Freedom of Contract vs. Legal Paternalism in Korean Public Procurement Contracts

*Joseph Cho**

In the Republic of Korea (RoK), public procurement contracts (PPCs) are agreements between a government entity and a private entity for the supply of goods, services or works that are necessary for the performance of the government division's proper functioning.[1] PPCs are different from private contracts in that they involve the use of public funds and have a broader impact on the economy and society at large.[2] In comparison, the private party contracting with the government may not bear

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* The author is a doctoral candidate at the Seoul National University School of Law and a dual qualified government contract lawyer (qualified in New York and in England). The author extends heartfelt gratitude to the editorial team at the *Asia Pacific Law & Policy Journal* for their diligent work and meticulous editing. Additionally, the author wishes to express sincere thanks to his mother, wife, and son Joey for their unwavering love and support. All errors remain the author's.

[1] Under Article 2 of the Government Contract Act (Government Contract Act), the Government Contract Act applies to contracts in which the government of the Republic of Korea is a party, including those related to government procurement that are awarded through international tendering procedures, as well as contracts entered into between the State and Korean nationals. Guggaleul dangsajalo haneun gyeyag-e gwanhan beoblyul [Act on Contracts to which the State is a Party], Article 2 (S. Kor.). Public procurement in the RoK can be broadly divided into defence procurement and general procurement, and general procurement is again divided into national procurement and local procurement. National defence procurement is based on the Defence Acquisition Program Act, while general procurement is based on the Government Contract Act and the Local Government Contract Act. Bang-wisa-eobbeob [Defense Acquisition Program Act], Article 32 (S. Kor.). Jibangjachidancheleul dangsajalo haneun gyeyage gwanhan beoblyul [Act on Contracts to which a Local Government is a Party] (S. Kor.). When the national government is the contracting party, the Government Contract Act is applied, and when the local government is the contracting party the Local Government Contract Act applies.

[2] *See* Cho Sung-Je, *A Study on the Improvement Methods for Suspension of Execution based on the Sanctions of Inappropriate Business Entity - Focusing on the Non-Suspension of Execution Principle Discussion*, 18 PUBLIC L. J. 339, 341 (2017).

the risk of payment.[3] This means the other party has an advantage when contracting that often results in unfair or unbalanced terms. Accordingly, stricter laws and regulations are required in the PPC context to ensure the fairness of the contract and to ensure compliance, including the prevention of corruption, fraud, and abuse of power by contracting officials.[4] PPCs can be an important tool for the government to achieve its policy goals and shape economic and social outcomes. By awarding contracts to the most qualified concerns and individuals, the government can steer resources and investment towards areas of priority. Directing public resources incentivizes certain behaviors and outcomes, while also promoting competition and innovation in various commercial spheres.[5]

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[3] As envisaged under art. 15 of the Government Contract Act, in a PPC, the State bears the financial burden, while payment is made through an advance and subsequent payments in consideration of the deliverables or service provided by the contracting party. Guggaleul dangsajalo haneun gyeyag-e gwanhan beoblyul [Act on Contracts to which the State is a Party], art. 15 (S. Kor.). The government is responsible for making such payments within a designated period specified by the Enforcement Decree after the contracting party has fulfilled their obligations, as determined by either inspection conducted by the head of a central government agency or contracting officer or based on an inspection report. Guggaleul dangsajalo haneun gyeyag-e beobyul sihaengryung [Guggagyeyagbeob sihaengryung] [Enforcement Decree of the Act on Contracts to which the State is a Party] art. 58 (S. Kor.). See also Daebeobwon [S. Ct.], Oct. 12, 2018, 2015Da256794 (S. Kor.) (holding that the above Government Contract Act provision is a mandatory provision applicable to all PPCs). The government is obligated to make each payment within the timeframe set by the presidential decree from the date of receipt of the demand for payment from the contracting party. In case of late payment, interest will accrue for the period of delay until the actual payment, as determined by the presidential decree. Guggaleul dangsajalo haneun gyeyag-e beobyul sihaengryung [Guggagyeyagbeob sihaengryung] [Enforcement Decree of the Act on Contracts to which the State is a Party] art. 59 (S. Kor.).

[4] PPCs aspire to transparency and fairness that aligns with the public's best interests. Despite such aspirations, illegal lobbying, collusion, and other corrupt practices are routinely observed during the bidding, award, contracting, and performance phases of PPC. JUNG WON, ONJU GUGGALEULDANGSAJALOHANEUNGYEYAG-E GWANHANBEOBLYUL JE5JOUI2 [ONJU GOVERNMENT CONTRACT ACT ART.5-2] 2 (2023) (S. Kor.). With a view toward pre-empting the problem of corruption, the Government Contract Act envisages an integrity pledge system under which the head of each central government agency or contracting officer shall conclude an oath of integrity with each bidder or counterparty that includes a clause stating that the bidder or contracting party shall not offer or receive money, gifts, or other benefits, directly or indirectly, during the bidding, capturing, contract signing, or execution of a given PPC to which the state is a party, with a view to boosting transparency and fairness in PPC. Guggaleul dangsajalo haneun gyeyag-e gwanhan beoblyul [Act on Contracts to which the State is a Party], art. 5 para. 2 (S. Kor.). If such an oath/clause is breached, the bidding or contract in question will be cancelled or terminated. *Id.*

[5] In OECD countries including the RoK, public procurement represents a significant portion of taxpayer funds, making up about 12% of the GDP and 29% of total government spending. *See* Professor Munseob Lee, Government Purchases and Firm Growth: Evidence from South Korea's Public Procurement Market, Seminar at the Stanford

According to the established jurisprudence of the RoK, a PPC made by the government is a private agreement, largely governed by the principles of private law, including the law of contract, rather than an agreement that is regulated by government intervention (Thesis).[6] This judicial interpretation and dogmatic stance denote that the government is subject to the same legal framework that applies to private parties when entering contracts, versus having special governmental rules.[7] Such doctrinal framework also recognizes that the government, like any other contracting party, has the freedom to negotiate the terms of the contract and to determine the rights and obligations of the parties under a PPC.[8]

This article aims to evaluate and critically analyze the thesis that PPCs in certain phases operate as private agreements under the South Korean legal framework. To achieve this objective, this article is structured into six parts. Part I examines the principle of freedom of contract in South Korean law. Part II provides an overview of regulatory measures and legal paternalism in the RoK. Part III explores the legal nature of PPC, and Part IV delves into contract interpretation under Korean law. This article then addresses two specific aspects of Korean government contracts: adjustment of contract price in Part V, and liquidated damages in Part VI. In both sections, a comparison between the RoK's laws and jurisprudence with their United States counterparts is drawn.

Through an examination of relevant judicial decisions and legal literature, this article demonstrates that PPC contracts in the RoK are fundamentally private agreements governed by principles of private and contract law. Concurrently, it will be noted that these contracts are subject to mandatory provisions within the framework of government contract law that protect important government agreements. This article argues that RoK PPC contracts are fundamentally private. However, it is crucial to note that these contracts are subject to mandatory legal rules and regulations. This highlights the complex interplay of PPCs within South Korea's legal framework.

University Freeman Spogli Institute for International Studies (May 18, 2018), https://fsi.stanford.edu/events/government-purchases-and-firm-growth-evidence-south-koreas-public-procurement-market.

[6] *See* a pedigree of precedents in this regard including Daebeobwon [S. Ct.], Sept. 20, 2012, 2012Ma1097 (S. Kor.).

[7] *Id*.

[8] *See* Article 5 of the Government Contract Act. Guggaleul dangsajalo haneun gyeyag-e gwanhan beoblyul [Act on Contracts to which the State is a Party], Article 5 (S. Kor.). Under this provision, a PPC is entered into when parties come to a mutual agreement on equal terms, and each party to the PPC is expected to fulfil their contractual obligations in good faith.

I. THEORETICAL FRAMEWORK

A. *Freedom of Contract in Korean Law*

According to RoK legal scholars, party autonomy is a cardinal working principle of the RoK civil law system.[9] Party autonomy refers to the concept that individuals are free to make their own agreements and is supported by three main principles: freedom of contract, freedom of ownership, and fault-based liability.[10] These three fundamental principles of civil law are based on an ideological foundation that values individual freedom in a far reaching and comprehensive manner.[11]

The principles of private autonomy and freedom of contract are most relevant when both parties enter a contract as equals and during the rational

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[9] *See* JEE WON LIM, MINBEOBGANGUI [CIVIL LAW LECTURE] 19 (18th ed. 2020) (S. Kor.) [hereinafter "JEE1"]; and YANG CHANG-SOO, MINBEOB IBMUN [INTRODUCTION TO CIVIL LAW] 437 (2020) (S. Kor.) [hereinafter "Yang"] (noting the foundation of the civil law in Korea is the principle of freedom of contract, which is rooted in the belief in human dignity).

[10] *See* JEE WON LIM, MINBEOB PANRYE [CIVIL LAW CASES] 5 (2021) (S. Kor.) [hereinafter "JEE2"]. *See also* YANG CHANG-SOO & KWON YOUNG-JOON, MINBEOB II [CIVIL LAW II] 630 (2021) (S. Kor.) [hereinafter "Yang & Kwon"]. In terms of fault-based liability, the Korean Civil Code's article 750 outlines the principle of personal fault as the general basis of fault-based liability. Minbeob [Civil Act] art. 750 (S. Kor.). This means that individuals are responsible for compensation if they cause harm or loss to another person through unlawful acts, whether willfully or negligently. In most situations, therefore, individuals are not liable for acts that occur without fault or for actions committed by another person. *See* EUN-JOO SHIN & ERIC ENLOW, TORTS, IN KOREAN BUSINESS LAW 296 (Jasper Kim ed., 2010). *See also* JEE1, *supra* note 9, at 20. Under art. 750 of the Korean Civil Code, the term wilfull(y) refers to a psychological state of intentionally engaging in an action while knowing that a certain outcome will occur (Daebeobwon [S. Ct.], July 12, 2002, 2001Da46440 (S. Kor.)), while the term negligent(ly) means one's failure to recognize that a certain outcome may occur as a result of neglecting the duty of care required in social life. The duty of care in this context is objectively and abstractly determined based on the average person in society, which refers not to an abstract person, but rather to an ordinary person in specific cases at a given time. Daebeobwon [S. Ct.], Jan. 19, 2001, 2000Da12532 (S. Kor.). In addition, under art. 390 of the Korean Civil Code, if a debtor fails to perform their obligation as required, the creditor may claim damages. However, this does not apply in cases where the debtor's performance has become impossible due to reasons beyond their control, such as force majeure or other circumstances not caused by the debtor's negligence or intentional fault. Minbeob [Civil Act] art. 390 (S. Kor.). In terms of what constitutes a force majeure event, the relevant Supreme Court precedent held that (i) the cause of such event must be beyond the party's control and (ii) despite the affected party's reasonable efforts, that party was unable to foresee or prevent such event. Daebeobwon [S. Ct.], July 10, 2008, 2008Da15940 (S. Kor.). Accordingly, the highest court held that the Asian financial crisis and the resulting setbacks in the supply of materials could not be deemed a force majeure event. Daebeobwon [S. Ct.], Sept. 4, 2002, 2001Da1386 (S. Kor.).

[11] KWON YOUNG-JOON, MINBEOBHAG-UI GIBON-WONLI [BASIC PRINCIPLES OF CIVIL LAW] 89 (2021) (S. Kor.) [hereinafter "KWON I"].

decision-making process that precedes it.[12] The principle of contract freedom allows the parties to have the freedom to decide the contents of the agreement without external intervention from the state or other parties.[13] Before signing, the parties typically negotiate and agree on the main terms of the agreement.[14] The terms agreed upon by the parties are legally binding under the principle of private autonomy so long as there are no special circumstances, such as the absence of requirements for a valid contract.[15] Consequently, when both parties agree on the contents of the underlying contract, it is generally understood that they are bound by it.[16]

In a free democratic state such as the RoK, the principle of freedom of contract is thus seen as a fundamental aspect of civil law.[17] It allows individuals to freely enter into legal agreements with others based on their own choices, without significant government interference. This principle also reflects the principles of a free-market economy, which values private property and economic freedom.[18]

Under a legal system recognizing freedom of contract, legal agreements are formed based on the intent of the parties involved and the

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[12] *See* Daebeobwon [S. Ct.], May 17, 2018, 2016Da35833 (S. Kor.). The principle of private autonomy, which has taken the form of the principle of freedom of contract in the domain of legal acts, refers to the freedom of the parties to determine the conclusion of a contract, the counterparty of the contract, and the manner and content of the contract in accordance with their own will. *See also* Lee Dong-Hyong, *A Study on Natural and Normative Interpretation of Legal Acts*, 132 JUSTICE 5, 6, (2012).

[13] *See* JEE1, *supra* note 9, 19.

[14] For a comparative analysis on the process leading up to the conclusion of a contract in the RoK and other jurisdictions including the United States, *see generally* Kim Dong-Hoon, *Legal Issues Before Conclusion of Contract*, 36 KOREAN. J. CIV. L. 323-349 (2007).

[15] Seo Hee-Seok, *Regulation on Standard Terms and Conditions and Contract Law*, 41 HUFS L.R. 41, 46 (2017).

[16] *Id.* at 43.

[17] According to Freedom House's Freedom in the World 2022 report on South Korea, the country is rated as "free" with a score of 88 out of 100. *See Freedom in the World 2022: South Korea*, FREEDOM HOUSE, (last visited Mar. 28, 2023), https://freedomhouse.org/country/south-korea/freedom-world/2022#CL; South Korea's political rights and civil liberties are generally respected and protected, and the country has a vibrant and competitive democratic system with regular free and fair elections. *Id.* The political system of the country is founded on a presidential model that ensures a clear separation of powers among the three branches of government, namely the executive, legislative, and judicial. *Id.* For judicial precedent in this regard, *see* Daebeobwon [S. Ct.], May 17, 2018, 2016Da35833 (S. Kor.).

[18] *See* JEE1, *supra* note 9, at 20. *See also* Lee Byung-Jun, *Subject of Content Control under the Terms and Conditions Regulation Act and its Restrictions*, 95 ADVANCED COM. L.R. 63, 70 (2021).

resulting legal effect corresponding to that intent.[19] The principle of freedom of contract allows for a wide range of rights and protections within contract law, such as the freedom to choose one's contracting partner, the means of forming the contract, and the terms of the contract.[20] This principle is consistent with the idea of self-determination, which upholds the right of individuals to make their own choices without being subject to the control of the state or any other group.[21]

B. *Jurisprudence*

The principles of private autonomy and freedom of contract also includes the freedom to not into binding agreements. Like its Korean Constitutional Court counterpart, the Korean Supreme Court generally recognizes and respects the principle of freedom of contract.[22] For example,

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[19] KWAK YOON JIK & KIM JAE HYUNG, MINBEOBCHONGCHIG [THE GENERAL PART OF CIVIL LAW] 252 (2013) (S. Kor.) [hereinafter "KWAK & KIM"].

[20] Lee Byung-Jun, *supra* note 18, at 70. *See* JEE1, *supra* note 9, at 19.

[21] The flip side of self-determination is arguably the principle of self-responsibility. According to the Court, the principle of self-responsibility is a cornerstone of individual legal relationships. This principle posits that individuals act based on their free choice and decision, and bear the consequences of their actions without attributing them to others. In the context of a contractual relationship in particular, the parties involved must assume responsibility for the benefits or losses that result from their free choice and decision. *See* Daebeobwon [S. Ct.], Aug. 21, 2014, 2010Da92438 (S. Kor.). The plaintiff in this case had lost approximately KRW 231 billion at the Kangwon Land casino facilities, and filed a lawsuit against the casino for damages, claiming that the defendant's employees had violated the entry restriction and betting limit regulations. The majority opinion of the Supreme Court held that the principle of self-responsibility generally applies to the legal relationship between a casino operator and a user, but in exceptional cases, the operator may be held liable for damages due to a violation of the duty of care towards users. *Id.* In this case, the Court rejected the plaintiff's claims as there was no violation of the entry restriction regulations, and the betting limit regulations did not envisage user protection as their intended purpose. *Id.* For a commentary on this en banc Court decision, *see* Lee Hyun-Kyung, *Self-responsibility and Duty to Protect of Casino Operator - Autonomy and Paternalism*, 38 J. PRIV. CASE L. STUD. 105-148 (2015).

[22] The Constitutional Court of Korea formally opened and began receiving cases in 1988, following the enactment of the basic law by the National Assembly, which established its powers and organization. *See* CHAIHARK HAHM, CONSTITUTIONAL COURT OF KOREA IN CONSTITUTIONAL COURTS IN ASIA: A COMPARATIVE PERSPECTIVE 141 (Chen, Albert H.Y. & Harding, Andrew, eds., 2018). The main responsibility of the Constitutional Court of Korea is to adjudicate on the constitutionality of laws, in addition to other functions, as provided in Article 111(1) of the Constitution of Korea. DAEHANMINKUK HUNBEOB [HUNBEOB] [CONSTITUTION] art.111 para.1 (S. Kor.). According to Article 107(1) of the Constitution, in the event that the constitutionality of a law is contested during a trial, the court is required to seek a ruling from the Constitutional Court and must adjudicate the case in accordance with the decision issued by the Constitutional Court. DAEHANMINKUK HUNBEOB [HUNBEOB] [CONSTITUTION] art.107 para.1 (S. Kor.). The Constitutional Court Act also provides for the organization and operation of the Constitutional Court. See Hunbeobjaepansobeob [Constitutional Court Act] (S. Kor.).

in *2016Da35833*, the Court held that the freedom of contract falls under the umbrella of private autonomy, and that this right grants parties the liberty to decide whether to enter into a contract, who their counterpart should be, and the terms of the contract.[23] This principle is grounded in the belief that a market economy operates most effectively by enabling market participants to seek out the most advantageous terms through competition, make modifications to their own conditions, and arrive at mutually agreeable terms for the contract.[24] As a result of such a judicial stance, limitations on contractual liability based on general principles of civil law, like good faith and trust, are not allowed except in very specific circumstances.[25] There are

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Art.111 (2) of the Constitution stipulates that the Constitutional Court shall consist of nine justices, including a Chief Justice, who are appointed by the President of Korea with the consent of the National Assembly. DAEHANMINKUK HUNBEOB [HUNBEOB] [CONSTITUTION] art.111 para.2 (S. Kor.); Hunbeobjaepanso [Const. Ct.], Oct. 29, 1998, 97HunMa345 (S. Kor.); Article 10 of the Korean Constitution provides that "all citizens shall have the right to pursue happiness." *See* DAEHANMINKUK HUNBEOB [HUNBEOB] [CONSTITUTION] art.10 (S. Kor.). In an en banc decision, the Korean Supreme Court observed that this constitutionally entrenched right to pursue happiness includes the freedom of general action, from which the principle of private autonomy is derived. *See* Daebeobwon [S. Ct.], May 17, 2018, 2016Da35833 (S. Kor.); Daebeobwon [S. Ct.], May 17, 2018, 2016Da35833 (S. Kor.).

[23] Daebeobwon [S. Ct.], May 17, 2018, 2016Da35833 (S. Kor.).

