

## Chapter 1

### Central purchasing in Korea: The Public Procurement Service

*Established in 1949 as the Provisional Office of Foreign Supply, the Public Procurement Service (PPS) took on its current role as a central procurement agency of Korea in 1961. PPS has a variety of responsibilities related to the purchase and management of resources needed for public administration, all of which are undertaken with a focus on transparent and effective delivery of services while also contributing to savings through consolidation and centralisation as well as furthering economic development in Korea. The present chapter provides an introduction to public procurement in Korea generally, and a more detailed examination of the various roles undertaken by PPS. This includes presentations of the legal authorities that govern public procurement in Korea, the responsibilities and organisation of PPS, and detailed information regarding the scope of public procurement activities.*

## Public procurement in Korea

### *Legal authorities*

The Act on Contracts to Which the State is a Party (“State Contract Act”) establishes a principle under which the government engages in legal acts as a private economic entity. Under this system, special laws relevant to government contracts are applied with priority, as they provide exceptional provisions. Then the State Contract Act is applied. Finally, civil law principles relating to contracts, such as the Principle of Party Autonomy, Principle of Good Faith, and Principle of Abuse of Rights apply to matters not addressed in the special laws or State Contract Act.

As in many country contexts, the broad scope of public procurement requires the distribution of responsibilities among a number of relevant ministries. While the Ministry of Strategy and Finance in Korea has primary responsibility for central procurement (including housing PPS), the Ministry of Government Administration and Home Affairs; Land, Infrastructure and Transport; Trade, Industry and Energy; Health and Welfare; Employment and Labour; and the Small and Medium Business Administration all have legal authorities related to public procurement (see Table 1.1).

These acts are then supported in implementation through the development of more detailed enforcement decrees, enforcement ordinances and regulations. As an example, a list of established and announced regulations from the Ministry of Strategy and Finance that are relevant to public procurement is presented in Box 1.1.

### *Mandatory use of centralised processes*

The public procurement system in Korea is comprised of a combination of centralised and decentralised procurement requirements, with legal requirements contained in different sources depending on the type of entity. Requirements for central government entities are contained in the State Contract Act; the Local Government Contract Act governs procurement by local government entities; and other public entities are governed by the Act on the Management of Public Institutions.

For central government agencies, the procurement of goods, services and construction works through PPS is mandatory when they exceed certain threshold amounts. This includes any construction projects valued at more than USD 2.54 million<sup>1</sup> (USD 254 300 for electric or communication projects), and commodity or services procurements with a value above USD 84 763. Central government entities are also required to purchase through PPS for goods or services with existing centralised contracts in place, whether they are unit price, third-party unit price or Multiple Award Schedule (MAS) framework contracts.

Over the last two decades, increased autonomy has been provided to local government entities to procure goods and services projects directly, through the reduction and elimination of mandatory thresholds for use of PPS (see Table 1.2). The requirements that local government entities, including educational institutions, use PPS for construction works projects have also been eliminated over time, as shown in Table 1.3.

Table 1.1. **Public procurement legal authorities in Korea**

Full title	Responsible authority	Description
Act on Contracts to Which the State is a Party (State Contract Act)	Ministry of Strategy and Finance	Prescribes basic rules on contracts made with central government organisations.
Act on Contracts to Which a Local Government is a Party (Local Government Contract Act)	Ministry of Government Administration and Home Affairs	Prescribes basic rules on contracts made with local autonomies.
Act on the Management of Public Institutions	Ministry of Strategy and Finance	Prescribes basic matters on management of public institutions.
Government Procurement Act	Ministry of Strategy and Finance (PPS)	Prescribes necessary matters related to operation and management of procurement business.
Framework Act on the Construction Industry	Ministry of Land, Infrastructure and Transport	Prescribes basic rules on survey, design, inspection, maintenance and technology management of construction works. Also stipulates necessary matters related to registering as a construction business, subcontracting of construction works and others.
Construction Technology Promotion Act	Ministry of Land, Infrastructure and Transport	Prescribes matters related to the advancement of construction technology and quality enhancement and safety management of construction works.
Electrical Construction Business Act	Ministry of Trade, Industry and Energy	Prescribes basic matters related to electrical construction business and technology management and subcontracting of electrical construction.
Small and Medium Enterprises Promotion Act (SMEs Promotion Act)	Small and Medium Business Administration	Prescribes matters related to strengthening the competitiveness of SMEs, business management and others.
Act on Facilitation of Purchase of Small and Medium Enterprise-Manufactured Products and Support for Development of Their Markets	Small and Medium Business Administration	Prescribes matters related to promotion of purchasing goods manufactured by SMEs, support for their market entry and others.
Framework Act on Small and Medium Enterprises	Small and Medium Business Administration	Prescribes basic matters related to policies to nurture SMEs, their visions and others.
Industrial Standardisation Act	Ministry of Trade, Industry and Energy	Prescribes matters related to dissemination of industrial standardisation and others.
Quality Control and Safety Management of Industrial Products Act	Ministry of Trade, Industry and Energy	Prescribes matters related to quality management and safety management of industrial products.
Government Organisation Act	Ministry of Government Administration and Home Affairs	Prescribes matters related to establishment, structure and scope of roles and functions of government organisation.
Framework Act on Low-Carbon Green Growth	Office for Government Policy Coordination (Prime Minister's Secretariat)	Prescribes matters related to creating an environment for low-carbon green growth and utilising green technology and industry as a growth engine.
Special Act on the Preferential Purchase of Products Manufactured by Persons with Severe Disabilities	Ministry of Health and Welfare	Prescribes matters related to support for preferential purchase of products manufactured by occupational rehabilitation centres and others which hire persons with severe disabilities.
Act on Support for Female-owned Businesses	Small and Medium Business Administration	Prescribes matters related to support for activities of female-owned businesses and their establishment.
Income Tax Act	Ministry of Strategy and Finance	Prescribes matters related to individual income and taxation.
Value-added Tax Act	Ministry of Strategy and Finance	Prescribes matters related to requirement and procedure of imposing value-added tax.
Social Enterprise Promotion Act	Ministry of Employment and Labour	Prescribes matters related to establishment, operation and promotion of social enterprises.

Source: PPS response to OECD internal questionnaire, 2014 with updates in 2015.

### Box1.1. Regulations and public notice for government contracts

Regulations established by the Ministry of Strategy and Finance:

- general terms and conditions of construction contracts
- construction bid instruction
- general terms and conditions of commodity purchase contracts
- commodity purchase bid instruction
- general terms and conditions of technical service
- technical service bid instruction
- qualification screening criteria
- guidance to pre-qualification screening
- government bid/contract execution criteria
- estimated price preparation criteria
- guidance to joint subcontract administration
- negotiated contract signing criteria
- guidance to comprehensive contract signing
- arbitration on international contract dispute mediation committee
- bid price standards for lowest-price system
- criteria for the successful bidder through a batch bidding.

