the income from any legalized business transactions. With the adoption of the NK Constitution of 1998, North Korea officially approved the circulation of necessities including foodstuffs bought and sold in the markets.⁹⁹⁾ In addition, under the NK Constitution of 1998, "livestock and buildings" are excluded from the objects which cooperative-working organizations or social organizations may own,¹⁰⁰⁾ thereby reserving ownership over livestock, houses or stores to the citizens of North Korea.¹⁰¹⁾ Second, the NK Constitution of 1998 provides, for the first time, that North Korean citizens shall

jeong-e Tta-reun Kyeong-je Bu-mun Byeon-hwa Cheon-mang [Prospective Changes in the Economy Sector following Revision of North Korean Constitution]," Korea Institute for National Unification (October, 1998). ("Soo-Young Choi"), p. 2. (Available at <http://www.kinu.or.kr/content/xml.asp?did=9953>; last visited May 3, 2005)

97) See the NK Constitution of 1992, Article 24.

98) See the NK Constitution of 1998, Article 24.

99) See Soo-Young Choi, *supra* note 96, p. 3.

100) See the NK Constitution of 1992, Article 22; the NK Constitution of 1998, Article 22.

101) The Shinuiju Law enacted after adoption of the NK Constitution of 1998 allows residents to use land, and to own or transfer to a third party, buildings, facilities and land use rights in the Shinuiju SAR. In addition, according to the Real Property Regulation for the Gaesung ICZ (or "Real Property Regulation") enacted on July 29, 2004 and the Regulations on Real Property in the Kumgangsan Tourism Region enacted on September 21, 2004, individuals and enterprises may own or transfer to third parties, buildings and their appurtenances and the rights to use land located in their respective zone/region.

have the freedom to reside and travel to any place.¹⁰²⁾ Since many citizens moved to other provinces to seek food during the food crisis, the North Korean government had no choice but to tolerate the migrations. Therefore, by specifying such freedom of movement in the NK Constitution of 1998, the North Korean government recognized the necessity of this right. Moreover, it reasoned that if North Koreans could practically own houses or buildings in accordance with certain administrative measures, North Koreans also could substantially enjoy the freedom of movement.¹⁰³⁾ Third, the NK Constitution of 1998 emphasizes the implementation of self-sufficient accounting systems together with the concepts of costs, prices and profits.¹⁰⁴⁾ Unlike the NK Constitution of 1992,¹⁰⁵⁾ the NK Constitution of 1998 allows social and/or cooperative-working organizations to conduct foreign trade activities without the State's supervision. Accordingly, individual actors in the economy have more autonomy and each factory or enterprise is held accountable for its profitability. Fourth, Article 37 of the NK Constitution of 1998 provides that "the State shall encourage institutions, enterprises or associations of North Korea to establish and operate equity and contractual joint venture enterprises with foreign corporations or individuals, and *various types of enterprises within a special economic zone*," (italicized text representing additions to the original text of the NK Constitution of 1992). With respect to the newly inserted language, it is worth noting that the term "*special economic zone*" provides a constitutional basis for creating a special economic zone including, for example, the Rajin-Sonbong FETZ. It is also worth noting that the term "*various types of enterprises*"¹⁰⁶⁾ allows investors to establish any kind of enterprise, not just equity or contractual joint venture

102) See the NK Constitution of 1998, Article 75.

103) See Soo-Young Choi, *supra* note 96, p. 8. Reportedly since 1980 houses have in fact been marketed in North Korea. Even though selling houses allocated by the State is illegal, the authorities seem to have tolerated such transactions. See Mi-young Kim, "NK Houses Sold on Back Market," *The Digital Chosun*, March 20, 2002. (Available at <http://www.chosun.com/w21data/html/news/200203/20020320e036.html>; last visited May 3, 2005)

104) See NK Constitution of 1998, Article 33.

105) See NK Constitution of 1998, Article 36. Under Article 36 of NK Constitution of 1992, foreign trade must be conducted by the State or under the supervision of the State.

106) As discussed below, both the Regulations on the Establishment and Operation of Enterprises in the Gaesung Industrial Complex Zone (or "Enterprise Regulation") enacted on April 23, 2003 and the Regulations on the Establishment and Operation of Enterprises in the Kumgangs Tourism Region enacted on May 15, 2003 provide that "an investor may establish *various types of enterprises* individually or together with other investor" in their respective zone/region".

enterprises or wholly foreign-owned companies; by implication, the NK Constitution of 1998 permits the formation of any limited liability company in North Korea, as long as it is established in accordance with the relevant laws. North Korea attempted to demonstrate its commitment to reform its economy with the adoption of the NK Constitution of 1998's more liberalizing provisions, even though the announcement of any measures could not guarantee North Korea's commitment to the open door policy and economic reform.

C. Inter-Korean Agreements

1. Characteristics of Inter-Korean Agreements

In terms of legal effectiveness, inter-Korean agreements were, by the 2000 Inter-Korea Summit, regarded as gentlemen's agreements that were not legally binding on the two Koreas because they had not been ratified by each party's legislatures. However, as South Koreans doing business in North Korea constantly raised concerns as to how to secure their investments in North Korea, the two Koreas, immediately after the 2000 Inter-Korea Summit, negotiated for a more stable and predictable legal infrastructure for inter-Korea transactions. Subsequently, the two Koreas executed four inter-Korean agreements ("The Four Inter-Korean Agreements") consisting of (a) the Agreement on Inter-Korean Investment Protection (the "IP Agreement"), (b) the Agreement on Prevention of Double Taxation (the "DT" Agreement), (c) the Agreement on Clearing Settlement (the "CS Agreement") and (d) the Agreement on Resolution Procedures for Commercial Disputes (the "the DRP Agreement").¹⁰⁷⁾ The Four Inter-Korean Agreements came into effect with the ratifications of both South and North Korean legislatures on August 18, 2003 and became legally binding on both South and North Korea thereafter.¹⁰⁸⁾ Furthermore, the two Koreas executed a number of additional inter-

107) The English versions of the Four Inter-Korean Agreements are available at <http://www.unikorea.go.kr/>. Information as to whether any inter-Korean agreement is ratified by South Korea's National Assembly is available at <http://search.assembly.go.kr/bill/>

108) As the Four Inter-Korean Agreements came into effect, from South Korea's perspective, North Korea is recognized as a legal entity having the power to govern, regulate any activities of the natural, juridical persons, and to impose taxes on such persons within the area of North Korea. In other words, North Korea is not simply an anti-government organization or a de facto government against South Korea and visa versa. These changes demonstrate

Korean agreements and are expected to execute more. Among them, nine inter-Korean agreements were ratified by South Korea's legislature by December 2004 and went into effect on August 5, 2005.¹⁰⁹⁾ From the legal point of view, the inter-Korean agreements that came into effect have become part not only of North Korea's legal system, but also that of South Korea. These inter-Korean agreements function as the basic legal structure securing South Korea's investment in North Korea. The following section will offer an overview of the Four Inter-Korean Agreements.

2. Agreement on the Protection of Inter-Korean Investment

The IP Agreement, consisting of a preamble and 12 articles, addresses the scope of protected investment assets, standards of treatment, relationship between the IP Agreement and other laws and contracts, expropriation and compensation for loss,

that the inter-Korea relationship is a transient one towards the goal of reunification and has been dramatically changing from political, military confrontation to economic, legal cooperation.

109) The following are the inter-Korean agreements ratified by both South and North Korea's legislatures and came into effect on August 5, 2005. :

- a. Agreement on Communication in the Gaesung Industrial Complex Zone (executed on December 8, 2002, ratified on December 9, 2004) (the "Communication Agreement");
- b. Agreement on Customs Clearance in the Gaesung Industrial Complex Zone (executed on December 8, 2002, ratified on September 23, 2004) (the "Customs Agreement");
- c. Agreement on Quarantine in the Gaesung Industrial Complex Zone (executed on December 8, 2002, ratified on September 23, 2004) (the "Quarantine Agreement");
- d. Agreement on Entrance and Exit, and Sojourn in the Gaesung Industrial Complex Zone and the Kumgangsan Tourism Region (January 29, 2004, ratified on September 23, 2004) (the "EES Agreement");
- e. Agreement on the Establishment and Operation of the Inter-Korean Commercial Arbitration Committee (executed on October 12, 2003, ratified on September 23, 2004);
- f. Agreement on Operation of the Inter-Korean Railroad (executed on April 13, 2004, ratified on December 9, 2004);
- g. Agreement on Operation of the Inter-Korean Road (executed on December 6, 2002, ratified on September 23);
- h. Inter-Korean Maritime Agreement (executed on June 5, 2004, ratified on December 9, 2004) ("Martine Agreement"); and
- i. Supplementary Agreement to the Inter-Korean Maritime Agreement (executed on June 5, 2004, ratified on December 9, 2004) ("Supplementary Agreement on Martine Agreement").

See Ministry of Unification, *Bo-do Ja-ryo [Press Release]*, August 5, 2005. Since this paper was prepared before August 2005, this paper does not cover detailed discussion about the above inter-Korean agreements.

subrogation etc. First, the investor to be protected under the IP Agreement means any natural or juridical person of either South or North Korea.¹¹⁰⁾ Therefore, any natural person having the citizenship of either South or North Korea may enjoy the legal protection under the IP Agreement, regardless of their residence. In respect of the juridical person, from the viewpoint of South Korea, any corporation established under the laws of either South or North Korea is construed as the investor under the IP Agreement, even if a foreigner controls the corporation (the "Foreign-Controlled Company"). Stated again, this means that any foreign investor having the intent to invest in North Korea will enjoy protection under the IP Agreement through its South Korean subsidiary. However, the Foreigner-Controlled Company shall be subject to the restrictions of the relevant laws and regulations of either South or North Korea.¹¹¹⁾

Second, the investment assets protected under the IP Agreement cover a wide variety of assets, so the scope of investment assets under the IP Agreement is similar to that under the 2004 Model Bilateral Investment Treaty of the United States.¹¹²⁾

110) See the IP Agreement, Section 1.2.

111) Foreign investment in South Korea is generally governed by the Foreign Investment Promotion Act, under which foreign investment is restricted in some business areas (i.e. newspapers, broadcasting). For more details, see, Ministry of Commerce, Industry & Energy, "Consolidated Public Notice on Foreign Investment," November 10, 2003. (Available at http://www.mocie.go.kr/eng/investing/legislation/leg_view.asp?num=41&page=1&table=eng_legislation&keyfield=&key=; last visited May 3, 2005). For example, under the Alien Land Act of South Korea, if any foreign-invested company (in which the equity interest of foreigners comprises 50% or more, or in which foreigners exercise control over the board of directors) wants to acquire the land located in military facilities protection areas, cultural relics protection areas, or natural sanitary protection areas, it should obtain prior approval from the relevant local authorities. As for North Korea, it seems to have, or be expected to enact, similar laws or regulations restricting foreign investment in North Korea.

112) Under the IP Agreement, Section 1.1, the investment assets to be protected under the IP Agreement include the following: (i) movable and immovable property, and other related property rights, (ii) monetary properties including reinvested returns and loans, and claims having economic value, (iii) intellectual property rights including copyrights, patents, trademarks, design rights and technical advancements and other similar rights, (iv) shares, stocks, debentures, government or public bonds, or other rights to a company or a public institution, (v) permission to explore, extract or develop natural resources and any other business concessions having economic value conferred by law or under the relevant contract, and (vi) all other assets invested by the Investor. Any changes in the form of assets that are invested or reinvested are recognized as the investment assets; provided that they do not contradict the laws and regulations of the host Party (i.e. North Korea).

For reference, under the 2004' Model Bilateral Investment Treaty of the United States (the "U.S. Model BIT"), Article 1, (1) the "investment" means every asset that an investor owns or controls, directly or indirectly, that has the characteristics of an investment, including such characteristics as the commitment of capital or other resources, the

Third, the IP Agreement encouraged inter-Korean investments by providing preferential treatment to any natural and judicial persons from South and North Korea who invest in the area subject to North or South Korea's jurisdiction. From the perspective of South Korean investors, North Korea is obligated to create an investor-favorable environment¹¹³⁾ by (a) providing favorable treatment for the entry, sojourn and movement of employees or counsels of the investor;¹¹⁴⁾ (b) granting the relevant permission or approval necessary for such investment in accordance with North Korea's laws and regulations;¹¹⁵⁾ (c) guaranteeing free management control over the invested enterprise by the investors in accordance with North Korea's statutes and the concerned enterprise's Articles of Association;¹¹⁶⁾ (d) guaranteeing free transfer and remittance of investment-related payments of the investors from North Korea to South Korea,¹¹⁷⁾ (e) providing South Korea with newly enacted, amended and supplemented statutes regarding investments¹¹⁸⁾ and (f) promptly

expectation of gain or profit, or the assumption of risk, and (2) forms that an investment may take include: (a) an enterprise; (b) shares, stock, and other forms of equity participation in an enterprise; (c) bonds, debentures, other debt instruments, and loans; (d) futures, options, and other derivatives; (e) turnkey, construction, management, production, concession, revenue-sharing, and other similar contracts; (f) intellectual property rights; (g) licenses, authorizations, permits, and similar rights conferred pursuant to applicable domestic law; and (h) other tangible or intangible, movable or immovable property, and related property rights, such as leases, mortgages, liens, and pledges. (The U.S. Model BIT is available at <http://www.state.gov/documents/organization/29030.doc>; last visited May 3, 2005.)

