Journal of Korean Law | Vol. 19, 249-262, August 2020

Notable Supreme Court Cases: Civil Law

*Dongjin Lee**

*Edited by JKL student editors***

The Supreme Court of Korea delivered a series of important decisions on the law of assignment last year. In this issue's *Notable Supreme Court Cases: Civil Law*, we will introduce these decisions and provide brief comments on each.

1. Supreme Court *en banc* Decision 2016Da24284, Decided December 19, 2019 (Assignment of a claim against anti-assignment clause)

[Facts of the Case]

Subcontractor *A* made a contract to undertake part of the construction of a building with general contractor *B*. The contract between *A* and *B* stipulates that *A* shall not assign its right against *B* arising from the contract to any third party. Nonetheless, *A* assigned its right to payment to *C*.

Thereafter, *A* went bankrupt and the trustee of the estate sued *B* for the payment. *B*, the defendant, objected that the estate did not have the right for the payment because *A*, its predecessor, already had assigned it to *C*. The claimant-trustee rebutted that the assignment was invalid against the anti-assignment clause so that the right still resided with the claimant-

* Professor, Seoul National University School of Law, Korea

** This article was edited by JKL student editors Jiwon Kim, Jongwoo Yooh, Hye Yeon Yoon and Sangwon Yoon.

trustee.

[Main Issue]

Whether the assignor or its trustee can assert the invalidity of an assignment on the ground that it is against the anti-assignment clause.

[Holding]

[1] Court opinion

The court opinion of this decision was joined by five Supreme Court Justices. It confirms that the Supreme Court has adopted a view that an assignment against an anti-assignment clause is invalid and declares that it would adhere to this approach. *A*'s right to the payment was not effectively transferred to *C* and thus the claimant-trustee could sue for it. The main reasoning is as follows:

> "a) The first sentence of Article 449 (2) of the Civil Code prescribes that the obligor shall not assign when both parties represent their shared will forbidding assignment, which implies the nullification of its obligatory right against anti-assignment clause. […] Moreover, the second sentence of Article 449 (2) of the Civil Code presupposes that assignment against an anti-assignment clause is void. […]
>
> c) The *numerus clausus* principle dominates proprietary relationships, i.e., the classification and content of proprietary interests are fixed by the statutes on proprietary relationships (Article 185 of the Civil Code). Meanwhile, the principles of private autonomy and freedom of contract dominate obligatory relationships, so that contractual parties can freely form their contractual rights and obligations. Thus, an anti-assignment clause made between the obligor and obligee constitutes a part and attribution of the obligatory right itself, which should be respected. […]
>
> f) An approach to negate assignment against anti-assignment clause itself is a way to construct the most problematic relationship with bad faith assignee in a clear and simple manner. If an assignment against an anti-assignment clause were valid in itself and simply constituted the assignor's breach of promise not to assign, then the debtor could pay the assignor even though the debt had

> already been passed to the assignee and thus no longer resided with the assignor. […] Moreover, it is theoretically difficult to understand why an anti-assignment clause with only an obligatory effect could bind a third party acting in bad faith out of this obligatory relationship.
>
> […]

[2] Dissenting opinion

Four Justices – Justice SI Kwon, JH Kim, CS Ahn, and JH Roh –, however, dissented on the court opinion. They opine that even assignment against an anti-assignment clause has a translative effect and the anti-assignment clause just gives the debtor a defense to neglect the transfer, i.e. to refuse to pay the assignee. Thus, the assignor or trustee of the assignor's estate cannot invoke the effect of the anti-assignment clause. The reasoning of the dissenting opinion is as follows:

> "a) A contract has binding force on the contractual parties, the obligor and obligee.
>
> […] If we want to attribute *erga omnes* effect to anti-assignment clauses, there must be a clear legal ground. The vague text of Article 449 (2) does not constitute such a legal ground to deprive a debt of its transferability. […]
>
> b) Article 449 (2) of the Civil Code also supports this approach. It should be understood that an anti-assignment clause simply obliges the obligor not to assign. The understanding that "shall not assign" means a deprivation of transferability from the debt would be contradict to the plain meaning of the text.
>
> c) The Civil Code declares that a debt is transferable in principle (Article 449 (1), the first sentence) and acknowledges limitation thereof only in exceptional cases (Article 449 (2)). An anti-assignment clause can be respected to the extent which it does not infringe the freedom of assignment.
>
> Most of obligatory rights, notably monetary claims, are of little personal bondage character. A value of debt as an asset is much the same as that of other properties and the degree of personal bondage between the obligor and obligee decreases as social and economic

conditions change. […]

g) The case law on the burden of proof that the assignor neither knew nor had reason to know the existence or violation of the anti-assignment clause can be understood more easily from the perspective of the abovementioned approach. The Supreme Court has regarded the burden of proof of the abovementioned fact as imposed on the one who wants to oppose the effect of assignment, mainly the assignor, which is hard to understand from the perspective of the court opinion.

[…]

B) The problem is how to understand the second sentence of Article 449 (2) of the Civil Code. Here is the answer:

The debtor should have a right to refuse to pay the assignee according to the second sentence of Article 449 (2) of the Civil Code when the assignment violates the anti-assignment clause. The debtor also can acknowledge the effect of the assignment without rejecting payment to the assignee. The assignor who assigned against the anti-assignment clause, however, cannot object to the effect of assignment and regard the assignor as the rightsholder. […]

If the debtor rejects to pay the assignor on the ground that the debt is already assigned to the assignee and then reject to pay the assignee on the ground that the assignee is bad faith on the violation of the anti-assignment clause, there might be a deadlock situation. Thus, we should allow assignor's claim against the debtor when the debtor rejected to pay the assignee, and assignee's claim against the debtor when the debtor rejected to pay the assignor. Otherwise, the debtor's rejection would be against good faith and fair dealing.

[Comments]

From a comparative perspective, there are two different streams on how to rule the legal construction and effect of assignment against an anti-assignment clause: the so-called proprietary effect theory and obligatory effect theory. The basic idea of the proprietary effect theory is that the anti-assignment clause should be incorporated in and constitute the attribution of the debt itself with the effect of depriving the debt of transferability. Thus, the assignment itself is null and void, and anybody can invoke the

effect of the anti-assignment clause. The basic idea of the obligatory effect theory is that the anti-assignment clause does not constitute to the attribution of the debt and stands alone, independent of the debt. Thus, the debt is transferred to the assignee by assignment while the violation of the anti-assignment clause simply constitutes a breach of contract, which can be invoked by the promisee, i.e. the debtor. In the instant case, the issue is whether assignor, and not debtor, can invoke the violation of the anti-assignment clause, and it is on this point that court opinion and dissenting opinion have differing views. The court opinion adheres to the proprietary effect theory and concludes that even assignor can maintain that its own assignment is null and void, while the dissenting opinion maintains that the assignment itself is valid and has translative effect of debt to assignee, while the assignor itself, at least, cannot invoke the effect of the anti-assignment clause.

The most decisive difference between the two theories is the validity of assignment. Article 449 (2) of the Civil Code prescribes that a debt shall not be assigned when parties express their shared will against assignment; however, they cannot oppose any *bona fide* third party with this representation of will. As the court opinion indicates, on the one hand, the second sentence of Article 449 (2) of the Civil Code presupposes that assignment against an anti-assignment clause is considered not to have occurred at least vis-à-vis the debtor unless the assignor did not know and, according to the case law, it had also no reason to know, that the assignment was against the anti-assignment clause. Thus, it is impossible to grant the debtor damages claim as the sole remedy for breach of anti-assignment clause and not to negate the assignment itself under the Civil Code, even when the obligatory effect theory is adopted, and this holds true even for a *mala fide* (bad faith) assignee, which, as court opinion indicated, is difficult for the obligatory effect theory to justify. On the other hand, a *bona fide* assignor, whatever it means, can acquire the debt despite the breach of the anti-assignment clause, even when the proprietary effect theory is adopted. Thus, all of the arguments regarding the freedom of assignment and the necessity to guarantee transferability of debt, especially those presented by the dissenting opinion, are flawed. Most of the problems surrounding the validity of an assignment against an anti-assignment clause are resolved by the legislator itself under the Civil Code so that the two theories do not

produce different outcomes in this regard.