Regulations announced by the Ministry of Strategy and Finance:

- announced price decided by the Minister of Strategy and Finance for the Act on Government Contracts
- projects announced by the Minister of Strategy and Finance.

*Source:* Korean Ministry of Strategy and Finance

Table 1.2. Threshold amount for goods and services purchasing by local government entities<sup>1</sup>

	Prior to 2004	Prior to 2006	Prior to 2008	Current
Must use PPS	Above USD 42 381 (USD 50 000 for foreign procurement)	Above USD 59 334 (USD 100 000 for foreign procurement)	Above USD 84 763 (USD 200 000 for foreign procurement)	Fully autonomous
May buy autonomously	Less than USD 42 381 (USD 50 000 for foreign procurement)	Less than USD 59 334 (USD 100 000 for foreign procurement)	Less than USD 84 763 (USD 200 000 for foreign procurement)	

1. The values for foreign procurement in this table were originally presented in USD.

*Source:* PPS response to OECD internal questionnaire, 2014 with updates in 2015.

Table 1.3. **Threshold amount for construction works by local government entities**

	Prior to 2005	Prior to 2007	Prior to 2008	Prior to 2010	Current
Must use PPS	Pre-qualification (PQ) construction, alternative tender construction, turnkey	PQ construction over USD 17 million, alternative tender construction, turnkey	PQ construction over USD 42.4 million, alternative tender construction, turn key	Alternative tender construction, turn key	Fully autonomous
May buy autonomously	Others	Others included in PQ construction less than USD 17 million	Others included in PQ construction less than USD 42.4 million	Others included in all PQ construction	

Source: PPS response to OECD internal questionnaire, 2014 with updates in 2015.

However, many still choose to request purchasing through PPS as a matter of policy, to take advantage of the centralised expertise that PPS offers. Local government entities are also still required to purchase goods and services through established PPS contracts in the case of unit price, third-party unit price, or MAS framework contracts.

Other public entities and quasi-government agencies are required to purchase through PPS for “competitive goods,” as defined in the SMEs Promotion Act, above certain thresholds announced by the Minister of Strategy and Finance. This requirement applies when purchasing competitive goods manufactured by SMEs either under open competition, or in the case of unit price, third-party unit price, or MAS framework contracts.

Despite the increased autonomy allowed to local government entities and other public entities, the number of PPS user entities has increased by almost 10% since 2010, with only 0.5% of this increase coming from new central government entities (see Table 1.4).

Table 1.4. **Number of public entities registered with PPS as "user entities"**

	Total	Central govt. entities	Local govt. entities			Other entities			
			Local govts.	Boards of education	Public enterprises	Quasi- governmental entities	Other public entities	Local govt. owned enterprises	Misc.
2010	42 405	5 145	6 713	10 837	864	1 020	445	163	17 218
2011	43 708	5 195	6 772	10 994	945	1 088	403	175	18 136
2012	45 055	5 245	6 836	11 121	966	1 100	425	186	19 176
2013	46 773	5 349	6 895	11 234	992	1 127	430	197	20 549
2014	48 681	5 430	6 944	11 368	1 005	1 333	461	206	22 934

Source: PPS response to OECD internal questionnaire, 2014 with updates in 2015.

These users include other entities that are entrusted to carry out tasks on behalf of, or act as agents of, central government or local government entities pursuant to relevant laws or regulations, which are approved by PPS on an individual basis. Registration for such external entities requires appropriate documentation, such as a certified copy of business registration for private schools, certificates of incorporation and articles of association for social welfare entities, or a copy of the entrustment contract, for other entities entrusted to carry out business on behalf of government.

### *Size of public procurement*

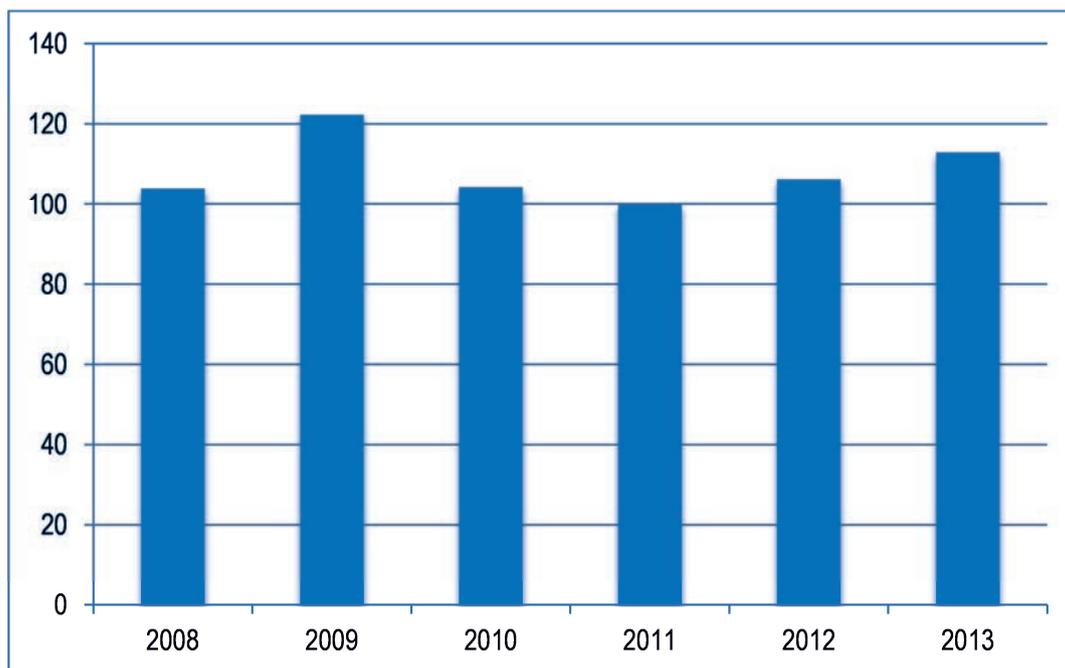
Statistics on overall public procurement in Korea are reported annually by the Small and Medium Business Administration (SMBA). SMBA carries out this data collection and reporting as part of its legal mandate to report on the progress achieved in using public procurement to support social objectives, such as the promotion of small and medium-sized enterprises.

Data for total public procurement volume includes the procurement of goods, services and public works by 516 entities that include central government, local government entities, boards of education, public enterprises, quasi-governmental entities, state-subsidised entities, local-government owned enterprises and public entities established by special laws. Procurement by the military of personal consumables, commercial goods and services is included, but other elements of defence procurement (for example, the development and purchase of weaponry) are not included. Procurement by the legislative and judicial branches is also excluded.

Total procurement volume peaked in 2009 as a result of stimulus spending measures in response to the economic crisis, and then declined as this spending decreased during 2010 and 2011. Since then, total procurement volume has again been rising incrementally, as demonstrated in Figure 1.1.

