

System Improvement from Offset to Industrial Cooperation; Win-Win Partnership for Companies at Home and Abroad

- Convert from the offset-trade system to industrial cooperation system
- Introduction of the value point system for foreign companies

-> Step-by-step implementation in the second half of 2018 starting with the amendment of defense program-related laws and regulations

Defense Acquisition Program Administration (DAPA) announced its full-scale overhaul plan of the offset system, which has remained almost unchanged for the last 37 years since its introduction in 1982, to a system focused on promoting the greater exports of parts, job creation and fostering of defense industries. The plan was resolved as part of the defense procurement meeting held on June 25, 2018.

Offset means the receipt of technology transfer, manufacturing/export of parts, logistics support, etc. in consideration for the purchase of weapons, etc. overseas. While offset has greatly contributed to the advancement and improvement of the defense/aerospace industry and defense technology in Korea, DAPA decided to turn its attention to increasing the export of parts in order to facilitate growth of Korean defense companies and create jobs. DAPA also recognized that many states and leading aerospace and defense companies applied stricter standards and barriers in connection with defense technology transfer and offset programs which ultimately limited DAPA's ability to secure core defense technologies.

1. Four key elements of the system improvement

A. Conversion of the 'offset' concept

The existing 'free offset' principle no longer exists. A decision on the implementation and size of offset will be made after industry-wide implications, characteristics, etc. thereof are contemplated for each industry.

B. Change of the focus and name of the policy

Focus: Acquisition of defense technologies -> Fostering of defense industries and export of parts for weapon systems

Name: Offset -> Industrial Cooperation¹

*¹: Mid-to long-term large-scale 'cooperation' between Korean defense 'industries' and foreign defense 'industries'

C. Introduction of a value point system

Regardless of certain mandatory obligations to participate in offset programs as a result of relevant defense projects and requirements, those international companies that conduct business and maintain healthy cooperative relationships with domestic companies will be deemed to have created a value point and such companies can accumulate those value points based on their prior experience and relationship. The more value points an international company accumulates could result in advantage when participating in future business biddings.

D. Introduction of the industrial cooperation quota system for procurement of international weapons systems

When procurement of international weapon system, a specific portion of such weapon's part system should be supplied or produced by domestic companies. This will allow domestic companies to build and expand their core technological capabilities and provide the Korean military with secure and stable logistical support.

2. Expected benefits

A. Increase of manufacturing/export of parts from the current 30% level to 80%

-> Additional exports of USD 270 million approximately from 2020 to 2024, and creation of about 3,700 new jobs

B. Promote working relationships with Small and Medium-sized Enterprises (SMEs)

-> If an international company works with a domestic SME in connection with its procurement project or defense business (e.g., SME to supply certain parts), such international company will receive a guaranteed incentive in the form of twice as many value points compared to working with a large domestic company.

3. Shin & Kim's competence to provide defense-related advice

Shin & Kim's Military Procurement & Defense Industry team has served clients in the aerospace, defense and government services industry, including major defense contractors and their suppliers, for more than three decades. Our lawyers and experts are well aware of the defense and public procurement process as our members have worked at various public agencies and served in every branch of the military including serving as counsel to key positions with DAPA, the Ministry of National Defense and the Joint Chiefs of Staff. The team consists of approximately 20 members and have the capability to support clients in all defense-related matters.

Should you have any questions regarding any of the foregoing, please feel free to contact us at any time.

Contacts

Seok Ko (Partner)	TEL. +82-2-316-4072	E-Mail. sko@shinkim.com
In-Hyoung Cho (Partner)	TEL. +82-2-316-1615	E-Mail. ihcho@shinkim.com
Chin Hyock Choi (Senior Foreign Attorney)	TEL. +82-2-316-1690	E-Mail. chchoi@shinkim.com