

Working Paper:

Report on Recent Bribery Scandals, 1996-2000

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1. Overview of the System of Political Finance in South Korea

After seven years of anti-corruption efforts and strife for political reform, the political system of South Korea is still suffering from the aftermath of more than 30 years of authoritarian rule. The military governments that ruled South Korea from 1961 to 1993 left a legacy of tightly knit relationships between government and big business, represented by large family-owned industrial conglomerates, the *chaebol*. Political and economic exchanges were and, as is shown by the corruption scandals discussed later in this report, still are often based more on informal and personal relationships than on institutionalized market transactions. Together with cultural factors such as a strong focus on regional origin and membership in clan organizations, and further stimulated by a presidential system that concentrates decision-making power in the hands of a rather small political elite, the close relationship between big business and government can be seen as the main cause for corruption in South Korea. Bribery scandals are frequently disclosed in the South Korean media, and public trust in politicians and business leaders is perpetually low.

After Kim Young-Sam took over the presidency in 1993 as the first democratically elected president since 1961, a series of political reform bills was enacted. Intended to erase political corruption and accompanied by a wide-ranging purge of the bureaucracy, politics and big business, a new election campaign law was introduced and penalties for corruption were increased. The new laws include a raise of government subsidies for political parties and higher allowances for candidates at all levels that should reduce spending by individual candidates. A new reporting system for political donations further allowed parties and candidates to hand out anonymous receipts for political donations which were issued by the Election Commission. This measure was intended to provide ruling and opposition parties with equal chances for political fundraising. Under the former authoritarian regimes, businesses or interest groups that supported opposition parties or candidates were regularly reprimanded by the ruling party, causing reluctance on the business side to support the opposition. At the same time, the introduction of a "real-name banking system" was meant to ensure more transparency in political finance by outlawing banking deposits held under pseudonyms. Previously, businessmen and politicians had used bank accounts under false names to pass on bribes or to deposit illegal campaign contributions or other illegally received funds without detection (Lee and Sohn 1995; Beal and Yea 1997; *Far Eastern Economic Review* 30 November 1995).

Kim Young-Sam's successor Kim Dae-Jung is continuing these reform efforts. In February 2000, revisions of the National Assembly Law, the Political Fund Law and the Political Party Law obliged, among else, candidates for public office to lay open their military service and tax records, streamlined political party operations, and introduced new means of political fundraising for parties and individual candidates. Despite these revisions, the South Korean political finance system still lacks regulations ensuring transparency of political funds (for further details, see for example Park Chan-Wook 2000). Under the increasing pressure of civil groups protesting against corruption and confronted with "blacklists" of corrupt or "incompetent" politicians, or so-called "rejection campaigns" at election times (such as the one conducted by a union of civic groups at the occasion of the parliamentary elections in April 2000), further reforms can be expected.

1.1. Politics and money in South Korea

Under the military regimes that ruled South Korea between 1961 and 1993, political power was concentrated in the hands of the president. Today, the presidential office still controls the prosecution, police and tax authorities, and has considerable influence on the financial system. Government ministers were (and still are) appointed by the president and he had thus direct line of command over the ministries and the bureaucracy. Also regional and local officials such as mayors and governors were appointed by the central government, giving the president direct control down to the local level. Political control was also strong in the economy. The South Korean economy was and still is highly regulated, and a high number of business transactions require government permits or licenses. Moreover, South Korean government ministries can change rules and regulations regarding commerce and other matters without the approval of the legislative branch (*Far Eastern Economic Review* 30 November 1995).