Figure 1.1. **Total procurement volume in Korea**

In USD billions



Source: PPS response to OECD internal questionnaire, 2014 with updates in 2015.

## PPS functions

### *Overview*

The mission of PPS is “to provide the best value service to its clients, save national budget spending and contribute to economic development by procuring and managing resources for public administration.” This mission is carried out through a variety of independent and interrelated functions (see Box 1.2). As with calculations for overall procurement volume, procurement of design or purchase of weapons systems and other defence procurement is excluded, but the purchase of some commodities and services in support of soldiers is included.

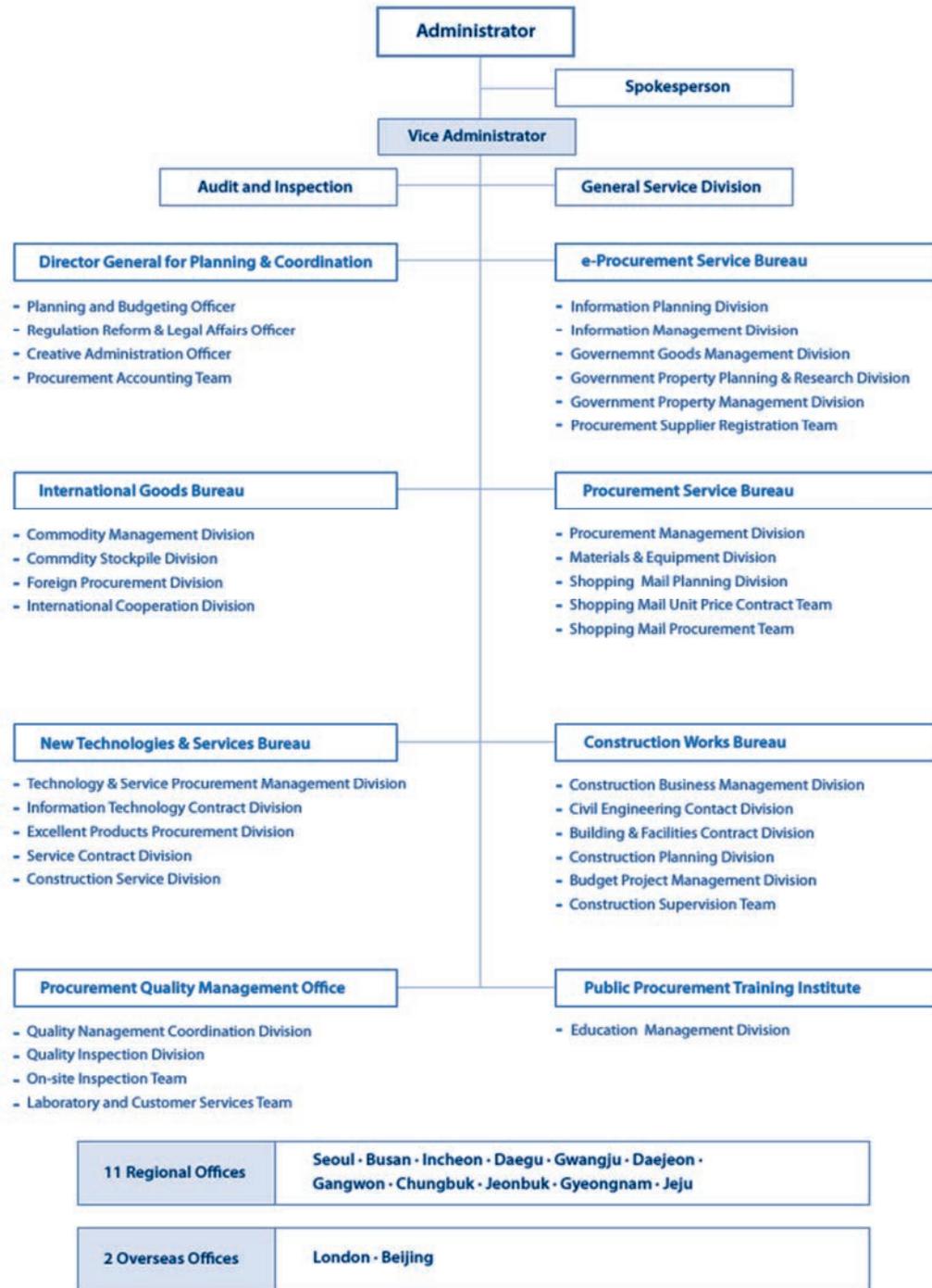
#### Box 1.2. PPS functions

- Procurement of goods and services
  - Domestic procurement: Goods, services and leases produced or supplied domestically
  - Foreign procurement: Goods and services produced or supplied from overseas in accordance with international standard practices
- Construction works and services
- Operation and management of the Korea ON-line E-Procurement System (KONEPS)
- Operation of stockpiling business
  - Stockpiles and releases major raw materials including aluminium to ensure price stability and to support SMEs
- Management of government goods and property
  - Establish policies to manage government-owned goods and supervision
  - Inspection of the management of government property

To support these functions, PPS also undertakes a number of procurement business processes. For goods and services, and the stockpiling function, this includes logistics management and supply processes. For construction works, PPS offers a broad range of business services throughout the process, including total project cost review, tailored development, and project management services following contract award. Additionally, other business projects, related or allowed by relevant law, are undertaken as appropriate.

To support this work, PPS is divided into a number of central divisions, bureaus and offices, as well as 11 regional offices and 2 overseas offices (see Figure 1.2). The total staff is 970, with 442 (45.5%) located at headquarters.

Figure 1.2. PPS organisational chart



Source: Korean Public Procurement Service, [www.pps.go.kr/eng/jsp/about/organization\\_eng](http://www.pps.go.kr/eng/jsp/about/organization_eng) (accessed 16 October 2015).

PPS roles and functions are wider than other central purchasing bodies (CPBs) in OECD. Almost all OECD member countries having a CPB (90%) have a CPB at the central level; while more than half (52%) also have distinct CPBs at the regional level. Additionally, in some OECD member countries CPBs are state-owned enterprises (15%), as in Finland, France and Italy. The majority of CPBs in OECD member countries (81%) either operate under a line ministry or function as a government agency.

In most OECD member countries, CPBs undertake the role of acting as a contracting authority aggregating demand and purchasing (85%), and as manager of the system for awarding framework agreements or other consolidated instruments, from which contracting authorities then order (73%). In contrast, in a few OECD member countries CPBs co-ordinate training for public officials in charge of public procurement (38%) and establish policies for contracting authorities (31%). CPBs in Greece, Ireland, Switzerland, the United Kingdom and the United States exercise all the above-mentioned functions whereas CPBs in nine OECD member countries (35%) have a single role, e.g. in Estonia, Luxembourg, and Poland (see Table 1.5).

