Chapter 2
Principles of the "European" Contract Law

In contrast to the way of thinking of Adat Law, the legal thinking behind the Law of Obligations (and Contract Law) of the Civil Code is very abstract. Because what is regulated is not so much the contract as the relationship between the parties depending on their promise and agreement, resulting in a number of legal obligations on the one hand, and rights and duties on the other.

Background of the Indonesian Contract Law.

It is often said that Indonesian Civil Law belongs to the group of the Continental "Civil Law Systems", as opposed to the "Common Law Systems".[1]

This description is not wrong to the extent that much of Indonesian law derives from the Dutch and the French. However, the statement is not entirely true.

As Sudargo Gautama[2] said that when the first Dutch ships landed in the Indonesian Archipelago, they did not find a juridical "empty land". The land was full of legal institutions. There was diversity of laws from the beginning of the days of the VOC (*Vereenigde Oost Indische Compagnie*) or United East Indian Company. From the beginning of Dutch colonization, the inhabitants of the Indonesian Archipelago, have been divided for legal purposes into various "population groups" (*bevolkingsgroepen*). This distinction was not entirely based on racial differentiation, but was also based on economic considerations. There was also a distinction between residents and non-residents, Dutch nationals

1. Timothy Lindsey, *An Overview of Indonesian Law,* in Indonesian Law and Society, Sydney: the Federation Press, 1999, p. 1.
2 Sudargo Gautama, *The Commercial Laws of Indonesia,* Bandung : Citra Aditya Bakti, 1998, p. 3.

and foreigners, but no distinction was more important than the division into population-groups, as regulated by State Gazette 1855 No. 2.

For example, matters concerning daily transactions in private life, such as what kind of contracts one could enter into, whether one could own land and where, from whom one could inherit and in what ways ; all such matters depended on the population group one belonged to. This was so, because different rules of contract law, property law and inheritance law existed for each group. Each group had its own legal system, separate regulations administered by separate government officials and regulated by separate codes or laws.

Very different systems of law existed side by side in Indonesia for centuries, although transactions between the various groups were possible which was governed by principles and rules of Interpersonal Law. In special cases unified regulations were made like in the case of the Criminal Code, which applied to all groups of inhabitants.

Application of the Civil Code and General Principles of Contract Law.

Part of Indonesian Private Law as inherited from the Dutch are the Civil Code (*Burgerlijk Wetboek*) and the Commercial Code (*Wetboek van Koophandel*). These codes (except for a few exceptions), were practically Dutch translations from the French Code Civil and Code du Commerce. The Civil Code was promulgated in Indonesia by Government Announcement on April 30, 1847, Government Gazette 1847 No. 23 and applied since the 1st January 1848.

Article II (the Transitional Regulation) of the Indonesian Constitution of 1945 states that all the existing state institutions and regulations will still apply, as long as no new ones have been established in accordance with this Constitution. This provision was made, in order to prevent a legal vacuum. Hence the old regulations and codes before our independence on August 17th,

1945 continue to apply till the present time. Nevertheless, the Government assisted by the National Law Reform Agency (Badan Pembinaan Hukum Nasional) is scrutinizing which of the old laws will have to be replaced by new ones. Some 400 laws and/or regulations will have to be replaced by new ones.

The recent development pertaining to contract law and commercial transactions has been the enactment of Act No. 1 of 1995 on the Limited Liability Company (PT), the Fiduciary Securities Act (No. 42 of 1999), and the Futures Trading Contract by Act No. 32 of 1997. Standard contracts are regulated in specific regulations such as Act No. 8 of 1999 on Consumer Protection and Act No. 18 of 1999 on Construction Services. At present a bill is being prepared for Mining Activities including mining and license contracts. Provisions concerning contracts which are prohibited can be found in Act No. 5 of 1999 concerning the Prohibition of Monopoly and Unfair Business Competition.

Contract as a Source of Obligations.