A purely ideological assumption that the obligatory effect theory values freedom of assignment more than the proprietary effect theory cannot be supported. The merit of a certain legal construction should be assessed only by the merit of the result it produces and the economy of its explanation. In this regard, the proprietary effect theory is preferable because it analyzes the legal relationship in a simpler and clearer way, which contributes to applying the theory to more complex issues contested. The obligatory effect theory is difficult both to apply and to predict the result when it comes to a complex case because it has no choice but to introduce a concept of obligation that has some effect to a third party other than the obligor and obligee, even though it binds only the original obligor and obligee of the anti-assignment clause, as the court opinion indicated. The text of Article 449 of the Civil Code and the legal theory on whether an anti-assignment clause can or must be incorporated to the debt itself do not show anything, as suggested by the fact that both court opinion and dissenting opinion maintain the plain meaning of Article 449 of the Civil Code and the legal theory on what should and can constitute a part of a debt support each's argument.

The remaining question is whether this means that even the assignor who agreed on, but later breached, its own anti-assignment clause can invoke the clause and maintain that the debt resides with itself despite having been assigned, on the grounds that the assignment goes against the anti-assignment clause. Theoretically or logically, this issue has nothing to do with choosing between the two conflicting theories. On the one hand, the obligatory effect theory confers the right to neglect assignment to the debtor and not to any third party outside of the personal relationship on the anti-assignment clause between the assignor and debtor. It does not exclude, however, the possibility of conferring the same right to the assignor, the other party of the agreement not to assign. Though we have good reason not to confer the right to the assignor who breached the agreement itself, we need not do so. It is still possible to allow even the assignor to invoke the anti-assignment clause. On the contrary, the proprietary effect theory does not exclude the possibility of barring the assignor's defense that the assignment that it itself made is invalid against the anti-assignment clause, because this defense can be seen as contrary to good faith and fair dealing (Article 2 (2) of the Civil Code). Again, this issue

does not rely on the theoretical or doctrinal construction of the effect of an anti-assignment clause. It is regrettable that the Supreme Court focused on the theoretical or doctrinal construction of the effect of anti-assignment clauses and did not mention the theoretical and practical needs and justification to either allow or deny the assignor's defense based on the anti-assignment clause.

2. Supreme Court Decision 2016Da8589, Decided May 16, 2019 (Assignment before notification and acceptance)

[Facts of the Case]

Contractor *A* assigned *B* its contractual right against client *C* in December 2006. Nonetheless, *A* garnished *C*'s beneficiary interests against trustee *D* based on its alleged right against *C*. *D* deposited the amount due with Seoul Central District Court for whoever had the beneficiary interests.

A argued that it held the right against *C*, and, relying on this assertion, the court drew up the payment table allocating the deposited amount to the interested. *C*'s another creditor *E* objected to the table and filed a lawsuit to modify the table in favor of *E* (Articles 151 through 154 of the Civil Execution Act).

Meanwhile, *C* acknowledged and accepted the assignment from *A* to *B*, which made manifest that *A* had already assigned its right before the court drew up the payment table.

Thus, *E* argued that since *A* was not a creditor when it applied to the court to allocate (part of) the deposited amount to itself and since *B*, the creditor, did not apply for allocation at all, neither could claim any part of the deposited amount. *B* participated in the lawsuit as the assignee of *A* and applied to represent *A* in the lawsuit (Article 81 of the Civil Procedure Act).