Table 1.5. The role of the central purchasing body in selected OECD member countries and non-member economies

	CPBs act as a contracting authority aggregating demand and purchasing	CPBs act as manager of the national system awarding framework agreements or other consolidated instruments, from which contracting authorities then order	CPBs co-ordinate training for public officials in charge of public procurement	CPBs establish policies for contracting authorities
Australia	•			
Austria	•	•		
Belgium		•		
Canada	•	•	•	
Chile		•	•	•
Denmark		•		•
Estonia		•		
Finland	•			
France	•	•	•	
Germany	•			
Greece	•	•	•	•
Hungary	•	•		
Ireland	•	•	•	•
Italy	•	•		
Korea	•	•	•	
Luxembourg	•			
New Zealand	•	•	•	
Norway	•			
Poland	•			
Portugal	•	•		
Slovak Republic	•			
Slovenia	•	•		
Spain	•	•		•
Switzerland	•	•	•	•
United Kingdom	•	•	•	•
United States	•	•	•	•
Brazil	•		•	•
Colombia		•	•	•
OECD26	22	19	10	8

Source: OECD (2015a), *Government at a Glance 2015*, OECD Publishing, Paris, [http://dx.doi.org/10.1787/gov\\_glance-2015-en](http://dx.doi.org/10.1787/gov_glance-2015-en).

PPS also supports its work through the operation of a special budget account, which provides a number of advantages. Revenue in the fund is primarily generated through the fees charged by PPS for contracts made on behalf of public organisations (see Box 1.3). The special account is used to support PPS labour costs and other contract-related expenses. In addition, the special account supports a revolving fund that is used to expedite payment to suppliers on behalf of the buying entity or end user, whose payment is then eventually returned to the special account. This process has reduced payment time to as little as four hours following approved delivery and inspection, in some cases. This function only applies to domestic procurement of goods and services, construction works and foreign procurement contracts are always paid directly from the buying entity or end user. Finally, the special account is also used to support stable supply and support for SMEs through the stockpiling function.

### Box 1.3. Fees for PPS services

The fees charged by PPS vary, depending on several factors. Both the nature of the procurement and the role that PPS plays in the process are the primary factors. Procurement fees were last updated in November 2014 by Article 10 of the Enforcement Decree of the Government Procurement Act. The following is a general description of the fees applied to different categories, while more detailed calculation methodology and rates are introduced on the PPS website.

**Purchase in local currency (KRW):** Fees are applied at a diminishing rate according to the amount of the contract. For contracts below USD 17 000, the fee is fixed at USD 178. For contracts between USD 17 000 and USD 42 400, the fee is fixed at USD 450. For the amount exceeding USD 42 400, USD 84 800, USD 848 000 and USD 8.48 million, rates of 1.07%, 0.76%, 0.48% and 0.38% apply respectively.

For orders through existing contracts, including unit price, third-party unit price or MAS framework contracts, a flat rate of 0.54% applies regardless of the amount of the contract (however, for oil products, a 0.27% rate applies).

**Purchase in foreign currency:** The fees are applied at a diminishing rate similar to those for purchase in local currency according to the amount of the contract. More specifically, 1.2% of the amount is charged as a fee for contracts below USD 1 million and for the amounts exceeding USD 1 million, USD 5 million and USD 10 million, rates of 0.9%, 0.7% and 0.4% apply respectively.<sup>1</sup>

**Construction work contracts:** Similarly for purchasing, fees are applied at a diminishing rate but they differ as well according to procurement process. The highest fees are charged for lowest-price selection, then pre-qualification (PQ), non-PQ, alternative and turnkey contracts. Different rates also apply between central government and bodies' contracts as well as those from local purchasing entities: fees are lower for local entities' contracts overall. Further, construction work above USD 8.48 million by local entities is exempt from fees if it is funded by a government subsidy.

**Purchase of technology/service:** Fees are higher for purchase of services compared to others. They are applied as well at a diminishing rate and differ slightly for services such as planning and construction supervision and management services.

**Tailored service:** Fees vary for review service, management of planning and design and construction management. Fees are applied based on the budget for the construction work, and vary according to the degree of the PPS's involvement. The rate at which the fee is charged decreases as the construction budgets based on which the fee is calculated increases.

**Review of total work expenses:** For review of total work expenses, PPS charges relatively low fees. More specifically, for review of appropriateness of design, fees are charged based on the amount of the work requested to be reviewed and, for amounts below USD 8.48 million, the rate of 0.04% fee is charged for central government bodies and local entities. However for amounts exceeding USD 8.48 million, local entities benefit from lower fees of 0.02% whereas central government bodies are charged the same rate of 0.04%. Furthermore, for reviews of price fluctuation, the same rate of 0.1% is charged for both central and local government bodies. In cases where PPS is carrying out the construction work contract, this fee is waived.

1. The values in the "Purchase in foreign currency" paragraph were originally presented in USD.

Source: PPS response to OECD internal questionnaire, 2014 with updates in 2015.

### *PPS procurement statistics*

Procurement of goods, services and construction works contracting through PPS represents approximately one-third of public procurement spending in Korea (see Table 1.6).

Table 1.6. **PPS procurement as percentage of total procurement volume**

In USD billions					
	2009	2010	2011	2012	2013
Total procurement volume	103.7	88.5	84.6	90.2	95.8
PPS procurement	36.2	32.0	28.2	29.0	32.1
Percentage	34.9%	36.2%	33.3%	32.2%	33.5%

Source: PPS response to OECD internal questionnaire, 2014 with updates in 2015.

A more detailed breakdown of PPS procurement, including foreign procurement, is provided in Table 1.7. In addition to the construction procurement conducted by PPS, construction-related services including construction project management, cost review, and total project cost review are provided for projects with values reflected in Table 1.8. Details related to the PPS commodity stockpiling function are provided in Table 1.9.

Table 1.7. **Annual procurement by PPS**

In USD billions							
	2009	2010	2011	2012	2013	2014	
Procurement contracting total	37.4	32.5	28.8	29.4	32.5	28.8	
Domestic procurement	Goods (includes leases)	13.5	12.3	12.8	15.9	14.3	15.9
	Services	2.5	2.4	2.4	3.1	2.6	3.2
	Subtotal	16.0	14.7	15.2	19.0	16.9	19.1
Foreign procurement	1.2	0.5	0.6	0.4	0.4	0.4	
Construction procurement	Construction	20.3	17.0	12.7	12.8	11.9	9.0
	Related services	Included in "domestic" category	0.3	0.3	0.3	0.3	0.3
	Subtotal	20.3	17.3	13.0	13.1	12.2	9.2

Source: PPS response to OECD internal questionnaire, 2014 with updates in 2015.

Table 1.8. **Value of projects for which PPS provides construction-related services**

In USD billions						
	2009	2010	2011	2012	2013	2014
Construction project management	2.4	2.8	2.0	2.6	2.3	1.0
Total project cost review	16.1	7.7	8.6	6.2	7.0	9.8
Cost review	1.9	1.3	0.7	0.9	2.0	1.7
Total	20.4	11.8	11.4	9.7	11.2	12.6

Source: PPS response to OECD internal questionnaire, 2014 with updates in 2015.