113) See the IP Agreement, Section 2.1.

114) See the IP Agreement, Section 2.1. In the Gaesung ICZ and the Kumgangsan TR, the EES Agreement will govern matters regarding entry, sojourn and movement of employees or counsels of the investor.

115) See the IP Agreement, Section 2.1.

116) See the IP Agreement, Section 2.3.

117) See the IP Agreement, Section 5.1.

118) See the IP Agreement, Section 9.1. Reportedly, in August 2004, North Korea published officially the code collections containing 112 laws and regulations including its constitution, civil code, criminal code revised (April 29, 2004), criminal procedure law revised (May 2004), and other foreign investment laws and regulations in force. This book seems to target not only investors but also North Korea's ordinary people. In the past North Korea published only collections regarding the Rajin-Sonbong FETZ, therefore this publication is understood as a meaningful change in practice. See Yonhap, "Buk Beop-jeon Bal-gan Jeong-bu Kwan-kye-ja-ui Ban-eung [South Korean Officials Comments on North Korea's Publication of Code Collections]," ChosunIlbo, January 16, 2005. (Available at http://nk.chosun.com/news/news.html?ACT=detail&cat_id=7&res_id=57851&page=1; last visited May 3, 2005.); Yonhap, "Interview: Chang Meong-Bong Buk-han-beop Yeon-gu-hoe-jang [Interview with Meong-bong Chang]," ChosunIlbo, January 16, 2005. (Available at http://nk.chosun.com/news/news.html?ACT=detail&cat_id=6&res_id=57842&page=1; last visited May 3, 2005.); Yonhap, "Buk Beop-jeon Kuk-nae Pan-mae

providing other investment-related information at the request of South Korea.¹¹⁹⁾

Fourth, with respect to expropriation, the IP Agreement covers indirect expropriation as well as direct expropriation.¹²⁰⁾ North or South Korea is, in case of expropriation, committed to pay "prompt, adequate and effective compensation".¹²¹⁾

Eo-Teon Ui-mi Gat-na [What Does the Sale of North Korean Code Collections mean?], ChosunIlbo, January 31, 2005. (Available at http://nk.chosun.com/news/news.html?ACT=detail&cat_id=6&res_id=58443&page=1; last visited May 3, 2005.)

119) See the IP Agreement, Section 9.2.

120) According to the U.S. Model BIT, Annex B, direct expropriation means the case that an investment is nationalized or otherwise directly expropriated through formal transfer of title or outright seizure, while indirect expropriation means the case that an action or series of actions by a host country has an effect equivalent to direct expropriation without formal transfer of title or outright seizure.

121) Article 4 of the IP Agreement provides as follows:

- (1) South or North Korea shall not nationalize, expropriate, or restrict the property rights of, or take any measures having the effect equivalent to nationalization, expropriation or restriction on, the investment assets (the "Expropriation"). Notwithstanding the above, the Expropriation can be carried out for a public purpose upon the Investment Assets from the investor; provided that the Expropriation occurs under legal procedures that do not discriminate against the investor compared to investors of the other party or investors from foreign countries.
- (2) South or North Korea shall, without delay, pay such compensation including interest at the general commercial rate starting from the date of the Expropriation until the date of payment. The amount of compensation shall equal the international market value of the investment immediately before the decision on the Expropriation became public knowledge.
- (3) South or North Korea shall accord to the investors of the other party treatment no less favorable than that accorded to its own investors or to investors of foreign countries with respect to restitution or compensation when the investors from the other party suffers losses related to the investment assets due to an armed conflict or other abnormal situations.

In this regard, Seong-Ho Jhe interprets that the IP Agreement does not cover creeping expropriation or other measures that could bring about the same effect as an expropriation or nationalization. (See, Seong-Ho Jhe, "Four Major Agreements on Economic Cooperation: Legal Measures for Implementation", *East Asian Review*, The Institute for East Asian Studies, Vol. 16, No. 4 winter 2004 ("Seong-Ho Jhe"), at 27.) However, his interpretation is not correct because, as reviewed above, the IP Agreement expressly addresses the indirect expropriation or creep expropriation by providing for "any measures having the effect equivalent to nationalization, expropriation or restriction on the Investment Assets". However, the detailed guideline for interpretation or application of indirect expropriation has not been sufficiently discussed in Korea so far. Therefore, whether any measures to be taken by North Korea constitute indirect expropriation may be arguable in the future. From South Korea's point of view, even though an inter-Korean transaction is not regarded as that between two foreign countries, some internationally recognized precedents could be applied *mutatis mutandis* to the inter-Korean agreement. For example, in *Metalclad Corporation v. the United Mexico States* case, one of the NAFTA cases, the arbitral tribunal ruled that "expropriation under the NAFTA includes not only open, deliberate and acknowledged takings of property, such as outright seizure or formal or obligatory transfer of title in favor of the host State, but also covert or incidental

These provisions are substantially similar to those found in bilateral investment treaties between other foreign countries.¹²²⁾ Fifth, the IP Agreement addresses the

interference with the use of property which has the effect of depriving the owner, in whole or in significant part, of the use or reasonably-to-be-expected economic benefit of property even if not necessarily to the obvious benefit of the host State.” See *Metalcal Corporation v. the United Mexico States*, ICSID Case No. ARB (AF)/97/1, Award rendered on August 30, 2000, paragraph 103. (The award is available at <http://www.worldbank.org/icsid/cases/conclude.htm>; last visited May 3, 2005.) The U.S. Model BIT, Annex B suggests the following guidelines for determining whether certain measures constitute indirect expropriation: (a) The determination of whether an action or series of actions by a contracting party, in a specific situation, constitutes an indirect expropriation, requires a case-by-case, fact-based inquiry that considers, among other factors, (i) the economic impact of the government action, although the fact that an action or serious of actions by a contracting party has an adverse effect on the economic value of an investment, standing alone, does not establish that an indirect expropriation has occurred; (ii) the extent to which the government action interferes with distinct, reasonable investment-backed expectations; and (iii) the character of the government action. (b) Except in rare circumstance, nondiscriminatory regulatory actions by a Party that designed and applied to protect legitimate public welfare objectives, such as public health, safety and the environment, do not constitute indirect expropriation (See *ibid*, U.S. Model BIT, Annex B).

122) See the IP Agreement, Article 4. For Reference, Article 5 (Expropriation) of the Agreement between the Government of South Korea and the Government of the Socialist Republic of Vietnam (“Vietnam”) for the Promotion and Protection of Investments provides as follows:

- (1) Investments of investors of either contracting party shall not be nationalized, expropriated or subjected to measures having an effect equivalent to nationalization or expropriation (“expropriation”) in the territory of the other contracting party except for a public purpose, under due process of law, on a non-discriminatory basis and provided that it is accomplished by prompt, adequate and effective compensation. Such compensation shall amount to the market value of the investment expropriated immediately before the expropriating action was taken or became public knowledge, whichever is earlier, shall include interest from the date of expropriation at the applicable commercial rate and shall be made without delay, be effectively realizable and be freely transferable.
- (2) An investor of one contracting party claiming that all or part of his investment has been expropriated shall have a right to prompt review, by a judicial or other independent authority of the other contracting party, of his or its case and of the valuation of his or its investment in accordance with the principles set out in paragraph (1) of this Article.
- (3) Where one contracting party expropriates the assets of a company which is incorporated or constituted under its laws and regulations, and in which investors of the other contracting party own shares or other forms participation, the provision of paragraph (1) and (2) of this Article shall apply.

(The English version of the above treaty is available at http://www.mofat.go.kr/ko/division/jo_treaty_list.mof?ipage=&b_code=treaty_1&div_m_code=NN; last visited May 3, 2005.)

The U.S. Model BIT, Article 6 (Expropriation and Compensation) specifies as follows:

- (1) Neither Party may expropriate or nationalize a covered investment either directly or indirectly through measures equivalent to expropriation or nationalization (“expropriation”), except: (a) for a public purpose; (b) in a non-discriminatory manner; (c) on payment of prompt, adequate, and effective

relationship between the IP Agreement and other statutes or contracts. If any of the (i) laws of the host party (i.e. South or North Korea in which investor invests), (ii) international treaties where both South and North Korea are members,¹²³⁾ or (iii) contracts between the host party and the investor, contain more favorable treatment than accorded by the IP Agreement, such laws, treaties or contracts shall, limited to those provisions specifying a more favorable treatment, prevail over the IP Agreement.¹²⁴⁾ Sixth, the IP Agreement retroactively applies to all investments made prior to its entry force.¹²⁵⁾ Therefore, Hyundai Asan’s investments made before August 2003 and any of its rights under Hyundai Kumgangsan Agreement, the 2000 SEZ Agreement and the 2002 SEZ Agreement will be protected as the investment assets under the IP Agreement. Furthermore, any disputes relating to, or arising out of, the violation of the rights vested by the IP Agreement, if not settled through mutual consultation, shall be resolved through the arbitration of the inter-Korean

compensation; and (d) in accordance with due process of law and Article 5 [Minimum Standard of Treatment] (1), (2), and (3).

- (2) The compensation referred to in paragraph 1 shall: (a) be paid without delay; (b) be equivalent to the fair market value of the expropriated investment immediately before the expropriation took place (“the date of expropriation”); (c) not reflect any change in value occurring because the intended expropriation had become known earlier; and (d) be fully realizable and freely transferable.
- (3) If the fair market value is denominated in a freely usable currency, the compensation referred to in paragraph 1 shall be no less than the fair market value on the date of expropriation, plus interest at a commercially reasonable rate for that currency, accrued from the date of expropriation until the date of payment.
- (4) If the fair market value is denominated in a currency that is not freely usable, the compensation referred to in paragraph 1 - converted into the currency of payment at the market rate of exchange prevailing on the date of payment - shall be no less than: (a) the fair market value on the date of expropriation, converted into a freely usable currency at the market rate of exchange prevailing on that date, plus (b) interest, at a commercially reasonable rate for that freely usable currency, accrued from the date of expropriation until the date of payment.
- (5) This Article does not apply to the issuance of compulsory licenses granted in relation to intellectual property rights in accordance with the TRIPS Agreement.

123) Since April of 2003, both South and North Korea are members of Berne Convention for the Protection of Literary and Artistic Works (Paris Text 1971) (“Berne Convention”). For more about Berne Convention, see website at <http://www.wipo.int/treaties/en/ip/berne/> (last visited May 3, 2005).

124) See the IP Agreement, Article 8. Therefore, if the Gaesung Law, the Kumgangsan Law or Hyundai Kumgangsan Agreement or others contains more favorable treatment than accorded by the IP Agreement, the relevant provision of such laws and contracts prevail over the IP Agreement.

125) See the IP Agreement, Article 11.

Commercial Arbitration Committee under the DRP Agreement.¹²⁶⁾ The issues as to the dispute resolution procedure will be discussed below.

3. Agreement on Prevention of Double Taxation

The DT Agreement, consisting of a preamble and 28 articles, addresses matters of preventing dual taxation related to, or arising out of, inter-Korean economic exchange and investment, on the premise that inter-Korean economic activities are domestic transactions among Korean peoples, not ones between different countries.¹²⁷⁾ Details of the DT Agreement are similar to those of the United States Model Income Taxation Convention dated September 20, 1996.¹²⁸⁾ The DT Agreement applies to a natural person liable to taxation and a juridical person for taxation purposes who are residents of South or North Korea or both.¹²⁹⁾ The DT Agreement applies the following taxes: (i) the corporation tax, the income tax and the inhabitant tax, in the case of South Korea; (ii) the enterprises income tax, the individual income tax and the local tax on income, in the case of North Korea.¹³⁰⁾ While the corporation tax rate in South Korea is 25% of tax base (13% where the tax base is not over 100 million Korean won) on and after January 1, 2005,¹³¹⁾ the enterprise income tax in the Gaesung ICZ is 14% of tax base (10% as for enterprise engaged in construction of infrastructure, high-tech industry, and light industry.) as reviewed below. Therefore, South Korean companies that invest in the Gaesung ICZ are expected to enjoy tax reduction benefits.