[Main issue]

Whether the assignor can arrest, garnish, or even apply to allocate deposited or collected money for assigned debt, without or before the notification or acceptance of assignment.

[Holding]

> "a) Until the requirement for opposability of assignment is met, the assignor remains to be the obligor vis-à-vis the debtor, and the assignor is thus able to take preliminary measures to secure future judgment execution including garnishment, which makes the allocation and payment to assignor based on this garnishment lawful. […]
>
> c) Considering the abovementioned ruling, assignee *B* cannot exercise its right unless the requirement for opposability is met, not to mention the need to apply for allocation of the deposited money in the judgment execution process. When a lawsuit to modify the payment table is filed after the assignment but before the requirement of opposability of assignment is met, as is in the instant case, the assignee can participate in the lawsuit and exercise its right to claim allocation of deposited or collected money after and only after the requirement for opposability is met. Thus, *B*'s application to represent *A* in the lawsuit is lawful. […]"

[Comments]

Article 450 (1) of the Civil Code prescribes that assignment is not opposable against the debtor and any other third party unless it is notified to or accepted by the debtor. The Civil Code adopts the opposability principle following its predecessor, the Japanese Civil Code, which is rooted in the French Civil Code of 1804.

The legal position of the assignor and assignee before the requirement of opposability, i.e. notification or acceptance, is met is one of the most controversial and difficult questions arising in the law of assignment with respect to the opposability principle. The Supreme Court has had opportunities to make rulings on the legal position of the assignee before the assignment is notified or accepted, and the basic line of case law development is to confer some power to the assignee even before the assignment is notified or accepted so that the assignee may take preliminary measures to secure its right. For example, the Supreme Court ruled that assignee's filing before the lapse of extinctive prescription period suspends the running of the period; that assignee's foreclosure of a

mortgage is valid if the debtor did not make objections that the assignment was neither notified nor accepted within the prescribed period. Although controversial, this line of case law is understood to purport to reinforce the status of the assignee before the requirement of opposability is met in order to mitigate the inconveniences of the opposability principle, and have been generally agreed as such.

Few expected, however, that the Supreme Court would also enable the assignor to exercise its right even though it had already assigned its right to the assignee and thus its exercise of assigned right might constitute a breach of promise or tort of conversion against the assignee. The Supreme Court, in fact, allowed this claim already in a decision delivered on February 12, 2009 (docket number 2008Du20199) on the grounds that "the assignor before notification or acceptance of assignment remains to be the obligor vis-à-vis the debtor." A decade later, the abovementioned ruling was quoted by the decision at hand, by which it became an established precedent.

What is more problematic is that the issue in the 2009 decision was the validity of preliminary measures made by the assignor, which is rather easily agreeable at any rate, while the issue in the instant case was the validity of allocation of deposited or collected money and, in the end, payment thereof to the assignor. If the debtor pays the assignor, the assignee can sue the assignor for restitution of the payment or damages from the tort of conversion.

These rulings are incompatible with each other. It is impossible that both assignor and assignee exercise the same right against the debtor even before the assignment is notified or accepted, and there is no reason to acknowledge the assignor's claim against the debtor even though the assignor does not have any right vis-à-vis the assignee. The requirement for opposability is there to protect the debtor and not the assignor who no longer has any justified interest in the debt. This kind of *ad hoc* approach may have resolved the instant case properly, but would undermine the fundamental stability of the legal relationship of assignment and confound the relationship amongst all interested parties including the assignor, assignee, debtor, and creditors of one of abovementioned. In fact, the decision at hand sacrificed the interest of *C*'s another creditor *E*, which appears to be hard to justify.