Businessmen and interest group representatives thus regularly lobby the administration in order to receive favorable treatment by the authorities. As a reward for getting rules changed in their interests or for receiving special privileges, the president or cabinet ministers receive large political contributions (Chon Soo-Hyun 2000, 66). Under authoritarian rule until 1993, however, the relationship between big business and the ruling party often also showed signs of blackmail. Presidents, from Park Chung-Hee to Roh Tae-Woo, formed their own private foundations and forced the *chaebol* to pay regular contributions as membership fees in proportion to their *revenues*.¹ Those who refused were reprimanded by the government and encountered problems when applying for licenses or business loans. Presidents also received political contributions that were made indirectly through cabinet ministers or religious organisations. Another source of income for the ruling party leaders was the acceptance of money from candidates for nominations on the party list in the national constituency in National Assembly elections. A part of the seats in the National Assembly is allocated in proportion to the number of seats a party wins in the local constituencies. The chances of a candidate in the national constituency to win a seat are determined by his or her rank on the party list. Traditionally, candidates on both the ruling party and the opposition party lists were ranked according to their political contributions to the party leadership. The ruling party used the bureaucracy to gather information about opposition support in individual constituencies and to actively discourage firms, interest groups, and individuals from funding the opposition. Opposition supporters or firms that donated money to opposition parties were, for example, likely to be audited by the tax authorities. The ruling party thus had a significant financial advantage over the opposition, for which candidate nomination fees were one of the main sources of income during the period from 1961 to 1993 (Chon Soo-Hyun 2000, 71-77).

Political contributions collected by the South Korean parties were and still are usually used to fund election campaigns. Although the South Korean election laws are very strict and state a clear limit on both the sources of funding and campaign expenses during the 20 days of the official campaign period, both presidential and National Assembly elections are usually very costly. Most candidates exceed the legal limit on campaign expenses, which is set at approximately 90 million won (around \$112,000) per candidate. Campaign workers range from 40,000 to 50,000 won (\$40-\$62) per day, and many candidates in the 1996 National Assembly elections, for example, used about 500 of these workers. A local saying stated that those who spend 2 billion won (\$2.5 million) will be elected, while those who spend only 1 billion will not gain a seat (Koh 1997). At the April 2000 National Assembly elections, Korean media changed this phrase, stating that candidates had to spend about 3 billion won (\$3.75 million) to win their local constituency (*Korea Herald* 20 March 2000). Most of the money is used to buy votes, by giving expensive presents to influential voters, by handing out cash (on average, about \$90 per person), or by holding lavish dinners for support groups. Other expenses include costs for staff and people to attend political rallies as well as gifts of money to journalists.

Similarly to Japan, most of these costs are not limited to election time, but are regularly required in order to secure re-election. South Korean National Assembly members' monthly allowance does not cover the costs for regular constituency service, including gifts and monetary contributions at weddings, funerals or other events in supporters' private lives, trips for organised support groups to the assembly in Seoul, contributions to events by local associations and clubs in the constituency, or regular gifts for journalists to secure the politician friendly press coverage. Like their Japanese colleagues, South Korean parliamentarians are thus in a permanent need for money and are willingly taking every chance to increase their election funds, even in violation of electoral regulations.

1.2. Changes under democratic rule since 1993

During the government of President Kim Young-Sam, presidential power weakened considerably. This change can partially be attributed to political reforms and related institutional changes initiated under Kim's rule. Equally important, however, is the loss of prestige on the side of the long-ruling party due to a series of corruption scandals that were disclosed under Kim Young-Sam's rule and that led to a wide-ranging purge of corrupt politicians, bureaucrats and business leaders. Both factors contributed to a stricter enforcement of election laws and a reduction of income of the ruling party. At the same time, the political reform laws enacted under the Kim Young-Sam government that channeled political contributions through the National Election Commission not only impeded some of the formerly prevalent corrupt practices, but also helped the opposition to increase its funds and thus ensured a more equal distribution of political funds. These changes were also furthered by the 1997-1998 economic crisis and the external pressure by the IMF on the South Korean government to reform the country's economic structure. Such pressure contributed to the decrease in influence and the gradual disintegration of the *chaebol*, thus eliminating an important source for political contributions.

With regard to the 1997 presidential elections that were won by the veteran opposition candidate Kim Dae-Jung, Chon Soo-Hyun (2000, 77-78) argues that the introduction of television debates between the leading candidates for the presidency reduced the importance of money for winning presidential elections. In her opinion, voters based their decision on what candidate to support in his claim for the presidency based on their performance in TV debates. However, in the National Assembly elections in April 2000, money still seemed to be the most decisive factor in order to win a seat.