4. Agreement on Clearing Settlement

Clearing settlement refers to a payment system in which North and South

126) See the IP Agreement, Article 7.

127) See the DT Agreement, Preamble.

128) See United States Model Income Taxation Convention as of September 20, 1996 (available at <http://www.treas.gov/offices/tax-policy/library/model996.pdf>; last visited May 3, 2005.)

129) See the DT Agreement, Article 2.

130) See the DT Agreement, Section 3.1. Further, the DT Agreement also applies to any identical or substantially similar taxes that are imposed after the date of signature thereof, in addition to, or in place of, the existing taxes. (See the DT Agreement, Section 3.2).

131) See Ministry of Finance & Economy, Korean Taxation 2004, p. 88. (Available at http://www.nta.go.kr/menu/users/ntseng/Tax_Guide1.htm; last visited May 3, 2005.)

Korea's enterprises do not pay their bill on every trade basis but instead put their bills on the books of a clearing account, which is opened in the clearing settlement banks, and then settle their bills on a yearly basis.¹³²⁾ The CS Agreement, consisting of a preamble and 10 articles, provides for the clearing system to apply to payments of inter-Korean traded goods and payment of services related to such traded goods.¹³³⁾ Under the CS Agreement, South Korea's Export-Import Bank of Korea and North Korea's Foreign Trade Bank of DPRK were designated as each party's clearing settlement banks. According to Ministry of Unification, working-level representatives of both clearing settlement banks reached and initialed the agreement on the clearing settlement operation on June 25, 2004.¹³⁴⁾

5. Agreement on the Resolution Procedures for Commercial Disputes

The advanced disputes resolution procedure is indispensable for the promotion and protection of investments in North Korea.¹³⁵⁾ In this context, the key legal framework establishing the predictable and transparent nature of inter-Korean commercial disputes is the DRP Agreement which addresses issues as to (i) the establishment of the inter-Korean Commercial Arbitration Committee, (ii) the arbitral tribunal, (iii) jurisdiction, (iv) the arbitral procedure, (v) governing law and (vi) the enforcement of arbitral award etc. Additionally, the two Koreas executed the Agreement on the Establishment and Operation of the Inter-Korean Commercial Arbitration Committee (the "Arbitration Committee Agreement").

First, the Inter-Korean Commercial Arbitration Committee will consist of two chairpersons and eight committee members appointed by both South and North

132) "If the direct settlement between the two Koreas be put into practice, South Korean enterprises will be able to receive their bill directly from the Export-Import Bank of Korea, contributing not only to cost and time saving compared to the previous system of the indirect settlement via a third nation, but also to easy receipt of money sent to North Korea" according to Ministry of Unification. See Ministry of Unification, "Issues in Focus," June 30, 2004. (Available at <http://www.unikorea.go.kr> (last visited September 6, 2005).)

133) See the CS Agreement, Article 1.

134) See Ministry of Unification, Issues in Focus, June 30, 2004. For more details of the CS Agreement, See Seung-Ho Ryu, "Cheong-san Kyeol-je Je-do Do-ip-ui Hyo-kwa [The Effect of Introduction of Clearing Settlement System]," Su-eun Hae-oe Kyeong-je [Su-eun Overseas Economy], November 2003.

135) Since the late 1980's, the inter-Korean trade has gradually increased and the volume of the inter-Korean trade in 2003 reached up to US\$ 720 billion. Accordingly, during the past fifteen years, a lot of commercial disputes

Korea for renewable periods of four years¹³⁶⁾ and will be established within 6 months commencing from August 5, 2005.¹³⁷⁾ The Inter-Korean Commercial Arbitration Committee is an independent judicial entity that is able to sign agreements, acquire and dispose of its property, and institute legal actions within the scope necessary for the performance of its function and duties in the two Koreas.¹³⁸⁾ The two Koreas are committed to securing the independence of the Inter-Korean Commercial Arbitration Committee and arbitral tribunal.¹³⁹⁾ Under the DRP Agreement, no decision of the Inter-Korean Commercial Arbitration Committee regarding any petition by the parties concerned relating to the arbitration procedure shall be subject to the jurisdiction of the courts of either South or North Korea.¹⁴⁰⁾ Second, the arbitral tribunal will consist of three arbitrators appointed by mutual agreement of the parties

between South and North Korea have occurred. Implausibly, however, no inter-Korean commercial dispute is known to have been resolved through the arbitration procedure of either South or North Korea. This is due to the fact that North Korea's counter parties were not familiar with the commercial arbitration system or the legal disputes resolution procedure, and that thus they objected to the arbitration procedure or the third country court's judgment. Subsequently, no judgment or arbitral award of South Korea has been recognized or enforced in North Korea and visa versa. Even if investor may obtain any arbitral award from South Korea or other countries, enforcement thereof in North Korea is not guaranteed because North Korea, unlike South Korea which ratified the United Nations Convention on the Recognition and Enforcement of Foreign Arbitral Awards (the "New York Convention") on February 8, 1973, is not a member of the New York Convention or any international conventions for recognition or enforcement of foreign arbitral awards or foreign judgments. As for East Germany before the unification of Germany, it was a member of the New York Convention and another similar international convention. So it may be inappropriate to apply German cases to the Korean case.

136) See the DRP Agreement, Article 2; the Arbitration Committee Agreement, Article 2.

137) The Inter-Korean Commercial Arbitration Committee was to be established within 6 months commencing from the date when the Arbitration Committee Agreement becomes into effect, and as discussed above the Arbitration Committee Agreement came into effect on August 5, 2005. See the Arbitration Committee Agreement, Section 14.4. But the Inter-Korean Commercial Arbitration Committee is not yet established by 2005.

138) See the Arbitration Committee Agreement, Article 1. The Inter-Korean Commercial Arbitration Committee will perform (i) arbitration or conciliation of commercial disputes subject to its jurisdiction as mentioned below (ii) enactment, amendment and supplementation of the arbitration rules and the regulations relating thereto, (iii) confirmation and registration of arbitrators appointed respectively by South and North Korea, (iv) appointment of arbitrators under the DRP Agreement, (v) any other functions conferred upon the Inter-Korean Commercial Arbitration Committee by mutual agreement of the two Koreas. (See the DRP Agreement, Article 3; the Arbitration Committee Agreement, Article 3.)

139) See the Arbitration Committee Agreement, Articles 9.2 and 9.3.

140) See the Arbitration Committee Agreement, Article 4.

concerned.¹⁴¹⁾ The arbitrators, said chairpersons and members of the Inter-Korean Commercial Arbitration Committee, will enjoy immunity from the legal process of either South or North Korea's courts with respect to the acts preformed by them directly in the course of their duties, unless the Inter-Korean Commercial Arbitration Committee waives this immunity upon a mutual agreement of both South and North Korea.¹⁴²⁾ Third, the Inter-Korean Commercial Arbitration Committee has jurisdiction over the following disputes: (a) commercial disputes arising in the course of economic exchanges and cooperation (i) between the parties concerned from South and North Korea or (ii) between the party concerned of one party (i.e. South Korea) and the competent authority of the other party (i.e. North Korea), and matters related thereto; (b) disputes between one party (i.e. North Korea) and investors of the other party (i.e. South Korea) arising from a violation of the rights vested by the IP Agreement.¹⁴³⁾ Fourth, the arbitral rules will be modeled after

141) If both parties concerned fail to reach an agreement as to appointment of arbitrators within a certain period, each party shall appoint one arbitrator from thirty registered arbitrator-candidates appointed by South or North Korea respectively, and two appointed arbitrators shall then, based on mutual consultation, select one additional arbitrator among the said registered arbitrator-candidates to act as a presiding arbitrator. If a presiding arbitrator is not appointed within fifty days from the date of the receipt of the application for arbitration, both chairpersons of the Inter-Korean Commercial Arbitration Committee shall appoint the presiding arbitrator among said registered arbitrator-candidates based on mutual consultation or by lot. If the Inter-Korean Commercial Arbitration Committee failed to appoint a presiding arbitrator within thirty days from the date of the receipt of the request thereof, it may commission the International Center for the Settlement of Investment Disputes ("ICSID") to appoint a presiding arbitrator. (See the Arbitration Committee Agreement, Article 10.) In this regard, North Korea is not a party to the Convention on the Settlement of Investment Disputes between States and Nationals of Other States (the "ICSID Convention" or "Washington Convention") while South Korea has been the party thereto after its ratification of it in 1967 (See ICSID website: <http://www.worldbank.org/icsid/constate/c-states-en.htm>; last visited May 3, 2005). Notwithstanding the above, Article 4 (1) of the Additional Facility Rule provides that any agreement providing for conciliation or arbitration proceedings under the Additional Facility in respect of existing or future disputes requires the approval of the Secretary-General of ICSID. (The ICSID Convention is available at <http://www.worldbank.org/icsid/basicdoc/basicdoc.htm> (last visited May 3, 2005) and the Additional Facility Rule is available at <http://www.worldbank.org/icsid/facility/facility.htm> (last visited May 3, 2005)).

142) See the Arbitration Committee Agreement, Article 9.4.

143) See the DRP Agreement, Articles 3 and 8. In the case of (a) above, it is, upon the application for arbitration, required to submit to the Inter-Korean Commercial Arbitration Committee the written agreement between the parties concerned under which the underlying dispute is subject to the arbitration of the Inter-Korean Commercial Arbitration Committee, and such written agreement to arbitrate cannot be retracted unilaterally by one party concerned. In the case of (b) above any party may submit the application for arbitration even though there is no written agreement to arbitrate.

international rules such as the United Nations Commission on International Trade Law (UNCITRAL)'s Arbitration Rules.¹⁴⁴⁾ Fifth, the arbitral tribunal shall render the award in accordance with the governing law mutually agreed upon between the parties concerned. In the absence of an agreement regarding the governing law,¹⁴⁵⁾ the arbitral tribunal shall apply the relevant laws and regulations of South or North Korea, general principles of international laws, and the customary practice of international trade in rendering an arbitral award.¹⁴⁶⁾ Sixth, the arbitral award, unless there are special circumstances¹⁴⁷⁾ to consider, may be enforced in the same manner as the final and conclusive judgment of the respective relevant court in South or North Korea.¹⁴⁸⁾ In this regard, one must pay attention to the statute of limitations regarding any claim established by judgment or any other process having the same effect as a judgment (including arbitral award). Under South Korea's Civil Code, the statute of limitation of such a claim is ten years.¹⁴⁹⁾ But under the Judgment &

144) At the seminar held by the Ministry of Justice of South Korea discussing the desirable resolution procedure of the commercial disputes arising out of inter-Korean exchange and cooperation on July 28, 2004, Seung-hwa Chang, a professor of Seoul National University, College of Law, suggested that draft arbitration rules be prepared. The Korean Commercial Arbitration Board held a policy seminar and academic rally on the theme 'Acceleration of Solutions to Commercial Disputes Following South-North Economic Exchanges' on September 4, 2004, at the seminar the following themes had been discussed: 'Basic Directions for Enactment of the Arbitration Rules of the Inter-Korean Commercial Disputes Committee' and 'Tasks for Resolution of the Inter-Korean Commercial Disputes Committee.' (Seminar Materials are available at <http://www.kcab.or.kr/>; last visited May 3, 2005). The participants at the above seminars suggested that the arbitral rules under the DRP Agreement be modeled after the internationally accepted arbitration rules.

145) From the practical point of view, most North Korean laws are inappropriate to regulate international transaction or commercial disputes. Also investors have been reluctant to resolve the disputes in the North Korean judicial system because they cannot predict the result due to the lack of transparency and relevant precedent. North Korean counterparts also have been reluctant to accept South Korean laws as a governing law. This is why many past contracts regarding inter-Korean investment or transaction did not contain a clause on the governing law.

146) See the DRP Agreement, Article 12. Since the Gaesung Law and its implementing regulations have been enacted by North Korea based on consultation with South Korea and the provisions thereof are more market-friendly than those of any other laws and regulations ever enacted by North Korea, the Gaesung Law and its implementing regulations may be one of the alternatives as a governing law, even though not sufficient. In addition, inter-Korean agreements regulating contract, corporation or other issues would be another option.

147) Whether such special circumstances exist shall be subject to the determination by the Inter-Korean Commercial Arbitration Committee; therefore, the guidelines for such determination need to be adopted and to be public to secure their predictability.

148) See the DRP Agreement, Article 16.3.

149) See South Korea's Civil Code, Article 165.