This problem also reflects the fundamental deficiency of the

opposability principle. Even in the Korean legal system, there are a few legislations that modify the opposability principle in this way, especially in the area of the securitization of debt. From a legislative perspective, it is necessary to generalize these special legislations and move from the opposability principle to the consent principle as the revised French Civil Code did. For the time being, however, a fundamental revision of the Civil Code is hard to expect. Another instant fix would be to overrule the abovementioned precedent as to deny the assignor's interference in the legal relationship of an already assigned right.

3. Supreme Court Decision 2017Da222962, Decided June 27, 2019 (Acceptance without reservation)

[Fact of the Case]

Bank *A* extended credit to *B*, a physician. *B* assigned his future reimbursement claim against the National Health Insurance (hereinafter NHI) to *A* as collateral for his debt.

B notified the assignment to the NHI, and the NHI faxed a letter to *B* confirming that it received notification that *B*'s reimbursement claim was assigned to *A*, which was in fact sent to *A*, perhaps according to *B*'s request. The letter included a warning stipulating that: all of the enclosed information should be kept confidential pursuant to the Personal Information Protection Act; the letter could not be submitted for the purpose other than the designated one, i.e. the confirmation of the said assignment; and there may exist some omissions on the details of the assignment, such as garnishment and the like.

On *B*'s default, *A* sued for the payment of the assigned reimbursement claim against the NHI. Reviewing *A*'s claim, the NHI found that *B* had a criminal record concerning payment fraud against the NHI, which meant that the NHI had a counterclaim against *B* (a sort of tortious liability). The NHI maintained that it could set-off its counterclaim against the assignor *B*, with the claim of the assignee *A* against itself. *A* argued that this set-off defense had been barred by the NHI's letter to *A* (with *B* as the addressee), which constitutes an acceptance of the assignment without any reservation by the NHI, the debtor.

[Main issue]

Whether the the NHI's letter can be seen as an acceptance of assignment without reservation to bar the set-off defense.

[Holding]

> "The first sentence of Article 451 (1) of the Civil Code prescribes that a debtor cannot oppose the assignee with its defense vis-à-vis the assignor when it made an acceptance of assignment according to Article 450 without any reservation. […]
>
> When a debtor accepts assignment according to this provision without reservation, neither express intent to renounce defenses nor intent that it does not have any objection to the assignment is necessary. Acceptance without reservation deprives the debtor of defenses vis-à-vis the assignor, however, hence it is required that the alleged acceptance induce the assignee's reliance on the non-existence of defenses. In order to decide whether the alleged acceptance has this effect, one should take into account factors such as what the alleged acceptance is, the intent and method with which the debtor performed the alleged acceptance, what purpose the debtor pursued, and how it behaved around the alleged acceptance.
>
> B) In view of the abovementioned ruling and the details of the case before the court, we do not agree with the second instance court because:
>
> a) The title of the confirmation letter is 'Assigned Reimbursement Claim Confirmation Letter,' which suggests the main purpose of the letter is to provide the dependent information on the details of notified assignment or garnishment. The purpose of this letter is restricted and any use of this letter for the purpose other than designated one is strictly forbidden.
>
> b) This assignment is a universal assignment of all the future reimbursement claims against NHI up to the 21 billion won (roughly corresponds to US $ 170 million) and it was uncertain then when and how much it would accrue. It is hard to say that the debtor renounces all the defenses in this situation when it accepted this assignment.

c) The defendant had reimbursed *B* more than 3.3 billion Korean won from January 23, 2014 to March 16, 2015, and appear to have recognized that *B* committed fraud against the NHI and was criminally punished after April 2015 during the procedure of another lawsuit. The defendant ceased to reimburse *B* immediately. If the defendant had known *B*'s fraud against the NHI from November 1, 2007 to 2008 on the assignment, it would have ceased reimbursement or set-off then. […]

d) When the defendant did not appear to have known that it had a counterclaim and thus could have set-off, it is hard to expect to reserve its specific defense vis-à-vis *B*. In the confirmation letter, there is a warning that any use of the letter for the purpose other than confirming the fact of assignment or garnishment is strictly forbidden and that the NHI would not take any responsibility based on the letter. This warning might be understood as a comprehensive exclusion of defense-barring effect of acceptance without reservation.