[24] *Id.*

[25] For example, in a 2004 decision, the Court stated that a creditor's exercise of rights can only be denied in exceptional cases where it would violate the principle of good faith and trust, and such denial should be a rare occurrence because it could endanger and threaten the principle of party autonomy and legal certainty. Daebeobwon [S. Ct.], Jan. 27, 2004, 2003Da45410 (S. Kor.). Meanwhile in multiple cases, the Court noted that there may be limited circumstances where circumventing a guarantor's obligation for debts that result from ongoing transactions between a creditor and debtor may be permitted when enforcing the guarantor's obligation would go against the principle of continuity, which is a legal principle that emphasizes the need for stability and consistency in contractual relations. *See* Daebeobwon [S. Ct.], July 12, 2013, 2011Da66252 (S. Kor.); Daebeobwon [S. Ct.], Jan. 27, 2004, 2003Da454104 (S. Kor.); and Daebeobwon [S. Ct.], Jan. 25, 2007, 2006Da25257 (S. Kor.). Furthermore, the Court observed that in the absence of exceptional circumstances, the intent of the parties in a contract should be recognized based on the written terms. If interpreting the text in a different way would change the parties' legal relations, the court should proceed cautiously and interpret the text narrowly. When interpreting the text of a contract, the court should follow a "plain meaning" approach and base its interpretation on the language used by the parties. However, if interpreting the text in a certain way would result in a significant change to the parties' legal relations, the court should proceed with caution and interpret the text narrowly to avoid unexpected consequences for the parties. *See* Daebeobwon [S. Ct.], Nov. 11, 2010, 2010Da26769 (S. Kor.); and Daebeobwon [S. Ct.], Dec. 8, 2011, 2011Da78958 (S. Kor.). Additionally, in the context of a legal retainer, the Court noted in an en banc decision that in cases where there is a written agreement between a lawyer and a client regarding the subject of fees and costs for handling a lawsuit, the lawyer who has completed the delegated work is generally entitled to claim the entire agreed-upon amount. However, in exceptional circumstances, the agreed-upon

less restrictions because they may significantly undermine the principle of party autonomy and legal certainty.[26] Accordingly, the court has shown strong reluctance to interfere with party autonomy based on principles of civil law, using phrases such as "very cautiously," "most exceptionally," and "grave threat" to indicate its high level of passivity in this area.[27]

C. *Analysis*

As referenced earlier, party autonomy in the RoK is a central tenet of the civil law system and is rooted in three main principles: freedom of contract, freedom of ownership, and fault-based liability.[28] These principles collectively uphold individual freedom and facilitate a free-market economy.[29] Freedom of contract allows parties to decide the terms of an

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remuneration may be deemed unreasonably excessive and contrary to the principles of good faith and trust. In such cases, the lawyer is entitled to claim only a reasonable amount of legal fees, taking into account the usual relationship with the client, the circumstances of the case, the difficulty and effort required to handle the case, the amount involved in the case, the specific benefits obtained by the client from winning the case, and any other relevant factors that may arise in the process. The Court emphasized that this limitation on remuneration only applies in exceptional circumstances as an exception to the principle of freedom of contract. *See* Daebeobwon [S. Ct.], May 17, 2018, 2016Da35833 (S. Kor.).

[26] *See e.g.,* Daebeobwon [S. Ct.], Jan. 27, 2004, 2003Da45410 (S. Kor.); Daebeobwon [S. Ct.], July 12, 2013, 2011Da66252 (S. Kor.); Daebeobwon [S. Ct.], Nov. 11, 2010, 2010Da26769 (S. Kor.); Daebeobwon [S. Ct.], May 17, 2018, 2016Da35833 (S. Kor.).

[27] *See e.g.,* Daebeobwon [S. Ct.], Jan. 27, 2004, 2003Da45410 (S. Kor.); Daebeobwon [S. Ct.], July 12, 2013, 2011Da66252 (S. Kor.); Daebeobwon [S. Ct.], Nov. 11, 2010, 2010Da26769 (S. Kor.); Daebeobwon [S. Ct.], May 17, 2018, 2016Da35833 (S. Kor.). *See generally* Kim Dong-Hoon, *The Principle of Private Autonomy in the Constitutional and Civil Law*, 30 KOOKMIN L.R 41, (2018). *See also*, Joo Ji-Hong, *Private Autonomy and its Restrictions- from the Perspective of Guarantee of Principle of Private Autonomy not by State Dominated Risk Management but by Free Market Risk Management*, *37* J. PROP. L. 103, (2021).

[28] *See supra* notes 9, 10, and 11.

[29] Freedom of contract is a foundational tenet of market economies that posits individuals must have the autonomy to partake in voluntary transactions without undue interference. Advocacy for restricting such exchanges, whether grounded in national interest, prevailing public sentiment, or price stabilization, contravenes this market economy principle. Meanwhile, freedom of ownership emphasizes that the absence of safeguarded private property rights impedes voluntary specialization and trade, precipitating a dip in societal wealth and economic stagnation. Lastly, fault-base liability is central to the notion that individuals are accountable for their choices and the ensuing repercussions, underscoring the prudence individuals exercise when faced with accountability in a market economy. *See generally* KONG BYUNG-HO, SIJANGKYUNGJEWONRI IYAGI JAYAKIEOPWON [STORIES OF MARKET ECONOMIC PRINCIPLES] (2019) (S. Kor.). *See also* Daebeobwon [S. Ct.], July 22, 2003, 2002Doe7225 (S. Kor.).

agreement without external interference, including state intervention.[30] Both the Korean Constitutional Court and the Korean Supreme Court have emphasized the importance of freedom of contract, as it is derived from the constitutional right to pursue happiness, underpinning the market economy.[31]

However, despite the wide-ranging freedoms within contract law, there are certain limitations to the freedom of contract. These restrictions are put in place to maintain a balance between the upholding party's autonomy and ensuring a fair and legal agreement. The courts have shown a strong reluctance to interfere with party autonomy based on principles of civil law, and only allow limitations on contractual liability in very specific circumstances. In Part II, this article will discuss these limitations on the freedom of contract and the rationale behind them.

II. PATERNALISM IN CONTRACT – ISSUE OF REGULATION

According to Professor Kwak Yoon-Jik at the Seoul National University College of Law, public welfare is considered a fundamental principle of civil law.[32] As a fundamental principle, public welfare is one of the few reasons that an individual's right to private autonomy may be limited.[33] Article 23 of the RoK Constitution provides as follows:

> (1) The property rights of all citizens shall be guaranteed, and the content

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[30] From a comparative perspective, the principle of freedom of contract in American jurisprudence is based on the idea that individuals have unique preferences that can be fulfilled through contracts. Jerome C. Knowlton, *Freedom of Contract*, 3 MICH. L. REV. 619, 619 (1905). The concept of "liberty of contract" emerged in the late 19th century, and the US Supreme Court recognized it as a constitutional right under the Fourteenth Amendment's due process clause. Allgeyer v. Louisiana, found a state law which effectively prohibited insurance contracts with companies based in other states of the United States to be unconstitutional. 165 U.S. 578, (1897). This doctrine reached its peak in Lochner v. New York and was later limited in the mid-1930s, signaling the end of the Lochner era and a more deferential approach towards state legislatures. *See* Lochner v. New York, 198 U.S. 45 (1905); and W. Coast Hotel Co. v. Parrish, 300 U.S. 379 (1937), respectively. In recent years, the freedom of contract has resurfaced in the context of arbitration agreements in consumer contracts. The US Supreme Court has upheld arbitration clauses that limit class action lawsuits in cases like AT&T Mobility LLC v. Concepcion and American Express Co. v. Italian Colors Restaurant. AT&T Mobility LLC v. Concepcion, 563 U.S. 333 (2011); and Am. Express Co. v. Italian Colors Rest., 570 U.S. 228 (2013). These decisions affirm parties' liberty to agree on arbitration terms, even if it restricts individuals' ability to pursue certain legal remedies, effectively prioritizing the freedom of contract over other concerns. See J. Maria Glover, *Disappearing Claims and the Erosion of Substantive Law*, 124 Yale L.J. 3052, 3071 (2015).

[31] *See supra* note 22.

[32] KWAK YOON-JIK, MINBEOBCHONGCHIG [THE GENERAL PART OF CIVIL LAW] 37 (2007) (S. Kor.).

[33] *Id.*

> and limits of such property rights shall be determined by law.
>
> *(2) The exercise of property rights shall be oriented towards public welfare.*
>
> (3) When it is necessary to expropriate, use, or restrict property rights due to public need, compensation shall be made in a just and reasonable manner, in accordance with the law.[34]

In a market economy, therefore, private autonomy—the freedom of individuals or entities to manage their own affairs—is important but not absolute as it may be subject to legal restrictions for the sake of public welfare.[35] For instance, in cases of health, safety, environmental protection, or other public policy concerns, the government may enact laws to restrict or regulate the exercise of private autonomy with a view to protecting the public interest.[36]

In the Korean Civil Code, there are two provisions which invalidate a legal act: if its purpose lacks social validity or fairness.[37] Article 103 regulates substantive control over social validity, while Article 104 regulates substantive control over fairness.[38] These provisions serve the

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[34] DAEHANMINKUK HUNBEOB [HUNBEOB] [CONSTITUTION] art. 23 (S. Kor.).

[35] *Id.*

[36] Real estate policy is an example of an area that requires government intervention to balance the principle of private autonomy with the public welfare. *See generally* Heo Kang-Moo, *Three Special Civil Acts on Real Estate and Common Welfare*, 84 PUB. LAND L. Rev. 1-19 (2018). Such policy, which is intertwined with various related public policies, including housing, taxation, finance, and statistics, is essential to everyday life and requires a timely response to social and environmental changes, which is deemed a role assigned to the government. *Id.* Therefore, the government has established and enforced special enhancements on real estate, including the Housing Lease Protection Act, Act on Ownership and Management of Condominium Buildings, and Commercial Building Lease Protection Act, to regulate specific matters that are difficult to regulate by the Civil Code and the accompanying principle of private autonomy alone. *Id.*

[37] Civil Law upholds the principle of freedom of legal acts while acknowledging the need for legal limits to ensure the validity of these acts. Legal acts that contravene the general order of society may be invalidated, regardless of the parties' intentions. Due to the complexity and diversity of legal acts, legal systems rely on general principles and standards, such as social validity and fairness, to govern their validity. Consequently, the validity of a legal act is determined on a case-specific basis, considering whether it adheres to the overarching principles of societal norms and the underlying legal system while factoring in the specific circumstances of each case. *See* KWAK & KIM, *supra* note 19, at 281.

[38] Article 103 of the Civil Code states that a legal act, or a "juristic act," will be null and void if it goes against good morals and social order. Minbeob [Civil Act] art. 103 (S. Kor.). This provision is intended to prevent legal acts that are harmful to society or go against widely accepted moral values from being enforced. *See generally* Han Sam-in, *Case Analysis of Article 103 of the Civil Code*, 7 L. & POL'Y REV. 47-75 (2001). Meanwhile, Article 104 of the Korean Civil Code states that a juristic act, which is a legal action performed by a person or a group of people with legal consequences, can be null and void

purpose of curbing any negative effects and safeguarding against any harm resulting from the unfettered exercise of individual freedom. [39] Simultaneously, they work to uphold private autonomy as a fundamental principle of the civil law.[40]

Article 103 of the Korean Civil Code precludes the legal effect of an act if its purpose is devoid of social validity.[41] Under this Article, any act that runs counter to legal or legitimate social standards is void of its legal effect.[42] Such norms serve to alert individuals and organizations to abide by legal and normative standards for the betterment of society.

Additionally, Article 104 of the RoK Civil Code precludes the legal effect of a legal act if its purpose is deemed to lack fairness.[43] Under this Article, an act aimed at obtaining unfair advantages over others may be invalidated. Such a provision aims to forestall individuals or organizations from acting with an unfair purpose. Article 104 of the Civil Code defines "unfair legal acts" as those that exhibit a significant imbalance between the creditor and the debtor, resulting in an unbalanced transaction that takes advantage of the distress, recklessness, or inexperience of the victim.[44] The purpose of Article 104 is to regulate exploitative acts against those in a more precarious position. [45] The conditions of distress, recklessness, or

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if it has conspicuously lost fairness due to strained circumstances, rashness, or inexperience of the parties involved. Minbeob [Civil Act] art. 104 (S. Kor.). This means that if a contract or other legal action is entered into under circumstances that are patently unfair or unjust, such as when one party takes advantage of the other's inexperience or desperate situation, the act may be deemed null and void. For such effect, *see* Daebeobwon [S. Ct.], June 7, 1966, 66Da228, (S. Kor.); Daebeobwon [S. Ct.], Nov. 7, 1963, 63Da479, (S. Kor.); and Daebeobwon [S. Ct.], June 24, 1994, 94Da10900, (S. Kor.).

[39] *See generally* Lee Eun-Young, *Regulations on Private Autonomy in Articles 103 and 104 of the Civil Code*, 52 CHONGBUK L.R. 189, (2017).

[40] *Id.*

[41] For example, it was unanimously ruled that, under Article 103 of the Civil Code, contingency fee agreements in criminal cases are deemed to be against good morals and public order. Daebeobwon [S. Ct.], 2015Da200111, July 23, 2015 (S. Kor.).

[42] Jae Hyung Kim & Joe Cho, *Formulating the Korean Supreme Court's Stature and Roles: With a Focus on the Relationship between Legislation and Precedents*, 14 U. PA. ASIAN L. REV. 136, 155 (2019) ("Kim & Cho").

[43] *See generally* Sung Joonho, *A Study on the Unjust Legal Transaction in Section 104 of the KBGB*, 55 KOR. J. CIV. L. 457-502 (2011).

[44] Minbeob [Civil Act] art. 104 (S. Kor.).

[45] In a Korean Supreme Court decision of January, 2011, the legal standards for determining an unfair contract practice were established. An unfair contract practice under Article 104 of the Civil Code is established if there is an objective imbalance between the obligations and benefits of the parties, and the transaction was concluded subjectively in such an imbalanced state, taking advantage of the urgency, recklessness, or inexperience of the victim. These requirements aim to regulate abusive practices that take advantage of

inexperience required for the establishment of an unfair legal act are not all necessary, having enough of one or a combination of two is sufficient to preclude legal effect.[46]

"Distress" in this context refers to "urgent distress" caused by economic, mental, or psychological reasons.[47] Whether a party was in a state of distress is assessed by considering various factors, such as their age, occupation, education, social experience, financial status, and the urgency of the situation the party was in.[48] However, an unfair legal act under Article 104 will not be established if there was no intention to exploit the aggrieved party's circumstances or if there was no significant imbalance between the creditor and the debtor, even if the victim was in a state of distress.[49]

Rooted in civil law's core principle of private autonomy, these provisions create a balanced framework that allows individuals and organizations to exercise their freedoms while also mitigating the risks of self-interest becoming detrimental to social responsibility.[50] By regulating the substance of legal acts with respect to social validity and fairness, the Korean Civil Code not only upholds the integrity of the legal system, but also ensures that private autonomy aligns with societal propriety and fairness standards.[51] The Civil Code works to preserve the normative nature of laws and protect legitimate social interests.[52] In this way, the RoK Civil Code strikes a delicate balance between individual liberty and the subject of regulation.[53] Having probed the subject of private autonomy and of restrictions thereon, this article now turns to the legal nature of PPC.

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the weaker party. The highest court noted that urgent distress must be assessed based on various factors, and an unfair contract practice under Article 104 does not apply if the other party did not act with an intention to take advantage of the victim's situation or if there is no objective imbalance between the parties. Daebeobwon [S. Ct.], Jan. 27, 2011, 2010Da53457 (S. Kor.).

[46] *Id.*

[47] Daebeobwon [S. Ct.], Oct. 22, 2002, 2002Da38927 (S. Kor.).

[48] *Id.*

[49] *See* Daebeobwon [S. Ct.], Jan. 27, 2011, 2010da53457 (S. Kor.); and Daebeobwon [S. Ct.], Oct. 22, 2002, 2002da38927 (S. Kor.).

[50] *See* KWAK & KIM, *supra* note 19, at 281-294.

[51] *Id.*

[52] *Id.*

[53] *See generally* Hanoch Dagan & Michael Heller, *Freedom of Contracts* (Columbia L. & Econ. Working Paper No. 458, 2013), https://scholarship.law.columbia.edu/faculty_scholarship/1825. (The presence of mandatory terms within a contract type can increase freedom by providing a baseline of agreement).

III. LEGAL NATURE OF PPC

Under Article 5.1 of the Government Contract Act of the RoK, a contract shall be concluded by agreement of the parties to the contract, on equal footing, and the parties shall perform the terms and conditions of the contract in good faith.[54] In other words, a PPC is a legally binding agreement that is formed when both parties voluntarily agree to its terms on equal footing. The parties to a contract are expected to act in good faith and fulfill their obligations according to the terms of the contract.[55]According to the Korean Supreme Court, the principle of good faith, which is codified in Article 2 of the Civil Code as a provision of general applicability, dictates that parties to a legal relationship should not exercise their rights or fulfil their obligations in a manner that violates the abstract norm of considering the other party's interests, fairness, or trust.[56] To challenge the exercise of rights that go against the principle of good faith, it is necessary to prove that the party exercising those rights acted in bad faith and that the other party had a legitimate expectation of good faith.[57] Moreover, it must be shown that the use of those rights unreasonably interfered with the other party's legitimate expectation of good faith, based on the overarching principles of

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[54] The Government Contract Act was established as an independent law system in preparation for the Government Procurement Agreement of the World Trade Organization (WTO), which came into effect on January 1st, 1997. The Act was created to align with the trends of internationalization and openness of government contracts and to accommodate the need for expanding indirect social capital facilities at the time, which was expected to result in a rapid increase in the budget and workload for governmentcontracts. In light of these circumstances, the sixth chapter of the former Budget Accounting Act was separated on January 5th, 1995, and established as an independent law named the Government Contract Act. The Act was then followed by the enforcement decree and enforcement rules on July 6th of the same year. Kim Tae-kwan, *The Legal Nature of the Adjustment Provision of the Contract Amount due to Price Fluctuation under the Government Contract Law - Centered on the Ruling of the Supreme Court 2017.12.21*., 17 ILKAM REAL EST. L. REV. 3, 16 (2018); *see also* Guggaleul dangsajalo haneun gyeyag-e gwanhan beoblyul [Act on Contracts to which the State is a Party], art. 5 para. 1 (S. Kor.).

[55] According to Prof. Kwon Young-joon, the principle of good faith, which had been developed in the context of the actio bonae fidei and the exceptio doli generalis in Roman law, has been codified in the field of contract law in France's Civil Code Article 1104, which stipulates that "(c)ontracts must be negotiated, formed and performed in good faith." *See* Trans-Lex.org, French Civil Code 2016, https://www.trans-lex.org/601101/_/french-civil-code-2016 (last visited Mar. 27, 2023). In the RoK, the principle of good faith has been elevated to a general principle of civil law applicable to all areas of civil law both in substantive and procedural aspects. Kwon Young-joon, *Prescription and Good Faith Principle*, 26(1) J. PROP. L. 1, 4-5 (2009). For instance, Article 1, paragraph 2 of the Civil Procedure Act stipulates that the parties and their representatives shall perform the litigation faithfully according to good faith, thereby accepting it as a principle of procedural law. *Id;* Min-sa-so-song-beob [Civil Procedure Act], art. 1 para. 2 (S. Kor.).

[56] Daebeobwon [S. Ct.], Oct. 29, 2020, 2018Da228868 (S. Kor.).