The Civil Code was promulgated in the year 1848 together with the Commercial Code. The law of contracts under the Civil Code (*Burgerlijk Wetboek*) is laid down in Book III of the Civil Code, starting with Article 1233 through Art. 1456. The 5th Chapter of Book III (art. 1457 to art. 1850 CC) regulates the so-called "nominated" or specific contracts, such as sale of goods, barter, hiring, etc.

Book III of the Civil Code, under the heading "Obligations", contains :

(a) the law of contracts as the principal source of obligations,
(b) the management of affairs without mandate, and
(c) the law of torts or wrongful acts.
(d) Nominated contracts.

Every obligation is born either by agreement or by legislation [3]. There is no definition on what obligation is in the Civil Code. Legal science stipulates that

[3] Article 1233 Civil Code.

obligation is a legal relation between two or more persons which site within the field of the law of property, establishing to one party the right to get something or have something to be done by the other party, who has the obligation to fulfill such right. Legal relations happen every day, so the law grants "rights" to one party, and "obligations" to the other party and vice versa. Elements of obligations are : legal relations, property, parties, and something to give or to be done (prestatie) [4]. If one of the parties does not respect or breaches such legal relationship, the law will be enforced in order that the relationship will be fulfilled or restored. For example : A agrees to sell a bicycle to B. As a result of that agreement, A is obliged to give his bicycle to B and at the same time has the right to its price from B, whilst B is obliged to pay the price of that bicycle to A. If A does not fulfill his obligations, then the law will "force" him to do so by legal means.

However, not all social relations result in the enforcement of the law of obligations. An agreement to go for an outing or a picnic will not bear an obligation, because such agreement is not an agreement in the legal sense. Such agreement falls within the category of moral obligations, because the non-performance of the obligation results in a reaction from other members of society as a bad attitude. The non-performance party will be hated by the other, but it is non-actionable before the court.

Sources of obligations are agreements (contract) and legislation. [5] Obligations born by Law can be born by mere Law (*uit de wet alleen*) or as a result of human action (*uit de wet ten gevolge van 's mensens toedoen*) [6].

Furthermore obligations as a result of human actions can be lawful or unlawful acts or torts (*onrechtmatige daad*).[7]

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[4] Mariam Darus Badrulzaman, *Civil Code Book III and Its Explanation* (KUHPerdata Buku III Hukum Perikatan dengan Penjelasan), Bandung, Alumni, 1993, p. 3.
[5] Article 1233 Civil Code.
[6] Article 1352 Civil Code.
[7] Article 1353 Civil Code.

Obligations born by mere Law are obligations between the parties concerned (with or without intention of the parties). For example : date of expiration (*verjaring*) is an event where the legislators determine an obligation to a particular person. Because of the date of expiration, someone might be released from doing something or acquiring a right or obligation to do for something ; the death of a person will result in legal obligations to his heirs, the birth of a child results in the obligation to the parents in order to take care of their infant (Article 321 Civil Code).

Obligations which arise from the Law as a result of human lawful acts are for instance a voluntarily handling of other people's interests (*zaakwaarneming*), because the Law determines that some rights and duties must be performed by the handler, similar to the rights and duties in such cases as if an agreement was made. Article 1354 Civil Code states that "if someone, without having obtained an order for it has voluntarily handled another person's matters, he has an obligation to continue and finish that matter (business) until the people represented is able to do that matter by himself. The person, whom the other person has represented, has an obligation to compensate all costs which was spent on his behalf.

Obligations resulting from the Law but caused by unlawful acts is enacted in Article 1365 of the Civil Code, saying that those who causes another person to suffer losses, based on his fault, must restore the losses.

As Article 1233 Civil Code states that "obligations are born from contract or from legislation". That means that Law and Contracts are sources of obligations. This gives the impression as if the sources of obligations are only limited to those two sources mentioned above. However, based on the extensive interpretation on natural obligations in an Supreme Court decision of March 12, 1926, obligations can also be based on good faith or decency (good deed) as a source of a "natural" obligation (*natuurlijke verbintenis*) which can not be sued before the court to obtain full compensation, but if performed, releases the performer of his obligation.