Table 1.9. PPS commodity stockpiling operation

		In USD millions				
		2009	2010	2011	2012	2013
Commodity stockpiling	Purchase	581.8	274.3	307.5	477.0	539.0
	Release	357.4	315.5	558.8	362.6	401.2

Source: Public Procurement Service (2013), “2013 annual report: Public Procurement Service, the Republic of Korea”, [www.pps.go.kr/eng](http://www.pps.go.kr/eng).

## Public procurement training and knowledge management

Considering the economic importance of public procurement, it is essential that procurement professionals have adequate knowledge and skills necessary to manage the interface with the private sector and mitigate the potential for corruption. As public procurement systems are used more frequently to pursue additional policy objectives, there is increased complexity involved in balancing these objectives, and a procurement workforce with the capacity to address these challenges is necessary. OECD work in public procurement has demonstrated that this is an area where many countries face challenges. In fact, adequate capability and management of the procurement function was identified as an area for improvement by 48.4% of respondents during the monitoring of the 2008 OECD “Recommendation of the Council on Enhancing Integrity in Public Procurement”. In more than one-third of OECD countries, procurement is not recognised as a specific profession. This focus on procurement workforce capacity is recognised in the 2015 OECD “Recommendation of the Council on Public Procurement” (hereafter, the “OECD Recommendation”). See Box 1.4 for the section on professionalisation in the OECD Recommendation.

### Box 1.4. OECD Recommendation on professionalisation

**IX. RECOMMENDS** that Adherents develop a procurement workforce with the **capacity** to continually deliver value for money efficiently and effectively.

To this end, Adherents should:

**Ensure that procurement officials meet high professional standards for knowledge, practical implementation and integrity by providing a dedicated and regularly updated set of tools**, for example, sufficient staff in terms of numbers and skills, recognition of public procurement as a specific profession, certification and regular trainings, integrity standards for public procurement officials and the existence of a unit or team analysing public procurement information and monitoring the performance of the public procurement system.

**Provide attractive, competitive and merit-based career options for procurement officials**, through the provision of clear means of advancement, protection from political interference in the procurement process and the promotion of national and international good practices in career development to enhance the performance of the procurement workforce.

**Promote collaborative approaches with knowledge centres such as universities, think tanks or policy centres to improve skills and competences of the procurement workforce.** The expertise and pedagogical experience of knowledge centres should be enlisted as a valuable means of expanding procurement knowledge and upholding a two-way channel between theory and practice, capable of boosting application of innovation to public procurement systems.

Source: OECD (2015b), “Recommendation of the Council on Public Procurement”, [www.oecd.org/corruption/recommendation-on-public-procurement.htm](http://www.oecd.org/corruption/recommendation-on-public-procurement.htm).

Training for procurement officials and for private sector stakeholders is provided through a number of sources in Korea. Centrally, PPS operates a training facility that provides training for approximately 5 000 people annually. This training centre offers residential courses of two or three days for PPS employees, employees of other central, local and public entities, and for private sector participants. For suppliers, PPS training usually consists of a two-day course covering public tenders generally and the use of the KONEPS system. Costs for buying entities are around USD 120 for a three-day course (including room and board at the training centre dormitory), while costs for a two-day course for suppliers are approximately USD 82.<sup>2</sup> The PPS training facility is also responsible for the certification process for procurement officials. In addition to the central training facility, 9 of the 11 regional PPS offices also offer training courses for KONEPS users.

Training is also available from a variety of other sources. The Federation of Small and Medium Enterprises, which is not a governmental entity, but a legal entity in the public interest, established by Small and Medium Enterprise Cooperatives Act, offers training for its members. This training programme is a one-day, comprehensive course in how to participate in public tenders and how to use KONEPS. It is offered region by region, and each region is served by one or two courses annually. Other trade associations, such as the Construction Association of Korea, also provide training relevant for their members. Private sector training offerings on the use of KONEPS are also widely available, with third-party training providers basing their curricula on KONEPS manuals published by PPS.

### ***Recommendations on training and knowledge management***

Despite these training availabilities, Korea faces some challenges in the area of procurement workforce development. At a general level, the lack of co-ordination among training offerings yields potential for duplication of effort. Though PPS cannot control or manage the training offerings conducted by third parties, a better understanding of those offerings, and a better integration of the curriculum of the PPS training centre based on that understanding, could potentially lead to better targeting of training resources. Additional attention to the procurement certificate programme is also warranted. Though the certificate is offered and managed by the PPS training centre, there was no clear indication that achieving certification yielded any particular benefits for a public procurement official. Capturing these training offerings for online sharing or otherwise developing online training materials or courses could also expand the number of users who can benefit from these efforts, as well as provide an always-available resource for refreshing knowledge as needed.

As an integrity measure, to ensure that public officials do not develop long-term attachments to particular contacts, the Korean civil service includes a requirement that individuals rotate through different positions every two or three years. This is a practice that is also followed in other civil service systems (see the German example in Box 1.5), but it can pose some challenges in the context of public procurement officials. For an organisation like PPS, it offers a clear benefit, as individuals who transfer through different divisions receive a broad experience with a number of different public procurement issues, through the course of a career. For other central government entities, where procurement is simply one function (usually located in the General Service Division) among many, it means that individuals responsible for public procurement are only engaged in that activity for a relatively short period of time. In such circumstances, defining an attractive career path related to public procurement can be a challenge.

### Box 1.5. Staff rotation in the German civil service

The basis for the civil service rotation practice in Germany can be found in No. 4.2 of the Federal Government Directive concerning the Prevention of Corruption in the Federal Administration, which reads:

*“The length of staff assignments in areas especially vulnerable to corruption shall in principle be limited; as a rule, it should not exceed a period of five years. If an assignment must be extended beyond this period, the reasons shall be recorded for the file.”*

The (formal) determination of *areas especially vulnerable to corruption* in that given sense has to regularly take place according to No. 2 of that directive, and is conducted according to a risk assessment system in place on the federal level (the states - *Länder* - maintain their own systems). According to the Directive concerning the Prevention of Corruption, and as further explained in the recommendations for its application (No. 3 in the brochure “Rules on Integrity”), each agency has to assess the areas of activity within the agency which are especially vulnerable to corruption, and to apply certain measures for staff entrusted with them. The rotation principle is one of them.

According to the Recommendation on Preventing Corruption, in areas of activity especially vulnerable to corruption,

- after identifying special vulnerability to corruption for the first time,
- after organisational or procedural changes,
- after changes to assigned tasks, or
- after no more than five years,
- the need for conducting a risk analysis should be examined.

This analysis involves a brief examination of the effectiveness of existing safeguards for each area of activity especially vulnerable to corruption; if the brief examination points to a need for action, a risk analysis is to be conducted. If action is needed, then the organisation and processes and/or personnel assignments are examined to see how they can be changed. In this case, the risk analysis will include recommendations and/or order additional measures.