[57] *Id*.

justice.[58]

Meanwhile, the term "equality of position" refers to the idea that the parties to a contract are, in principle, equal in terms of the level of their respective bargaining power, related access to information, and understanding of the terms of the contract.[59] Each party is also expected to have the ability to negotiate the terms of the contract before agreeing to it volitionally.[60] A level playing field helps ensure that the contract is fair, entered chiefly based on the parties' mutual agreement, commercially considerate, and subsequently performed in good faith.[61]

The PPC is considered a private contract in legal nature, and the laws that apply to it are seen as internal regulations for the government contracting officers to review and follow.[62] Thus, the Court treats the regulations mentioned in the Government Contract Act and its enforcement ordinance as internal regulations of the government.[63] The Court further noted that while these regulations ensure fair and efficient handling of government contracts and provide necessary guidelines for government officials, the laws developed for PPCs are still only internal regulations, as opposed to substantive law.[64]

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[58] *See e.g.,* Daebeobwon [S. Ct.], Dec. 10, 1991, 91Da3802 (S. Kor.).

[59] For such equality in the context of M&A and civil penalty, *see* Chae Dong-Heon, *The Standard of Classification between the Advance Determination of the Amount of Damages and the Penalty - Review on the Supreme Court July 14, 2016 Decision 2012Da65973*, 59 PUSAN L.R. 359, 386 (2018).

[60] *See supra* note 8.

[61] The concept of equality of position refers to a relationship between the government and the counterparty in a PPC that is considered to be horizontal rather than vertical in nature. *See* JUNG WON, ONJU GUGGALEULDANGSAJALOHANEUNGYEYAG-E GWANHANBEOBLYUL JE5JOU [ONJU GOVERNMENT CONTRACT ACT ART.5] 6 (2023) (S. Kor.). In a horizontal contractual relationship, the parties involved are in principle on equal footing, with neither having an inherent advantage over the other and thus without imbalances of bargaining power. *See* Guggaleul dangsajalo haneun gyeyag-e gwanhan beoblyul [Act on Contracts to which the State is a Party], art. 5 para. 1 (S. Kor.). Accordingly, Article 4 of the Government Contract Act posits that each head of a central government agency or contracting officer must not establish a special agreement or contract condition that unreasonably restricts the contractual interests of the contracting party as prescribed by laws, regulations, and related laws in concluding a contract. Guggaleul dangsajalo haneun gyeyag-e gwanhan beoblyul [Act on Contracts to which the State is a Party], art. 4 (S. Kor.). This contractual scheme evinces a strong will to prevent abuse of the government's monopolistic position by guaranteeing the contractual interests of the contracting party.

[62] CHUNG, TAE HAK ET AL., GUGGAGYEYAGBEOB [GOVERNMENT CONTRACT LAW] 14 (2020) (S. Kor.).

[63] Daebeobwon [S. Ct.], Dec. 11, 2001, 2001Da33604 (S. Kor.).

[64] Daebeobwon [S. Ct.], Dec. 27, 1983, 81Nu366 (S. Kor.) (a contract concluded under the Budget and Accounts Act, the predecessor to the Government Contract Act, is considered a contract under private law).

A. *Application of the Civil Code and Civil Procedure*

According to relevant jurisprudence, the Civil Code, which governs private contracts, applies equally to PPCs between the government and legal entities.[65] This means that the rules and provisions in the Civil Code apply to these types of contracts in the same manner as they would to private contracts.[66] In addition to the Civil Code, there exists a body of special enactments including the Government Contract Act, the Local Government Contract Act, and the Government Procurement Act, which embody internal norms to be abided by government contracting officials when contracting with private entities. These provisions may be incorporated as the terms of a given PPC, which may then bind the counterparty.[67]

Due to the Korean Supreme Court's determination that government procurement contracts are considered private contracts, disputes arising from government procurement are handled through the application of civil procedure.[68] The justification for this determination is attributable to Article 5 of the Government Contract Act, which provides that procurement contracts should be established through mutual assent and executed in good

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[65] According to relevant precedent, the contract referred to as a "public contract" between a local government and the state, as governed by the Government Contracts Act and applied by the Local Finance Act, is considered a contract under private law. It is entered into by both parties on equal footing as private entities, and its main elements are no different from a contract between private individuals. Therefore, the principles of private law such as autonomy and freedom of contract apply, except as otherwise provided. *See* Daebeobwon [S. Ct.], Dec. 11, 2001, 2001Da33604 (S. Kor.).

[66] *Id.*

[67] Guggaleul dangsajalo haneun gyeyag-e gwanhan beoblyul [Act on Contracts to which the State is a Party] (S. Kor.); Guggaleul dangsajalo haneun gyeyag-e gwanhan beoblyul [Act on Contracts to which the State is a Party] (S. Kor.); Jodalsaeobe gwanhan beoblyul [Government Procurement Act] (S. Kor.); *See generally* Lee Hyong-Sik & Kim Gee-Hwan, *Monetary Penalties for violating Direct Production Obligation of Public Procurement Contract*, 32 CHOONGNAM J.L. 49-93 (2021).

[68] According to the Supreme Court, contracts concluded under Article 36 of the Budget Accounting Act, the predecessor to the Government Contract Act, are considered judicial or private contracts, and the bid bond under Article 70-5 of the same Act, which is intended to ensure the bidder's obligation to enter into a contract, is considered a form of damages to be paid to the state in the event of breach, as it compensates the state for its losses. Therefore, the government's retention of the bid bond is an act performed by the state as the owner of property rights, not as an exercise of its administrative power or as an integral part of exercising administrative power, and disputes regarding this matter should be subject to civil litigation, not administrative litigation. Daebeobwon [S. Ct.], Dec. 27, 1983, 81Nu366 (S. Kor.). In terms of jurisdiction, disputes involving PPC are the subject of civil litigation under the rules of civil procedure, rather than before an administrative tribunal or court. *See* Daebeobwon [S. Ct.], Sept. 26, 2003, 2002Doe3924 (S. Kor.). *See also* Daebeobwon [S. Ct.], June 19, 2006, 2006Ma117 (S. Kor.); Daebeobwon [S. Ct.], Dec. 20, 1996, 96Nu14708 (S. Kor.); and Daebeobwon [S. Ct.], Dec. 27, 1983, 81Nu366 (S. Kor.).

faith by the parties to a PPC.[69] Therefore, disputes related to PPC are handled through civil litigation under the rules of civil procedure, rather than by an administrative tribunal or court.[70] However, there is an exception: if a government agency debars a contractor under the PPC, it constitutes an administrative measure and the legality of such measure can be challenged in front of an administrative judge or tribunal.[71]

IV. CONTRACT INTERPRETATION

A. *Contract and Statutory Interpretation*

As previously noted, judicial precedent holds that the nature of a PPC is considered private, meaning the terms of a PPC clause are negotiated and determined by the parties involved in the contract.[72] In this framework, the provisions of the Government Contract Act provide certain internal regulations that the government must abide by when entering into a PPC.[73] When disputes arise out of a PPC and an amicable resolution is not feasible between the parties, litigation is the parties' usual recourse.[74] In such cases, the court is responsible for carefully examining the intent of the parties to

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[69] Kim Daein, *Korean Administrative Cases in the "Law and Development" Context*, *in* LITIGATION IN KOREA 199, 212-213 (Cho Kuk ed., 2010).

[70] *Id.*

[71] Daebeobwon [S. Ct.], May 28, 2020, 2017Du66541 (S. Kor.). *See also* Lee Kwang-Youn & Kim Chul-Woo, *Study on Administrative Contracts*, 28 SUNGKYUNKWAN L. REV. 79-107 (2016); and Jun Hyun-Cheol, *The Legal Character & Freedom of Contract Principle of Government Procurement Contracts -Focusing on the Judicial Precedents*, 46 DANKOOK L. REV. 169-201 (2022).

[72] *See supra* note 62.

[73] *See* Daebeobwon [S. Ct.], Dec. 11, 2001, 2001Da33604 (S. Kor.).

[74] In this regard, Article 51 of the General Terms and Conditions of Construction, published and updated by the Ministry of Economy and Finance from time to time, provides in part as follows:

Article 51 (Settlement of Disputes)

① Any disputes arising between the parties to a contract during the performance of the contract shall be resolved through consultation.

② If the consultation under paragraph (1) fails, the dispute shall be resolved by a court judgment or arbitration under the Arbitration Act.

Gongsagyeyag-ilbanjogeon [General Conditions for Construction Contracts], art. 57 (S. Kor.).

When the parties in a PPC are unable to resolve their disputes through mutual agreement, they often turn to litigation. Arbitration, while available, is infrequently utilized in the context of PPCs. *See* Jang Jae-hyung, Bunjaeng Haegyeolbangbeobe Gwanhan Gukga Gyeyakbeobui Choegun Gaepyeonggwa Gwanryeonhayeo [Recent Amendments to the Government Contract Law Regarding Dispute Resolution Methods], Law Times (Mar. 6, 2018), https://www.lawtimes.co.kr/news/140880.

the PPC and determining the legal consequences of the provision in question.[75] Since a PPC is a private agreement governed by the principles of civil law, the ultimate issue in any dispute becomes the interpretation of the contract and which rules of construction are applicable to the case.

In certain situations, it is necessary for a PPC clause to adhere to mandatory laws and regulations, such as those outlined in the Government Contracts Act, to ensure that the contract does not violate any compulsory legal requirements.[76] Adherence to these requirements is particularly important to avoid potential legal disputes that could arise from non-compliance. In disputes regarding the compatibility of a PPC clause with mandatory laws and regulations, the court analyzes the specific language of that clause in light of the relevant legal framework to determine whether it is consistent with any mandatory legal requirements.[77] This process can be complex, sometimes involving contract and statutory interpretation, which will be covered in the next part of the article.[78]

B. *Contract Interpretation in the Civil Law Context*

The interpretation of contracts is a crucial aspect of RoK contract law, and the objective of the court is to determine the meaning of the contract and its terms to the parties, or a hypothetical reasonable person.[79] This is done by looking at the language of the contract and the intentions of the parties.[80] The interpretation process can often involve a multi-layered analysis, taking into account the language used in the contract, the context in which the contract was entered into, and any relevant legal principles.[81]

When it comes to interpreting contracts, the Korean Civil Code provides limited guidance. Article 106 (entitled "De Facto Custom") provides that a custom that differs from any provisions of acts or subordinate statutes, which are not concerned with good morals or other social order, shall prevail if the intention of the parties to a juristic act is unclear.[82] However, this provision does not cover all possible contract

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[75] Daebeobwon [S. Ct.], Mar. 15, 2001, 99Da48948 (S. Kor.).

[76] Daebeobwon [S. Ct.], Oct. 12, 2018, 2015Da256794 (S. Kor.).

[77] *Id.*

[78] *See infra* Part B.

[79] *See infra* Part B.1-3.

[80] *See infra* note 86.

[81] Daebeobwon [S. Ct.], May 26, 1992, 91Da35571 (S. Kor.).

[82] Article 106 (De Facto Custom) of the Civil Code provides as follows:

If there is a custom which differs from any provisions of Acts or subordinate statutes which are not concerned with good morals or other social order, and if the intention of the parties to a juristic act is not clear, such custom shall prevail.

Minbeob [Civil Act] art. 106 (S. Kor.).

interpretation scenarios.[83] Consequently, Korean courts have developed their own rules for interpreting contracts over time.[84] These canons of interpretation include the following: natural interpretation, normative interpretation, and supplementary interpretation.[85]

1. Natural Interpretation

Contract interpretation is a fundamental aspect of contract law that aims to determine the true intent of both parties beyond the formal text of the contract.[86] In order to achieve this objective, the courts rely on various factors such as the nature and purpose of the agreement, the language used in the contract, and the parties' words and deeds.[87] This approach seeks to determine the parties' intent to be bound by the contract.[88]

When interpreting a contract, the courts generally give weight to the plain meaning of its terms as reflected in the written text of the contract.[89]

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[83] Regarding Article 106, the Supreme Court of Korea clarified that collective bargaining agreements in labor relations impact only those union members and employees actively engaged at the time of the agreements' enactment, excluding retired individuals. For retirees to assert a customary extension of these agreements to themselves, there must be an established and recognized practice among the current workforce and the company, where such agreements are implicitly accepted as part of the company's operational norms. Without evidence of this collective understanding or practice, retirees are barred from invoking such customs to augment or inform the interpretation of the law. Daebeobwon [S. Ct.], Apr. 23, 2002, 2000Da50701 (S. Kor.).

[84] KIM JUNHO, MINBEOBGANGUI [CIVIL LAW LECTURE] 192 (2022) (S. Kor.) [hereinafter, "KIM JUNHO"].

[85] *See infra* Part B.1-3.

[86] Daebeobwon [S. Ct.], Oct. 26, 1993, 93da2629 2636 (S. Kor.). Note: these two cases were heard and decided together.

[87] *Id*.

[88] Kwon Young-joon, *Contract Interpretation under Korean Law, in* CONTENTS OF CONTRACTS AND UNFAIR TERMS 210 (Mindy Chen-Wishart & Stefan Vogenauer eds., 2020).

[89] For instance, in a 1996 judgement involving a real estate sales contract, the Court noted that if both parties have agreed to buy and sell a particular plot of land (甲) as the object of the contract but have made an error regarding the plot's registration number and the contract consequently designates a different plot of land (乙) as the object of the contract, the contract is still considered to be valid with respect to the intended plot of land (甲), as opposed to the land (乙), as long as both parties have agreed to it. If the transfer of ownership registration has been completed in the name of the buyer based on this sales agreement regarding the land (乙), then it will be deemed invalid as lacking a cause. Daebeobwon [S. Ct.], Aug. 20, 1996, 96Da19581 (S. Kor.). In addition, in a 1997 Court decision, it was held that in a valid real estate sales contract, the existence of the parties' agreement on the buy and sell of the real estate at issue should be acknowledged as long as

This is known as natural or textual interpretation, which involves the construction of contractual terms based on the intention of the parties.[90] However, in situations where the terms of the contract are unclear, the courts may consider extrinsic evidence to interpret the contract, including prior negotiations or correspondence between the parties, industry standards and practices, and any relevant legal principles or existing case law.[91]

It is important to note that the courts will aim to interpret contracts in a manner that gives effect to the parties' intentions, while avoiding any interpretation that would lead to an unreasonable or unjust result. Furthermore, in cases where there is an agreement between the parties that is inconsistent with the underlying text of the contract, such agreement will govern.[92] To this end, the court will rely on the totality of relevant elements to determine the contract's validity.[93]

2. Normative Interpretation

When a disagreement between the parties regarding the interpretation of a contract arises and the dispute cannot be resolved based on natural interpretation alone, the courts look to the reasonable determination of the parties' intent.[94] The Supreme Court has stated that in

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there are no special circumstances contradicting such agreement, and if the registration number of the land designated as the object of the sales contract is revealed to be that which did not exist on the date of sale specified in the contract, it becomes necessary to determine whether the sales date is true as per the parties' claims or to determine whether the parties made a mistake regarding the registration number of the object of the contract and mistakenly indicated the object of the contract. Daebeopwon [S. Ct.], Apr. 11, 1997, 96Da50520 (S. Kor.).

[90] According to RoK legal scholars, the gist of Natural Interpretation consists in when the parties to a contract have practically agreed upon the meaning of a certain expression, it should be recognized as having legal effect according to its agreed meaning. *See* SONG DUCKSOO, CHAEGWONBEOBCHONGLON [THE GENERAL PART OF LAW OF OBLIGATIONS] 181 (2021) (S. Kor.); and KWAK and KIM, *supra* note 19, at 288.

[91] Kwon Young-joon*, Contract Interpretation under Korean Law, supra* note 88 at 210.

[92] Daebeobwon [S. Ct.], June 11, 2009, 2007Da88880 (S. Kor.). According to this decision, in general, when interpreting a contract, it is important to consider not only the formal language but also the true intentions of both parties. If there is a disagreement between the parties regarding the interpretation of the contract, it is necessary to consider the language used, the circumstances under which the agreement was made, the purpose of the agreement, and the true intentions of both parties in order to interpret the contract in a rational and reasonable manner based on logic and experience.

[93] *Id.*

[94] KIM JUNHO, *supra* note 84, at 194 (where he states normative interpretation involves examining the objective normative meaning of an expressive act. The way to carry out a normative interpretation thus varies on a case-specific basis. To make reasonable decisions in each instance, a range of interpretive tools and approaches should be considered and employed).

such cases, the contract should be interpreted reasonably and logically, considering a variety of factors such as the written text, the parties' motives and actual intent, as well as relevant circumstances and objectives being pursued.[95] This approach is consistent with what is known in academic circles as "normative interpretation," which involves and proceeds on interpreting a contract according to what a reasonable counterparty would have meant or intended.[96]

Thus, in the event of a disagreement over the interpretation of a contract, the adjudicating court will attempt to discern the objective meaning that the parties accorded to their actions with the resulting terms and conditions.[97] The court will consider the form and contents of the underlying contract, the purpose of that contract, the parties' will and intent, and trading practices in a reasonable manner.[98] This approach ensures that the parties' intentions are accurately reflected in the contract, and that any ambiguity or inconsistency is resolved in an objective, reasonable manner.[99] In fact, like the United States, normative interpretation represents the dominant mode of contract interpretation adopted by the Korean Supreme Court.[100]

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[95] Daebeobwon [S. Ct.], Mar. 25, 1994, 93Da32668 (S. Kor.).

[96] Young-joon*, Contract Interpretation under Korean Law, supra* note 88, at 211. *See* Daebeobwon [S. Ct.], June 24, 2005, 2005Da17501 (S. Kor.). According to the Court, when interpreting a legal act, the primary goal is to clearly establish the objective meaning that the parties accorded to their actions, rather than the subjective intention of the parties. Such intention of the parties is a reference to be resorted to when the meaning of a contract cannot be objectively established. *See e.g.*, Daebeobwon [S. Ct.], Sept. 27, 1988, 86Daka2375 (S. Kor.); Daebeobwon [S. Ct.], Nov. 13, 1990, 88Daka15949 (S. Kor.); Daebeobwon [S. Ct.], May 26, 1992, 91Da35571 (S. Kor.); Daebeobwon [S. Ct.], Dec. 22, 1992, 92Da30320 (S. Kor.); Daebeobwon [S. Ct.], Apr. 23, 1993, 92Da41719 (S. Kor.); Daebeobwon [S. Ct.], June 8, 1993, 92Nu18009 (S. Kor.); and Daebeobwon [S. Ct.], Jan. 11, 1994, 93Da17638 (S. Kor.); Daebeobwon [S. Ct.], Sept. 30, 1994, 94Da32986 (S. Kor.); and Daebeobwon [S. Ct.], Aug. 11, 1995, 94Da26745 (S. Kor.).

[97] Daebeobwon [S. Ct.], June 28, 2018, 2016Da221368 (S. Kor.). See also Daebeobwon [S. Ct.], Dec. 21, 1990, 90Da6583 (S. Kor.); Daebeobwon [S. Ct.], May 26, 1992, 91Da35571 (S. Kor.); Daebeobwon [S. Ct.], Oct. 26, 1993, 93Da3103 (S. Kor.); Daebeobwon [S. Ct.], Mar. 25, 1994, 93Da32668 (S. Kor.); Daebeobwon [S. Ct.], Mar. 17, 1995, 93Da46544(S. Kor.); Daebeobwon [S. Ct.], June 30, 1995, 94Da51222(S. Kor.); and Daebeobwon [S. Ct.], Oct. 25, 1996, 96Da16049(S. Kor.).

[98] *Id.*

[99] *See e.g.*, Daebeobwon [S. Ct.], Nov. 17, 2015, 2013Da61343 (S. Kor.).