General Provisions and Open System of Book III of the Indonesian Civil Code

The law of contract is an "open system", which means that everybody is free to make any kind of contract. Special contracts or "nominated contracts" are regulated in the Civil Code being only the most popular kinds of contracts. Because Book III of the Civil Code is an open system, the articles in Book III actually provide only General Guidelines of Contract Law. With such general provisions, people could conclude whether or not they have made a legally valid contract.

Freedom of Contract

The freedom to make contracts of whatever kind is regulated in Article 1338 paragraph 1 of the Civil Code, which provides that all contracts which have been legally concluded, have the same force as a legislative act for the parties who had concluded the contract. As a consequence of the open system of the law of contracts, the provision laid down in Book III of the Civil Code have the character of optional law. This means that the parties are free to ignore those provisions by making for themselves rules in their contracts deviating from or even contrary to those provisions laid down in Book III[8], except that they cannot deviate from the basic rules of legality, justice, good intentions and fairness, whenever the parties have not made any provision concerning a certain matter in the contract.

Book III of the Civil Code consists of a General Part (art. 1233 – 1456), containing the general rules of the law of obligations and contracts and a Special part regulating special contracts (art. 1457 – 1855). The general principles of the law of contracts in the Civil Code form the principles not only for contracts regulated in the Civil Code itself, but also for those regulated in the Commercial Code and in other special acts or regulations.

Most articles of the law of contract, private law in general, are additional legal provisions (*aanvullend recht*), which apply in case the parties had not agreed otherwise. The additional legal provisions also apply only when both parties consent to that. Here the legislators made a fiction of presumed intention of the parties. Such fiction is needed in order to synchronize with the principle of consensus of the parties. Apart from that, such legal presumption is needed to determine the rights and duties of the parties and also to prevent any legal dispute, or for the sake of legal certainty.

The elements of obligations are : the parties, legal relations, property, and something to give or to be done (prestatie).[9]. In Book III the law of obligations is part of the law of property (*vermogensrecht)*, which distinguishes between absolute rights and relative rights. Absolute rights (or rights in rem) are regulated in Book II of the Civil Code, whilst relative rights are regulated in Book III of the Civil Code. Property rights are rights which have economic value or can be counted in sums of money. So it should be clearly understood that the obligation to give or do something (prestatie) valued in money or other economic value has an important role in the law of obligation. This legal character is to be distinguished from the moral obligation which are not enforceable by law.

The Civil Code also regulates a number of so called "nominated" contracts, such as the contract of sale, barter or exchange, lease, contract of labour, partnership, association, donation, deposits, loans, "natural contracts" like gambling and life annuity, agency, guarantee and compromise.

Contracts of insurance and transportation overseas are regulated by the Commercial Code, and contracts of transportation over land and by air are regulated by special laws or ordinances.

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[8] R. Subekti, *The Law of Contracts in Indonesia, Remedies of Breach,* Jakarta : Haji Masagung, 1989.
[9] Mariam Darus Badrulzaman, *Civil Code Book III and Its Explanation (KHUPerdata Buku III Hukum Perikatan dengan Penjelasan),* Bandung : Alumni, 1993, p. 3.

Other commercial transactions have been provided by many Laws outside the Civil Code and Commercial Code such as the Contract for the establishment of a Limited Liability Company (PT) regulated in Act. No. 1 of 1995 on Liability Company, Fiduciary Securities in Act. No. 42 of 1999, and Futures Trading Contracts in Act. No. 32 of 1997. Standard contracts have been enacted in special rules such as in Act. No. 8 of 1999 on Consumer protection and Act No. 18 of 1999 on Construction Service, while at present a bill is being prepared for mining activities, including mining and license contracts. Finally, in Act. No. 5 of 1999 concerning Prohibition of Monopoly and Unfair Business Competition there are provisions on contract clauses, which are prohibited.

Definition and Scope of Contract Law

Chapter II of Book III of the Civil Code concerns "Obligations born from Contract or Agreement". The use of the words "contract" or "agreement" in Book III have identical meaning, Article 1313 of the Civil Code define a contract (or agreement) as an "act by which one or more persons bind themselves towards two or more other persons, with the intention to create obligations".