Decision Enforcement Law of North Korea anyone having such claim should file an application of the execution thereof within two months (or three months if approved by the relevant court) commencing from the date when such judgment or decision becomes final and conclusive,¹⁵⁰⁾ and such restriction is likely to apply to the arbitral award. Since North Korea's enforcement procedure has not been developed, the arbitral award holder may have considerable difficulties in enforcing such an award in North Korea within two or three months.¹⁵¹⁾

D. The Gaesung Law and its Regulation

1. The Developer and the Administrative Agency

Like the China-Singapore Suzhou Industrial Park, one of China's special economic zones, whose management was commissioned to the Singapore government (as a main developer) by the Chinese government at its early stage,¹⁵²⁾ North Korea entrusted the development and management of the Gaesung ICZ to South Korea, especially the designated developer (the "Developer") and the administrative organization (the "Administrative Agency") of the Gaesung ICZ. Therefore, more attention needs to be paid to the roles of the Developer and the Administrative Agency to understand the legal framework in the Gaesung ICZ. First, the Developer has not only the exclusive right to develop the Gaesung ICZ, but also to enjoy concessions regarding construction, transportation, storage, and advertisement business, and the Developer has the right to use the land located at the Gaesung ICZ for the period of 50 years commencing from the certificate issuance

150) See the Judgment & Decision Enforcement Law of North Korea, Article 14.

151) In this regard, there are two options: (i) for both South and North Korea to execute the amendment to the DRP Agreement addressing the statute of limitations of the above claim or (ii) for North Korea to revise the statute of limitations under the Judgment & Decision Enforcement Law of North Korea together with its enforcement procedure.

152) The China-Singapore Suzhou Industrial Park was established on February 26, 1994 when both the Chinese and Singaporean government reached the Agreement on the Joint Development of Suzhou Industrial Park, under which Singapore had a 65% share in the joint venture in charge of development of the park from 1994 to 2001 and led the development of the park. Having acquired 65% of the shares in the joint venture in 2001, China has led the management of the park. For more details, see its website at <http://www.sipac.gov.cn/english/default.htm> (last visited May 3, 2005).

date.¹⁵³⁾ In this regard, North Korea designated Hyundai Asan as the Developer on December 23, 2002, and issued to Hyundai Asan the certificate of the land use rights to over 20 million pyongs or approximately 66 million m² at that time. However, owing to financial difficulties, Hyundai Asan assigned its right to develop the industrial park district of the Gaesung ICZ to KLC by executing the December 4, 2002 Agreement (the “2002 SEZ Agreement”).¹⁵⁴⁾ Further, the Developer is responsible, by itself, by joint venture with other investors, or by subcontracting, for constructing the infrastructure necessary for the Gaesung ICZ, while North Korea’s central government is responsible for, removing preexisting buildings, and relocating residents at the Developer’s expense.¹⁵⁵⁾ The Developer enjoys tax exemption with respect to its property and any development-related business.¹⁵⁶⁾ Currently, KLC and Hyundai Asan are constructing the infrastructure for the first stage site of the Gaesung ICZ.¹⁵⁷⁾

Second, the Developer has the right to appoint the first president (the “President”) of the Administrative Agency or the local administrator of the Gaesung ICZ. The President may, at his or her discretion, appoint, and dismiss, members of the Administrative Agency, and establish any department thereof.¹⁵⁸⁾ The Administrative Agency, consisting mainly of South Korean experts, was established in the name of the “Gaesung Industrial District Management Committee” in October 20, 2004 after Hyundai Asan, together with KLC, appointed the President with

153) See the Gaesung Law, Articles 10, 11 and 20; Development Regulation 19.

154) The 2002 SEZ Agreement was executed among Hyundai Asan, KLC, North Korea’s Asian-Pacific Peace Committee and Association of National Economic Cooperation.

155) See the Gaesung Law, Articles 15 and 17.

156) See Tax Regulation, Article 17.

157) Most of the infrastructure necessary for the one million pyong of the first stage site (including the pilot site) are being constructed based on South Korea’s support and supervision. Korea Electric Power Corporation, a South Korean government invested corporation, started to provide electricity to companies in the pilot site from South Korea on a commercial basis after March 16, 2005. Korea Telecom, a South Korean telecommunication provider, is scheduled to establish facilities for internet and telephone services from South Korea to the Gaesung ICZ in the near future as reviewed below.

158) See the Gaesung Law, Article 24; Administrative Agency Regulation, Article 5, 6 and 8. Matters regarding appointment and dismissal of the President, except for appointment of the first President, are subject to the bylaws of the Administrative Agency. For reference, the President above indicates *Yisajang* (in Korean), which is usually translated into chairman of board of directors. Regardless of the usual implication thereof, however, I translate *Yisajang* in this paper into ‘President’ to emphasize that the role of *Yisajang* is to represent, administrate, the Administrative Agency of the Gaesung ICZ.

approval of Ministry of Unification of South Korea.¹⁵⁹⁾ The Administrative Agency handles such affairs as (i) the preparation and implementation of the plan for development of the Gaesung ICZ, (ii) the issuance of approval and permits required for any business or enterprises or construction, (iii) the registration of real properties and vehicles, (iv) the supervision of labor relations, (v) the control of foreign exchanges, (vi) promulgating any sub-regulations necessary for the implementation of the Gaesung Law and other regulations, etc. in accordance with the Gaesung Law and its implementing regulations, under guidance of North Korea’s central guidance agency (the “Central Guidance Agency”).¹⁶⁰⁾ In addition, the Administrative Agency has the authority to regulate (a) all economic activities in the Gaesung ICZ, in accordance with the Gaesung Law and its regulations, or (b) any other economic matters not provided in the Gaesung Law and its relevant regulations through consultation with the Central Guidance Agency.¹⁶¹⁾ As far as economic activities are concerned, the Administrative Agency functions as a local government, which, to some extent, is independent from North Korea’s central government. However, the Administrative Agency cannot use any taxes collected under the Tax Regulation. Rather it will be operated with the operation fund consisting of some fees and, if necessary, an amount equivalent to 0.5% of the enterprises’ total monthly wages, to be paid by enterprises.¹⁶²⁾ At the initial stage of the Gaesung Project, no operation

159) The official website of the Gaesung Industrial District Management Committee is <http://www.kidmac.com/> (last visited September 6, 2005).

160) The Central Guidance Agency under the Gaesung Law refers to *Jung-ang -teuk-gu -gae-bal -ji-do -chong-guk* [Central Guidance Agency for Special Economic Zone Development] of Cabinet. Also North Korea’s central government controls matters regarding tax and public security. See the Gaesung Law, Chapter 3; Administrative Agency Regulation, Article 2, 4, and 13. The key role of the Central Guidance Agency is as follows: (i) to designate the Developer; (ii) to supervise the development plan of the Gaesung Project; (iii) to promulgate rules necessary to implement the Gaesung Laws and their implementing regulations; (iv) to secure provision of manpower, water and raw materials requested by investors; (v) to sell the products manufactured in the Gaesung ICZ in other areas of North Korea; (vi) to administer taxation; and (vii) other matters provided in individual implementing regulations. See the Gaesung Law, Article 22. Meanwhile, the Administrative Agency is subject to the guidance of the Central Guidance Agency. But the term ‘guidance’ is not a clearly formed concept. While it may be said that the Central Guidance Agency is formally superior to the Administrative Agency, the Administrative Agency is in practice a counter partner to the Central Guidance Agency on an equal basis. Further, the Ministry of Unification of South Korea supervises the Administrative Agency as well.

161) See the Gaesung Law, Article 9.

162) See the Gaesung Law, Article 27; Administrative Agency Regulation, Article 19. Such fees will be determined by the Administrative Agency.

funds could be raised from the enterprises, so the Administrative Agency was being operated with funds financed by the South Korean government. In addition, South Korea's Gaesung Industrial Complex Support Team members are composed of government officials and private sector experts who are closely working with the Administrative Agency.

2. Real Property

The Real Property Regulation, consisting of 58 articles, was promulgated based on consultation between the two Koreas. The concept and legal framework thereof is basically similar to those of South Korea's Civil Code (especially real property law), although the private ownership to land is not recognized. Under the Real Property Regulation, real property includes the land use right, buildings and their appurtenances. Any investors (South Korean, Korean overseas, foreigner and company controlled thereby) may acquire, transfer, lease, establish mortgage on, or inherit the said real property.¹⁶³⁾ With respect to the land use right, the Developer has already acquired the right to use the whole land of the Gaesung ICZ for 50 years. Unlike the Rajin-Sonbong FETZ where transfer of the land use right is subject to the prior approval of the land administration office,¹⁶⁴⁾ any investor may freely acquire the land use right regarding a certain area, or sublease such an area, from the Developer or its assignee. In such case the term of such land use right or lease should be within the remaining period of the said 50 years.¹⁶⁵⁾ The land use fee will

163) See Real Property Regulation, Chapter 1. Importantly, Real Property Regulation also applies to real property which an investor acquires to construct infrastructure connected from the outside area to the Gaesung ICZ, even though such real property is located on the outside. (See Real Property Regulation, Article 2) Meanwhile, the said transfer, lease, and establishment of mortgage on real property (except for inheritance thereof) will be effective only after it is registered with the Administrative Agency. The detailed procedure for registration of real property is controlled or managed by the Administrative Agency in accordance with the relevant rule to be made by the Administrative Agency. (See Real Property Regulation, Articles 5, 9, 11, 25, 33 and 54.) This registration requirement for effective transaction under Real Property Regulation is the same as that under South Korean Civil Code.

164) See the Land Lease Law of North Korea, Article 15. In the Rajin-Sonbong FETZ, the Land Lease Law and its implementing Regulations govern matters only related to the land use right, while 'Regulations on Transfer and Mortgage of Buildings in the Free Economic and Trade Zone' governs matters related to buildings.

165) See Real Property Regulation, Article 11. According to Hyundai Asan and KLC, the parcel-out cost of the Gaesung ICZ is expected to be 150,000 Korean won (US\$ 150 or less) per pyong.

be charged on the investor (except for the Developer) having the land use right only after 10 years elapse commencing from the execution date of the lease agreement between the Developer and the Central Guidance Agency.¹⁶⁶⁾ If the relevant authority cancels the lease before the expiration of the original lease term due to unavoidable circumstances,¹⁶⁷⁾ it should make proper compensation for loss or offer the investor other land with the same conditions of original lease.¹⁶⁸⁾ After expiration of the said 50-years lease term, the term for the land use right could be renewed upon the investor's request, unless an unavoidable circumstance occurs. In case the relevant authority rejects the renewal of the land use right and there are buildings or facilities located on the underlying land, the relevant authority should make proper compensation for such buildings or facilities.¹⁶⁹⁾ Detailed guidelines for compensation will be determined in accordance with the IP Agreement, discussed in Part III.C above. Investors may own buildings only if they have the land use right or the registered lease¹⁷⁰⁾ with respect to the pertinent land.¹⁷¹⁾ Furthermore, investors may establish mortgages, land use rights, registered leases, and buildings to secure its or the third party's obligation in favor of creditors.¹⁷²⁾ Investors may freely acquire, transfer or inherit the registered lease and mortgage as well.

166) See Real Property Regulation, Article 15. Interestingly, in July 31, 2002 immediately after the said 7.1 Measures, the North Korean Cabinet made the decision to impose the land use fee on most individuals, enterprises and institutions having land for farming purpose. The relevant documents were disclosed at http://www.bekkoame.ne.jp/ro/renk/20041205/renk_flash4.htm (last visited May 3, 2005)(in Japanese and Korean). This measure implies, like China, that the land is de facto in the process toward privatization, allowing individuals to use and dispose of the value of such land.

167) The term "unavoidable circumstance" is one of the undefined terms. Detailed guidelines need to be included in the rule to be made by the Administrative Agency.

168) See Real Property Regulation, Article 16

169) See Real Property Regulation, Article 18.

170) There are two types of leases in the Gaesung ICZ: one is the unregistered lease where the lessee may exercise its lease only against the lessor, thus if the third party acquires the land use right to the pertinent land, the third party could evict the said lessee; and the other is the registered lease which the lessee may exercise against both lessor and the third party. See Real Property Regulation, Article 25.

171) See Real Property Regulation, Articles 19.

172) See Real Property Regulation, Articles 23, 25, 26, 27 and 45. For reference, South Korean investors' assets in the Gaesung ICZ could be used as collateral on and after February 3, 2005. Therefore, the companies in the Gaesung ICZ can borrow money from the Export-Import Bank of Korea by mortgaging their buildings, machinery and the land use rights in the Gaesung ICZ at the maximum rate of 40% to 70% depending on the investment assets. See Ministry of Unification, Bo-do Ja-ryo [Press Release], February 2, 2005. (Available at <http://www.unikorea.go.kr/>(last visited September 6, 2005).)