[100] The Korean Court's focus on Normative Interpretation aligns with the views of Justice Oliver Wendell Holmes and Judge Learned Hand. Both American jurists prioritize the words used in a contract over the parties' subjective intent. Holmes argues that contracts are formed based on overt actions, not mental states. Hand similarly emphasizes that legal obligations arise from explicit acts and words, and that personal intent is irrelevant unless mutually expressed. *See* OLIVER WENDELL HOLMES, THE COMMON LAW 240, 242 (Mark

3. Supplementary Interpretation

If the parties to a contract fail to include important elements in the agreement and such lacuna gives rise to a dispute, the courts may fill in those gaps by applying an applicable statutory provision.[101] If no statutory provision exists, the courts may insert a provision based on the parties' hypothetical intent.[102] This mode of interpretation is known as supplementary interpretation.[103] The highest court determined that if a mutual mistake between the parties leads to a lack of agreement on the subject of the mistake, the court has the authority to interpret the contract by adding terms and conditions that the parties would have agreed to but for the mistake.[104] Supplementary interpretation thus allows the court to complete the contract where necessary, based on the parties' hypothetical intent as opposed to their actual or subjective intent.[105] The court also allows the parties to adjust any contractual loopholes that can be inferred objectively from the purpose of the contract, trade practices, applicable regulations, and the principle of good faith and trust.[106]

4. Statutory Interpretation

The principles of contract interpretation, as noted above, are similar to the principles of statutory interpretation that have been adopted by the Korean courts. Thus, the importance of the text is often emphasized in statutory interpretation, as shown by the expression "[t]he text . . . remains the alpha and omega of interpretation."[107] Therefore, when performing textual interpretation, it is crucial to determine the meaning of the text and the meaning it conveys in the context of the contract. In most relatively noncontroversial cases, Korean precedents have focused on textual or

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DeWolfe Howe ed., Harvard Univ. Press 1963) (1881). *See also* Hotchkiss v. Nat'l City Bank of N.Y., 200 F. 287, 293 (S.D.N.Y. 1911), aff'd, 201 F. 664 (2d Cir. 1912), aff'd, 231 U.S. 50 (1913); JEE1, *supra* note 9, at 211.

[101] Daebeobwon [S. Ct.], Nov. 23, 2006, 2005Da13288, (S. Kor.).

[102] KIM JUNHO, *supra* note 84, at 195.

[103] *Id.*

[104] Daebeobwon [S. Ct.], Nov. 23, 2006, 2005Da13288, (S. Kor.).

[105] *Id.*

[106] Daebeobwon [S. Ct.], Nov. 13, 2014, 2009Da91811 (S. Kor.); Daebeobwon [S. Ct.], Nov. 23, 2006, 2005Da13288 (S. Kor.).

[107] *See* Mary Ann Glendon, *Comment*, *in* A MATTER OF INTERPRETATION 106, 106 (Amy Gutmann ed., 1998). *See generally* Kim Jae Hyung, Hwang-geumdeulnyeok-ui Aleumdaum: Beobhaeseog-ui Han Danmyeon [Splendor of Autumn Fields of Gold: an Aspect of Legal Interpretation], 1 BEOBHAK PYOUNGRON [SNU L. REV.] 223–229 (2010).

literary interpretation.[108] However, when a statute is ambiguous or unclear, the court may look beyond the text of the statute and consider its legislative intent to arrive at a clear interpretation and application of the statutory text.[109] In terms of germane legal precedent, in an *en banc* Court decision, the court held that the law is a norm of society that has universal and binding force, and as such, it must be interpreted with objectivity and clarity, with a view toward ensuring legal stability.[110] Thus, the goal of statutory interpretation is to achieve consistent legal validity that is acceptable to the general public, while also keeping legal instability at bay. This requires an interpretation of the ordinary meaning of the language used in the statute, as well as systematic and logical means of interpretation, taking into account the legislative purpose and objectives, the legislative history, harmonization with the entire legal order, and the relationship with other enactments.[111] Ultimately, the aim of statutory interpretation is to strike a proper balance between maintaining legal stability and finding a just and reasonable solution for each individual case.[112]Against this legal framework, as a general principle, statutory interpretation should adhere to the ordinary meaning of the language used in the statute as much as possible.[113] However, while substantive law provides a framework for legal principles and rules, its application may not always be straightforward in the complexities of real-life situations.[114] Therefore, it is necessary to carefully consider the unique facts of each case and apply the law in a manner that fits each individual situation on a case-by-case basis.[115]

C. *Analysis*

The principles of statutory interpretation in Korea are similar to those of contract interpretation in that the court's goal is to determine the meaning and intent of the underlying instrument. While textual interpretation is the primary approach, other factors such as context, legislative or individual intent, and the purpose of the statute or agreement in question may also be considered.[116] The approach to statutory

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[108] *See generally* Kim & Cho, *supra* note 42.

[109] Daebeobwon [S. Ct.], June 21, 2018, 2011Da112391 (S. Kor.).

[110] *Id.*

[111] *Id.*

[112] *Id.*

[113] Daebeobwon [S. Ct.], May 14, 2020, 2018Da298409 (S. Kor.).

[114] Daebeobwon [S. Ct.], Oct. 27, 2022, 2022Du44354 (S. Kor.).

[115] *Id.*

[116] Daebeobwon [S. Ct.], June 21, 2018, 2011Da112391 (S. Kor.).

interpretation is different from the interpretation of contracts, where the subjective intent of the parties is given more weight.[117] In the case of statutory interpretation, the focus is on the objective intent of the legislature as expressed through the text of the statute and other sources of legislative history such as committee reports, debates, and other germane materials.[118] The objective intent of the legislature and the purpose of the statute are considered in order to arrive at a clear and consistent interpretation that serves the intent and purpose of the statute. [119]

V. ADJUSTMENT OF CONTRACT PRICE

In the recent Supreme Court case of *2012Da74076*, the tension between the principle of contractual freedom and governmental regulation in the realm of PPC was brought to the forefront.[120] The crux of the dispute revolved around the interpretation of Article 19 of the Government Contract Act, which addresses adjustments to PPC contract prices in response to price fluctuations and whether its provisions are obligatory.[121] The next section will examine the pertinent legislative framework, proceed to analyze the case in question, and present a thorough evaluation of the case's implications.

A. *Statutory framework*

As noted above, the general framework of Article 5 of the Government Contract Act provides two essential principles that must be adhered to in the PPC contracting process.[122] It requires parties to enter into contracts on an equal footing.[123] This principle is critical to protecting the interests of the counterparty in the contracting process, as it ensures that any unreasonable agreements or conditions made by the central government agency head or contract officer that unduly prejudice the counterparty are

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[117] For a judicial example of this interplay, see Kim & Cho, *supra* note 42, at 152.

[118] *Id.* at 141.

[119] Daebeobwon [S. Ct.], June 21, 2018, 2011Da112391 (S. Kor.).

[120] Daebeobwon [S. Ct.], Dec. 21, 2017, 2012Da74076 (S. Kor.).

[121] Guggaleul dangsajalo haneun gyeyag-e gwanhan beoblyul [Act on Contracts to which the State is a Party], art. 19 (S. Kor.).

[122] Guggaleul dangsajalo haneun gyeyag-e gwanhan beoblyul [Act on Contracts to which the State is a Party], art. 5 (S. Kor.); Guggaleul dangsajalo haneun gyeyag-e gwanhan beoblyul [Act on Contracts to which the State is a Party], art. 5 para. 1 (S. Kor.).

[123] Guggaleul dangsajalo haneun gyeyag-e gwanhan beoblyul [Act on Contracts to which the State is a Party], art. 5 para. 3 (S. Kor.).

addressed.[124]

Meanwhile, Article 19 of the Government Contract Act, together with Article 64 of the Enforcement Decree to the Government Contract Act, outlines the circumstances under which the head or contracting officer of a central government agency in the RoK may adjust the amount of a PPC.[125] The provisions of the Enforcement Decree specify that any adjustment may occur after 90 days from the date on which the initial contract was made and imposes certain restrictions on when the contract price may be adjusted again.[126] The provisions outline three specific situations where the contract price may be adjusted.[127] These include when the adjustment rate of goods increases or decreases by not less than 3/100, when the index adjustment rate increases or decreases by not less than 3/100, and when the requirements for contract price adjustment due to foreign exchange fluctuation are met.[128]

B. *Facts*[129]

The plaintiffs in *2012Da74076*, *Keangnam* Enterprises, Ltd. and Lotte Engineering & Construction, entered into a contract with the defendant, Korea Land Housing Corporation, on April 16, 2007, for the construction of a large-scale energy facility in the *Asan Baebang* District.[130] As provided for in Article 15 of the Special Terms and Conditions, the portions of the contract price that were related to overseas entities were to remain fixed and unchangeable throughout the agreement's duration, as the parties had already accounted for any potential price fluctuations. Consequently, the contractor could not submit civil or criminal petitions regarding the fixed contract price.[131]

As a tier 1 construction contractor with extensive experience in large facility contracts, the plaintiffs were fully aware of the Special Terms and Conditions when they reviewed the Request for Proposals distributed by the defendant.[132] In June 2007, the defendants acquired gas turbines from

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[124] *See* i*nfra* note 153.

[125] Guggaleul dangsajalo haneun gyeyag-e beobyul sihaengryung [Guggagyeyagbeob sihaengryung] [Enforcement Decree of the Act on Contracts to which the State is a Party] art. 64 (S. Kor.).

[126] *Id*.

[127] *Id*.

[128] *Id*.

[129] This portion is collated from Daebeobwon [S. Ct.], Dec. 21, 2017, 2012Da74076 (S. Kor.).

[130] *Id*.

[131] *Id*.

[132] *Id.*

Siemens for 274,530,117 SEK (Swedish krona) and steam turbines from S.N.M. for 623,278,000 JPY (Japanese yen).[133] The 2008 global financial crisis subsequently led to a significant increase in exchange rates, prompting plaintiff *Keangnam* Enterprises to request a price adjustment for the underlying agreement.[134] However, the defendant rejected this request, citing the Special Terms and Conditions.[135]

The subject agreement's Special Terms and Conditions offered guidance on the acceptable range of gas and steam turbine suppliers but did not specify the currency for payment or settlement.[136] Despite this, the plaintiffs failed to take measures to hedge against potential exchange control risks associated with purchasing turbines from foreign suppliers.[137] Consequently, the plaintiffs filed a lawsuit seeking restitution of unjust enrichment from the defendant, arguing that the Special Terms and Conditions violated Article 19 of the Government Contract Act regulating contract price adjustments due to price fluctuations.[138]

C. *Court Holdings*[139]

1. Majority Opinion[140]

According to the majority opinion, PPCs involving the State or a public corporation operate under private law principles, similar to contracts between private individuals.[141] The Government Contract Act allows for adjustments in contract amounts due to price fluctuations to ensure contract fulfillment and prevent wastage of taxpayer money.[142] Meanwhile, contract officers can exclude these adjustments based on various factors, including price trends and economic risks.[143] The Government Contract Act ensures fairness in the State's dealings with private entities and does not restrict special mutually agreed terms.

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[133] *Id.*

[134] *Id.*

[135] *Id.*

[136] *Id.*

[137] Daebeobwon [S. Ct.], Dec. 21, 2017, 2012Da74076 (S. Kor.).

[138] *Id.*

[139] Since the full text of the decision, including the dissenting opinion, is substantial in length, this piece discusses the majority opinion and touches on the concurring opinion and the dissenting opinion written by other Justices.

[140] Daebeobwon [S. Ct.], Dec. 21, 2017, 2012Da74076 (S. Kor.) (Justice Kim Chang-suk and Justice Jo Hee-de, concurring in support of the majority opinion).

[141] *Id.*

[142] *Id.*

[143] *Id.*

The Court reasoned that PPCs involving the State or a public corporation are fundamentally similar to contracts between private individuals.[144] They are governed by principles of private law, such as private autonomy and freedom of contract, unless specific statutory stipulations dictate otherwise.[145] In a PPC, parties agree on equal terms and perform contractual obligations in good faith pursuant to Article 5(1) of the Government Contract Act.[146] The provision for contract amount adjustment due to price fluctuations in the Government Contract Act aims to prevent situations where a party renounces or fails to perform contractual obligations because of unanticipated price fluctuations, which could undermine the purpose of PPC.[147] Additionally, this provision seeks to avoid the wasting of government resources by allowing contracting officers to adjust contract amounts in case of significant price changes, ensuring neither party is unfairly advantaged or disadvantaged.[148]

Contracting officers may agree with counterparties to exclude the application of the price fluctuation adjustment provision when considering factors such as the contract's specific features, price and supply trends, currency fluctuation risk, policy needs, and reasonable risk allocation due to economic fluctuations.[149] This is especially true because counterparties might incur unanticipated losses if the Government demands a downward adjustment of the contract amount following a price drop.

The contract adjustment provision of the Government Contract Act aims to ensure fair, reasonable, and efficient processing of relationships between the State and private individuals or entities. It does not prohibit or restrict the State from imposing special terms and conditions based on agreements with counterparties.[150] The effects of such contractual terms should not be easily dismissed, considering the principles of private autonomy and freedom of contract.

Article 4 of the Enforcement Decree of the Government Contract Act mandates that contracting officers must refrain from incorporating special terms or conditions that unduly curtail a counterparty's interests, as such limitations would invalidate the special terms and conditions.[151] To

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[144] *Id.*

[145] *Id.*

[146] *Id.*

[147] Daebeobwon [S. Ct.], Dec. 21, 2017, 2012Da74076 (S. Kor.) (Justice Kim Chang-suk and Justice Jo Hee-de, concurring in support of the majority opinion).

[148] *Id.*

[149] *Id.*

[150] *Id.*

[151] This provision became incorporated into art. 5 para. 3 of the Government Contract Act as of Nov. 26, 2019. *See* Guggaleul dangsajalo haneun gyeyag-e gwanhan beoblyul [Act on Contracts to which the State is a Party], art. 5 para. 3 (S. Kor.).

determine whether a special agreement in a public contract infringes upon the contracting counterparty's legitimate interests and reasonable expectations, it is insufficient to merely establish that the agreement is to some degree disadvantageous to the counterparty. Instead, the counterparty must prove that the special agreement unfairly disadvantages the contracting counterparty due to the *state's* inclusion of the agreement in the contract.[152] Accordingly, evaluating whether specific terms and conditions unjustly constrain a counterparty's contractual interests requires a comprehensive examination of various factors, including the magnitude of potential prejudice to the counterparty, the likelihood of disadvantage occurring, the impact on the overall contract, the events leading up to the contract's execution, and relevant statutory and regulatory provisions.[153]

2. Dissenting Opinion[154]

According to the dissenting opinion, the Government Contract Act dictates adjustments to contract amounts based on price or currency shifts.[155] Sharp price changes can disrupt contracts or misuse taxpayer money. Contract officers are mandated to make post-contract adjustments to ensure fairness and budget optimization. Specific criteria in the Enforcement Decree guide these adjustments[156] This provision is mandatory for public contracts, and any exclusion is void.

The Government Contract Act and its Enforcement Decree thus establish explicit provisions regarding contract amount adjustments due to price or currency fluctuations.[157] These provisions aim to prevent the counterparty from suspension or renunciation of contractual performance due to economic hardship or excessive expenditure of governmental and public institutional resources.[158] The goal under this regime is to achieve the public interest purpose of optimizing budget execution, while avoiding the frustration of contractual objectives or excessive social costs.[159] While allocating the risk of price or currency fluctuations through agreements

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[152] Daebeobwon [S. Ct.], Dec. 21, 2017, 2012Da74076 (S. Kor.) (Justice Kim Chang-suk and Justice Jo Hee-de, concurring in support of the majority opinion).

[153] *Id.*

[154] Daebeobwon [S. Ct.], Dec. 21, 2017, 2012Da74076 (S. Kor.) (Justice Kim Jae-hyoung and Justice Ko Young-han, dissenting).

[155] *Id.*

[156] *Id.*

[157] *See supra* note 126.

[158] Daebeobwon [S. Ct.], Dec. 21, 2017, 2012Da74076 (S. Kor.) (Justice Kim Jae-hyoung and Justice Ko Young-han, dissenting).

[159] *Id.*

during public contract signing can be effective, Article 19 of the Government Contract Act mandates *ex post adjustments* instead, requiring the State and counterparty to adhere to the legislation except in exceptionally rare cases.[160]

Adjustment of the contract amount under this provision is applicable only when the situation meets the statutory requirement of being "necessary to adjust the contract amount due to price or currency fluctuation."[161] Requirements are further specified in the Enforcement Decree and the Enforcement Rule, ensuring a fair outcome through interpretation and application of the regulations.[162]

According to the dissenting opinion, therefore, the Government Contract Act provision at issue should constitute a mandatory provision pertaining to statutory validity, restricting the principles of private autonomy and freedom of contract in PPC.[163] The State and counterparty should adjust the contract amount fairly and equitably, considering the risk of loss due to price or currency fluctuations. [164] Any agreement excluding this adjustment should be voided.[165] This conclusion should have been evident in the statutory provision's text, language, public contract nature, legislative intent, and the provision's overall structure, organization, and purpose.[166]

D. *Analysis*

1. General Observations: Is the PPC Private or Public in Nature?

In contract law, autonomy and guardianship are central values, with autonomy serving as the cornerstone.[167] Private autonomy and freedom of contract empower individuals to make decisions for their benefit while competing fairly in the market.[168] However, public contracts differ from private contracts between individuals in that they directly or indirectly impact public interests, are funded by taxes, and are often entered into and

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[160] *Id.*

[161] *Id.*

[162] *Id.*

[163] *Id.*

[164] Daebeobwon [S. Ct.], Dec. 21, 2017, 2012Da74076 (S. Kor.) (Justice Kim Jae-hyoung and Justice Ko Young-han, dissenting).

[165] *Id.*

[166] *Id.*

[167] KWON YOUNG-JOON, MINBEOBPANLYEYEONGU I [CIVIL LAW CASE STUDIES I] 221-232 (2019) (S. Kor.).

[168] *See generally* Lee Byung-Jun, *supra* note 18.

implemented under the influence of the State.[169] Consequently, forming, performing, and terminating public contracts requires a nuanced approach, considering each case's unique characteristics instead of merely applying the principles intended for private contracts.

In this regard, this equality is often unattainable because in most PPCs, a private contracting party often lacks leverage to negotiate terms, hindering their ability to alter unreasonable fixed contract amount covenants.[170] On the other hand, public officials typically favor fixed contract amount covenants for their convenience, predictability, and budget savings. In the landmark case of *2015Da215526*, the Supreme Court ruled on the validity of special terms, excluding contract price adjustments under the Government Contract Act.[171] The Court held that such terms are not inherently invalid because they represent the brainchild of party autonomy par excellence.[172] However, they may be deemed invalid if they unjustifiably restrict the counterparty's contractual interests, thereby violating Article 4 of the Enforcement Decree of the Government Contract Act.[173]

It is important to note, however, that while the validity of these terms is subject to the principles of freedom of contract and private autonomy in the realm of civil law, their analysis should be approached in terms of controlling the discretion of the contracting officer in shaping the contract within the domain of government contract law.[174]

This is true considering Article 19 of the Government Contract Act does not appear to preclude the contracting officer's discretion to establish a contract for the adjustment of the contract amount in the public interest.[175] In order to ensure the validity of the holding in *2015Da215526*, the court should apply the strict application of Article 4 of the Enforcement Decree of State Contract Act. Such an initiative is likely to entail meaningful judicial oversight over any special terms that exclude the adjustment of the contract amount. In this regard, the government may also find it desirable to improve the bidding process to provide sufficient information for pricing with a view toward achieving a rational allocation of risks related to the adjustment of

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[169] Daebeobwon [S. Ct.], Dec. 21, 2017, 2012Da74076 (S. Kor.) (Justice Kim Jae-hyoung and Justice Ko Young-han, dissenting).