The term "act" between two or more persons in this article should be understood as "legal act", because both parties are required to consciously know or could or should have known of the legal consequence which would occur in the future. Hence the parties intentionally were engaged in such act for the purpose of its legal consequence. In other words, the legal consequence was indeed something that was intended by the parties. For example in the decision of the Court of Central Jakarta in the case between **Alfa Indonesia** vs, **Jakarta Lloyd** No. 64/1979, the defendant posed that the shipping agreement included a special agreement (*benoemde overeenkomst*). Article 506 of the Civil Code namely stated that a Bill of Lading is a letter in which was written that on a certain date the carrier received a certain (kind or amount of) goods to be delivered at a certain place of destination where it should be delivered to a certain person. The bill of lading also contains a set of conditions for transfer

goods. Therefore it was convincingly clear that the **Bill of Lading** was indeed a unilateral declaration (*eenzijdig*) made by the carrier/defendant and that it was not an agreement between the two parties (*overeenkomst*) as stipulated in Article 1313 Civil Code.

The law of Book III of the Civil Code concerns contracts in the field of private law. Agreements in public institutions or organizations are not covered by the Civil Code. Public law concerns public law relations, namely relations between states or between public institutions and organizations. However, in the last thirty years increasingly the state conclude contracts with individual persons or private companies concerning private law matters. Such as whenever the government has to buy computers or stationaries from a private company for the purpose of government procurement.

In recent times there are two opinions on that issue. If the state acted in the quality of the state (*iure imperii*) the legal relationship results in a public law relation. Whereas if the state acted in her economic capacity (iure gestiones) [10] as for instance as a state company, private law on the matter should be settled by private law provisions. In such case the provisions of Book III of the Civil Code apply.

For example in the decision of the District Court (*Residentiegerecht*) of Batavia, March 18, 1927 in the case of **"Excess Teaching Hours"**.[11] A, a mathematic teacher, who was appointed by the Department of Education became Head of a Preparatory Team for the opening of the Medical School in Surabaya, had been given the task to give mathematic lessons to the student candidates. The task as a teacher has exceeded the number of teaching hours agreed upon, because the change of teaching schedules from the Department of Education.

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[10] Compare with Barry E. Carter and Phillip R, Trimble, *Foreign Sovereign Immunity and the Act of State Doctrine,* Boston : Little, Brown & Co., 1991, pp. 449 – 697.

[11] Translated from J. Satrio, *Hukum Perikatan, Perikatan Yang Lahir dari Perjanjian,* Bandung : Aditya Citra Bakti, 1995, pp. 30 –32.

Based on those reasons he sued the Department of Education c.q. State in order to pay the "excess of teaching hours". The legal reasoning of the Court Decision said that the legal relationship between plaintiff and defendant was a relation between employee and the state. Such relationship was not a private agreement, but had a public law character. Article 40. I.S. (*Indische Staatregeling*) stipulates that payment of wages for public employees is unilaterally decided by the state. Therefore, intervention by another party, eventhough by the Court, was not excepted. This indicated the difference between public law and private law. In other words, the private law provisions in Book III do not applied for agreement in the field of public law.

This was the situation in 1927. But recently there is a group of lawyers, who have modified this theory, saying that in specific cases Book III CC might be applicable to government contracts.

General Conditions for Validity of Contract

Article 1320 Civil Code provides for the general conditions by which a contract is valid. Such conditions concern the subject and the object of the contract. This article stipulates that for a contract to be valid, it must comply with 4 (four) conditions, namely : (1) consent between those who bind themselves (the parties); (2) capacity of the respective parties to conclude an obligation;, (3) a certain (specific) subject matter, and (4) a legal cause.

When the conditions mentioned above are fulfilled, a contract is complete and valid. The validity of a contract is, as a rule, not bound to formalities. Only by exception the law prescribes formalities for a certain number of contracts.[12] The first two conditions are conditions pertaining to its subject, and the last two conditions are conditions pertaining to its object. A contract containing defective subject, namely concerning the consent of the parties or whenever one party has not obtained the capacity to conclude an obligation, does not

[12] R. Subckti, op. cit.

invalidate such contract (*nietig*), but often only raises the possibility for the other party to claim that the contract is void (*vernietigbaar*).
On the contrary, whenever the subject matter is not certain or whenever the cause is not legal, such defects on the object of the contract result in the contract being void by law.