Meanwhile, the rights and interests of the investors, as well as the right to inherit their invested properties (including not only real property but also any other property) and interests, are protected under the Gaesung Law, its implementing regulations and the IP Agreement.¹⁷³⁾ With respect to nationalization or expropriation, the IP Agreement, as discussed above, will apply to the Gaesung ICZ as well. In expropriation cases, the Gaesung Law requires, as an additional procedure, prior consultation with the investor.¹⁷⁴⁾ Furthermore, since September 2004, the South Korean government has provided, through the Export-Import Bank of Korea, an insurance program covering losses against political risks in the Gaesung ICZ up to 90% of the invested amount within 2 billion Korean won per investor.¹⁷⁵⁾

3. Incorporation and Operation of Enterprises

As discussed above, the NK Constitution of 1998 permits investors to establish “various types of enterprises” in a special economic zone, and the Gaesung Law and Enterprise Regulation allow to investors (South Korean, Koreans abroad, foreigners and their companies or associations) to establish (i) ‘various types of enterprises’, either individually or together with other investors and (ii) its representative office or branch.¹⁷⁶⁾ More importantly, such enterprises may issue stocks or bonds in accordance with their Association of Incorporation,¹⁷⁷⁾ while the three types of foreign-invested enterprises¹⁷⁸⁾ under the Rajin-Sonbong FETZ legal system were not allowed to issue stocks or bonds. Therefore, investors in the Gaesung ICZ may, in principle, establish any kind of enterprise,¹⁷⁹⁾ regardless of whether such an enterprise issues stocks and bonds. Details of the forms of enterprises in the Gaesung ICZ are

173) See the Gaesung Law, Article 7; IP Agreement, Article 4.

174) See the Gaesung Law, Article 7.

175) See Ministry of Unification, Bo-do Ja-ryo [Press Release], September 23, 2004. (Available at <http://www.unikorea.go.kr/> (last visited September 6, 2005))

176) See the Gaesung Law, Article 3; Enterprise Regulation, Article 4.

177) See Enterprise Regulation, Article 17.

178) The three types of foreign-invested enterprises refer to equity joint venture enterprises, contractual joint venture enterprises and wholly foreign-owned companies as discussed above. See *supra* note 32.

179) In principle any joint venture enterprise based on a joint venture agreement between South and North Korea could be incorporated in accordance with the Gaesung Law and Enterprise Regulation. However, no North Korean institutions, enterprises or associations could engage in business in the Gaesung ICZ without agreement with

subject to the Gaesung Law and Enterprise Regulation, since other statutes for the Rajin-Sonbong FETZ and the Shinuiju SAR do not apply to the Gaesung ICZ.¹⁸⁰⁾ With respect to financial businesses (except for the insurance business as discussed below), like the Rajin-Sonbong FETZ where investors may establish the foreign invested bank or branch of a foreign bank with approval of the relevant authorities in accordance with the Foreign Invested Bank Law of 1993, any investor in the Gaesung ICZ may establish a wholly investor-owned bank or branch (“Investment Bank” as defined) in accordance with the Gaesung Law and its regulations.¹⁸¹⁾

Incorporation of an enterprise is subject to the approval of the Administrative Agency, which reviews the business of the enterprise together with the applications and decides whether to grant a license.¹⁸²⁾ Subsequently, if any enterprise changes its business or adds to its business, it should obtain additional approval from the Administrative Agency.¹⁸³⁾ In this regard, the Gaesung Law and Enterprise Regulation encourages investment in infrastructure, light industry and high-tech industry, while prohibiting businesses which do harm to national security and environmental protection, or hinder the development of the national economy, or which are technically out-dated.¹⁸⁴⁾ More details as to whether any business is encouraged, prohibited or restricted is subject to the detailed rules to be made by the

the Central Guidance Agency. See the Gaesung Law, Article 6. Also investors investing in the Gaesung ICZ are expected to prefer the wholly foreign-invested enterprise regardless of whether or not it issues stocks or shares rather than the joint venture enterprise with a North Korean party based on the past experience in the Rajin-Sonbong FETZ.

180) See the Gaesung Law, Article 9.

181) Enterprise Regulation does not include a specific provision regarding banks. Under the Foreign Exchange Regulation, however, the Administrative Agency controls foreign exchange and designates key currency as well. Also any investment bank established by investor in the Gaesung ICZ should submit the report regarding foreign exchange semi-annually to the Administrative Agency. Therefore, it is construed that establishment of Investment Bank or foreign banks branch is subject to the approval of the Administrative Agency. In this regard, Woori Bank, a South Korean bank, opened its branch in the Gaesung ICZ on December 7, 2004, which provides financial service to investors and the Administrative Agency. See website of Woori Bank at <http://www.wooribank.com/> (last visited May 3, 2005). Establishment of the said branch in the Gaesung ICZ was made with approval of, and registration with, the Administrative Agency in accordance with the Enterprise Regulation.

182) See the Gaesung Law, Article 35; Enterprise Regulation, Article 3.

183) See the Gaesung Law, Article 38.

184) See the Gaesung Law, Article 4. Enterprises doing business in encouraged areas could be given preferential treatment including reduction and exemption of taxes, favorable condition for leased land. See Enterprise Regulation, Article 3.

Administrative Agency based on consultation with the Central Guidance Agency.¹⁸⁵⁾ After obtaining approval to incorporate an enterprise, the investor must make an investment in the form of cash, property in kind, right to property, etc., within the investment schedule in accordance with the written approval.¹⁸⁶⁾ The enterprise to which the scheduled investment was made is required to register its establishment with the Administrative Agency, Customs Office, and the local tax office,¹⁸⁷⁾ and is legally incorporated on the date when the Administrative Agency issues the certificate regarding its incorporation.¹⁸⁸⁾ Thereafter the enterprise may do business. Since the Administrative Agency, consisting mainly of South Korean experts, plays a key role in issuing permits or the approval necessary for the incorporation of enterprises, the incorporation procedure does not impede investors from doing business in the Gaesung ICZ.

The Enterprise Regulation does not provide for specific corporate governance but requires, upon applying for approval regarding incorporation of an enterprise, the investor to submit to the Administrative Agency its articles of incorporation specifying its chief executive officer, auditor and management committee and its members.¹⁸⁹⁾ Given that an enterprise may issue stocks or bonds,¹⁹⁰⁾ and that dissolution of an enterprise is subject to the resolution of an investors' general meeting or board of directors,¹⁹¹⁾ each enterprise's association of incorporation needs to contain provisions regarding shareholders' meeting and board of directors. Notwithstanding the above, detailed corporate governance is determined by the enterprise's articles of incorporation.¹⁹²⁾ Meanwhile, it is noteworthy to mention that stocks or bonds issued in accordance with the articles of incorporation may be in circulation without any authorities' approval.¹⁹³⁾

Investors may enjoy protections under the IP Agreement, as discussed in Part

185) Even though the detailed rule has not been made public, the Administrative Agency has approved at its discretion ten or more projects for incorporation of enterprises in the Gaesung ICZ so far.

186) See Enterprise Regulation, Articles 10 and 11.

187) See Enterprise Regulation, Articles 12, 13, 14 and 15.

188) See Enterprise Regulation, Article 14.

189) See Enterprise Regulation, Articles 5 and 8.

190) See Enterprise Regulation, Article 17.

191) See Enterprise Regulation, Article 25.

192) In this regard, more comprehensive corporation law needs to be enacted in the near future.

193) In the Rajin-Sonbong FETZ, disposition of an investor's shares or interest is subject to approval of the

III.C.2. In addition to this, the Enterprise Regulation guarantees enterprises may (i) freely carry any materials necessary for business activities into the Gaesung ICZ and (ii) freely carry products and procured materials out of the Gaesung ICZ, as long as such materials are subject to a customs inspection.¹⁹⁴⁾ No tariff will be imposed on products carried into the Gaesung ICZ from South Korea,¹⁹⁵⁾ because inter-Korean transactions are regarded as domestic ones. Further, investors, or enterprises incorporated under the Enterprise Regulation may advertise their business or product in accordance with the Advertisement Regulation¹⁹⁶⁾ and they must purchase certain types of policies such as fire insurance policy, automobile insurance policy, gas insurance policy and casualty insurance policy from the insurance company designated by the Central Guidance Agency.¹⁹⁷⁾

Any enterprise may dissolve or liquidate itself based on a resolution of its investors' general meeting or board of directors without approval of the Administrative Agency.¹⁹⁸⁾ But members to be appointed to the liquidation committee are subject to approval of the Administrative Agency.¹⁹⁹⁾

4. Labor

The Gaesung Project is to combine North Korea's low-wage labor with South Korea's technology and capital. Most of the Gaesung Project's initial investors are labor-intensive companies. In this regard, Labor Regulation, consisting of 49 articles, addresses several investors' concerns. First, the Administrative Agency controls and supervises the enterprise's employment of workers and their work

relevant authority. See Equity Joint Venture Law of 1984 (revised in 1999), Article 12; the Contractual Joint Venture Law of 1992 (revised in 1999), Article 10; the Foreigner's Investment Law of 1999, Article 26.

194) See Enterprise Regulation, Articles 18 and 19. Entrance and Exit Regulation and the EES Agreement regulate detailed matters regarding carrying in-and-out procedures.

195) See Customs Regulation, Article 7.

196) Advertisement in the Gaesung ICZ is under supervision of the Administrative Agency. See Advertising Regulation, Article 4.

197) See Insurance Regulation, Articles 2, 3, 5, 6 and 7. The Insurance Regulation provides that only the insurance company designated by the Central Guidance Agency may do business in the Gaesung ICZ, which South Korea objected to.

198) See Enterprise Regulation, Article 25.

199) See Enterprise Regulation, Article 26.

conditions.²⁰⁰⁾ Second, enterprises may employ North Korean workers through the labor arrangement agency.²⁰¹⁾ While enterprises in the Rajin-Sonbong FETZ cannot reject the workers dispatched by the labor arrangement agency and can only contract with the labor arrangement agency (not directly with individual worker),²⁰²⁾ enterprises in the Gaesung ICZ may select qualified employees, via an interview or skill test, from the candidates provided to them by the labor arrangement agency,²⁰³⁾ and the enterprise may directly execute employment contracts with selected workers.²⁰⁴⁾ In addition, although enterprises are required, in principle, to employ North Korean workers, they may, if necessary, employ South Koreans, Koreans overseas or foreigners who are management personnel, technicians and skilled workers of special job classifications by notifying the Administrative Agency and the Central Guidance Agency of the details regarding such employees (i.e. name, position etc).²⁰⁵⁾

Third, wages must be higher than the minimum wages and they are to be determined by negotiations between employer and employee.²⁰⁶⁾ At the initial stage, the minimum monthly wage is US\$ 50 per month, which may increase up to 5% annually based on the agreement between the Administrative Agency and the Central Guidance Agency.²⁰⁷⁾ Enterprises may give incentives, such as rewards or bonuses, to their employees and payment must be made directly to individual workers by cash (in case of a reward, by cash or allowance in kind).²⁰⁸⁾ In providing

200) See Labor Regulation, Article 7.

201) See Labor Regulation, Article 8.

202) See Foreign Invested Enterprises Labor Regulation, Article 10. This regulation regulates labor conditions for workers employed by the said three types of foreign invested enterprises in the Rajin-Sonbong's legal system.

203) See Labor Regulation, Article 9. Therefore, if no qualified workers exist among candidate workers, enterprises may refuse to employ them, and request the labor arrangement agency to arrange another candidate group.

204) See Labor Regulation, Article 9. In such case, the labor arrangement agency may receive a commission from the relevant enterprise. The amount of commission will be determined based on consultation with the Administrative Agency, but has not been made public yet. See Labor Regulation, Article 11.

205) See the Gaesung Law, Article 37; Labor Regulation, Articles 3 and 12. For reference, in the Rajin-Sonbong FETZ, employment of foreigners is subject to the approval of the relevant authority. See Foreign Invested Enterprises Labor Regulation, Article 3.

206) See Labor Regulation, Articles 5 and 26.

207) See Labor Regulation, Article 25.