[170] Kwon, Youngjoon, *A General Review on the Supreme Court Decisions on Civil Cases in 2018,* 60 SEOUL L. J. 255, 325 (2019).

[171] Daebeobwon [S. Ct.], Dec. 21, 2017, 2012Da74076 (S. Kor.).

[172] *Id.*

[173] Daebeobwon [S. Ct.], Dec. 21, 2017, 2012Da74076 (S. Kor.) (Justice Kim Chang-suk and Justice Jo Hee-de, concurring in support of the majority opinion).

[174] Daebeobwon [S. Ct.], Dec. 21, 2017, 2012Da74076 (S. Kor.) (Justice Kim Jae-hyoung and Justice Ko Young-han, dissenting).

[175] *Id*.

the contract amount, accompanied by legislative initiatives to clearly identify mandatory provisions under the Government Contract Act.[176]

2. Contradictory Case Law

In contrast to the Court's interpretation of the Government Contract Act in *2015Da215526*, the highest court of the RoK has emphasized in other cases the importance of the legal requirements and procedures that must be followed in the context of the Government Contract Act.[177] Thus, in relation to Article 11 of the Government Contract Act,[178] the Court ruled that under the Government Contract Act and other relevant laws, it is mandatory to produce a written contract that explicitly spells out the purpose of the agreement, contract amount, performance period, contract guarantee, liquidated damages, and any other necessary details when seeking to enter into a contract.[179] The contract becomes binding once it has been signed, sealed, or marked with the names of the responsible government officials and the other party, as required by law.[180] Judicial decisions have established that, as outlined in Article 11 of the Government Contract Act, the State's adherence to legal requirements and procedures during the negotiation and finalization of contracts is a mandatory prerequisite for a valid PPC.[181] Consequently, the State must ensure compliance with these legal mandates and procedures when entering into a contract or facing the

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[176] *See generally* Lim Sung-hoon, *Validity of the Special Terms Excluding the Adjustment of Contract Amount in Public Contract*, 23 STUD. ON PUB. ADMINISTRATION CASES 311-350 (2018).

[177] Daebeobwon [S. Ct.], Jan. 27, 2004, 2003Da14812 (S. Kor.).

[178] Guggaleul dangsajalo haneun gyeyag-e gwanhan beoblyul [Act on Contracts to which the State is a Party], art. 11 (S. Kor.). This provision requires the State to prepare contracts, with signatures or seals from officials and contracting parties, in entering into a PPC.

[179] Daebeobwon [S. Ct.], Jan. 27, 2004, 2003Da14812 (S. Kor.). Likewise, even if a contract has been concluded between the State and a private party, without complying with the requirements and procedures set forth in art. 11 of the Government Contract Act, such a contract would be invalid. *See* Daebeobwon [S. Ct.], Jan. 15, 2015, 2013Da215133 (S. Kor.). The Court's jurisprudence on art. 11 of the Government Contract Act reflects that the legal requirements and procedures contained in the Government Contract Act provision are mandatory and determine the validity of PPCs between the state and private parties. This decision appears to regard the provisions regarding the formation of contracts in the Government Contract Act as a mandatory regulation that affects the effectiveness of PPCs, rather than a mere guideline for public officials to ensure fair and efficient management of contracts between the state and private parties.

[180] In the context of the RoK Government Contract Act, see article 11. *See* Article 14 of the Local Government Contract Act, which imposes identical obligations on the local government.

[181] CHUNG, TAE HAK ET AL., *supra* note 62, at 169-170.

possibility of the contract being deemed void.[182]

Meanwhile, with respect to Article 15 of the Government Contract Act, the Court has held that, if the government receives a demand for payment from the counterparty under a contract, it is required to make the payment within the specified period as outlined in Article 58(1) of the Enforcement Decree to the Government Contract Act's other related laws.[183] If the government fails to pay within this period, it may be liable to pay interest as specified by the relevant provisions on interest for delayed payment of consideration.[184] Such liability is regarded as a mandatory regulation.[185]

For example, in a case where a contractor entered into an agreement with the Defense Acquisition Program Administration (DAPA), the contractor claimed that it had incurred additional costs due to changes in exchange rates and inflation.[186] The Court held that any request for an increase in contract amount must be approved by the government as it

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[182] Daebeobwon [S. Ct.], May 27, 2005, 2004Da30811, 2004Da30828 (S. Kor.).

[183] Guggaleul dangsajalo haneun gyeyag-e gwanhan beoblyul [Act on Contracts to which the State is a Party], art. 15 (S. Kor.). Under this provision, for contracts involving construction, manufacturing, purchasing, services, or any other contract that burdens the RoK National Treasury, the head or contract officer of each central government agency must pay the price after an inspection or creating an inspection record (para. 1). The price must be paid by the deadline specified by the Presidential Enforcement Decree (i.e. 5 days) after receiving the invoice, but if payment is not possible by the deadline, interest for the overdue days will be paid as prescribed by the Presidential Enforcement Decree (para 2); Guggaleul dangsajalo haneun gyeyag-e beobyul sihaengryung [Guggagyeyagbeob sihaengryung] [Enforcement Decree of the Act on Contracts to which the State is a Party] art. 58 para. 1 (S. Kor.).

[184] Guggaleul dangsajalo haneun gyeyag-e beobyul sihaengryung [Guggagyeyagbeob sihaengryung] [Enforcement Decree of the Act on Contracts to which the State is a Party] art. 58 para. 2 (S. Kor.).

[185] Daebeobwon [S. Ct.], Oct. 12, 2018, 2015Da256794 (S. Kor.).

[186] DAPA, which was first set up in 2006 in order to enhance transparency, efficiency and specialty by integrating disperse institutions responsible for defense capability improvement programs including the Korean Ministry of National Defense, Army, Navy, and Air Force, is responsible for the procurement of domestic and overseas defense goods and services for Korean militaries. *See* ABOUT DAPA, https://www.dapa.go.kr/dapa_en/sub.do?menuId=412 (last visited June 17, 2022). Pursuant to Article 18 of the Defense Acquisition Program Law (titled Research and Development), No. 8852 (Feb. 29, 2008), DAPA Commissioner is responsible for securing the core technology necessary for the research and development of weapons systems. And pursuant to the Enforcement Decree to the Agency for Defense Development Law, ADD, which is the sole defense research tank in the RoK, operates under the fiscal and operational oversight of DAPA. Head of DAPA or Commissioner sits on the ADD Board of Directors. *See* Enforcement Decree of the Agency for Dense Development Law [In Korean], Presidential Decree No. 23610 (2010), art. 9, 10 and 20 (S. Korea); Daebeobwon [S. Ct.], Nov. 9, 2017, 2015Da215526 (S. Kor.).

constitutes a demand for an increase in government funding.[187] The Court further emphasized that the agreement in question pertained to the development of core components for the Korean military helicopter project, which entailed transferring the right to use the technology to the contractor for the purpose of securing the basis for independent production of military or civilian helicopters in due course.[188] The agreement therefore constituted a public contract, and any dispute out of it was subject to administrative litigation.[189] This ruling underscores the principle that the government's involvement in contracts with private parties may go beyond mere commercial transactions, and that any disputes arising from such contracts may involve public law issues that are to be resolved by way of administrative litigation.[190]

3. Comparative Analysis (vs. Federal Acquisition Regulation)

Comparing *2012Da74076* with the previous cases, it appears that the criteria for determining whether a given PPC is a public law contract or a private law contract are not yet well established in academia or practice.[191] In fact, this area continues to have ongoing debates among legal scholars, including civil law experts.[192] In the meantime, as evidenced by the jurisprudence, it is fairly evident that specific provisions within the Government Contract Act impose limitations on contractual freedom. These limitations encompass the liberty of parties to select their partners, the freedom to determine the preferred method of contract formation, and many other contractual issues.[193]Comparative Analysis (vs. Federal Acquisition

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[187] Daebeobwon [S. Ct.], Nov. 9, 2017, 2015Da215526 (S. Kor.).

[188] *Id.*

[189] *Id.*

[190] *Id.*

[191] *See generally* Kim Daein, *Research & Development Agreement and the Distinction between Public Law and Private Law — Commentary on the Supreme Court of Korea,* 9 November, 2017, 2015 Da 215526, 26 SEOUL L. REV. 222-258 (2018).

[192] *Id*. at 231-232.

[193] The Government Contract Act contains a provision restricting the principle of freedom to make contracts, taking into account the peculiarities of public contracts that aim to achieve the public interest, even if the PPC itself is considered private in legal nature. Especially with regard to the freedom of parties to choose a contracting partner, while in principle, open competition is the norm in relation to a PPC and related tenders (Article 7), the eligibility of a bidder may be restricted if there is concern that fair competition or proper contract performance may be compromised, or if the bidder is involved in tax evasion or any enumerated illegal activity (Article 27, paragraph 1, Article 27-5, paragraph 1). See in this regard, Lee Young-sun, *Effectiveness of an Agreement Excluding the Application of the Provision on the Adjustment of Contract Amount due to Price Fluctuation under the Act on Contracts to Which the State Is a Party*, 43 JURIS 587-625 (2014). Unlike other civil law, private contracts, which do not require a specific form of expression regarding the freedom

Regulation)

In the United States, a "public contract" is a contract to which the executive branch of the United States is a party.[194] These are contracts "where the sovereign steps off the throne and engages in purchase and sale of goods, lands, and services, transactions such as private parties, individuals, or corporations also engage in among themselves." [195] Government contracts are subject to various statutes, such as the Competition in Contracting Act, the Federal Acquisition Streamlining Act and numerous regulations that oversee acquisitions made by executive branch agencies. The primary regulatory framework governing government acquisitions is the Federal Acquisition Regulation (FAR), which is codified in Title 48, Chapter 1, Parts 1-53 of the Code of Federal Regulations.[196] In addition to the FAR, executive branch agencies have the authority to issue their own regulatory supplements such as the Defense Federal Acquisition Regulation Supplement (DFARS), which governs defense-related acquisitions. [197] These supplements are intended to further clarify and specify the FAR's requirements and provisions. The FAR is amended through the Administrative Procedure Act and proposed changes are jointly issued by the FAR Council, which includes members from the Department of Defense (DoD), General Services Administration (GSA), and National Aeronautics and Space Administration (NASA).[198]

Under the FAR, a firm-fixed-price (FFP) contract in principle establishes an unchangeable price, unaffected by the contractor's cost

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of contracting method, the Government Contract Act mandates a specific form of expression. Thus, when concluding a PPC, a contract document that clearly specifies the purpose of the contract, the contract amount, the performance period, the contract guarantee deposit, the risk burden, the delay damages, and other necessary matters must be prepared (Article 11). Guggaleul dangsajalo haneun gyeyag-e gwanhan beoblyul [Act on Contracts to which the State is a Party], art. 11 (S. Kor.). Contracts that do not meet these requirements and procedures set forth at law are invalid. *See* in this regard *e.g.*, Daebeobwon [S. Ct.], Jan. 27, 2004, 2003Da14812 (S. Kor.).

[194] 41 U.S.C. § 1121 (2023) codifies general laws of the United States relating to public contracts.

[195] Kania v. United States, 650 F.2d 264, 268 (Fed. Cir. 1981).

[196] Competition in Contracting Act of 1984 (CICA), 41 U.S.C. § 253 (2022); Defense Federal Acquisition Regulation Supplement (DFARS), 48 C.F.R. pts. 201-299 (2023); Federal Acquisition Regulation (FAR), 48 C.F.R. (2023); 48 C.F.R. ch. 1, pts. 1-53.

[197] Federal Acquisition Streamlining Act (FASA) of 1994, Pub. L. No. 103-355, 108 Stat. 3243

[198] Administrative Procedure Act (APA) of 1946, 5 U.S.C. §§ 551-559, 701-706 (2022); Office of Federal Procurement Policy Act Amendments of 1988, Pub. L. No. 100-679, 102 Stat. 4056 (1988).

experience during contract execution.[199] This arrangement places the highest risk on the contractor, holding them fully accountable for all costs, profits, and losses.[200] It offers the contractor strong motivation to manage costs and ensure optimal performance, while also minimizing the administrative demands on both parties involved.[201] Courts have interpreted the FAR to preclude adjustments or reimbursements for the value of fixed-price contracts.[202] This means that if a contractor enters into a fixed-price contract with the government and incurs costs that exceed the contract price, they typically cannot recover those additional costs. In a fixed-price contract, the contractor is responsible for all costs and resulting profits or losses.[203] In cases where the cost of the agreed-upon services surpasses the contracted price, the contractor is responsible for bearing the financial burden.[204] Conversely, if the costs are lower than the contract price, the contractor can realize a profit.[205]

According to a recent guidance from the DoD, even where inflation has caused increased costs for contractors, fixed-price contracts typically do not provide for any price adjustments based on the contractor's cost of performance.[206] As a result, contractors are responsible for any cost overruns.[207] This can create challenges for contractors when inflation increases their costs of performance beyond what they anticipated. For firm-fixed price contracts specifically, the DoD advises its contracting officers (COs) to reject requests for equitable adjustments (REAs) attributed to "unanticipated inflation."[208] The DoD's stance in this regard is that inflation is not considered a modification to the project's scope of work, but rather, an altered economic situation that does not warrant additional compensation.[209]

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[199] Fed. Acquisition Reg. § 16.202-1.

[200] *Id. See also* Prime v. Post, Buckley, Schuh & Jernigan, Inc., No. 6:10-CV-1950-ORL-36, 2013 WL 4506357, at 9 (M.D. Fla. Aug. 23, 2013).

[201] Fed. Acquisition Reg. § 16.202-1.

[202] *See* Info. Sys. & Networks Corp. v. United States, 64 Fed. Cl. 599, 606 (2005).

[203] S & B/BIBB Hines PB 3 Joint Venture v. Progress Energy Florida, Inc., 365 F. App'x 202, 203 (11th Cir. 2010).

[204] *Id.*

[205] *Id.*

[206] OFFICE OF THE UNDER SECRETARY OF DEFENSE, GUIDANCE ON INFLATION AND ECONOMIC PRICE ADJUSTMENTS, (May 25, 2022), https://federalnewsnetwork.com/wp-content/uploads/2022/05/DPC-Guidance-on-Inflation-and-EPA-25-May-2022.pdf (hereinafter, "DoD Guidance").

[207] *Id.*

[208] *Id.*

[209] *Id.*

For FFP contracts, there can be no modification to the contract price unless (a) there is a valid change order duly issued by the contracting officer[210] or (b) the contract contains a valid Economic Price Adjustment

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[210] The relevant FAR provision provides as follows:

52.243-4 Changes.

As prescribed in 43.205(d), insert the following clause. The 30-day period may be varied according to agency procedures.

Changes (JUN 2007)

(a) The Contracting Officer may, at any time, without notice to the sureties, if any, by written order designated or indicated to be a change order, make changes in the work within the general scope of the contract, including changes -

(1) In the specifications (including drawings and designs);

(2) In the method or manner of performance of the work;

(3) In the Government-furnished property or services; or

(4) Directing acceleration in the performance of the work.

(b) Any other written or oral order (which, as used in this paragraph (b), includes direction, instruction, interpretation, or determination) from the Contracting Officer that causes a change shall be treated as a change order under this clause; provided, that the Contractor gives the Contracting Officer written notice stating (1) the date, circumstances, and source of the order and (2) that the Contractor regards the order as a change order.

(c) Except as provided in this clause, no order, statement, or conduct of the Contracting Officer shall be treated as a change under this clause or entitle the Contractor to an equitable adjustment.

(d) If any change under this clause causes an increase or decrease in the Contractor's cost of, or the time required for, the performance of any part of the work under this contract, whether or not changed by any such order, the Contracting Officer shall make an equitable adjustment and modify the contract in writing. However, except for an adjustment based on defective specifications, no adjustment for any change under paragraph (b) of this clause shall be made for any costs incurred more than 20 days before the Contractor gives written notice as required. In the case of defective specifications for which the Government is responsible, the equitable adjustment shall include any increased cost reasonably incurred by the Contractor in attempting to comply with the defective specifications.

(e) The Contractor must assert its right to an adjustment under this clause within 30 days after (1) receipt of a written change order under paragraph (a) of this clause or (2) the furnishing of a written notice under paragraph (b) of this clause, by submitting to the Contracting Officer a written statement describing the general nature and amount of proposal, unless this period is extended by the Government. The statement of proposal for adjustment may be included in the notice under paragraph (b) above.

(f) No proposal by the Contractor for an equitable adjustment shall be allowed if asserted after final payment under this contract.

(End of clause)

48 Fed. Reg. 42,478 (Sept. 19, 1983) (amended by 52 Fed. Reg. 30,079 (Aug. 12, 1987); 72 Fed. Reg. 27,389 (May 15, 2007)).

(EPA) clause.[211] In terms of the change order, the contracting officer can make changes to the work, specifications, method of performance, use of government-furnished property or services by written order. [212] The contractor may treat any change resulting from a written or verbal order as a change order, provided that written notice to that effect is furnished.[213] In the event that a change results in an increase or decrease in the cost or time required to perform the contracted services, the contractor has the right to seek an equitable[214] To do so, the contractor must submit a written statement within 30 days.[215]

In terms of the EPA clause, the EPA is a mechanism used in contracts based on the cost index of labor or material.[216] It is typically utilized under three circumstances: (1) when the contract encompasses an extended period of performance, and significant costs will be incurred more than one year after the start of performance; (2) when the sum of the contract amount that can be adjusted is considerable; and (3) when the economic conditions concerning labor and materials are so unpredictable that it is unreasonable to apportion risk between the contractor and the government without the inclusion of an EPA clause, as defined in the Federal Acquisition Regulation (FAR) of 2017.[217] With an EPA clause, the contract price can be adjusted either upward or downward in response to specified contingencies in the clause.[218]

4. Christian Doctrine

U.S. government contract law includes the Christian Doctrine, which mandates the inclusion of a significant or deeply ingrained public

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[211] *See* DoD guidance, *supra* note 206.

[212] *Id.*

[213] 48 Fed. Reg. 42,478 (Sept. 19, 1983) (amended by 52 Fed. Reg. 30,079 (Aug. 12, 1987); 72 Fed. Reg. 27,389 (May 15, 2007)).

[214] According to relevant jurisprudence, equitable adjustments are implemented to maintain the contractor's financial standing when the government modifies a contract, serving as corrective measures. The main objective of these adjustments is to protect the contractor from incurring additional expenses as a result of the modification. Hence, it is evident that the compensation awarded to the contractor should be linked to their revised position in light of the modification, rather than being based solely on the value received by the government. *See* Nager Electric Company v. United States, 442 F.2d 936 (Fed. Cir. 1971).

[215] 48 Fed. Reg. 42,478 (Sept. 19, 1983) (amended by 52 Fed. Reg. 30,079 (Aug. 12, 1987); 72 Fed. Reg. 27,389 (May 15, 2007)).

[216] 48 C.F.R. § 16.203-1.