2. Major bribery scandals involving political contributions, 1993-2000

2.1. The "Slush Fund Scandal" (October 1995)

When Kim Young-Sam was inaugurated as the first democratically elected president of South Korea since 1961, he chose political reform and an end to corruption as one major goal for his government. The "major focal point" of the reform (Beal and Yea 1997) was the so-called "Slush Fund Scandal," which led to the arrest of former President General Roh Tae-Woo and also produced corruption investigations against the leaders of all 30 top industrial conglomerates. In October 1995, it was disclosed that former President Roh had collected political donations amounting to 500 billion won (around \$650 million) from businesses as contributions to his (secret) governing fund while holding public office between 1988 and 1993. Koh (1996) states that the discovery of this fund and of the fact that over a third of the money (\$245 million) was still in his possession was "the most stunning development in South Korean politics in recent years". On October 19, 1995, Park Kye-Dong, a National Assembly member of the opposition Democratic Party provided the Supreme Public Prosecutor's office with copies of bank records that proved the existence of the fund. Several days later, Roh's former chief bodyguard and later director of the Agency for National Security Planning, Lee Hyun-Woo, admitted to the prosecution that he had managed the fund.

What shocked South Koreans was not only the size of the fund. Koh (1996) quotes calculations that Roh must have collected \$10 million per month while he was in public office. Shocking for South Korean voters was also to find out that virtually all top South Korean business firms had regularly made donations to Roh's fund. Prosecutors later could prove that these donations were paid as bribes or kickbacks for favors. The top four donors were Hyundai and Samsung group with 25 billion won (\$32.7 million) each, Daewoo Group (24 billion won, \$31.4 million) and Lucky Goldstar Group (21 billion won, \$27.5 million). Together with Roh, who was eventually indicted and tried, 36 leading businessmen, among them the chairmen of the 30 top South Korean businesses, were investigated. Nine, including the chairmen of Daewoo and Samsung, were indicted on bribery charges. In August 1996, the Seoul district court sentenced Roh to twenty-two-and-a-half years in prison for bribery and other charges related to his authoritarian government, but later an appellate court reduced the sentence to 17 years. Five heads of chaebol, among them the chairmen of Daewoo and Samsung, received two-and-a-half-year sentences for paying bribes to Roh (and his predecessor Chun)² in exchange for favors. Their sentences, like those of most of the businessmen indicted in this case, were suspended (Koh 1997).

In the course of the scandal, veteran opposition leader and current President of South Korea, Kim Dae-Jung, admitted to having taken 2 billion won (\$2.6 million) in campaign contributions from Roh. He also hinted that then President Kim Young-Sam had received money from Roh - an allegation that Kim Young-Sam strongly denied (Koh 1996; Beal and Yea 1997; *Far Eastern Economic Review* 30 November 1995).

The indictment of the two former presidents highlighted how prevalent corruption had been under authoritarian rule. It also showed, however, that the new democratic government was determined to end such practices. While then President Kim Young-Sam first enjoyed high publicity ratings for having his predecessor prosecuted in a corruption case, public support rates plunged in 1997 when his own campaign violations and an influence-peddling scandal involving his youngest son, Kim Hyun-Chul, were disclosed.

2.2. The Hanbo Scandal (January 1997)

The Hanbo Scandal erupted in January 1997, when the Hanbo Group, which had been under corruption investigation several times before, went bankrupt. Hanbo, South Korea's fourteenth largest conglomerate, had received special treatment in return for massive political contributions to then President Kim Young-Sam's 1992 presidential election campaign. In return, Hanbo received government approval for the construction of a new steel mill. After receiving permission to build the steel mill, Hanbo founder and former Chairman Chung Tai-Soo bribed legislators and bankers to press banks to approve loans for the project. With assets of barely more than \$100 million, the company managed to borrow about \$6 billion for the construction of a steel mill that was planned to be the fifth largest in the world. The company went bankrupt in January 1997, and Chul made his case public (Beal and Yea 1997). The bankruptcy of the Hanbo Group contributed to the financial problems South Korea encountered in 1997 to 1999. In relation with the scandal, prosecutors investigated nine politicians of the then ruling New Korea Party for taking tens of millions of won as a reward for mediating massive bank loans for Hanbo.

