Kluwer Arbitration Blog

Blip on the Radar: An Anomalous Refusal to Enforce on Public Policy Grounds in Korea or a Sign of More to Come?

Hyewon Yoon, Seokwoo Jang (Yonsei Law School) · Thursday, June 2nd, 2022 · KCAB Next

Under Article V(2)(b) of the Convention on the Recognition and Enforcement of Foreign Arbitral Awards (1958) (the New York Convention, "**NYC**"), a court may refuse to recognize or enforce a foreign award if "recognition or enforcement of the award is contrary to the public policy of that country."

The NYC does not define the term "public policy" and instead permits each state to interpret the rule. Nonetheless, similar to many other jurisdictions (*see, e.g.*, here and here), the courts in the Republic of Korea have traditionally adopted a narrow interpretation of Article V(2)(b), establishing a high threshold for a given circumstance to be deemed contrary to public policy.

In November and December of 2018, the Supreme Court of Korea issued back-to-back decisions in which the public policy argument failed in the first but prevailed in the second. The latter case was notable because it was a rare publicly available Supreme Court judgment to (partially) deny enforcement of a foreign award on grounds of Article V(2)(b). Although these decisions were rendered a few years ago, they may have slipped "under the radar" to some extent. In light of the relative dearth of publicly available case law on public policy challenges in Korean courts, these ones are worth revisiting.

Overview of Korean Arbitration Act and "Public Policy"

Korea's Arbitration Act is based on the UNCITRAL Model Law. However, the Act does not adopt Chapter VIII of the Model Law concerning enforcement and recognition of foreign awards. Instead, Article 39 of the Act states that "recognition and enforcement of foreign arbitral awards subject to the NYC shall be governed by the NYC."

Consequently, there is no direct statutory guidance on what constitutes "public policy" in the Korean legal regime. There is a comparable legal term "good customs and other social order" ("**good customs**") that appears in Article 217(1)(3) of the Civil Procedure Act, Article 10 of the Act on Private International Law, and Article 103 of the Civil Act. The prevailing view is that "good customs" in the meaning of the Civil Procedure Act is most comparable to the "public policy," since Article 217 governs the enforcement of foreign court judgments.

The Norm: Rejection of the Public Policy Argument

In *2016Da18753*, decided in November 2018, the Supreme Court affirmed the decision of the Seoul High Court to grant enforcement of a foreign award despite its inconsistencies with domestic law.

The award in dispute was rendered by a tribunal seated in The Netherlands which ordered a South Korean company, Shinhan Apex, to transfer two of its patents to a Dutch company, Euro-Apex B.V.

Importantly, the tribunal ordered an "indirect compulsory performance" (*i.e.*, a monetary enforcement measure) if Shinhan Apex failed to transfer the patents. On its face, this was contrary to Korean law because indirect compulsory performance is not permitted for transfer of patents, according to the Civil Execution Act.

Nonetheless, the Supreme Court held that the award does not contravene Korea's public order to the extent that enforcement must be denied. It reasoned, *inter alia*, that indirect compulsory performance does not amount to a major restriction on the freedom of choice, because it merely applies psychological pressure to induce voluntary performance.

This pro-arbitration approach conforms with previous Supreme Court decisions. Starting from *93Da53054* and reiterated in several other cases, the Supreme Court repeatedly noted that "the fact that a foreign law applied to an award contravenes the mandatory provisions under the Korean law does not necessarily become grounds for non-recognition." Further, in *2001Da20134*, the Supreme Court held that the stability of the international trade order must be considered together with the domestic circumstances. This position, in effect, restricts the scope of the denial of enforcement.

The Exception: Acceptance of the Public Policy Argument but in Unusual Circumstances that Only Arose After the Award Was Rendered

However, in December 2018, the Supreme Court accepted the public policy argument in another case, *2016Da49931*. LSF-KDIC Investment Company Ltd. ("**LSF-KDIC**"), a company jointly established by Korea Resolution & Collection Co., Ltd. ("**KR&C**"), requested that KR&C be held liable for 50% of the additional expenses incurred as a result of the sale of real estate, which included corporate taxes of KRW 23.7 billion. An ICC tribunal sided with the LSF-KDIC, which then sought enforcement in Korean courts.