[217] *Id.*

[218] *Id.*

procurement policy in a government contract.[219] In other words, the Christian Doctrine operates on the principle that such policies are automatically incorporated into contracts by law. The Christian Doctrine originated from the *G.L. Christian & Associates* case, which involved the U.S. Army's cancellation of a contract for housing construction due to Fort Polk's deactivation.[220] The contractor filed claims for breach of contract, as the Army did not have a Termination for Convenience clause in the contract, which would have allowed for termination without liability.[221] The Court of Claims found that a Termination for Convenience provision was required by law and should be read into the contract, thus relieving the Army of liability.[222] Subsequent cases, such as *S.J. Amoroso Construction Company v. United States* and *General Engineering & Machine Works v. O'Keefe*, limited the scope of the Christian Doctrine, stating that courts must only consider including contract provisions by operation of law if they are both mandatory and express "a significant or deeply ingrained strand of public procurement policy."[223]

Whether the EPA clause is subject to the Christian Doctrine is unchartered territory. In a recent case, however, involving a decision by the Armed Services Board of Contract Appeals, a contractor was denied the ability to recoup higher labor expenses stemming from an increase in the minimum wage in the RoK due to a contracting officer's deliberate omission of an EPA clause.[224] Therefore, an intentional exclusion of an EPA clause in a contract would likely preclude a recovery of increased costs in a firm-fixed price contract.[225] This ruling implies that if an EPA clause is intentionally left out of a contract, it is likely to prevent the contractor from recovering any increased costs associated with a firm-fixed price

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[219] *See generally* J.P. Shedd, *The Christian Doctrine, Force and Effect of Law, and Effect of Illegality on Government Contracts*, 9 PUB. CONT. L.J. 1(1977).

[220] G.L. Christian & Associates v. United States, 312 F.2d 418 (Ct. Cl. 1963).

[221] *Id.*

[222] *Id.*

[223] S.J. Amoroso Const. Co. v. United States, 12 F.3d 1072, 1073 (Fed. Cir. 1993); Gen. Eng'g & Mach. Works v. O'Keefe, 991 F.2d 775, 777 (Fed. Cir. 1993); Judge Plager critiqued the "significant or deeply ingrained" element of the Christian doctrine standard, stating that it is "tied to anything or nothing, and is therefore inherently unpredictable." S.J. Amoroso Const. Co. v. United States, 12 F.3d 1072, 1079 (Fed. Cir. 1993). *See* in this regard, Michael D Pangia, *The Unpredictable and Often Misunderstood Christian Doctrine of Government Contracts: Proposed Approaches for Removing Harmful Uncertainty*, PUB. CONT. L.J. 617, 637 (2020).

[224] *See* Appeals of -- Kf&s Corp., ASBCA No. 62223, 21-1 B.C.A. (CCH) ¶ 37759 (Dec. 9, 2020).

[225] *Id.*

contract.[226] Consequently, applying the Christian Doctrine to such cases may not be straightforward because the doctrine typically considers the inclusion of mandatory clauses that express a significant or deeply ingrained strand of public procurement policy.

E. *Further Analysis*

As per the Government Contract Act, PPCs are categorized into two types in terms of cost structure: fixed-price contracts and cost-plus contracts.[227] Typically, the contracting agency estimates the price before executing the contract and chooses the successful bidder through a bidding or negotiation process.[228] Based on this selection, the contract amount is established, and the entire subject matter of the contract is bid on or negotiated on a lump-sum basis.[229] Consequently, the total fixed-price contract emerges as the fundamental form of PPC.[230]

Not unlike the FAR regime, fixed-price contracts under Korea's Government Contract Act typically do not provide for any price adjustments based on the contractor's cost experience in performing the contract, which means that contractors are responsible for cost overruns in the absence of any special agreement or covenant to the contrary between the parties to a PPC.[231] For example, in *2015Da215526*, the government and the

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[226] In a 2016 Armed Services Board of Contract Appeals (ASBCA) case involving Lockheed Martin Integrated Systems, Inc. (LMIS), the ASBCA ruled in favor of LMIS after the Defense Contract Audit Agency (DCAA) accused them of failing to manage subcontractors and challenged over $127 million in reimbursed subcontract costs. Lockheed Martin Integrated Sys., Inc., ASBCA No. 59508, 17-1 B.C.A. (CCH) ¶ 36597 (Dec. 20, 2016). The ASBCA found that the government failed to establish a valid contractual duty for LMIS to manage its subcontractors as per FAR 42.202. *Id.* This case highlights the importance of including a FAR clause, specifically FAR 42.202, in a government contract to ensure a prime contractor's obligation to oversee subcontractor costs, as there is no generic contractual obligation for prime contractors to manage subcontracts without this clause.

[227] JUNG WON, ONJU GUGGALEULDANGSAJALOHANEUNGYEYAG-E GWANHANBEOBLYUL JE23JOU [ONJU GOV'T CONT. ACT ART.23] 1 (2023) (S. Kor.). Meanwhile, under art. 23.1 of the Government Contract Act, cost-plus contracts are concluded when it is difficult to fix a contract price at the time of contract; such price is fixed in due course while the contract is being performed. *See* Guggaleul dangsajalo haneun gyeyag-e gwanhan beoblyul [Act on Contracts to which the State is a Party], art. 23 para. 1 (S. Kor.). For a discussion on cost-plus contracts in the context of defense procurements, *see* KIM HYUN SOO, BANGWISAEOBBEOBUIIHAE [UNDERSTANDING OF DEFENSE ACQUISITION PROCUREMENT LAW] 155 (2020) (S. Kor.) [hereinafter "SH Kim"]

[228] *See* Jung Won, *supra* note 227.

[229] *Id.*

[230] CHUNG, TAE HAK ET AL., *supra* note 62, at 312.

[231] Daebeobwon [S. Ct.], Jan. 28, 2016, 2013Da207958 (S. Kor.) (if a defense contractor has entered into a subcontract on a firm and fixed basis, the contract price gets

counterparty chose not to carve out any exception to this underlying nature of fixed-price contracts when it came to overseas supplies involving foreign currencies.[232] The state of contractual terms was within the parties' discretion under the freedom of contract, and as the majority opined, this outcome was in alignment with the legal nature of PPCs constituting private agreements based on the principles of private law.[233] According to the majority, given such mutual agreement on the foreign supplies at issue stemmed from the fact that what was involved was a firm and fixed contract, under which the risk of any increase or decrease in prices solely rests with the contractor.[234]

In the absence of any dogmatic equivalent of the Christian doctrine in the RoK, the majority opinion makes sense. Determining otherwise and thus holding that Article 19 of the Government Contract Act constitutes a mandatory provision that can be foisted after-the-fact on the government even in the absence of an agreement to the contrary would be tantamount to dismantling the basis of the Government Contract Act system largely based on firm and fixed contracts. Such a finding would be detrimental to the ongoing maintenance of legal certainty.

Furthermore, the majority's finding came with the stipulation that contracting officers must avoid incorporating special terms or conditions that could be detrimental to a counterparty's interests.[235] To determine whether a special agreement in a public contract violates the contracting counterparty's legitimate interests and reasonable expectations, it is inadequate to simply establish that the agreement is somewhat disadvantageous to the counterparty. Rather, it is necessary for the counterparty to prove that the special agreement unjustly disadvantages the contracting counterparty as a result of the state's inclusion of the agreement in the contract.[236] Assessing whether specific terms and conditions unfairly restrict a counterparty's contractual interests demands a thorough examination of multiple factors, such as the extent of potential harm to the counterparty, the probability of disadvantage occurring, the impact on the overall contract, the events preceding the contract's execution, and pertinent statutory and regulatory provisions.

This article has explored the topic of cost adjustment under the

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fixed at the time of the contract and the reasonableness of the subcontract amount should be determined as of the time of the subcontract).

[232] Daebeobwon [S. Ct.], Nov. 9, 2017, 2015Da215526 (S. Kor.).

[233] *Id.*

[234] Daebeobwon [S. Ct.], Dec. 21, 2017, 2012Da74076 (S. Kor.) (Justice Kim Chang-suk and Justice Jo Hee-de, concurring in support of the majority opinion).

[235] *Id*.

[236] *Id.*

Government Contract Act, including relevant legal cases and a comparative analysis, all within the context of the Thesis. It now shifts its focus to the subject of liquidated damages.

VI. LIQUIDATED DAMAGES

In the RoK's civil law regime, Liquidated Damages (LD) involve pre-estimating damages payable by a debtor in case of a contract breach.[237] LD streamlines the legal relationship between parties, simplifying the process of obtaining damages and reducing litigation risks and their related costs.[238] LD agreements are triggered by a specific breach and the amount is agreed upon in advance by both parties.[239] The purpose of including LD clauses in contracts is to provide a pre-agreed upon amount to be paid in the event of a breach of contract by one of the parties.[240] The LD amount serves as a fair estimation of the damages that could arise from a breach and helps to avoid disputes in case of a breach.[241]

Under the rubric of the Government Contract Act, LD pertains to the sum a contractor must pay the government if they delay contract performance without good cause.[242] This pre-agreed penalty incentivizes contractors to fulfil their milestone-based obligations. To impose LD, a contract must have a clear, enforceable LD clause outlining the circumstances under which it will be triggered, and the event must then occur.[243] In government contracts, the government pays the contractor, who in turn performs obligations like providing goods or services. If the government defaults, the other party is generally entitled to interest on late payments.[244] However, without an express late performance provision, it becomes difficult for the government to prove the connection between a contractor's default and the damages

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[237] JEE1, *supra* note 9, at 1143.

[238] *See* Daebeobwon [S. Ct.], Mar. 27, 1991, 90Da14478 (S. Kor.); and Daebeobwon [S. Ct.], Apr. 23, 1993, 92Da41719 (S. Kor.).

[239] *See* Daebeobwon [S. Ct.], Feb. 28, 1997, 96Da49933 (S. Kor.); and Daebeobwon [S. Ct.], Mar. 27, 1998, 97Da36996 (S. Kor.).

[240] *See* Daebeobwon [S. Ct.], Mar. 27, 1991, 90Da14478 (S. Kor.); Daebeobwon [S. Ct.], Apr. 23, 1992, 92Da41719 (S. Kor.); and Daebeobwon [S. Ct.], Dec. 12, 1995, 95Da28526 (S. Kor.).

[241] *Id*.

[242] Guggaleul dangsajalo haneun gyeyag-e gwanhan beoblyul [Act on Contracts to which the State is a Party], art. 26 (S. Kor.). *See also* CHUNG, TAE HAK ET AL., *supra* note 62, at 312.

[243] KANG HYUN ET AL., JUSEOG GUGGAGYEYAGBEOB [ANNOTATED GOVERNMENT CONTRACT ACT] 433 (2017) (S. Kor.).

[244] Guggaleul dangsajalo haneun gyeyag-e gwanhan beoblyul [Act on Contracts to which the State is a Party], art. 27 para. 1 (S. Kor.).

incurred. A LD clause mitigates this risk by establishing a pre-agreed amount payable in case of breach, easing the government's burden of proof and preventing disputes.[245]

A. *Pertinent Laws and Regulations*

1. The Korean Civil Code and Government Contract Act

In the rubric of the Korean Civil Code, LD is codified under Article 398.[246]

> Article 398 (Liquidated Damages)
>
> (1) The parties may determine in advance the amount of damages payable in the event of the non-performance of an obligation.
>
> (2) Where the amount of damages determined in advance is unduly excessive, the court may reduce the amount to a more reasonable and appropriate sum.
>
> (3) The determination in advance of the amount of damages shall not affect the obligee's demand for performance or rescission of the contract.
>
> (4) The agreement of a penalty is presumed to be a pre-determined amount of damages.
>
> (5) Even where the parties have agreed beforehand that something other than money shall be applied as compensation for damages, the provisions of the preceding paragraphs shall apply mutatis mutandis.

Under Article 26 of the Government Contract Act, in the event of a contractor's late or delayed contractual performance without good cause, the government is entitled to levy liquidated damages on the contractor as the approximation of actual damages.[247] In this context, since a contractor's late or delayed performance refers to the contractor's failure to render timely performance, LD is seen as a pre-estimation of damages assessed and levied per each non-excusable day of delay.[248] As envisaged under Article

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[245] KIM SUNG GEUN, JEONGBUGYEYAGBEOB HAESEOL II [GOVERNMENT CONTRACTS ACT COMMENTARY II] 51 (2012) (S. Kor.).

[246] Minbeob [Civil Act] art. 398 (S. Kor.).

[247] Guggaleul dangsajalo haneun gyeyag-e gwanhan beoblyul [Act on Contracts to which the State is a Party], art. 26 (S. Kor.).

[248] YANG CHANG HO, JEONGBUGYEYAGJEDO HAESEOL [GOVERNMENT CONTRACTING EXPLAINED] 468 (2020) (S. Kor.).

74 of the Enforcement Decree to the Government Contract Act, the government shall require the contractor to pay out LD in the event of the contractor's late or delayed performance.[249] The amount of LD will be computed by multiplying the contract price by the rate of LD set forth in the contract as prescribed by Article 75 of the Enforcement Rules to Government Contract Act.[250] In this regard, Article 74(3) of the Enforcement Decree foists a cap on the maximum amount of LD at thirty (30) percent of the contract price.[251]

2. Legal Analysis Including Related Jurisprudence

Liquidated damages in the Republic of Korea are categorized into two types: (i) a pre-estimate of loss, and (ii) a penalty.[252] In the RoK, both (i) and (ii) are recognized but considered distinct. As surveyed above, LD as a pre-estimate of loss involves an agreement between parties to compensate for actual losses resulting from a breach.[253] Meanwhile, a penalty serves dual purposes: it compensates for damages and punishes the party in breach.[254] Korean courts typically uphold penalty clauses.[255]

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[249] Guggaleul dangsajalo haneun gyeyag-e beobyul sihaengryung [Guggagyeyagbeob sihaengryung] [Enforcement Decree of the Act on Contracts to which the State is a Party] art. 74 (S. Kor.).

[250] Under art. 74 of the Enforcement Decree to the Government Contract Act, LD are calculated as follows: LD = (i) contract price x (ii) the rate of LD x (iii) total days of delay. Guggaleul dangsajalo haneun gyeyag-e beobyul sihaengryung [Guggagyeyagbeob sihaengryung] [Enforcement Decree of the Act on Contracts to which the State is a Party] art. 74 (S. Kor.). In relation to this formula, the contract price refers to the amount of contract at the time of contract execution, provided that in the event of any subsequent adjustment to the price due to design changes or price fluctuations, the adjusted contract price is to be used. In cases involving a contract for a long-term continuing construction project, for the long-term continuing manufacture of goods, or for long-term continuing services, the contract price refers to each annual contract price. Lastly, if a completed portion of a contract deliverable has been accepted through an inspection (including portions managed and used without acceptance), provided that such deliverable involves construction or supply of goods or services and is divisible in nature, LD shall be calculated based on the amount computed by subtracting the amount for such portion from the contract price. *Id.*

[251] Guggaleul dangsajalo haneun gyeyag-e beobyul sihaengryung [Guggagyeyagbeob sihaengryung] [Enforcement Decree of the Act on Contracts to which the State is a Party] art. 74 para. 3 (S. Kor.).

[252] KIM JAE-HYUNG, MINBEOBPANLYEBUNSEOG [CIVIL CASE LAW ANALYSIS] 185 (2015) (S. Kor.). *See also* Kim Jae-Hyung, *From Liquidated Damages to Agreed Payment for Non-performance-Can the Court Reduce the Amount of Penalty?*, 21 J. COMP. PRIV. L. 625, 627 (2014) ("Kim Jae-Hyung LD").

[253] *See supra* notes 241 and 242.

[254] *See* Daebeobwon [S. Ct.], Mar. 23, 1993, 92Da46905 (S. Kor.; and Daebeobwon [S. Ct.], Dec. 26, 2013, 2013Da63257 (S. Kor.).

[255] Daebeobwon [S. Ct.], Dec. 10, 2015, 2014Da14511 (S. Kor.).

The key distinction between these categories lies in the court's authority to alter the quantum of pre-estimated loss, which it cannot increase, but can reduce ex officio.[256] However, for penalties, while the claimant may seek compensation for losses exceeding the penalty amount, the court is not allowed to decrease the agreed-upon penalty amount ex officio.[257] Under the provisions of Article 398(4) of the Civil Code, a liquidated damages agreement is assumed to be an estimate of potential losses, unless there are exceptional circumstances.[258] The same assumption applies to a LD clause under the Government Contract Act, but ultimately hinges on the terms of the contract.[259]

Article 398.4 of the Civil Code presumes that a LD agreement, including those under the Government Contract Act, represents an estimate of potential losses, barring exceptional circumstances.[260] In public construction contracts where the Government Contract Act may apply, the Korean Court consistently treats LD clauses as pre-estimates of loss.[261] It has ruled that a LD clause in a construction subcontract is considered an estimate of damages in anticipation of the contractor's delay, given the subcontract's purpose to complete a construction project.[262] Therefore, unless there are special or extenuating circumstances, a subcontractor is obliged to pay LD if they fail to complete the work on time and deliver the finished product to the owner promptly.[263] Furthermore, the Court has recognized that when a construction subcontract incorporates model general terms and conditions of subcontracting published by the Ministry of Land, Infrastructure, and Transport,[264] and if these terms include a LD clause

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[256] *See* Minbeob [Civil Act] art. 398 para. 2 (S. Kor.).

[257] YOON DAE-HAE, PANLYELO IHAEHANEUN GONG-GONG-GYEYAG [UNDERSTANDING PUBLIC CONTRACTS WITH CASE LAW] 226 (2021).

[258] *See* Minbeob [Civil Act] art. 398 para. 4 (S. Kor.).

[259] CHUNG, TAE HAK ET AL., *supra* note 62, at 362., *see also* YOON DAE-HAE, *supra* note 258, at 226.

[260] Minbeob [Civil Act] art. 398 para. 4 (S. Kor.).

[261] *See* Daebeobwon [S. Ct.], Mar. 26, 1999, 98Da26590 (S. Kor.); and Daebeobwon [S. Ct.], Sept. 4, 2002, 2001Da1386 (S. Kor.).

[262] *Id.*

[263] *Id.*

[264] Each model term published by the Ministry under the Enforcement Decree of the Government Contract Act, which covers construction, manufacturing (including the supply of goods), and services, incorporates a provision for Liquidated Damages. See Guggaleul dangsajalo haneun gyeyag-e gwanhan beobyul sihaengryung [Guggagyeyagbeob sihaengryung] [Enforcement Decree of the Act on Contracts to which the State is a Party] art. 46 para. 1 (S. Kor.). In particular, when computing the amount of LD to be levied, the contracting officer is to exclude excusable days of delay, for which delay the contractor is not responsible due to the causes listed in each set of model terms,

alongside a clause on damages payment in case of contract termination or cancellation, the LD clause is considered a pre-estimate of damages, which may be invoked if the subcontractor does not perform their obligations timely.[265]

The primary function of a LD clause is to pre-estimate damages that a debtor must pay in case of a contract breach.[266] LD effectively reduces the creditor's burden of proving the existence and amount of loss, minimizes potential disputes between parties regarding the presence and quantum of losses, and encourages the debtor to comply with the contract terms.[267] Consequently, even if the debtor demonstrates that no loss has occurred or that the actual loss is less than the pre-estimated damages, they are still required to compensate the creditor according to the terms of the LD clause.[268] Conversely, even if the creditor can prove that the incurred loss exceeds the pre-estimated damages' maximum amount, they are not entitled to the excess unless a separate agreement states otherwise.[269]

According to Article 398(2) of the Korean Civil Code, the court may reduce an unduly excessive predetermined damages amount to a more reasonable and appropriate sum.[270] To determine whether LD is excessively high, the court considers the total amount of LD payable, not the rate specified in the LD clause.[271] While exercising its discretion under Article 398.2, the court deems a LD clause excessive in consideration of the totality of relevant circumstances, such as the contracting parties' status, the agreement's purpose and related terms, rationale behind the LD clause, the proportion of pre-estimated damages compared to the total contract price,

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from the total days of delay. *See e.g.*, Gongsagyeyag-ilbanjogeon [General Conditions for Construction Contracts], art. 25 (S. Kor.).