To make matters worse for President Kim Young-Sam, parallel investigations showed that his youngest son, Kim Hyung-Chul, was involved in the Hanbo Scandal and also in other cases of influence-peddling, such as the acceptance of bribes in return for support in getting licenses to set up TV stations. Kim's son also was allegedly using his influence to fill key positions in the presidential office and intelligence organisations with people loyal to himself. When at the same time a leading party official at a press conference admitted that President Kim Young-Sam's 1992 election campaign cost the party up to 130 billion won (more than three-and-a-half times the legal limit of campaign expenses), public support rates for President Kim Young-Sam dropped from 80% at the start of his term in 1993 to 3.8% in April 1997 (*Far Eastern Economic Review* 15 May 1997; Park Tong-Whan 1998; *Korea Herald* 22 January 1999).

Kim's son Kim Hyung-Chul was later sentenced to three years in jail for receiving a kickback from the company to gain government contracts. In August 2000, he profited from a presidential amnesty in celebration of the Korean national holiday and was released from prison (*Korea Herald* 3 August 2000).

For South Korean voters, the Hanbo Scandal destroyed the illusion that the end of authoritarian rule also meant an end to corruption and related practices. The fact that the President's son was involved in influence-peddling and

corruption also illustrated the still high importance of personal ties and family or clan membership in Korean politics. A scandal that affected the cabinet of Kim Young-Sam's successor Kim Dae-Jung illustrates this aspect of political corruption in Korea even further.

2.3. "Furgate" or the "Clothes Bribery Scandal" (May 1999)

Shortly before two parliamentary by-elections in June 1999, a scandal involving the wives of senior government officials and a jailed business tycoon made headlines in South Korea. The corruption case surrounds allegations made by the wife of the head of Shindongah Group, Choi Soon-Young, that she and her husband bought expensive clothes for the wives of several senior government officials in exchange for favors with a bribery investigation against Choi. Choi's wife, Lee Hyung-Ja, belonged to a club of wives of high-ranking government officials and wealthy businessmen that met every week for volunteer activities. After finishing their volunteer tasks, the women would often spend the afternoon shopping in Seoul's elegant boutiques and also discuss current political and monetary affairs. In December 1998, Lee Hyung-Ja whose husband Choi was under investigation for diverting a huge sum of foreign currency abroad, was approached by the wife of former Unification Minister Kang In-Duck and the wife of then Justice Minister and former Prosecutor General Kim Tae-Jong. Both women allegedly promised to use their influence in order to acquire lenience for Choi. As a reward, Lee was expected to pay for expensive clothes and a fur coat, all together worth about 24 million won (\$300,000). After she declined the request, her husband was arrested and Lee made the case public. The wives of the two Cabinet members denied the allegations, and the prosecution did not succeed in building a case. However, the scandal did serious damage to the government of President Kim Dae-Jung. The public had expected him to oust the two ministers, which Kim declined to do due to lack of proof. Moreover, the media raised suspicions that the presidential office had actively tried to keep prosecution from investigating the case. Kim's party, the National Congress for New Politics, lost the two by-elections which seriously damaged the ruling coalition (*Korea Herald* 27 May 1999; 28 May 1999; 31 May 1999; 7 June 1999; 9 June 1999; 30 August 1999). For most Korean voters, the scandal was a moral

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For most Korean voters, the scandal was a moral problem, involving the wives of high-ranking government officials spending high sums of money on luxury items while at the same time the economy was in a crisis and many people were confronted with bankruptcy and unemployment. For the analysis of political corruption in Korea, however, the scandal illustrates again the important role of family members, such as wives of high-ranking politicians, as targets for bribery and corrupt activities. The two scandals disclosed in 2000 that also involve foreign companies further illustrate this channel for corruption in South Korean politics.

The two scandals presented in the following are still under investigation.