In the case of exceptions authorised by the Federal Government Directive, the most typical reasons why members of staff posted in areas especially vulnerable to corruption had been remaining on the same post for more than five years are (in that order):

- specialists who cannot rotate
- other members of staff with specific knowledge which cannot be replaced, having due regard to continuity,
- members of staff who will very soon leave active service,
- members of staff who will soon change over to another position,
- members of staff for whom an appropriate other position on the same remuneration level cannot be provided.

In such cases, the Recommendation on Preventing Corruption in the Federal Administration indicates:

*“[i]f in exceptional cases rotation is not possible due to the nature of operations or to (personnel) management considerations (e.g. lack of expert staff), then other appropriate and effective measures to prevent corruption should be used instead (e.g. extending the application of the principle of greater scrutiny, working in teams and exchanging tasks within organisational units, transferring responsibilities, intensifying administrative and task-related supervision).”*

### Box 1.5. Staff rotation in the German civil service (*continued*)

Such *other appropriate and effective measures to prevent corruption* can include the application of the “principle of greater scrutiny” (co-signature requiring a second staff member to check work results) or intensifying administrative and task-related supervision.

In Germany, most corruption cases in the past had been committed by members of staff who were on the same post for more than five years. As “situational corruption” is very rare in Germany, and corruption cases rather concern “structural corruption”, third parties first have to “invest” in the relationship with the member of staff who is to be corrupted. Such “investment” does not pay once it is clear that the relevant member of staff will be rotating to another position in some years. If third parties try to build up good relations with administrative staff, the purpose is rather not to gain sympathy from a specific member of staff, but rather to maintain a good working relationship with the agency as such.

The purpose of the introduction of the rotation principle is not only to prevent corruption. Many agencies, in particular ministries, it also allows to regularly allow a person who is new to a position to have a “fresh view” on the matters that he or she is now responsible for. It is encouraged that, in particular on specific higher positions, members of staff are generalists who gain experience in many fields of work, and who are used to getting acquainted with new tasks quickly. The experience gained in former positions allows them to identify crosslinks between specific subjects. For this reason, according to many staff development plans, promotion to a higher position (and remuneration level) requires a specified number of different positions held on the former level; in many cases, this forms a mandatory prerequisite for such promotion.

*Source:* Adapted from Federal Ministry of the Interior (2014), “Rules on integrity”, [www.bmi.bund.de/SharedDocs/Downloads/EN/Broschueren/2014/rules-on-integrity.html](http://www.bmi.bund.de/SharedDocs/Downloads/EN/Broschueren/2014/rules-on-integrity.html).

For this reason, the development of methods and procedures for knowledge management becomes very important. One example, disclosed during the fact-finding mission, was the development of a survey report by a procurement official designed to identify all of the various secondary policy requirements that applied to public procurement. In addition to secondary policy objectives that apply to all of the government, some ministries and offices have additional requirements or recommendations to pursue social policy objectives through public procurement. In this case, the official’s report identified 8-10 mandatory requirements, and up to 46 recommended procurement priorities. While this report was developed independently to help procurement officials manage internal prioritisation at a central government agency, central identification of all of the objectives required by law and regulation, presented in a simplified format, would be a useful tool, and a well-designed online presentation of such a tool could also allow individual ministries or entities to append their own specific requirements for easier reference.

The fact-finding mission also identified that there was no formal technical mechanism through which information could be shared more broadly among the public procurement workforce. Some opportunities for knowledge sharing occur - for example, regional procurement consultation meetings held each year bring together public procurement officials from various central government agencies – but they are one-off, ad hoc opportunities. One means of addressing this circumstance would be the development and support of a network of public buyers as an ongoing, regular forum for communication among public procurement officials in Korea. While regular in-person meetings might prove cost prohibitive, a dedicated and central online forum that could allow both communication and the collection and sharing of relevant information could provide a

better sense of community and serve as a substantial support mechanism for new public buyers, and a valuable source of information over time.

While the buying entities and suppliers interviewed during the fact-finding mission were generally very satisfied with the level of support they received from PPS, both in terms of the call centre and the availability of staff to support their activities, one buyer mentioned an additional challenge that results from the rotation policy for civil servants: occasionally as one staff member rotates out and a new one rotates in, there are some delays in connecting with the new staff member responsible for the account. Better management of client relationships, for example through the creation of a detailed client file and a protocol for making contact when responsibilities are transferred, could address this issue.

## Oversight of the public procurement function

Proper internal and external controls are an important element of a well-functioning public procurement system, and the OECD Recommendation contains additional details regarding necessary considerations (see Box 1.6). Public procurement activities in Korea are subjected to oversight both internally, in the form of an audit office for each central agency, as well as externally through the activities of the Board of Audit and Inspection of Korea (BAI) and the Fair Trade Commission (FTC).

### Box 1.6. OECD Recommendation on accountability

**XII. RECOMMENDS** that Adherents apply oversight and control mechanisms to support **accountability** throughout the public procurement cycle, including appropriate complaint and sanctions processes.

To this end, Adherents should:

...

**Ensure that internal controls (including financial controls, internal audit and management controls), and external controls and audits are co-ordinated, sufficiently resourced and integrated** to ensure:

- the monitoring of the performance of the public procurement system;
- the reliable reporting and compliance with laws and regulations as well as clear channels for reporting credible suspicions of breaches of those laws and regulations to the competent authorities, without fear of reprisals;
- the consistent application of procurement laws, regulations and policies;
- a reduction of duplication and adequate oversight in accordance with national choices; and
- independent ex-post assessment and, where appropriate, reporting to relevant oversight bodies.

*Source:* OECD (2015b), “Recommendation of the Council on Public Procurement”, [www.oecd.org/corruption/recommendation-on-public-procurement.htm](http://www.oecd.org/corruption/recommendation-on-public-procurement.htm).

### *Audit authorities*

PPS has in place both *ex ante* and *ex post* audit processes. The PPS Audit Team supervises execution and contract process of contracts (above certain price thresholds) executed under the budget of PPS or procured by PPS where certain risks are expected. Details regarding the PPS audit activities are contained in Table 1.10.