[265] Daebeobwon [S. Ct.], Mar. 26, 1999, 98Da26590 (S. Kor.); and Daebeobwon [S. Ct.], Sept. 4, 2002, 2001Da1386 (S. Kor.).

[266] Daebeobwon [S. Ct.], Apr. 23, 1993, 92Da41719 (S. Kor.); and Daebeobwon [S. Ct.], Dec. 12, 1995, 95Da28526 (S. Kor.).

[267] Daebeobwon [S. Ct.], Nov. 13, 2008, 2008Da46906 (S. Kor.).

[268] *Id*.

[269] Daebeobwon [S. Ct.], Sept. 27, 1988, 86Daka2375 (main suit), 86Daka2376 (counter suit) (S. Kor.).

[270] Minbeob [Civil Act] art. 398 para. 2 (S. Kor.).

[271] Daebeobwon [S. Ct.], Sept. 4, 2002, 2001Da1386 (S. Kor.) (Where a contractor is obligated to pay LD due to the contractor's failure to complete the work and deliver it to the counter-party within the agreed period, the court may, pursuant to art. 398(2) of the Civil Code, reduce the amount of LD by considering all pertinent circumstances such as the status of the contracting party, the purpose and content of the contract, the motive behind LD, the amount of LD compared to that of the actual damages, and custom and practice and economic situations at that time).

and the anticipated loss volume.[272] These factors help ascertain whether the LD payable is unfairly oppressive against the debtor, warranting a reduction in line with prevailing social norms.[273] It is essential to note that determining the existence of factors warranting a reduction in LD and the extent of such reduction falls solely under the purview of the fact-trier.[274]

3. The Concept of Liquidated Damages Under FAR

According to Black's Law Dictionary, the term "liquidated damages" is defined as "[a]n amount contractually stipulated as a reasonable estimation of actual damages to be recovered by one party if the other party breaches."[275] Consistent with this definition, parties entering into a contract may stipulate the damages to be paid in case of a breach, provided that such provisions align with the principle of compensation.[276] In this context, a LD clause serves as a pre-agreed amount of damages that will be payable in the event of a contract breach.[277] The clause provides certainty and clarity for both parties regarding the amount of damages that will be payable if the contract is breached. The LD mechanism can avoid the need for a lengthy and costly process of determining actual damages and provides a quicker resolution of the dispute.[278]

While contract law may differ from state to state under the United States common law system, many jurisdictions in the United States have adopted the American Law Institute's Second Restatement of Contracts (the Restatement) as a means of determining the enforceability of LD provisions

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[272] Daebeobwon [S. Ct.], Dec. 26, 2013, 2013Da213090 (S. Kor.) (If a contract stipulates delayed damages for a debtor's failure to perform, and the pre-estimated amount of damages is subject to court review for excessiveness, it is necessary to consider whether enforcing the pre-estimated quantum of damages would lead to unfairness between the parties, in light of their respective economic positions, the contractual terms and their objectives, the circumstances that led to the establishment of the stipulated damages, the proportion of the damages to the debt amount, the magnitude of the pre-estimated damages, the prevailing trade practices and economic conditions, and the nature of the debtor's breach). *See also* Daebeobwon [S. Ct.], Aug. 18, 2017, 2017Da228762 (S. Kor.); and Daebeobwon [S. Ct.], July 11, 2017, 2016Da52265(S. Kor.).

[273] Daebeobwon [S. Ct.], Dec. 26, 2013, 2013Da213090 (S. Kor.).

[274] YANG CHANG HO, *supra* note 249, at 474.

[275] *Damages*, BLACK'S LAW DICTIONARY (11th ed. 2019).

[276] Rohlin Const. Co. v. City of Hinton, 476 N.W.2d 78 (Iowa 1991).

[277] Jennie-O Foods, Inc., 580 F.2d at 413-14; *see also* FAR 48 C.F.R. §11.501. (noting that use of a liquidated damages clause is proper if damages "would be difficult or impossible to estimate accurately or prove" and that the "rate must be a reasonable forecast" of the anticipated damages).

[278] Gator Apple, LLC v. App. Tex. Rests., Inc., 442 S.W. 3d 521, 535 (Ct. App. Tex. 2014).

in contracts.[279] The Restatement contains the following provision on Liquidated Damages:

> Damages for breach by either party may be liquidated in the agreement but only at an amount that is reasonable in the light of the anticipated or actual loss caused by the breach and the difficulties of proof of loss. A term fixing unreasonably large liquidated damages is unenforceable on grounds of public policy as a penalty.[280]

> While largely consistent with the conceptual contours of LD in the common law regime, as further noted below, there appears to be no hostility toward LD under the Restatement: The parties to a contract may effectively provide, in advance, the damages that are to be payable in the event of breach as long as the provision does not disregard the principle of compensation. The enforcement of such provisions for liquidated damages saves the time of courts, juries, parties, and witnesses, thereby reducing the expense of litigation. This is especially important if the amount in controversy is relatively small. However, the parties to a contract are not free to provide a penalty for its breach because the central objective behind the system of contract remedies is compensatory, not punitive. Punishment of a promisor for having broken his promise has no justification on either economic or other grounds and a term providing such a penalty is unenforceable on grounds of public policy.[281]

In a similar vein, Section 2-718(1) of the Uniform Commercial Code, which is an all-encompassing legal framework that regulates virtually every aspect of commercial transactions in the United States,[282] provides:

> Damages for breach by either party may be liquidated in the agreement but only at an amount which is reasonable in the light of the anticipated or actual harm caused by the breach, the difficulties of proof of loss, and the inconvenience or

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[279] Such adoptions have provided greater clarity and uniformity for and between contracting parties.

[280] Restatement (Second) of Contracts § 356 (1981).

[281] Restatement (Second) of Contracts § 356 (1981), comment a. parties in a contract can pre-determine the damages payable in case of a breach, as long as it adheres to the principle of compensation. Enforcing liquidated damages provisions helps save time and resources in legal proceedings, especially for small amounts. However, the contract cannot include penalties for breach, as the main goal of contract remedies is to compensate, not to punish. Penalty clauses are unenforceable due to public policy reasons.

[282] *Uniform Commercial Code*, UNIF. L. COMM'N, https://www.uniformlaws.org/acts/ucc (last visited Mar. 27, 2023).

> nonfeasibility of otherwise obtaining an adequate remedy. A term fixing unreasonably large liquidated damages is void as a penalty.[283]

As seen above, "…the fundamental purpose of a valid liquidated damages provision is to provide a reasonable measure of compensation in the event of a breach where, at the time the provision is agreed to the damages are indeterminable or will be otherwise difficult to prove."[284] The main objective of a legitimate liquidated damages clause is to offer a fair amount of compensation in the case of a contract violation when the exact damages at the time of agreement are uncertain or challenging to substantiate.[285]

In assessing whether a given liquidated damages clause is enforceable, the U.S. courts generally examine three elements set out in *Banta V. Stamford Motor Co*.[286] The first is the element of uncertainty, which involves the parties' reasonable *ex ante* expectation that calculation of actual damages caused by the breach will be difficult.[287] In relation to such substantive uncertainty, it was noted that LD "serve a particularly useful function when damages are uncertain in nature or amount or are unmeasurable, as is the case in many government contracts."[288] It was further noted that "…when damages are uncertain or hard to measure, it naturally follows that it is difficult to conclude that a particular liquidated damages amount or rate is an unreasonable projection of what those damages might be."[289]

The second element revolves around whether or not the amount of liquidated losses is a reasonable *ex ante* measure of estimated damages.[290] The key criterion here is the proportionality of liquidated damages to the

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[283] U.C.C. § 2-718(1) (amended 2003).

[284] Williston on Contracts, § 65:3 (4th Ed.).

[285] The LD clause is instrumental in the legal system, especially for contract disputes, by setting predetermined damages for breaches, thus simplifying and hastening dispute resolutions. For instance, a construction contract might specify a completion date and an LD clause imposing a set penalty for each day's delay. Should the company lag behind schedule, the LD clause offers a predetermined compensation, obviating the need for lengthy court proceedings to determine actual damages, such as lost profit or business opportunities. This mechanism ensures prompt resolution and clarity on potential liabilities for both parties.

[286] Banta v. Stamford Motor Co*.,* 89 Conn. 51, 92 A. 665 (Conn. 1914); *See also* In re Dow Corning Corp., 419 F.3d 543 (6th Cir. 2005).

[287] *Id*.

[288] Priebe Sons, Inc. v. United States, 332 U.S. 407, 411 (1947).

[289] DJ Mfg. Corp. v. United States, 86 F.3d 1130, 1134 (Fed. Cir. 1996).

[290] Barry Wright Corp. v. ITT Grinnell Corp., 724 F.2d 227 (1st Cir. 1983).

anticipated harm to the creditor.[291] That said, "[a]t the time the contract is made, a forecast of liquidated damages must be based on a reasonable possibility that the Government will sustain damages if the contract is breached, and the stipulated liquidated amount must be a reasonable estimate of the anticipated harm to the Government."[292] If the amounts levied as liquidated damages by the Government are reasonably related to the Government's anticipated injury, the damages will be considered reasonable, and therefore enforceable.[293] If not, then such losses will be considered contrary to public policy, and hence an unenforceable penalty.[294] As will be further seen and discussed below, the courts will not enforce liquidated damages if they are deemed punitive and not compensatory.[295]

Lastly, the court probes the parties' intention.[296] In this regard, as the Court noted in *Wise*:

> When that intention is clearly ascertainable from the writing, effect will be given to the provision, as freely as to any other, where the damages are uncertain in nature or amount or are difficult of ascertainment or where the amount stipulated for is not so extravagant, or disproportionate to the amount of property loss, as to show that compensation was not the object aimed at or as to imply fraud, mistake, circumvention or oppression.[297]

In determining whether a contract provision intends for liquidated damages or for a penalty, what is determinative of such quest is the intention of the parties to the contract, not the phrase used in the provision.[298]

4. Applicable FAR Provisions

Against the foregoing doctrinal backdrop and related precedents, the FAR contains a LD clause that a Contracting Officer may include as part of construction contracts, with the exception of any cost-plus-fixed-fee contract, and of contracts involving Supplies, Services, or Research and

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[291] 172 Van Duzer Realty Corp. v. Globe Alumni Student Assistance Ass'n, Inc., 25 N.E.3d 952 (2014).

[292] *See* Wise v. United States, 249 U.S. 361, 365 (1919).

[293] *Id.*

[294] *172 Van Duzer Realty,* 24 N.Y.3d at 528.

[295] *See infra* notes 343 and 345.

[296] *See e.g.* Alvin C. Brightman, Liquidated Damages, 25 Colum. L. Rev. 277 (1925) (emphasizes the importance of the parties' intention in determining whether a pre-agreed sum in a contract is considered as "liquidated damages" or a "penalty").

[297] Wise v. U.S., 249 U.S. at 365.

[298] Am. Car Rental, Inc. v. Comm'r of Consumer Prot., 273 Conn. 296, 869 A.2d 1198 (Conn. 2005).

Development.[299] As per the general policy set forth in FAR 11.501, and largely in alignment with the jurisprudence already surveyed, a LD clause "should be used only when both (1) the time of delivery or performance is such an important factor in the award of the contract that the government may reasonably expect to suffer damage if the delivery or performance is delinquent, and (2) the extent or amount of such damage would be difficult or impossible to ascertain or prove."[300]

Thus, the policy behind LD envisaged under FAR is that LD "are used to compensate the Government for probable damages."[301] The purpose of liquidated damages then is to provide a pre-determined amount of compensation to the government in the event of a breach of contract by the contractor.[302] This allows the government to recover damages without having to prove the exact amount of damages suffered as a result of the breach. LD provisions in contracts help to ensure that the government is fairly compensated for any losses resulting from the contractor's failure to perform. Therefore, the rate of a LD "must be a reasonable forecast of just compensation for the harm that is caused by late delivery or untimely performance of the particular contract."[303] To this end, use of "a maximum amount or a maximum period for assessing liquidated damages" is envisaged "if these limits reflect the maximum probable damage to the Government."[304] Additionally, the US government is permitted to use multiple LD rates "when the contracting officer expects the probable damage to the Government to change over the contract period of performance."[305]

LD clauses enable the U.S. government to recover damages for any injury or loss caused by a breach. More specifically, in the context of FAR, LDs are meant to replace actual damages in the event of non-excusable, late performance breaches by the contractor in completing or delivering contractual deliverables.[306] In contract clauses, FAR provides for a set of contract clauses to be used in solicitations and contracts involving "Supplies, Services, or Research and Development," and pertaining to construction,

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[299] Liquidated Damages (LDs). FAR §11.502; FAR §36.206; FAR §52.211-12, DFARS Subpart §211.5.

[300] *Id.*

[301] *Id.*

[302] *Id.*

[303] *Id.*

[304] *Id.*

[305] *Id.*

[306] *Id.*

respectively.[307]

B. *Analysis Between FAR and Government Contract Act*

In the context of the RoK Government Contract Act and in alignment with Article 398 of the Korean Civil Code, LD purports to provide a reasonable forecast of damages the debtor is obligated to make good on in the event of the debtor's default on the agreement.[308] In the absence of a LD provision, the creditor is in principle required to prove the occurrence of loss caused by the default and the quantum of such loss under Article 390 of the Korean Civil Code.[309] The burden of proof for damages is challenging and often leads to disputes. LD is a useful tool that simplifies this by setting pre-agreed amounts, reducing conflicts, and encouraging debtor compliance. Courts can also adjust LD amounts under Article 398(2) of the Korean Civil Code to address any imbalance in bargaining power.[310]

The RoK regime recognizes and enforces penalty provisions under the principle of party autonomy. In the event of a breach, a creditor is entitled to seek a penalty against the debtor in addition to and aside from the actual damages incurred.[311] Such penalty provisions usually form an integral part of the parties' agreement. However, under Article 398(4) of the Civil Code, a LD provision is presumed to be a pre-estimate of damages, as opposed to a penalty, and the burden of proof usually falls on the party asserting the validity of a penalty provision to prove extraneous circumstances warranting the enforcement of such a provision.[312] Given the discrepancy between the two regimes when it comes to the subject of a civil penalty, an analysis on the subject will now be explored.

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[307] 48 CFR § 52.211-11 - Liquidated Damages - Supplies, Services, or Research and Development.

[308] *See* Daebeobwon [S. Ct.], Mar. 26, 1999, 98Da26590 (S. Kor.); and Daebeobwon [S. Ct.], Sept. 4, 2002, 2001Da1386 (S. Kor.).

[309] Minbeob [Civil Act] art. 390 (S. Kor.). *See generally* Ahn Tae-Yong, *Damages under Korean Law, in* STUDIES IN THE CONTRACT LAWS OF ASIA I: REMEDIES FOR BREACH OF CONTRACT (Chen-Wishart, Mindy, Alexander Loke, and Burton Ong, eds. Oxford Univ. 2016).

[310] For instance, in a case involving a contract that stipulated high interest rates for late payments by buyers, but excluded any interest on prepayments in cases of construction delays by the suppliers of new houses, the Supreme Court of the RoK ruled this arrangement as disproportionately unfavorable to the customers. The Court determined that such disparity in the contractual terms breached the principles of good faith as outlined in Article 6 of the Act on Regulation of Terms and Conditions, pointing to the lack of equitable treatment for both parties under the contract in question. Daebeobwon [S. Ct.], Aug. 23, 2007, 2005Da59475 (S. Kor.).

[311] Daebeobwon [S. Ct.], July 14, 2016, 2013Da82944 (main suit) and 2013Da82951 (counter suit) (S. Kor.).

[312] *Id.*

1. Penalty in the RoK Regime

As mentioned previously, under the RoK civil law regime, a penalty clause can be distinguished from a clause relating to liquidated damages.[313] While the Civil Code contains no stand-alone provision on penalty, in order to be considered a valid penalty clause, it must be clearly stated in the contract that the payment will be made in addition to any actual damages.[314] Additionally, a generic penalty clause is assumed to be a clause relating to liquidated damages unless special circumstances can be substantiated to prove the clause envisaged a penalty.[315] Contrary to LD, the court in principle is not free to adjust the amount of a penalty under Article 398(2) of the Civil Code.[316] The Court ruled that if a penalty is excessively harsh compared to the benefit gained from enforcing performance, it can be partially or fully voided for violating public order or good morals.[317] This, in effect, grants the court the ability to adjust the mutually agreed amount of a penalty in exceptional cases. One caveat here is that the court's power is to be used sparingly and with the utmost precaution based on a thorough review of the process leading up to the underlying agreement and agreed terms, among others, as it may entail intrusion into the parties' private autonomy.[318]

In the context of the RoK defense industry in particular, Article 58 of the DAPA Act provides for a civil penalty when a defense contractor has attained unjust enrichment *vis-à-vis* the government from the presentation of fraudulent costing data.[319] In such a case, with a goal to deter such deleterious conduct and to ensure an efficient implementation of the defense budget involved, the government is entitled to claim not only any unjust enrichment as well as interest and delay damages that the contractor materialized as a result of forged or otherwise fraudulent costing data, but

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[313] *See* Daebeobwon [S. Ct.], Mar. 26, 1999, 98Da26590 (S. Kor.); and Daebeobwon [S. Ct.], Sept. 4, 2002, 2001Da1386 (S. Kor.).

[314] Daebeobwon [S. Ct.], July 14, 2016, 2012Da65973, (S. Kor.).

[315] *Id.*

[316] Daebeobwon [S. Ct.], Dec. 10, 2015, 2014Da14511 (S. Kor.). In this decision, the Court noted that great caution must be exercised when interpreting the scope of private autonomy, including penalty clauses, through the prism of the clause of general applicability on public order and morality. This requires a thorough review of the circumstances and terms of the contract under scrutiny. The case thus evinces the Court's consistent stance that when it comes to penalty clauses, which represent a brainchild of party autonomy, it is not advisable to hastily invoke public order and morality to invalidate all or part of them. *See also* KWON YOUNG-JOON, MINBEOBPANLYEYONGU I [CIVIL LAW CASE STUDIES I] 165 (2019) (S. Kor.).

[317] Daebeobwon [S. Ct.], Jan. 28, 2016, 2015Da239324 (S. Kor.).

[318] Daebeobwon [S. Ct.], Dec. 10, 2015, 2014Da14511 (S. Kor.).