2.4. The Paekdu military intelligence project - from corruption to sex scandal (May 2000)

In early May 2000, South Korean media reported that prosecutors were considering reopening investigations into suspicions that a Korean-American woman illegally lobbied government officials and politicians to help a US wiretapping equipment producer, E System, to win a major military contract during the Kim Young-Sam administration. Linda Kim, the suspected lobbyist, was presented with travel restrictions. Ms. Kim was under investigation for allegedly bribing Korean military officials and politicians. Among the suspects in the case are former Defense Minister Lee Yang-Ho, former chairman of the National Assembly Defense Committee, Hwang Myung-Soo, former Environment Minister Chung Jong-Taek, and former Diet member and Minister for Commerce, Industry and Energy, Kum Jin-Ho. The case under investigation was part of the national military reinforcement program, the so-called Paekdu project which started in 1991. Part of this project was the import of reconnaissance planes and remote military intelligence systems worth \$210 million. In 1996, the Defense Ministry selected the US company E System as a supplier for the project, against competitors from Israel and France. Linda Kim worked as a lobbyist for the US firm. South Korean media reported that the US firm's bidding price was much higher than its rivals, but that E System won the contract due to Ms Kim's contacts to top-level government and political officials. In February 1998, the Defense Ministry and the Board of Audits and Inspection started first investigations in the case. Prosecutors said they could not find any proof of bribery; however, recent findings (including love letters from the former Minister of Defense to Ms Kim) suggested that Ms Kim had several affairs with the former defense minister and other high-ranking officials in 1996 when the bidding took place. To date, the prosecution is unclear about whether sexual favors should be considered bribery (*Korea Herald* 4, 11, 15 May 2000).

2.5. The Alsthom Scandal (May 2000)

The second scandal involving foreign firms refers to a 22.2 trillion won (\$2.11 billion) project for a high-speed railway linking Seoul and Pusan, the biggest-ever national project in South Korea. In 1994, the French firm Alsthom won the contract over the German GEC. The Board of Audits found data showing that Alsthom won the contract in the sixth and final round of bidding, although GEC had been ahead of Alsthom until the fifth round. In May 2000, prosecutors arrested Ms Ho Ki-Chun, the Korean wife of Alsthom's Seoul branch manager on suspicions of accepting \$3.86 million from the French firm for lobbying. Prosecutors also announced to soon publicise a list of politicians and administration officials suspected of having had contacts with an L.A.-based lobbyist, Choi Man-Sok, who allegedly served as an unofficial lobbyist for Alsthom. Choi is well-known for having had wide-spread contacts in the government of Kim Young-Sam. In 1994, after Alsthom won the contract, he reportedly received \$11 million in commission. Alsthom's then official agent, former Miss Korea Kang Kwi-Hee, mentions in her 1998 autobiography that former President Kim Young-Sam denied the proposal for a 3% commission for the project. To date, prosecutors are undecided whether and how to continue their investigation. (*Korea Herald* 11 and 15 May 2000).

3. Conclusion

The scandals presented above illustrate a high incidence of corruption and especially of political bribery in South Korean politics. Although reform measures are on the way and are pushed forward by a public increasingly impatient with collusive relations between government and business in South Korea, reforms still have a long way to go until the aim of "clean politics" can be achieved. The recent disclosure of scandals involving foreign firms has to be seen as especially problematic. While the abuse of personal contacts and family or clan ties hitherto could be interpreted as a relic of traditional relationships in Korean politics, the use of these structures by foreign firms suggests not only the survival, but rather a revival of these structures, thus further complicating political reform and the fight against corruption in South Korea.

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- 1 Chun Doo-Hwan, for example, founded the Ilhae Foundation in 1984 to which the top 12 chaebol had to give.
 - 2 Chun Doo-Hwan, the predecessor of Roh Tae-Woo was also indicted, tried and sentenced to death for staging a military coup in December 1979 and for his part in putting down a student rebellion in 1980, the so-called Kwangju massacre, as well as for bribery charges. Chun had succeeded in allocating even higher funds than Roh - more than \$900 million. Chun's life was later spared by an appellate court and his sentence was changed to life imprisonment.