1. Mutual Consent Between Those Who Bind Themselves

In concluding a contract there has to be at least two persons who take opposite positions and have the intention to come to a mutual agreement (consent). Hence, a consent means a meeting of minds [13].

According to Prof. Sudargo Gautama :

"By a free consensus (meeting of minds) is meant that both parties have voluntarily given their consent or have voluntarily agreed to the contract. According to article 1321 of the Civil Code the consent is not valid when it is the result of error, coercion or deceit".

The mere meeting of minds between two persons would not sufficiently conclude an obligation. The core consent is indeed an offer which was accepted by the other party. Offer and acceptance could come mutually from both parties. Therefore, the elements of offer and acceptance is very important to determine the birth of a contract. Unfortunately, the legislator did not provide a pattern which could be used to determine to what extent an offer or an acceptance is binding.

According to Sudargo Gautama [14] the principle of consensus concerns the formation of a contract. Generally no formal requirements are needed to make a contract binding. The mutual consent of the parties will be sufficient. The exceptions however made by the law are :

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[13] R. Subekti, op. cit
[14] Sudargo Gautama, *Essays in Indonesian Law*, Bandung : Citra Aditya Bakti, 1991, pp. 188 – 189.

(a) Besides the mutual consent of the parties, the delivery of the subject will be required to make the contract binding. This is the case in the following contracts : depository (sect. 1694 Civil Code); loan for use (sec. 1749 Civil Code); loan for consumption (sect. 1754 Civil Code).

(b) As regards certain contracts the mutual consent is required to be made in a certain written law form, namely an authentic deed (contract of donation, Article 1692 Civil Code), and the formation of a limited liability company, (Article 30 Commercial Code) or private deed (contract of compromise, Article 1851 Civil Code).

In the Netherlands it has been enacted in the *Nieuwe Burgerlijk Wetboek* (*New Civil Code*) Article 217 to 225. Here the legislator gave some provisions on offer and acceptance. According to Articles 219 – 225, a contract is formed by an offer and its acceptance. Articles 219 – 225 apply unless the offer consists of another juridical act or usage produces a different result. An offer is valid, null and void, or subject to annulment according to the rules which are applicable to multilateral juridical acts.

There are at least 4 (four) theories regarding the doctrine of consensus, namely : the Will's theory (*wilstheorie*), the sending theory (*verzendtheorie*), the knowledge theory (*vernemingstheorie*), and the trust theory (*vertrouwenstheorie*). The will's theory states that consensus is reached at the moment both parties have expressed their will, for instance by writing a letter to the other party. The sending theory says that consensus is reached at the moment the will to except is expressed by the acceptor to the offeror. The knowledge theory states that consensus is reached whenever the offeror should have known that his offer was accepted. And the trust theory states that consensus is reached, whenever one can reasonably presume that the offer has been accepted by the acceptor.

Asser [15] divided conditions for the validity of contract, in the core part (*wezenlijk oordeel*) or "essensialia" and the non-core part (*non wezenlijk oordeel*) or "naturalia" and "aksidentalia". Essensialia is a condition which is mandatory to a contract, something without which the contract cannot exist (*constructive oordeel*). Such are the conditions of consensus and the object of a contract. Naturalia is a part which "naturally" adheres to a contract, such as the obligation to assure that no defect goods shall be sold (*vrijwaring*). Aksidentalia means conditions adhered to a contract which should be expressly agreed upon by the parties, such as the provisions on the parties' domicile.

Capacity of the Parties

Everybody is capable of concluding a contract, except those who are declared incapable by law. According to Article 1330 of the Civil Code, the following are incapable of concluding contracts : minors, those who are under guardianship and married women. By a decision of the Supreme Court in 1963, the provision as regards married women is declared illegal, so that now married women are capable of concluding contracts, without the assistance of their husbands. In case an incapable person has concluded a contact, his/her legal representative has the right to demand before the court the annulment of the contract. The person himself also can demand annulment, when he becomes capable or regains his capability. It is understood that the other party (that is the party who is capable) has no right to demand annulment of the contract.