208) See Labor Regulation, Articles 24, 31, and 32.

these economic incentives, investors may, in principle, directly influence an individual workers' will to work. In addition to the minimum wage, enterprises must pay 15% of its total wages paid to its North Korean employees to the bank designated by the Central Guidance Agency as a social insurance fee.²⁰⁹⁾

Fourth, enterprises may dismiss their employees prior to the expiration of the employment terms in any of the following cases: (a) where the employee is incapacitated due to occupational disease, or a non-work related injury or disease; (b) where reduction of employees is unavoidable due to changes in managerial or technology environments; (c) where the employee is unable to carry out his or her occupational work due to the lack of skill or technology; and (d) where the employee has caused a great loss to the enterprise or seriously violated labor discipline.²¹⁰⁾ Whereas an employee dismissal in the Rajin-Sonbong FETZ requires a prior agreement from both the labor arrangement agency and the labor union,²¹¹⁾ dismissal of an employee in the Gaesung ICZ is not subject to the approval of any agencies. However, if the dismissal of an employee having worked over one year is due to a cause attributable to the enterprise, the dismissed employee is entitled to a severance payment equivalent to 30 days' average wages for each year of his continuous employment.²¹²⁾

Fifth, political organizations are prohibited from interfering with an enterprise's business. In the Rajin-Sonbong FETZ, under the Foreign Invested Enterprises Labor Regulation, the labor union is a party to the employment agreement and has the right to consent to the dismissal of employees and other matters regarding employees' rights and interests.²¹³⁾ Also in the Rajin-Sonbong, under the Implementing Regulation of Foreigner's Enterprise Law, the labor union may receive 1% to 2% of the total wages paid to its North Korean employees from the enterprise.²¹⁴⁾ However, in the Gaesung ICZ, it is questionable whether a labor union is permitted in the Gaesung ICZ because the Labor Regulation does not provide for a labor union. Even

209) With respect to the social security policy in North Korea, enterprises bear no other monetary obligation than the said social insurance fee. See Labor Regulation, Article 42.

210) See Labor Regulation, Article 14.

211) See Foreign Invested Enterprises Labor Regulation, Article 15. The said labor union refers to Jik-eop-dong-maeng in Korean, which is not only similar to the labor union but also of the nature of a political organization.

212) See Labor Regulation, Article 19.

213) See Foreign Invested Enterprises Labor Regulation, Articles 8, 14, 15 and 67.

214) See the 1994 Implementing Regulation of Foreigner's Enterprise Law, Article 62.

if the labor union is permitted, it is not entitled to receive any money from the enterprise. North Korea cannot mobilize employees for purposes unrelated to the relevant employer's business, but it may mobilize employees in case of a natural disaster etc., but only if the relevant employer agrees on the mobilization.²¹⁵⁾

Finally, enterprises are required to provide safe and hygienic work conditions, and safety and technical training, to their employees.²¹⁶⁾ If the employee dies or is injured or poisoned on the job, the enterprise must immediately notify the Administrative Agency of the accident, and the Central Guidance Agency, in consultation with the Administrative Agency, will investigate the accident.²¹⁷⁾ The overall legal structure of the Labor Regulation provides investors with a more favorable management environment than that provided by the Rajin-Sonbong FETZ.

5. Market System and Foreign Exchange

In principle, prices and wages are to be determined based on the laws of supply and demand, which are similar to the 7.1 Measures mentioned above. In other words, the prices for goods (including consumption goods, production goods) and services in the Gaesung ICZ are to be determined by the negotiation/agreement of the parties concerned, based on the international market prices.²¹⁸⁾ Wages are also to be determined based on negotiations between employer and employee under the Administrative Agency's guidelines as discussed above. Further, foreign exchange rates are also to be determined based on the international exchange markets.²¹⁹⁾

The foreign exchange management system in the Gaesung ICZ is more liberalized compared to that of the Rajin-Sonbong FETZ. The Administrative Agency plays a key role in regulating foreign exchange in accordance with the Foreign Exchange Regulation, while the Central Guidance Agency administers only revenue in the form of foreign exchange collected such as taxes and the social

215) See Labor Regulation, Article 6. For reference, in the Rajin-Sonbong FETZ, employees could be mobilized in case of natural disasters without the relevant enterprise's consent. See Foreign Invested Enterprises Labor Regulation, Article 6.

216) See Labor Regulation, Articles 33 and 36.

217) See Labor Regulation, Article 39.

218) See the Gaesung Law, Article 40.

219) See Foreign Exchange Regulation, Article 6.

insurance fee.²²⁰⁾ The Foreign Exchange Regulation applies to invested enterprises, representative offices or branches, or South Koreans, Koreans overseas, and foreigners,²²¹⁾ while the Foreign Exchange Law of 1993 (revised in 1999 and 2002) applies to North Koreans and North Korea's enterprises, institutions and associations.²²²⁾ Under the Foreign Exchange Regulation, freely convertible foreign exchanges are to be circulated in the Gaesung ICZ after being designated by the Administrative Agency in agreement with the Central Guidance Agency.²²³⁾ In this regard, the United States dollar is being circulated. There are two types of banks in the Gaesung ICZ. One is the bank established by investors ("Investment Bank"), which may provide foreign exchange services and other financial services except for exchange services related to the Chosunwon or North Korea's currency.²²⁴⁾ The second bank ("NK Bank") is the bank which was or is to be established in the Gaesung ICZ and is controlled by North Korea. The NK Bank may collect and manage taxes, land use fees and social insurance fees and provide foreign exchange services related to the Chosunwon to North Korea's institutions, enterprises, associations and workers.²²⁵⁾ Further, investors (enterprises and individuals) may freely and limitlessly carry foreign exchange in and out of the Gaesung ICZ.²²⁶⁾ More

220) See Foreign Exchange Regulation, Article 3. As discussed above, the Inter-Korean Agreement regulates foreign exchange in the Gaesung ICZ as well.

221) See Foreign Exchange Regulation, Article 2.

222) In North Korea, circulation of foreign exchange is, in principle, prohibited. North Korean or North Korea's enterprises, associations or institutions cannot use or spend foreign exchange unless these currencies are converted into Chosunwon through the authorized bank. See, the Foreign Exchange Law of North Korea, Article 6. In this regard, it should be noted that the effect of economic incentives under the Labor Regulation would be reduced to some extent if North Korean workers could not spend their wages paid in U.S. dollars without conversion into Chosunwon and North Korean relevant authorities could impose heavy taxes or fees on such wages upon such conversion. But, reportedly, U.S. dollars and Euros have been circulated in the markets and hotels of North Korea.

223) With respect to the Administrative Agency's designation of freely convertible currency, Article 41 of the Gaesung Law requires agreement with the Central Guidance Agency, while Article 5 of the Foreign Exchange Regulation requires consultation with the Central Guidance Agency. This seems to be an error of North Korea's legislature. Even though the legislature's intention is arguable, this paper is based on the position that the Gaesung Law is superior to the Foreign Exchange Regulation. Meanwhile, the taxes should be paid in U.S. dollars. See Tax Regulation, Article 11.

224) See Foreign Exchange Regulation, Article 8.

225) See Foreign Exchange Regulation, Article 10.

226) See Foreign Exchange Regulation, Article 16. As reviewed above, the IP Agreement, Section 5.1 guarantees free transfer and remittance of investment-related payments of the investors between the two Koreas.

specifically, investors may remit profits, salaries, or other legally earned money to South Korea or other foreign countries without any tax.²²⁷⁾ Individuals (excluding North Koreans) may, without limit, possess and deposit in the Investment Bank or NK Bank foreign exchange that they carried or earned in the Gaesung ICZ²²⁸⁾ and enterprises may also deposit their money in the Investment Bank and NK Bank.²²⁹⁾ With respect to the deposited foreign exchange, the bank must maintain the confidentiality of its clients' account and it must pay interest accrued thereon.²³⁰⁾ The Investment Bank is required to submit, semi-annually, a statement containing detailed foreign exchange deposits and withdrawals with respect to the individuals' accounts to the Administrative Agency.²³¹⁾ In addition, enterprises are required not only to open at least one account with any Investment Bank or NK Bank, but also to semi-annually report a statement containing the revenues and expenditures in the form of foreign exchange with respect to accounts opened with banks other than the Investment Bank and NK Bank.²³²⁾

6. Entrance, Exit, Sojourn and Residence: Communication and Traffic

The EES Regulation and the EES Agreement²³³⁾ govern matters regarding the entrance, exit, sojourn and residence of investors (including South Koreans, Koreans overseas and foreigners) in the Gaesung ICZ. The regulatory authorities overseeing these matters are the pertinent departments within the Administrative Agency, North Korea's Immigration Office, Customs Service, and Quarantine Service, and the joint committee for inter-Korean traffic.²³⁴⁾ In principle, any investor may travel freely into and out of the Gaesung ICZ from South Korea, without a North Korean visa but, in such case he or she should carry: (i) the pass certificate issued by the Administrative

227) See Foreign Exchange Regulation, Article 17.

228) See Foreign Exchange Regulation, Article 15.

229) See Foreign Exchange Regulation, Article 7.

230) See Foreign Exchange Regulation, Article 11. The interest rate is to be determined based on the principle of supply and demand.

231) See Foreign Exchange Regulation, Article 9.

232) See Foreign Exchange Regulation, Articles 7 and 14.

233) The EES Agreement is superior to EES Regulation as discussed above. See the EES Agreement, Article 14.

234) See EES Regulation, Article 3; Customs Regulation, Article 3; Quarantine Agreement, Article 4; and EES Agreement, Article 12.

Agency's Seoul office and (ii) South Korea's official identification card (for South Koreans) or a passport (for foreigners).²³⁵⁾ While a visa application is subject to a prior and thorough review by which the host country may discretionarily determine whether to issue visa, the pass certificate for the Gaesung ICZ is intended to be a systematic measure to administer the passage of investors.²³⁶⁾ The Administrative Agency's Seoul office issues the pass certificate to investors without delay unless the applicant falls under any of the followings: (a) an international terrorist; (b) a drug abuser or lunatic; (c) an infectious case; (d) a person carrying a forged, unrecognized or expired certificate; and (e) a person whom the two Koreas agreed to forbid to travel.²³⁷⁾ The designation and change of a traffic route is subject to the agreement of the two Koreas.²³⁸⁾ The two Koreas have completed construction for reconnecting both the trans-Korean railroad and trans-Korean expressway by 2004. Meanwhile, travel into, and out of, the Gaesung ICZ from other areas of North Korea requires a North Korean visa.²³⁹⁾

When staying in the Geasung ICZ, investors are required to register their status, such as a long-term sojourner or resident, with the North Korea Immigration Office.²⁴⁰⁾ Under the Gaesung Law,²⁴¹⁾ North Korea cannot arrest or detain investors or search an investor's body or house unless such actions are permitted under the relevant law. If there is an inter-Korean agreement or treaty between North Korea and a foreign country concerning criminal cases and guarantees of personal liberty, such inter-Korean agreement or treaty will apply. In other words, investors would be subject to North Korea's criminal jurisdiction pursuant to North Korea's laws unless a relevant inter-Korean agreement or treaty exists. In this regard, the two Koreas agreed, at the request of South Korea, to execute the EES Agreement.²⁴²⁾ Under the

235) See EES Regulation, Articles 8 and 10; EES Agreement, Article 4.

236) See Ministry of Unification, Bo-do Ja-ryo [Press Release], January 29, 2004. (in Korean) (Available at <http://www.unikorea.go.kr/>; last visited May 3, 2005)

237) See EES Regulation, Article 7; EES Agreement, Article 8.

238) See EES Agreement, Article 3. If North Korea's Immigration Office intends to change the designated route, it should discuss this with the Administrative Agency. See EES Regulation, Articles 5 and 6.

239) See EES Regulation, Article 25; EES Agreement, Article 11.

240) See EES Regulation, Articles 15-24; EES Agreement, Article 7.

241) See the Gaesung Law, Article 8.

242) The EES Agreement, Section 10.1 provides that "[North Korea] shall ensure the inviolability of investors' personal liberty, property and private residence".

EES Agreement, if any investor (including foreigners) violates the laws of the Gaesung ICZ, North Korea may take any of the following measures only after it has interrogated the violator and notified South Korea of the details of the investor's violation: (i) warning the violator, (ii) imposing a penalty on the violator, or (iii) expelling the violator from the Gaesung ICZ.²⁴³⁾ During its interrogation, North Korea is obligated to ensure the investor's basic human rights.²⁴⁴⁾ It is important to note that in the EES Agreement investors are immune from North Korea's criminal jurisdiction.²⁴⁵⁾ This compromise shows North Korea's serious desire to develop the Gaesung ICZ. However, the violator is not exempt from either civil liability or South Korea's criminal jurisdiction. Further, under the EES Agreement South Korea is committed (a) to deal with the case pursuant to South Korean law while taking into consideration North Korea's opinion, (b) to take the measures necessary to prevent a recurrence of such violation, and (c) to cooperate with North Korea with respect to compensation.²⁴⁶⁾ If the violator is a foreigner and there is a relevant treaty by and between North Korean and such foreigner's home country, the violator will be subject to the procedure under the treaty.²⁴⁷⁾

Postal and telecommunication services between South Korea and the Gaesung ICZ are regarded as inter-Korean cooperation and exchange.²⁴⁸⁾ Under the Communication Agreement, the two Koreas are committed to ensure the freedom and confidentiality of communications within the Gaesung ICZ, and between South Korea and the Gaesung ICZ, and not to use such communications for political or military purposes.²⁴⁹⁾ In this regard, "KT Corporation" and "Korea Post and

243) See EES Agreement, Section 10.2. However, some serious cases to be agreed by the two Koreas will be dealt with in accordance with the separate agreement between the two Koreas.