Table 1.10. **Scope of PPS audit activities**

Types of audit	Area of audit	Information audited
Ongoing audit	E-procurement system	Bid-rigging and price collusions Appropriateness and legality of electronic bidding execution Appropriateness of change in qualification criteria including notified qualification conditions, starting date of bidding, and reserve price Other general management issues of e-procurement system
<i>Ex ante</i> audit	Enforcement of main policies	Enforcement of policies or projects that are categorised as main policies or main projects that require progress assessment or review of the results
	Contracts for goods and services	The choice of awarding method of contracts of total amount estimated to be above USD 2 500
	Budget management	Execution of more than USD 8 500 per one of the following budget classes: <ul style="list-style-type: none"> <li>• Utility + overhead costs</li> <li>• Maintenance cost of facility equipment</li> <li>• Equipment costs</li> <li>• Extra costs on equipment</li> <li>• Property acquisition costs</li> <li>• Budget account that is executed, executed for other purposes, carried forward or settled</li> <li>• The decision on choice or change of the organisation's main bank of transaction</li> <li>• Official meeting where more than 100 people participate (e.g. workshop)</li> </ul>
	Goods management	Stock management change of more than USD 42 400 of book amount Sale or disposal of stock of more than USD 42 400 of book amount Loss and damage disposal
	Other	Items prescribed by the Head of the PPS to be audited <i>ex ante</i> Main terms of human resources management including appointment of an employee, rewards and disciplinary actions Management of affiliated organisations
Inspection audit	Inspection of goods	Inspection of goods (on items selected during <i>ex ante</i> audit)

*Source:* PPS response to OECD internal questionnaire, 2014 with updates in 2015.

For completed contracts, there are two types of *ex post* audits conducted by the PPS Audit and Inspection Officer. A number of regular audits occur each year; contracts are usually selected using information available in the KONEPS data warehouse, and the PPS Audit and Inspection Officer then inspects them for compliance. Additionally, targeted or themed audits are possible on an ad hoc basis. These audits usually occur in response to challenges from suppliers with respect to a particular contract action. They may also include a focus on a particular subject, for example the operation of the system or a particular feature of its use. PPS does not currently track the number or percentage of contracts subjected to more detailed audit, as part of either the regular or ad hoc process, but estimates that approximately 10% of all contract actions are reviewed in more detail by the internal PPS Audit and Inspection Officer. Detailed audit requires substantial time and resources. To most effectively utilise limited resources, PPS focuses on developing analytical techniques that utilise information from the KONEPS data warehouse in order to identify problems in general procurement processes.

PPS has responsibility for contracts established by PPS. Other contracts issued through KONEPS by other buying entities are subjected to oversight from their own internal audit offices. Additionally, the BAI has authority to review public procurement activity. The Board of Audit and Inspection Act gives the BAI broad access to data from central government agencies. PPS does not maintain a specific data-sharing agreement or direct data link with the BAI or with audit offices in other organisations, but the information available in the KONEPS data warehouse is generally sufficient to support these needs. As the KONEPS data warehouse contains more information than is publicly available, the BAI or other audit office will ask the PPS Audit and Inspection Officer for the data. In cases where the audit office requests data in a new form or format, the PPS IT division is capable of responding quickly to address the need.

These audits are generally focused on contract matters and compliance, focusing on contracts themselves, though some audits focus on the overall results of the procurement system. If illicit conduct is found during the course of an audit, the relevant procurement officer is penalised, depending on the severity of the problem. In minor cases, a warning may be issued, but in more serious cases penalties can include suspension of employment, deduction of wages, demotion or termination. With respect to the contract action, the application of civil law indicates that the only case where a contract is terminated is when the basis of the contract was legally void, for example in cases of deception. In other cases, the signed contract is still considered valid, despite any problems identified by an audit. In these cases, dissatisfied suppliers may bring legal action, but a successful suit would result in payment for damage rather than the dissolution of the contract.

### ***Recommendations on audit and oversight***

There is no formal and ongoing collaboration with the PPS Public Procurement Training Institute to capture the audit results as inputs into training development. Instead, most errors identified through audits are disseminated on an ad hoc basis, for instance through an audit fact sheet or through meetings of the headquarters and regional offices. PPS also looks for situations where a problematic audit finding could be addressed through a modification of KONEPS; in such cases the Audit and Inspection Officer will request that the information technology (IT) division update the system to address the potential problem. While these steps are important, finding a means of more fully integrating the results of audit activities into the training of procurement officers could yield benefits for the system.

### ***Fair Trade Commission***

The Fair Trade Commission (FTC) works with public buying entities to identify cartel activity and potential cases of bid rigging in public procurement. This work is particularly relevant at this time, as a number of potential cases related to increased spending in response to the 2009 economic crisis have been identified. During 2009 and 2010, Korea launched a number of large public works projects in a short period of time, and there are now claims that contractors colluded to divide this work.

To identify cases of collusion, the FTC traditionally relied on voluntary reporting by cartel members seeking leniency, and on reports by competing suppliers. These remain the most reliable sources of identification of potential collusion. In 2006, the FTC developed the Bid Rigging Indicator Analysis System (BRIAS) to supplement these methods of identification.

Drawing information directly from KONEPS, BRIAS looks to data elements including bidding price (as a ratio compared to reference price), the number of participants, and the competition method, and applies a formula that generates a potential bid-rigging score. If above a certain threshold, this then suggests the need to collect more information regarding the contract action. Based on this closer look, an investigation is opened in cases where it is warranted.

BRIAS collects information from KONEPS on a daily basis, and each month the system is run on collected data from the previous month. For goods and services, BRIAS is run on tenders above USD 423 800. For public works, the threshold is USD 4.2 million. As of 2012, BRIAS was run on 20 000-30 000 biddings per year; of approximately 20 000 runs in 2012, the system generated 200 hits that warranted an additional look. The establishment of this kind of automated system for the detection of red flags in public procurement is a good practice implemented successfully in other countries such as Brazil (see Box 1.7).

Whether identified through BRIAS or through traditional means, investigation of potential cases of collusion involves collection of additional information from PPS followed by site visitations and other investigative steps to find evidence of information exchange. These investigations can take anywhere from one to three years, from initial reporting to final verdict, and the FTC has established a separate investigation unit focused solely on public procurement. When found guilty, sanctions can range from orders for corrective action, which are essentially warnings for minor offenses, through a financial penalty of up to 10% of the contract volume involved. Additional criminal charges can also be filed with prosecutors. In 2012, more than 40 cases led to findings of guilt, leading to fines in excess of USD 847 million. The number of investigations and findings of guilt has been increasing.

In terms of direct contribution, the results from BRIAS have been limited: only three cases initially identified by BRIAS have led to findings of guilt. In part, this is attributable to the fact that the capacity to investigate is limited, and cases based on voluntary reporting or challenges by other suppliers begin with a more firm investigative basis than the circumstantial red flag generated by BRIAS. But during the period of its operation, voluntary reporting by cartel participants has increased significantly, and some of this increase is attributed to the raised awareness and fear of being caught generated by the implementation of the BRIAS system. This result is consistent with the OECD Recommendation on Public Procurement, which identifies the publication of risk management strategies, including systems for generating red flags, as an important element of their effectiveness.

To further expand the benefits of the BRIAS system, the FTC established a committee between project commissioners (including PPS and other large enterprises) to try to encourage adoption of a similar system at other public enterprises. In addition to providing the same functionality in a broader range of public procurement cases, spreading systems like this will allow the FTC to develop broader expertise, based on the differences in procurement practices at different entities, to better identify and prosecute cases of collusion. Dissemination activities are also undertaken to spread awareness and identify typical cases of collusion. In addition, the PPS training centre recently developed a separate training course on collusion, implemented in collaboration with the FTC.