A Certain Subject Matter.

By a certain subject matter is meant a clear description of what is agreed to resulting in the certainty of the subject matter. This is necessary to enable the Judge to determine the duties of each party, when there arises a dispute. For example : a contract of sale of "rice for one hundred dollars"; shall be declared

[15] Scc Mariam Darus Badrulzaman, ibid.

null and void for the reason that a certain subject matter is lacking, as it is not clear what kind or quality of rice is sold; moreover nothing is said about the quantity.

A Legal Cause.

By a legal cause is meant that what has to be performed by either party is not contrary to the law, public order or public morality. A contract whereby one of the parties undertakes to commit a crime is null and void, because it has an illegal cause.

From what is said above, we can draw the conclusion that, in case of incapacity of one of the parties or in case of lack of free consensus, the injured party has to demand the annulment of the contract from the judge. In such cases the contract is voidable. On the other hand, in case of ambiguity about the subject matter, or in case of illegal cause, the contract is null and void from the start. In these cases the judge shall ex officio declare the contract null and void. In case of incapacity of one of the parties or in case the imperfectness of the contract, whereas in the case of ambiguity about the subject or in the case of an illegal cause he is supposed to know the imperfectness of the contract at first sight.

The action for annulment of a voidable contract shall be brought within five years. This period shall begin : (1) In case of incapacity of one of the parties from the time that the incapable person becomes capable or gains his capacity; (2) In case of error, coercion or deceit, from the moment of detection or discovery of the error or the deceit or from the moment the coercion has ceased (Article 1454 of the Civil Code).

Breach of Contract.

There are four different manifestations of breach of contract, i.e. whenever : (a) The debtor has not done anything to carry out his duty; (b) the debtor has done his duty but nor equivalent to what was promised in the contract; (c) The debtor has fulfilled his task, but too late; and (d) The debtor has done something that is contravention to the contract.

In all these cases the debtor is considered to be in default, as he has been neglecting his contractual duties. The law has laid down certain sanctions for such a debtor.

Debtor's Fault.

Where the debtor has done something that is in contravention to the contract, it is obvious that he is in default. Also when a time limit is fixed in the contract for carrying out the duty and the debtor has passed this time limit, it is clear that the debtor is in default. But in other case, the creditor has first to remind or to summon the debtor to fulfill his contractual duties, as for instance, when the debtor has to pay a sum of money and it is not stipulated when he has to make the payment, or when the performance by the debtor, according to the creditor is not equivalent to what was promised in the contract.

According to judicial decisions an oral reminder is enough. To be safe, it is advisable for the creditor to remind by registered letter, so that he has proof of the reminder. According to the Civil Code there are four sanctions attached to a breach of contract : Compensation (costs, damages, and interest) : Cancellation of the contract; Transfer of risk of responsibility for the object of the contract; Payment of cost procedure; when it leads to recourse to a court.

Article 1266 of the Civil Code provides for a claim of cancellation of the contract against a debtor who is in default to fulfill his obligation. The cancellation of the contract is meant as a punishment for a debtor who has neglected his duties. Indeed it is sometimes felt hard by a debtor, especially when he has already incurred expenses for the fulfillment of his contractual duties. Article 1266, therefore, provides that the court could allow a period of grace to the debtor to give him an opportunity to perform. When the court is of the opinion that a cancellation of the contract will be disastrous to the debtor, while his fault is not serious, the court will refuse to cancel the contract, though, possibly, he will entertain a claim for compensation.

The right of a seller in a cash sale to reclaim the goods sold and already delivered to he buyer in case the buyer neglects his duty to pay the price of the goods, is in fact a right to cancel the sale without the intervention of the court. This right is to be exercised by the seller within thirty days from the date of the sale while the goods are still in the possession of the buyer (Article 1145).