244) See EES Agreement, Section 10.3.

245) For reference, the Korean Peninsula Energy Development Organization ("KEDO") staffs and members of KEDO delegations are immune not only from North Korea's criminal, civil and administrative jurisdiction but also from personal arrest or detention and from seizure of their personal baggage as well. See Protocol between the Korean Peninsula Energy Development Organization and the Government of the Democratic People's Republic of Korea on the Juridical Status, Privileges and Immunities, and Consular Protection of the Korean Peninsula Energy Development Organization in the Democratic People's Republic of Korea, Article 5. This protocol is available at <http://www.kedo.org/pdfs/ProtocolPrivImmun.pdf> (last visited May 3, 2005).

246) See EES Agreement, Section 10.4 and 10.5.

247) See the Gaesung Law 8; EES Agreement, Section 10.6.

248) See Communication Agreement, Section 2.1.

249) See Communication Agreement, Sections 2.2, 2.4 and 2.5.

Telecommunications Corporation" (North Korea's telecom monopoly) executed the Supplementary Agreement for Communication Services²⁵⁰⁾ on March 24, 2005, pursuant to which construction for telecommunication services was completed in the first half of 2005. It is noteworthy that the agreed telephone number system in the Gaesung ICZ is based on that of South Korea, even though North Korea insisted on its communication sovereignty.

Meanwhile, the Custom Regulation, the Custom Agreement and the Quarantine Agreement govern the traffic of goods into and out of the Gaesung ICZ from South Korea. The detailed procedures for customs and quarantines are similar to those in other countries.

7. Tax and Tariff

The local tax office, under guidance of the Central Guidance Agency, imposes the taxes on investors (enterprises and individuals) as provided for in the Tax Regulation.²⁵¹⁾ The taxes under Tax Regulation are the enterprise income tax, individual income tax, property tax, inheritance tax, transaction tax (as for manufacturing enterprises) or business tax (as for enterprises engaged in the hospitality industry), and local tax (including urban management tax and vehicle tax). The enterprise income tax, equivalent to a corporate tax, is imposed on the enterprise's taxable income at the following rates: (i) 10% for enterprises engaged in the construction of infrastructure, light industry and high-tech industry, and (ii) 14% for other enterprises.²⁵²⁾ In addition, if enterprises have been engaged in an encouraged business (i.e. construction of infrastructure, light industry and high-tech

250) See KT Corporation, Press Release, March 29, 2005. (Available at http://www.kt.co.kr/kthome/eng/press/press/press_kt_view.jsp?family_flag=1&news_seq=63¤tPage=1; last visited May 3, 2005.) According to KT Corporation, "the [supplementary agreement] has great significance in that telecommunications can be provided to [the Gaesung ICZ] with a direct optical cable network between the two Koreas, the first-ever since the partition of the Korean peninsula and 60 years of artificial severance of the telephone connection between South and North Korea."

251) See Tax Regulation, Articles 2 and 3.

252) See the Gaesung Law, Article 43; Tax Regulation, Article 19. For reference, in Shenzhen and Suzhou, China's special economic zones, the corporate income tax rate applied to foreign invested enterprise is 15%. See Shenzhen government's website at <http://www.sz.gov.cn/english/gs/gi-1.htm> (last visited May 3, 2005) and Suzhou Industrial Park's website at <http://www.sipac.gov.cn/english/Investment/t20040329-5272.htm> (last visited May 3,

industry)²⁵³⁾ or the manufacturing industry for more than 15 years, such enterprises will be fully exempt from the enterprise income tax for 5 years after beginning to make a profit and 50% exempt for the subsequent 3 years. If enterprises have been engaged in the hospitality industry for more than 10 years, such enterprises will be fully exempt from the enterprise income tax for 2 years after beginning to make a profit and 50% exempt for one subsequent year. If any enterprise reinvests their profit for more than 3 years, such enterprise may deduct the amount equivalent to 70% of such reinvested profit from the following year's enterprise income.²⁵⁴⁾ Furthermore, the Developer may enjoy tax exemptions with respect to its property, or development related business.²⁵⁵⁾ In addition to the above, investors may enjoy protection from dual taxation under the DT Agreement.

Meanwhile, all taxes collected are to be delivered to, and used only by, North Korea's central government. However, since local government agencies are generally funded through local taxes, and the Administrative Agency functions as a local government agency, the Administrative Agency needs to be entitled to use some of the taxes (especially the local tax and property tax) collected from enterprises and individuals to meet its operational needs.

No tariff will be imposed on goods (a) carried into or out of the Gaesung ICZ from South Korea, and (b) commissioned to, and processed by, North Korea's institutions, enterprises or associations in other areas of North Korea. However, if goods from foreign countries are to be sold in the other areas of North Korea, such sales will be subject to tariff requirements.²⁵⁶⁾

8. Dispute Resolution Procedure; Administrative Appeal Procedure

Any disputes in the Gaesung ICZ will be resolved through the procedure under the DRP Agreement, the Gaesung Law and its implementing regulations. First, with

2005).

²⁵³⁾ As reviewed above, encouraged business areas include construction of infrastructure, light industry and high-tech industry. See Enterprise Regulation, Article 3.

²⁵⁴⁾ See Tax Regulation, Article 29. The above tax incentives are more favorable to investors than those in China. For more details, see the above websites of Shenzhen government and Suzhou Industrial Park.

²⁵⁵⁾ See Tax Regulation, Article 17. For reference, Article 7 of the Kumgangsan Law also provides that "no taxes shall be imposed with respect to the developer's development of the Kumgangsan TR and any business activity".

respect to civil and commercial disputes arising in the course of the business of investors or enterprises between the parties concerned from South and North Korea or between the party concerned from South Korea and the competent authority in North Korea (or visa versa), such disputes will eventually be subject to (a) arbitration or court trial in North Korea (if there is no written agreement regarding arbitration under the DRP Agreement) or (b) arbitration under the DRP Agreement (if there is such arbitration agreement).²⁵⁷⁾ Since North Korea does not have sufficient experience in arbitration, investors are expected to prefer arbitration under the DRP Agreement to arbitration under North Korea's law. Meanwhile, Article 48 of the Labor Regulation provides that "any disputes relating to labor relations shall be resolved through consultation between the parties concerned or (if not resolved through such consultation) labor arbitration procedures." However, since there are no known laws or regulations providing for the details regarding the labor arbitration procedure, it is unclear whether Labor Regulation intends to establish a separate arbitral tribunal having exclusive jurisdiction over labor related disputes.²⁵⁸⁾ If so, it is necessary for North Korea to promulgate another regulation providing the details for an arbitral tribunal for labor disputes.

Second, with respect to disputes between North Korea's authorities (i.e. the Central Guidance Agency, the Administrative Agency, the Customs Office, the Tax

²⁵⁶⁾ See the Gaesung Law, Article 33; Customs Regulation, Article 7.

²⁵⁷⁾ The Gaesung Law provides in article 46 that any dispute concerning development and administration of, and enterprise's activities in, the Gaesung ICZ will be resolved through (i) consultation between the parties concerned, (ii) arbitration under the DRP Agreement, or (iii) arbitration or court trial of North Korea". Article 27 of the Insurance Regulation also provides that "any disputes with respect to the insurance risk shall be resolved through consultation between the parties concerned, arbitration or court trial, of North Korea, or arbitration under the DRP Agreement." And see the DRP Agreement, Article 8. Meanwhile, 'arbitration in North Korea' could be understood as arbitration under the External Economic Arbitration Law enacted in 1999. The arbitral tribunal under the External Economic Arbitration Law has jurisdiction over the disputes (a) between North Korean institutions, enterprises, or associations and foreign invested enterprises or foreign enterprises, or (b) between North Korean institutions, enterprises, or associations, foreign invested enterprises, or foreign enterprises and other foreign invested enterprises, other foreigner enterprises or Koreans overseas with respect to trade, investment, service, maritime transportation, marine aid. See the External Economic Arbitration Law, Articles 2 and 4. Also arbitration in North Korea, like arbitration under the DRP Agreement, also requires written agreement regarding arbitration between the parties concerned. See the External Economic Arbitration Law, Article 5. For more details regarding the External Economic Arbitration Law, see Kwang-Rok Kim, "Settling Business Disputes with North Korea in the Advent of the External Economic Arbitration Law," 16 *Transnat'l Law*. 401 (Spring 2003). (Available at LexisNexis).

²⁵⁸⁾ For reference, there are three kinds of arbitration in South Korea: commercial or civil arbitration, labor

Office, etc.) and investors or their subsidiaries arising out of, or relating to, a violation of investors' rights vested under the IP Agreement, investors or their subsidiaries may choose arbitration or court trial under North Korean laws or arbitration under the DRP Agreement.²⁵⁹⁾ In the meantime, the relevant authorities in the Gaesung ICZ may impose legal sanctions such as penalties or suspension of business against any enterprise or individual for their violation of the relevant regulations.²⁶⁰⁾ If the relevant authorities violate the investor's rights under the IP Agreement, the investor may apply for arbitration under the DRP Agreement. With respect to customs, imposed taxes, or sanctions imposed for violation of the Labor Regulation, individuals or enterprises may ask the relevant authorities to reconsider such measures or file an administrative appeal with the Central Guidance Agency.²⁶¹⁾ However, there is no provision providing for the relationship between the administrative appeal procedure and arbitration under the DRP Agreement. Considering that the Gaesung Law and the DRP Agreement are superior to their implementing regulations and do not provide for an administrative appeal, the administrative appeal should not be construed as a guaranteed procedure for investors.

IV. Evaluation

A. Is North Korea's Legal System Meaningful?

Thus far, North Korea has failed to earn trust from foreign investors. The enactment of the Joint Venture Law of 1984 and the 1992 designation of the Rajin-Sonbong FETZ as a special economic zone were undertaken without a constitutional basis, which may suggest that the guidance of the Labor Party or central government

arbitration and press arbitration. The labor arbitration seems to be inserted based on the above classification.

259) See DRP Agreement, Article 8; IP Agreement, Article 7; the Gaesung Law, Article 46.

260) See Tax Regulation, Article 85 (imposing fine for default); Custom Regulation, Articles 41 and 42 (Seizing or confiscating contraband, imposing fine); Labor Regulation, Article 46 (imposing fine or suspension of business); Foreign Exchange Regulation, Article 18 (suspension of bank transaction, imposing fine); Advertisement Regulation, Article 21 (suspension of advertisement, revocation of advertisement business license or imposing fine); Real Property Regulation, Articles 56, 57 and 58 (imposing fine); and Insurance Regulation, Article 26 (imposing fine).

are superior to the written laws in North Korea. In addition, although the Equity Joint Venture Law of 1984 provided for foreign investors' rights to manage the joint venture company in proportion to the investment amount, North Korea did not abide by the law to protect such investors' rights. This was one of factors that forced investors to give up their investment in North Korea at that time. Concerning the Rajin-Sonbong FETZ, North Korea, albeit temporarily in 1997, retreated from its open door policy due to concerns about regime stability and the negative influence of the open door policy on the rest of North Korea, signaling to investors that North Korea's open door policy is unpredictable and unreliable. Therefore, it is not unexpected that foreign investors have their doubts regarding the Gaesung ICZ's legal system, regardless of its content.

With respect to foreign investors' skepticism, the following discussion will cautiously suggest that the Gaesung ICZ's legal system would be meaningful, even if flawed, for the protection of investors' rights. First, assuming that North Korea as a state, even as a communist country, needs to maximize its national interest like China or Vietnam,²⁶²⁾ the economic factor of the Gaesung ICZ could be useful to verify whether the Gaesung ICZ's legal system is reliable. According to the game theoretic explanation,²⁶³⁾ although a host state is committed to guarantee the foreign investors' rights by enacting laws, the host state's laws itself do not make the host

261) See Tax Regulation, Article 86; Custom Regulation, Article 43; Labor Regulation, Article 49.

262) In this regard, if this position could not be agreeable, any kind of negotiation with North Korea (including the Agreed Framework, the Six-Party Talks) would be also useless. However, many South Koreans believe that negotiation with North Korea has not proved to be meaningless, rather not fully performed.