[319] Bang-wisa-eobbeob [Defense Acquisition Program Act], art. 58 (S. Kor.) [DAPA Act].

also an additional punitive surcharge.[320]

2. More In-Depth Analysis on the Surcharge Regime

The most salient feature of the defense system purchasing contract is the monopolistic nature of supply.[321] The underlying defense articles are supplied by a limited pool of contractors designated for each defense article being procured. As such, when concluding a defense procurement contract, there generally exists no comparable record of actual transaction prices.[322] Further, since the object of the contract usually involves newly developed products or ones with customized military specifications, the government routinely requests the supplier submit cost-related data for verification.[323] When such data are deemed insufficient for authentication purposes, the government may choose to conduct on-site verifications on the supplier's costing data.[324] Based on the foregoing flow of process, DAPA prepares a cost statement and determines the contract price.[325]

Under Article 58 of the DAPA Act, a contractor that has submitted false and other improper cost data to DAPA and thereby attains unjust enrichment, must return the unjustly earned benefit and the surcharge equivalent to not more than double the fraudulent gains to DAPA.[326] This system of disgorging the contractor's unjust enrichment, coupled with the relevant surcharge is designed to empower the agency to impose a legal and contractual obligation of submitting reliable cost data. The contractor, in the context of weapon system purchasing contracts, heavily relies on such data under the lead contractor's custody.[327] In other words, the system is designed to ensure the reliability of contractor-generated data and related materials.

According to relevant judicial precedents in the RoK, a penalty

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[320] Daebeobwon [S. Ct.], July 14, 2016, 2013Da82944 (main suit) and 2013Da82951 (counter suit) (S. Kor.).

[321] *See generally* Joe Cho, *Antitrust Implications of Defense Development Projects in South Korea: The Case of the KSS-III Project*, 25 KOR. J. DEF. ANALYSIS 37-57 (2013).

[322] *See* Jeong Jae-min and Jo Seong-woo, *Effectiveness and Justification of Cost Verification of Partner Companies*, Korea Defense Industry Association Paper Series, 1, 5, available at https://www.kdia.or.kr/kdia/contents/ (last visited Nov. 2, 2023).

[323] *See generally* Koo, Jung-tak, *A Study on the Contract of Purchasing Weapons Systems under the Contracts to which the State is a Party in view of Civil Law*, 22 KOR. ASSOC. OF DEF. INDUS. STUD. 77-94 (2015).

[324] *See* Mul-pum Jejo.Guma Gyeyak Teuksujo-geon Pyojun (Ilban Mit Bangsan) [Standard Special Conditions for Goods Manufacturing and Purchase Contracts (General and Defense Industry)], art. 47 (S. Kor.).

[325] *See* Jeong and Jo, *supra* note 323, at 15.

[326] Bang-wisa-eobbeob [Defense Acquisition Program Act], art. 58 (S. Kor.) [DAPA Act].

[327] Koo, *supra* note 324, at 83-84.

agreement is presumed to be a pre-estimate of loss in nature under Article 398(4) of the Civil Code.[328] Therefore, for such agreements to be construed as a penalty for breach of contract, exceptional circumstances must be pleaded and substantiated.[329] Against this legal framework, whether a given agreement involving a pre-estimated damages qualifies as a penalty or liquidated damages involves a question of the parties' intent on a case-specific basis.[330] If the claimant succeeds in proving the relevant, and usually circumstantial evidence, that the agreement was entered into as a private penalty for the purpose of coercing performance by the debtor of an agreed-upon obligation, the court will be inclined to consider it as a penalty for breach of contract, as opposed to LD. Considering this context, if the clause is deemed to be a penalty, the claimant may recover not only the actual damages incurred but also the penalty as stipulated.[331] Conversely, if LD are in question, the claimant's recovery is limited to the sum specified in the LD clause, although the court retains discretion to adjust this amount in accordance with the provisions of the Civil Code.[332]

The DAPA Act and its special terms and conditions provide a system for addressing contractor's unjust enrichment and relevant surcharges. This system includes several key points. First, in cases of cost fraud, it is stipulated that the contractor must pay not only the cost difference, which is considered normal damage, but also an additional surcharge equivalent to this difference. In addition, given the unique nature of weapon system procurement contracts, where actual transactional prices are often not available as benchmarks, identifying cost fraud is a significant challenge for the government. Such frauds are usually within the supplier's control. To discourage submission of false or fraudulent costing data, the system imposes a monetary penalty on contractors responsible for cost fraud. [333]

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[328] Minbeob [Civil Act] art. 398 para.4 (S. Kor.).

[329] Daebeobwon [S. Ct.], July 14, 2016, 2013Da82944 (main suit) and 2013Da82951 (counter suit) (S. Kor.).

[330] Daebeobwon [S. Ct.], July 14, 2016, 2012Da65973 (S. Kor.).

[331] Daebeobwon [S. Ct.], July 14, 2016, 2013Da82944 (main suit) and 2013Da82951 (counter suit) (S. Kor.).

[332] Minbeob [Civil Act] art. 398 para.2 (S. Kor.).

[333] Daebeobwon [S. Ct.], Jan. 28, 2016, 2013Da207958 (S. Kor.). In this case, DAPA entered into a mid-term fixed contract with Hanwha Thales to purchase tank components. Hanwha Thales then subcontracted with EO System to supply parts related to these components. When DAPA conducted cost verification in 2011, both companies only submitted initial cost calculation data and not subsequent data, including the 2006 cost settlement for the prime contract. Consequently, DAPA sought to recover unjust enrichment and a corresponding surcharge from Hanwha Thales, based on the false costing data provided by EO System. The Court noted that the Special Terms and Conditions (Article 26.1) of the prime contract required the contractor to present legitimate cost data. If the contractor obtained unjust enrichment due to errors in cost data or calculations, they

Lastly, the surcharge is not intended as a pre-estimate of damages aiming to streamline the legal relationship between parties in anticipation of disputes that might involve whether a loss has occurred from the alleged cost fraud and, if so, the extent of such damages. Rather, it would be more rational to view the surcharge as a punitive means to exert pressure on the contractor. Additionally, it serves to secure the contractor's compliance with data-related obligations and acts as a monetary penalty in case of contract breach.[334]

3. Penalty in the US Regime

The United States is known for its punitive awards in tort actions, but most states adhere to the common law rule that punitive damages for contract breaches are not allowed unless accompanied by tortious conduct.[335] This hostility to punitive penalties in contract law extends to LD clauses that are deemed punitive rather than compensatory. Section 355 of the Restatement (Second) of Contracts echoes this sentiment, stating that punitive damages are not recoverable for a breach of contract unless the conduct also constitutes an individual tort for which punitive damages are recoverable.[336]

U.S. contract law aims to enforce agreements between parties and ensure fair compensation in the event of a breach. One method to achieve this is through LD clauses, which are pre-determined amounts parties agree to pay if a breach occurs. However, courts will not enforce LD clauses that amount to penalties, as they are considered punitive and contrary to the compensatory nature of contract law.[337] For a LD clause to be enforceable in the U.S., it must satisfy two criteria: (1) the amount must reasonably reflect the damage caused by the breach, and (2) the harm resulting from

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must immediately return such gain to the government. Furthermore, if false or tainted cost data led to unjust enrichment, the government could claim both the unjust enrichment and an additional surcharge equivalent to the unjust enrichment. This contractual scheme holds the contractor responsible for providing accurate cost data and grants the government the right to seek compensatory and punitive damages in case of a breach of contract by the contractor, whether due to negligence or willfulness. *Id.*

[334] *See* Daebeobwon [S. Ct.], July 14, 2016, 2013Da82944 (main suit) and 2013Da82951 (counter suit) (S. Kor.).

[335] Leslie E. John, *Formulating Standards for Awards of Punitive Damages in the Borderland of Contract and Tort*, 74 CAL. L. REV. 2033, 2033 (1986).

[336] Restatement (Second) of Contracts § 355 (Am. Law Inst. 1981).

[337] *See Wise,* 249 U.S. at 365. *See also* United States v. Bethlehem Steel Co., 205 U.S. 105, 27 S.Ct. 450, 51 L.Ed. 731 (1907). According to Black's Law Dictionary, the term penalty is defined as a "contractual provision that assesses against a defaulting party an excessive monetary charge unrelated to actual harm. • Penalty clauses are generally unenforceable. — Often shortened to penalty." *Penalty Clause*, BLACK'S LAW DICTIONARY (11th ed. 2019).

the breach must be difficult or impossible to predict.[338] A clause that fails to meet these criteria may be deemed a penalty and rendered unenforceable. As Professor Corbin stated, "calling an outrageous penalty by the more kindly name of liquidated damages does not absolve it from its sin."[339] If a LD clause is deemed unenforceable, the government may sue for actual damages incurred because of the breach.[340]

The aversion to punitive penalties in government contracts can be traced back to 1954, when the U.S. Court of Appeals for the Sixth Circuit held that a provision for liquidated damages would be enforced only if it truly represented liquidated damages and not a penalty.[341] The court highlighted that the intention of the parties and the circumstances under which the contract was executed are crucial in determining whether a stipulated sum is liquidated damages or a penalty.[342]

In *Lake River Corp. v. Carborundum Co.*, Judge Richard Posner reiterated that a liquidated damages clause must be a reasonable estimate of the likely damages from a breach at the time of contracting and that the need for estimation must be shown by the likely difficulty of measuring actual damages after the breach.[343] If damages are easy to determine, or if the estimate greatly exceeds a reasonable upper estimate of the likely damages, it is deemed a penalty.[344]

C. *Freedom of Contract and LD/Penalty*

According to the Korean Supreme Court, the Government Contract Act provisions governing the management of contract affairs by contracting officials in contractual relationships between the state and private entities are internal state regulations.[345] These provisions outline the necessary guidelines for public officials handling contract matters, and unless there

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[338] In the case of K-Con Bldg. Systems, Inc. v. United States, as decided in 2011 by the Federal Claims Court, it was determined that the contractor was not able to prove the excessive nature of the stipulated liquidated damages of $551 per day. This amount was deemed a reasonable estimation of potential damages the Government might incur due to the contractor's failure to fulfill obligations related to the design and construction of a prefabricated metal building. Consequently, the agreed-upon liquidated damages clause was upheld as enforceable. K-Con Bldg. Sys., Inc. v. United States, 778 F.3d 1000 (Fed. Cir. 2015).

[339] Arthur L. Corbin, *The Right of a Defaulting Vendee to the Restitution of Installments Paid*, 40 YALE L.J. 1013, 1017 (1930).

[340] Brecher v. Laikin, 430 F. Supp. 103, 106 (S.D.N.Y. 1977).

[341] Steffen v. United States, 213 F.2d 266 (6th Cir. 1954).

[342] *Id.*

[343] Lake River Corp. v. Carborundum Co., 769 F.2d 1284 (7th Cir. 1985).

[344] *Id.*

[345] Daebeobwon [S. Ct.], Apr. 26, 1996, 95Da11436 (S. Kor.).

are special provisions in the law, the principles of civil law, including the freedom of contract are typically applied to them. The provision on LD under the Government Contract Act is one such provision.[346] Accordingly, the adjudicating court is entitled to reduce the amount of LD if deemed excessive under Article 398 of the Korean Civil Code.[347]

The freedom of contract principle posits that private contractual agreements should be strictly enforced, as they represent the mutual assent of the parties.[348] Invalidating doctrines such as fraud, mistake, and unconscionability are used when the mutual agreement is compromised.[349] In the United States, the law of liquidated damages is an exception to this principle as it prohibits the enforcement of penalty clauses even if they were the result of private bargaining between parties of equal bargaining power. The principle behind the enforcement of reasonable liquidated damages clauses is to provide just compensation, but only if it does not result in an unfair windfall. The just compensation principle requires that the plaintiff show actual, foreseeable harm and that he/she is influenced by the principles of freedom of contract and just compensation.

Meanwhile, in the RoK, the principle of freedom of contract allows parties to agree on the terms and conditions of a contract, including penalty clauses, as long as they are not deemed illegal or against public policy.[350] Upholding agreed-upon penalty clauses helps promote certainty in contractual arrangements and encourages parties to enter into agreements, thereby reducing the need for litigation. Unlike the FAR regime, the RoK recognizes and enforces penalty provisions under the principle of party autonomy. Under this legal scheme, in the event of a breach, a creditor is entitled to seek a penalty against the debtor in addition to the actual damages incurred.[351] Such a penalty and what conditions trigger it usually stem from the provision being an integral part of the parties' agreement. However, this

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[346] *Id.*

[347] *See* Minbeob [Civil Act] art. 398 para.4 (S. Kor.).

[348] DiMatteo, Larry A., *A Theory of Efficient Penalty: Eliminating the Law of Liquidated Damages*, 38 AM. BUS. L.J. 633, 641 (2001).

[349] For these doctrines, Minbeob [Civil Act] art. 110 (S. Kor.) [dealing with fraud]; Minbeob [Civil Act] art. 398 para.4 (S. Kor.)[dealing with mistake]; and Minbeob [Civil Act] art. 104 (S. Kor.) [dealing with unconscionability]; *see also* KWAK & KIM, *supra* note 19, at 289-294 (for unconscionability); 315-322 (for a detailed analysis regarding mistake including relevant jurisprudence); and 322-327 (for a detailed explication on fraud including pertinent precedents).

[350] Daebeobwon [S. Ct.], Dec. 10, 2015, 2014Da14511 (S. Kor.). For a comparative analysis including a common law perspective, *see* Oluwadamilola Odetola, *Penalties and Liquidated Damages in a Changing World: Rethinking the Common Law Position*, 6 J. OF SUSTAINABLE DEV. L. & POL'Y 247-271 (2015).

[351] Daebeobwon [S. Ct.], July 14, 2016, 2013Da82944 (main suit) and 2013Da82951 (counter suit) (S. Kor.).

mutual agreement is subject to the caveat from Article 398.4 of the Civil Code: a LD provision is presumed to be pre-estimate of damages, as opposed to a penalty.[352] The burden of proof usually falls on the party asserting the validity of a penalty provision to prove extraneous circumstances warranting the enforcement of such a provision.

Meanwhile, as former Justice Kim Jae-Hyung[353] and sitting Justice Kwon Young-Joon[354] of the RoK Supreme Court aptly point out, a dichotomy between a pre-estimate of damages and a penalty seems not only unnecessary, but overall counterproductive. First, as former Justice Kim notes, expanding the scope of Article 398 in a way that renders the provision applicable both to pre-estimates of damages and penalties in a generic manner under the penumbra of LD seems desirable.[355] In support, the Ministry of Justice Civil Code Amendment Committee decided this at their plenary sessions in 2013.[356] This type of statutory amendment, if ever implemented, would bring the Civil Code into line with international model civil rules including UNIDROIT Principles of International Commercial Contracts (PICC), Principles of European Contract Law (PECL), and Draft Common Frame of Reference (DCFR), regulating the subject of pre-estimated damages and penalties under one umbrella of stipulated LD.[357]

In the absence of any imminent legislative changes to Article 398 of the Civil Code, Justice Kwon espouses application of Article 2013 to a penalty provision by way of analogy or analogical interpretation.[358] Such mode of statutory interpretation generally entails the technique of *praeter legem* or statutory interpretation beyond the text where there is a legal lacuna or defect in a legislation, to make up for such an inherent gap or flaw.[359] In practice, applying Article 398(2) to a penalty clause by analogy should pose no practical concern in that a penalty provision is in substance akin to a LD clause.[360] When equity is demanded, the court can apply provisions of Article 398 for pre-estimated damages to a penalty, ensuring fairness in each case and maintaining consistent reasoning.[361] If adopted by

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[352] Daebeobwon [S. Ct.], Mar. 24, 2016, 2014Da3115 (S. Kor.).

[353] Kim Jae-Hyung LD, *supra* note 253, at 627.

[354] *See generally* Kwon Young-joon, *Reduction of Liquidated Damages Ex Officio and a Penalty Clause – the Issue of Analogical Application*, 155 JUSTICE 199-244 (2016).

[355] Kim Jae-Hyung LD, *supra* note 253, at 648-649.

[356] *Id*.

[357] *Id.* at 661-663.

[358] *See generally* Kwon Young-joon, *supra* note 355.

[359] *Id.* at 217-226. For the subject of Supplementary Interpretation, *see supra* Part B.3.

[360] *Id.*

[361] *See generally* Kwon Young-joon, *supra* note 355.

the RoK judiciary, this would allow a penalty provision to be reduced *ex officio* if it is deemed unduly excessive.[362] In this regard, however, what has reigned supreme in related court jurisprudence to date appears to be the priority accorded to the principle of private autonomy.[363] This situation was apparently manifested in the most recent court case as well.[364]

VII. CONCLUSION

In conclusion, this article has critically analyzed the Thesis that government contracts in the RoK operate as private agreements under the South Korean legal framework. Through an examination of the principle of freedom of contract, regulatory measures, legal paternalism, and the legal nature of PPCs, it has been demonstrated that government contracts in the RoK are indeed fundamentally private agreements governed by principles of private law, including contract law. The RoK's laws and jurisprudence on contract interpretation, adjustment of contract price, and liquidated damages also support this article's Thesis.

The article has also highlighted the important caveat that RoK government contracts are amenable to mandatory legal rules and regulations. These mandatory provisions within the framework of government contract

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[362] *Id.*

[363] In this regard, it is worthwhile to note the RoK Supreme Court's observation in 2010 that punishment or sanctions against norm violators are not generally pursued in private law and as a result, it becomes necessary to apply them cautiously. What is perhaps implicit in this statement is that in the realm of private law, the main goal is to enforce agreements between private parties based on the protection of their autonomy to freely negotiate and execute their own contracts. As such, the focus is usually on compensating the parties for any harm caused by a breach of contract rather than punishing the party responsible for the breach. Penalty clauses are an exception to this rule, as they are a way for parties to contractually agree to a predetermined amount of damages in the event of a breach. However, since penalty clauses can have a punitive effect, courts will need to exercise an abundance of care and caution in that such provisions may pave a way for a party to reap a windfall from the breach of the counterparty. Daebeobwon [S. Ct.], Sept. 30, 2010, 2010Da50922 (S. Kor.).

[364] Daebeobwon [S. Ct.], July 21, 2022, 2018Da248855 (main suit), 2018Da248862(counter suit) (S. Kor.). According to the majority opinion in this case, the concept of liquidated damages functions as a punitive measure for contractual non-compliance. In accordance with the principle of private autonomy, it is crucial to respect the parties' intentions, as the non-compliant party voluntarily consents to compensate the counterparty. Furthermore, extensive judicial intervention in liquidated damages may inadvertently undermine their effectiveness in ensuring debt performance, thus, caution should be exercised in allowing judicial interference. *Id.* Conversely, Justices Kim Jae-hyung, Park Jung-hwa, An Chul-sang, Lee Heung-goo, Chun Dae-yeop, and Oh Kyung-mi presented a dissenting view, positing that it is advisable to analogously apply the provisions concerning the estimation of damages to the reduction of penalties, given their functional similarities. These justices maintained that the RoK Supreme Court gradually relaxed the demarcation between pre-estimated damages and penalties, which had led to considerable doctrinal disparities and inconsistencies. *Id.*

law, as well as other compulsory statutory provisions, reflect the unique nature of PPCs in that they involve the use of public funds, have broader economic and societal implications, and seek to prevent corruption, fraud, and abuse of power. As a result, the RoK government contracts can be characterized as essentially private in nature with a nuanced interplay of mandatory legal rules and regulations.

The comparative analysis between the RoK's laws and jurisprudence and their United States counterparts has revealed similarities and differences in the approach towards government contracts. While both jurisdictions primarily treat PPCs as private agreements, the balance between private law principles and mandatory legal rules may vary. This article's findings can thus contribute to the understanding of the South Korean legal landscape and its unique approach to government contract law, providing insights for policymakers, legal practitioners, and scholars alike.