### Box 1.7. Public Spending Observatory in Brazil

The Office of the Comptroller General of the Union launched the Public Spending Observatory (*Observatório da Despesa Pública*) in 2008 as the basis for continuous detection and sanctioning of misconduct and corruption. Through the Public Spending Observatory, procurement expenditure data are cross-checked with other government databases as a means of identifying atypical situations that, while not *a priori* evidence of irregularities, warrant further examination.

Based on the experience over the past several years, a number of daily actions are taken to cross procurement and other government data. This exercise generates “orange” or “red” flags that can be followed up and investigated by officials within the Office of the Comptroller General of the Union. In many cases, follow-up activities are conducted together with special Advisors on Internal Control and internal audit units within public organisations.

Examples of these tracks related to procurement and administrative contracts include possible conflicts of interest, inappropriate use of exemptions and waivers and substantial contract amendments. A number of tracks also relate to suspicious patterns of bid-rotation and market division among competitors by sector, geographic area or time, which might indicate that bidders are acting in a collusive scheme.

Finally, tracks also exist regarding the use of federal government payment cards and administrative agreements (*convenios*). In 2013, there were 60 000 instances of warnings originated from the computer-assisted audit tracks used by the Office of the Comptroller General of the Union to identify possible procurement irregularities, like:

- |   |   |
|---|---|
| 1. business relations between suppliers participating in the same procurement procedure               | 11. personal relations between suppliers and public officials in procurement procedures   |
| 2. fractioning of contracts in order to use exemptions to the competitive procurement modality        | 12. use of bid waiver when more than one “exclusive” supplier exists  |
| 3. non-compliance by suppliers with tender submission deadlines                                       | 13. bid submission received prior to publication of a procurement notice  |
| 4. registration of bid submissions on non-working days  | 14. possibility of competition in exemptions  |
| 5. supplier’s bid submissions or company records with the same registered address                     | 15. participation of newly established suppliers in procurement procedures  |
| 6. contract amounts above the legally prescribed ceiling for the procurement modality used            | 16. contract amendments above an established limit, in violation of the specific tender modality  |
| 7. contract amendments within a month of contract award, in violation of the specific tender modality | 17. commitments issued prior to the original proposal date in the commitment registration system  |
| 8. evidence of bidder rotation in procurement procedures  | 18. bidding procedures involving suppliers registered in the Information Registry of Unpaid Federal Public Sector Credits ( <i>Cadastro Informativo de Créditos Não Quitados do Setor Público Federal</i> ) |
| 9. use of reverse auctions for engineering services   | 19. micro- and small-sized enterprises linked to other enterprises  |
| 10. micro- and small-sized enterprises with shareholders in other micro- and small-sized enterprises  | 20. micro- and small-sized enterprises with earnings greater than BRL 0.24 million or BRL 2.40 million, respectively.   |

Source: OECD (forthcoming), *Compendium of Good Practices for Integrity in Public Procurement*.

Finally, additional work is underway to improve the function of the BRIAS system. While this sort of system of generating red flags will always generate only circumstantial indications of potential collusion, the FTC is conducting an ongoing evaluation of the formula and indicator elements to improve accuracy. In addition to adjustments for increased accuracy, monitoring of the formulas involved in this sort of system and changing them over time is necessary to address changes in the market. Collusion presents an evolving fight, as cartels adjust their practices to adapt to new means of identifying bid rigging.

## Key findings and recommendations

The Korean public procurement system, viewed through the role and responsibilities of PPS, is a high functioning and mature public procurement system. At its centre, the system is defined through a coherent and stable legal and regulatory framework. Such a framework is necessary for ensuring fair access to public procurement opportunities for all potential competitors, as recognised in Element IV (i) of the OECD Recommendation.

As a centre of efficiency, PPS serves the role of a central purchasing body, and implements many good practices consistent with Element VII (iii) of the OECD Recommendation, which encourages countries to “develop and use tools to improve procurement procedures, reduce duplication and achieve greater value for money, including centralised purchasing, framework agreements, e-catalogues.” The success of PPS in effectively implementing this recommendation is demonstrated by the fact that use of PPS’ purchasing services continues to increase, despite the fact that mandatory use of these services by local and other entities has been phased out over time.

This increased use, along with reports of satisfaction from users of the wide variety of PPS’ services, indicates that PPS offers a value proposition for the end user, demonstrating implementation of Element VII (ii) of the OECD Recommendation to “implement sound technical processes to satisfy customer needs efficiently.” The adoption of a revolving budget account to facilitate prompt payment of suppliers, the availability of a call centre to address technical questions from end-user buyers and suppliers, and the general efficiency of the Online Shopping Mall experience are all evidence of success in this area.

In general, necessary training opportunities are available, consistent with Element IX of the OECD Recommendation, though more could be done to co-ordinate trainings offered by various sources. As in some other civil service systems, a rotational assignment policy is implemented to foster integrity, consistent with Element III (ii) of the OECD Recommendation: “implement general public sector integrity tools”. This process poses some challenges for the professionalisation of the public procurement function, but these challenges can be addressed through the further development of the procurement certification programme and the development of a network of public buyers to share information and resources.

Finally, the oversight functions of the PPS Audit Office, the BAI and the FTC are appropriately identified to ensure co-ordination and limited overlap, consistent with Element XII (iv) of the OECD Recommendation. The PPS Audit Office provides appropriate attention to *ex ante* monitoring processes, including both standard system monitoring and specific attention to high-risk contract actions. Information necessary for the actions of BAI is provided as needed from the KONEPS data warehouse. As part of its activities to identify collusion and bid rigging, the FTC continues to develop a red

flags system to identify suspicious cases. Publication of this risk management strategy appears to be generating additional results in the form of self-reporting by cartel members concerned about being caught. These actions are good examples of implementation of Element XI of the OECD Recommendation, which encourages integrated risk management through the development of tools and the publication of such strategies.

### *Summary of recommendations for action*

- Better co-ordinate training offerings to compliment and supplement other available training.
- Examine procurement certification programmes to establish relevant and meaningful benefits for public procurement officials who obtain certification.
- Develop a network of public buyers as a forum for communication, collaboration and information dissemination. This network can also serve a knowledge management function, over time, as shared information is collected.
- Develop client management files and appropriate outreach protocols for transfer of responsibility.
- Consider integration of audit findings with regular curriculum development for training activities, to better incorporate lessons learned.

## Notes

1. Values in this report have been converted from KRW to USD using a rate of 0.0084763 USD per KRW, obtained on 15 September 2015. In some cases, data were originally presented in USD; these cases are identified with appropriate endnotes.
2. The costs for training were originally provided in USD.

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