263) Among some attempts to apply game theory to the commitment problem is David W. Leebron's analysis regarding the host state's commitment and its foreign investment regulations.

According to Leebron, "[while] the state is not a party to most economic transactions, it is one of the background conditions that allow those transactions to be structured in certain ways, including the making of commitments. If the state cannot be relied upon, and is not replaced by some enforcement mechanism, economic transactions must be structured either without credible commitments or by making commitments credible even in the absence of the state enforcement mechanism." Furthermore, "[a] commitment might be credible in either of two ways. First the commitment may be credible because at the time the action agreed to is to be carried out, if it will be in the self-interest of the party to do so. In this case no commitment by the party is really necessary. Alternatively, external sanctions may be brought to bear in the event that the party fails to abide by its commitment; this makes the commitment credible. The availability of such sanctions is really a special case of the action being in the party's interest; external pressures and sanctions alter the consequences that would otherwise follow from the action, or they prevent the party from taking an action that would be in its self-interest. State enforcement is simply one example of this coercive credibility." See David W. Leebron, "A Game Theoretic Approach to the Regulation of Foreign Direct

state's commitment credible because such laws could be changeable at the host state's discretion. Instead, the host state's commitment might be credible in either of the following ways or both: (a) where the host state has a self-interest in abiding by the laws; or (b) where, in case of the host state's breaching its commitment, the cost to be borne by the host state is higher than the benefit that the host state can enjoy. In this context, more attention needs to be paid as to what the Gaesung Project means to North Korea. Since North Korea could not overcome its structural economic difficulties without considerable external investment in North Korea, North Korea has no choice but to open, and reform, its economy. Failing to attract the foreign investment with the Rajin-Sonbong and Shinuiju projects, North Korea opened Gaesung and Kumgangsan, realizing that South Korea's capital might be of a great importance quantitatively and qualitatively to its economy. According to economic analyses, the Gaesung ICZ, if developed as scheduled, is expected to offer North Korea a considerable economic benefit.²⁶⁴ On the other hand, if North Korea fails at the Gaesung ICZ, few options remain available. Thus it would be reasonable to assume that the development of the Gaesung ICZ is in the self-interest of North Korea. This need is the reason for North Korea entrusting South Korea with the development and management of the Gaesung ICZ, the reason for North Korea making investors immune from its criminal jurisdiction by executing the EES Agreement and the reason for North Korea allowing investors to use South Korea's telephone number system despite its asserted opposition. Further, given that the development of the Gaesung ICZ could be achieved if based on a stable and predictable legal system, abiding by the Gaesung ICZ's legal system is in the self-interest of North Korea.

Secondly, South Korea's role in developing the Gaesung ICZ should be taken into account in reviewing the credibility of the Gaesung ICZ's legal system. Any investments by South Korean enterprises in the Gaesung ICZ are subject to prior approval and under the continuous supervision of the South Korean government pursuant to the Law on Inter-Korean Exchange and Cooperation. The South Korean government not only implements the Inter-Korean Agreements that constitute the Gaesung ICZ's legal system, but also closely controls and supports the Administrative Agency. In addition, South Korea provides investors, through the

Investment and the Multinational Corporation," 60 *U. Cin. L. Rev.* (Fall, 1991) at 309-310.

Export-Import Bank of Korea, with an insurance program covering, to some extent, the political risks associated with the Gaesung ICZ. In case of payment to the investors due to expropriation or similar measures taken by North Korea, the Export-Import Bank of Korea is required to take measures necessary for collection of the paid amount. Thus, if North Korea fails to abide by its own commitment, South Korea will impose economic sanctions such as blocking any further investment in, or economic activities relating to, the Gaesung ICZ. The possibility of South Korea's economic sanction could be a strong factor that makes North Korea abide by its commitments.

B. Flawed Legal System Under Experiment

The Gaesung ICZ's legal system is at the beginning stage. By August 2005, one law and 13 regulations have been enacted and are in effect, together with the Four Inter-Korean Agreements, but this is not enough. Problems still exist in the Gaesung ICZ's legal system. First, like the Rajin-Sonbong FETZ's legal system,²⁶⁵ the legal drafting in the Gaesung Law and its implementing regulations is underdeveloped. For example, Article 4 of Enterprise Regulation allows investors to establish "various types of enterprises", and such enterprise may issue "stocks and bonds"; however the terms of "various types of enterprises" and "stocks and bonds" are not defined in the Enterprise Regulation or other implementing regulations and no corporation law providing for the meaning of such terms exists. Article 48 of the Labor Regulation provides for a labor arbitration procedure, without further details, making it difficult for investors to understand how such an arbitration procedure functions. North Korea's failure to define such terms, or omission of detailed provisions, can probably be attributed to a lack of relevant legal experience and knowledge, and thus additional implementing regulations addressing omitted or undefined terms need to be promulgated. Moreover, contract law and corporation laws need to be adopted.

Second, some provisions under the Insurance Regulation are contrary to the spirit of the Gaesung Law and other implementing regulations. In other words, North Korea granted the Administrative Agency, controlled by South Korea, the power to

²⁶⁴ See Suhk-sam Park and Sun-Jick Hong, *supra* note 80.

issue any permits and approvals required for any business or enterprise,²⁶⁶⁾ especially for the establishment and management of an Investment Bank. These provisions imply that the insurance business should also be under the supervision of the Administrative Agency. However, the Insurance Regulation requires enterprises in the Gaesung ICZ to purchase certain kinds of insurance policies from the insurance company designated by the Central Guidance Agency,²⁶⁷⁾ which gives the Central Guidance Agency the power to issue insurance business licenses. In fact, the Insurance Regulation was promulgated without consultation with South Korea, which made many investors question whether North Korea's commitment is credible. Such questions have not clearly been resolved. If North Korea attempts to promulgate another regulation without consultation with South Korea and the contents of such a regulation are contrary to the purpose of the Gaesung legal system agreed between the two Koreas, the Gaesung Project will face serious difficulties. This issue is directly related to how sincerely North Korea guarantees the autonomy of the Administrative Agency. If the Central Guidance Agency and other relevant agencies, such as the Tax Office and Customs Service, interfere with the Administrative Agency's function, the Administrative Agency could not consistently exercise its authority in the Gaesung ICZ, which would be contrary to the purpose of the Gaesung legal system and North Korea would lose credibility from investors. Therefore, whether North Korea guarantees the autonomy of the Administrative Agency will be seen as a litmus test of North Korea's commitment towards the success of the Gaesung Project.

Third, the judicial system in the Gaesung ICZ remains problematic. The inter-Korean Commercial Arbitration Committee should be established in the near future. But, to realize the rule of law in the Gaesung ICZ through the Inter-Korean Commercial Arbitration Committee, it is necessary for North Korean arbitrators to be knowledgeable on the market economy and the legal system, and it is also necessary for North Korea to make any arbitral award easily enforceable anywhere in North Korea including the Gaesung ICZ.

265) See *supra* note 38.

266) See the Gaesung Law, Article 25; Administrative Agency Regulation, Article 13; Enterprise Regulation, Articles 7 and 16.

V. Conclusion: Beyond the North Korea's Nuclear Crisis

North Korea has given the stability of its regime the highest priority after the collapse of the U.S.S.R and Eastern Communist regimes. However, driven by its structural economic difficulties, it has experienced difficulties in its pursuit of economic reform through an open door policy. The goal of North Korea to stabilize its regime seems to conflict with its need to reform and open its economy. However, such conflict could be settled if North Korea follows a China/Vietnam-style open door policy. Whether North Korea does sincerely and actively put itself on the way toward a market economy is still disputed. Nonetheless, from South Korea's point of view, South Korea needs to encourage North Korea to revitalize its economy by assisting North Korea in adjusting its economic policies to be more conducive to a market economy.

Since the 2000 inter-Korean Summit, the two Koreas have continuously carried out the Gaesung Project while overcoming some challenges. At the outset of the Gaesung Project, North Korea's military objected to opening Gaesung in order to maintain the military defense line. North Korea made the decision to open Gaesung toward South Korea to revitalize its economy by persuading its military to tolerate the Gaesung Project. Meanwhile, in the summer of 2002, when the two Koreas began to move ahead with the Gaesung Project by re-connecting the inter-Korean expressway and railroad crossing the DMZ, the United States strongly resisted the two Koreas' attempts. Reluctantly the United States agreed on the Gaesung Project and the reconnection of inter-Korean expressway and railroad only after diplomatic dialogue between South Korea and the United States.²⁶⁸⁾ Immediately afterwards, the two Koreas agreed on a detailed schedule for the reconnection of the inter-Korean

267) See Insurance Regulation, Articles 3 and 6.

268) According to Selig S. Harrison, "the United States strongly resisted the thaw, refused to approve the de-mining, and threatened to block the [Gaesung Project] by restricting the use of U.S.-licensed and other sensitive technology by companies investing in the [Gaesung ICZ]. (U.S.-South Korea tensions over the technology issue have since intensified.) But in August 2002, South Korea's then president, [Kim Dae-Jung], personally appealed to President George W. Bush to drop his objections, and on September 12 [2002], after an intense diplomatic struggle, the Pentagon reluctantly gave the go-ahead for de-mining." Selig S. Harrison, "Did North Korea Cheat?," *Foreign Affairs*, January/February 2005. (Available at <http://www.foreignaffairs.org/20050101faessay84109/selig-s-harrison/did-north-korea-cheat.html>; last visited May 3, 2005)

To reconnect the inter-Korean expressway and railroad crossing the DMZ, it is necessary for the two Koreas to

expressway and railroad on August 30, 2002, and North Korea designated Shinuiju, on September 12, 2002, Kumgangsan, on October 23, 2002, and Gaesung, on November 13, 2002, as special economic zones. To date, the two Koreas have established, through painstaking negotiations, the foundational work for the Gaesung ICZ's legal system.

The successful development of the Gaesung ICZ depends on various factors. Importantly, Gaesung ICZ's legal system must become stable and predictable. To this end, North Korea needs to respect the autonomy of the Administrative Agency, to introduce more laws and regulations addressing the issues reviewed in Part III.D, and to sufficiently train lawyers and market economy experts. Meanwhile, the United States' economic sanctions against North Korea²⁶⁹ hinder investors from carrying high-tech related facilities (strategic goods or dual-use items) into the Gaesung ICZ, and exporting products made in the Gaesung ICZ to the United States, which makes South Korea's major companies or SMEs dealing in high-tech industries hesitate to invest in the Gaesung ICZ. But such economic sanctions would be lifted only after North Korea's current nuclear issues are resolved. Thus, whether, and how North Korea's nuclear issues are resolved will be another key factor influencing the development of the Gaesung ICZ. At this stage, where the foundational work for the Gaesung legal system is complete, it is important to constantly develop the Gaesung ICZ's legal system toward a market economy based on consultation between the two Koreas.

de-mine the DMZ, which is under the control of the parties to the Armistice Agreement (the United Nations headquarter, North Korea and China). Therefore, de-mining the DMZ requires the approval from the United Nations headquarters which the four-star U.S. Army general in fact commands. Under these circumstances, the Pentagon seems to have objected to the Gaesung Project at that time.

²⁶⁹) Review on economic sanctions against North Korea is excluded because it is beyond the scope of this paper.

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South Korea's System of Export Control on Strategic Items and Its Effective Enforcement Policy to Facilitate Economic Cooperation between South and North Korea

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Abstract

Because of the heightened concerns over terrorism and national security raised by the attacks of September 11, 2001 in the United States (U.S.), multilateral export control regimes tightened export controls of dual-use items for national security. Multilateral export control regimes initiated by the U.S. seek to prevent the proliferation of nuclear, chemical, biological, and conventional weapons. South Korea is a party to all relevant nonproliferation regimes (NSG, AG, MTCR) and the Wassenaar Arrangement. South Korea introduced "Catch-all" controls to its export control system in January 2003, and established the Strategic Items Control Division (SICD) within the Ministry of Commerce, Industry and Energy (MOCIE) in February 2004. In August 2004, the Strategic Trade Information Center (STIC) opened as a nongovernmental organization to serve as a consultation or information center regarding the export of strategic items and to assist private sector compliance with export control regulations. South Korea's export control regulations on strategic items include the Foreign Trade Act (FTA: Articles 21, 54, 56, 58), Enforcement Decrees of FTA (Articles 39-45) and the Public Notice of Export/Import (consisted of 68 Articles and 25 Annexes). They have been revised to reflect the changes in the multilateral export control regimes, and apply to exports and re-exports of civilian and dual use items (products, software, technology). Violations of the export control regulations may be

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