All the above-mentioned factors taken into account, it is hard to say the defendant made acceptance of the assignment without reservation in this case."

[Comment]

Article 451 (2) of the Civil Code prescribes that the debtor can invoke its defense vis-à-vis the assignor when the assignee exercises the assigned right, if the defense has already existed before the notification. Though there are some nuances in interpreting and applying this provision, the basic idea behind this provision is that the debtor preserves its defenses irrespective of assignment, which is a corollary to the freedom of assignment.

The first sentence of Article 451 (1) of the Civil Code, however, restricts this principle in the case of the so-called acceptation without reservation. This provision prescribes that the debtor cannot oppose the assignee with defenses vis-à-vis the assignor when the debtor accepted the assignment without any reservation "according to the previous provision," which is the provision to declare the opposability principle. The second sentence of Article 451 (1) of the Civil Code provides that, in that case where the first sentence is applied, i.e. where the debtor should be responsible to the assignor despite of the defense vis-à-vis the assignor, the debtor can sue for

restitution when the debtor paid or delivered something to the assignor, or can negate the obligation when the debtor is obliged in order to satisfy the assigned debt. Thus, Article 451 (1) or acceptance without reservation has been understood as having a defense-barring effect in the law of assignment.

The problem is that the extent of the defense-barring effect is apparently overbroad. The provision suggests that "acceptance" in Article 451 (1) of the Civil Code is the same "acceptance" as that in Article 450 of the Civil Code. Acceptance in Article 450 of the Civil Code, as a requirement for opposability of assignment against the debtor and any other third party, does not ask whether the debtor intended to acknowledge the assignment. It is just a manifestation that the debtor knows that the debt is assigned to the assignee, which makes notification unnecessary. As the abovementioned decision's ruling makes clear, the connotation of "without reservation" does not require any prior action on the side of the debtor. Rather, it requires an omission thereof. In addition, the Civil Code does not expressively limit the sort and scope of defenses barred by Article 451 (1). All things considered, the Civil Code appears to bar all the defenses of the debtor just for saying, "I know the debt was assigned," rather than that it was notified that the debt was assigned.

The legal literature noticed this problem and developed a theory that Article 451 (1) of the Civil Code purported the protection of the assignee's reliance, hence that it should apply only when the assignee did not know and had no reason to know the existence of the assignment (the so-called reliance theory). The case law followed this line.

More limitations and refinements are necessary, though. In some cases, bad faith assignees do not deserve to be protected by Article 451 (1) of the Civil Code. In others, however, even bad faith assignees deserve to enjoy the protection of Article 451 (1) of the Civil Code, especially when the debtor renounces its defense consciously and deliberately. More importantly, even in cases where the assignee acquired the debt in good faith, there may be circumstances where barring all defenses is too harsh for the debtor considering that it simply said "I know the debt was assigned." This is far from giving reliance on the non-existence of defenses vis-à-vis the assignor. In the instant case, for example, the assignee Bank *A* did not appear to have been aware of the NHI's counterclaim against the assignor, physician *B*.

The abovementioned decision introduces another limitation on the

defense-barring effect of Article 451 (1) of the Civil Code. The reasoning is somewhat confusing, though. On the one hand, the decision appears to problematize the wording of the acceptance. If the acceptance did not reserve any defenses but warned not to put any reliance other than assignment, it might not have had a defense-barring effect. On the other hand, the decision appears to problematize that the debtor accepted the assignment without knowing that it had grounds for defense against the assignor. Either way will do and perhaps combining both approaches would be preferable as both approaches catch different factors – the accepting debtor's intent to renounce defenses and whether it deserves further protection. From the legislative perspective, Article 451 (1) of the Civil Code should be decoupled from the acceptance in Article 450 of the Civil Code and needs to be refined.