During the enforcement stage, LSF-KDIC prevailed in a separate lawsuit against the local tax authorities. The corporate taxes were slashed to just KRW 370 million. Based on this decision, KR&C argued that, in light of the public policy exception, the award should not be enforced because, under Article 44 of the Civil Execution Act, a debtor may file a "lawsuit of demurrer" to suspend or block the compulsory execution of a binding decision.

Although KR&C's public policy argument was unsuccessful in the lower courts, the Supreme Court sided with KR&C and remanded the case to the Seoul High Court.

The Supreme Court determined enforcement would constitute a contravention of "public order and good morals," given the following circumstances:

1. The tax was significantly reduced.
2. LSF-KDIC was already dissolved.
3. Awards are not subject to appeal, so such changes must be taken into consideration during the enforcement stage.

The Court noted that there were circumstances amounting to Article 451(1)(8) of the Civil Procedure Act – the alteration of an administrative disposition (*i.e.*, taxation) by a different judgment or administrative disposition – which is grounds for a retrial.

However, since retrial is not permitted in international arbitration, the Court reasoned that KR&C must be able to raise such an objection during the enforcement stage as a last resort. In this case, it was clearly contrary to the "good morals" of Korea for KR&C to accept the enforcement of the award.

One notable contrast with *2016Da18753* (*i.e.*, the case decided in November 2018) was that unlike in that case, where the Court found the level of contravention of Korea's public order and good customs to be minor, here, the Court found the magnitude of contravention to be highly significant. This seems to indicate that the Court takes into account the level of practical impact on the parties.

Subsequently, in *2018Na10878*, the Seoul High Court partially denied the enforcement of the award by deducting the exempted tax amount. It could be argued that denial of enforcement in this context is akin to correction of an arbitral award based on new circumstances that arose after the rendering of the award, and one might observe that the main reason why a court is forced to make the correction is that the tribunal has become *functus officio*.

At the same time, the High Court stressed the importance of maintaining a high threshold for the public policy argument:

1. Arbitration is a form of alternative dispute resolution based on the parties' consent.
2. Parties usually have equal standing in arbitration.
3. If domestic courts around the world attempt to prioritize local interests and deny enforcement of awards in the name of public policy, international trade will become unstable, and the arbitration will lose its effectiveness.
4. NYC encourages widespread recognition and enforcement of awards.

As such, the High Court reasoned that the "public policy" under NYC is an "international public order." Accordingly, denial of enforcement requires a violation of the fundamental principles of the domestic legal system which may not be allowed despite the international character of the dispute.

This case illustrates that even when public policy arguments are partially successful, Korean courts are cautious about denying enforcement of a foreign award.

Conclusion

Following the Supreme Court's reasoning in *2016Da49931*, there is a possibility that other grounds for retrial under Article 451(1) of the Civil Procedure Act may provide a basis for a demurrer, and consequently, denial of enforcement according to Korean "public policy."

The following grounds for a retrial under Article 451(1) appear particularly relevant in the context of a potential public policy challenge of a foreign award:

- "When a party has been led to make a confession, or obstructed in submitting the method of offence and defense to affect the judgment, due to the criminally punishable acts of another person" (Article 451(1)(5));
- "When a document or any other article used as evidence for the judgment has been forged or fraudulently altered" (Article 451(1)(6));
- "When the false statements by a witness, an expert witness or an interpreter, or those by a sworn party or legal representative have been adopted as evidence for the judgment" (Article 451(1)(7));
- "When a judgment is contrary to the final and conclusive judgment which has been previously declared" (Article 451(1)(10));

It is yet to be seen if the "public policy" argument will prevail under grounds for retrial other than Article 451(1)(8). Given the paucity of Supreme Court cases concerning "public policy," future judgments are necessary to settle this issue.

Nonetheless, those who seek to rely on the "public policy" argument will face an uphill battle. Korean courts maintain a pro-arbitration approach by presenting a narrow definition of "public policy," looking beyond the domestic legal system and heeding the international trade order.

This entry was posted on Thursday, June 2nd, 2022 at 8:57 am and is filed under Enforcement, Korea, New York Convention, Public Policy
You can follow any responses to this entry through the Comments (RSS) feed. You can leave a response, or trackback from your own site.