

# Creating Clarity in International Commercial Contracts for Guaranteeing Legal Certainty in Indonesia

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## Creating Clarity in International Commercial Contracts for Guaranteeing Legal Certainty in Indonesia

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### ABSTRACT

The enforcement of the obligation to use the Indonesian language in international commercial contracts, which is a mandate from Act No. 24 of 2009 regarding the National Flag, Language, Coat of Arms, and Anthem, has become an issue and been brought to court. The Supreme Court finally decided in 2015 that an English language international commercial contract is void. The decision has provided clarity on the controversy after seven years of enforcing this obligation due to the lack of implementing a regulation that could further explain the phrase “must” in the provision of Article 31 of said law, which led to multiple interpretations among stakeholders. Although precedent is not recognized in Indonesia, this issue still brings uneasiness among investors, especially foreign ones. In facing this issue, this article discusses what steps must be taken by investors to avoid a lawsuit demanding the annulment of their foreign language contracts. Government Regulation 57/2014 (2014), as an ancillary of Act 24/2009, is silent on the use of the Indonesian language in international commercial contracts. This article therefore argues that a presidential decree to implement the regulation as mandated by Article 31 of Act 24 of 2009 should be enacted immediately to provide legal certainty to foreign investors who may have contracts with Indonesian private parties.

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## INTRODUCTION

A recent Indonesian Supreme Court ruling (Court Decision No. 601 K/PDT/2015) has upheld its lower courts' decisions regarding the mandatory use of the Indonesian language in an international loan contract concluded in Indonesia between PT Bangun Karya Pratama Lestari (BKPL) and NINE AMLtd. The West Jakarta District Court, as the first court for this case, declared in June 2013 that an English-language Loan Agreement contract was null and void (Court Decision No. 451/Pdt.G/2012/PNJktBar). The Court ruled that the contract must be written in Indonesian, as it involved Indonesian parties. According to Art. 31. para. 1 of Act No. 24 of 2009 on National Flag, Language, Coat of Arms, and Anthem, (the Indonesian Gazette No. 109) (Act 24/2009), the Indonesian language must be used in any MOU or international contracts involving Indonesian state agencies or government institutions, Indonesian private entities, or individuals of Indonesian nationality. The government enacted Act 24/2009 on 9 July 2009 as an implementing regulation for Article 36C, the Second Amendment Indonesian Constitution 1945, which states that provisions on the national flag, language, coat of arms and anthem shall be regulated in a law.

The District Court judged that the contract in question did not fulfil one of the four conditions for lawful contracts as prescribed by Article 1320 of the Indonesian Civil Code (hereinafter ICC), in particular the requirement that an agreement must be entered into for a lawful cause, i.e., not

in violation of any laws or regulations. Therefore, the contract was deemed null and void and the Court ordered BKPL to pay back the loan, as if the agreement had never bound the parties. This decision was then upheld by the Jakarta High Court on May 7, 2014 (Appellate Decision No. 48/Pdt/2014/PT.DKI), which simply concurred with the court of first instance and failed to discuss the substantive legal issues involved.

Concerning the Supreme Court ruling, one should keep in mind that as a civil law jurisdiction, the Indonesian judicial system does not recognize the principle of *stare decisis*, a common law concept of binding judicial precedent. Therefore, the Indonesian courts are not bound by the Supreme Court decision and are free to adopt a different position, although the decision may have persuasive impact in terms of a uniform application of the law as highlighted by Butt (2008), that cassation's main function is to ensure a uniform application of the law, which only considers the legal aspect of the case. Previously, there was no case similar with the case discussed in this article. Nevertheless, in Indonesia as a civil law system country that derived from French and Germany models, courts are not bound by decisions of courts at the same level or higher - called precedent common law system (University of Melbourne, 2018). Thus, in this context, the Courts have a significant point in giving clarity and transparency that the sole English contracts are void if involving Indonesian parties.

According to the courts, the use of the Indonesian language in international

contracts is mandatory, as reflected in the word “must” in Article 31 of Act 24/2009. The article also stipulates that any MOU or agreement involving foreign parties may be written in the national language of the foreign party and/or English. Indonesian need not be selected as the governing language, but an Indonesian text is required if the agreement involves an Indonesian party. Although precedent is not recognized in Indonesia, this issue still brings uneasiness among investors, especially foreign ones. This article analyses the case thoroughly in order to clarify issues concerning international commercial contracts written exclusively in English.

#### METHOD

This article utilizes the primary sources of law: the decisions of the courts, Act 24/2009, and other legal instruments as the basis for legal analyses of the legal certainty of international commercial contracts in Indonesia. It also utilizes secondary sources, such as articles on law, books and other reading materials on law to support its arguments. This article employs a regular, empirical approach to legal research and uses case, statute, and conceptual approaches.

#### RESULTS AND DISCUSSIONS

The Indonesian courts have ruled that the use of the Indonesian language in international commercial contracts is mandatory when Indonesian nationality is involved. Despite its controversies, and seven years after the enforcement of this

obligation, the rulings have provided clarity, given the lack of a regulation that could further explain the phrase “must” in Article 31 of Act 24/2009. Although the government issued an ancillary/implementing regulation (Government Regulation 57/2014) on July 2014, this regulation only focuses on the promotion and protection of Indonesian language and literature and is silent on the question of contractual language. Thus, contracts involving Indonesian parties must be executed in Indonesian, although versions in other languages are permitted.

#### The International Commercial Contract as the Key Issue

The contract in the case under discussion is written in English, notwithstanding the parties’ choice of Indonesian law as the governing law of this loan contract. A deed of fiduciary security executed in the Indonesian language was concluded to secure the loan. Thus, the contract terms are certainly legally binding to the parties, terms dealing with issues within the contract, including the obligations and duties of both parties as well as the language of the contract. In this context, Kessler (1943) maintained that there was no contract without assent, but once the objective manifestations of assent were present, their author was bound.

Initially, the contract was working well, until December 2011, when BKPL began to discontinue repayment, even though it had paid a large portion of the loan, which totalled US \$4.422.00. NINE AM then brought this case before the court, seeking payment of the overdue principal and interest, after its demand letter (*somasi*)

failed. BKPL responded to this claim by asserting that the contract itself did not conform to the requirements of Act 24/2009 because it was written only in English. The District Court ruled that the contract in question is contradicted by Article 1320 ICC, which stipulates that a lawful contract should fulfill four requirements, namely, free consent of the parties, legal capacity of the parties, a defined object and the presence of a legal cause. The contract did not fulfil the last requirement and thus became null and void (vide Art. 1335 jo. 1337 ICC). The Court disregarded a letter by the Minister of Law and Human Rights (MOLHR) concerning the implications and implementation of Act 24/2009 because it was not on the list of the order of laws and regulations stipulated by Article 7 of Act 12/2011 on the Formation of Law and Regulations (Indonesian Gazette No. 5234).

### **The Nature of A Commercial Contract**

Young (2010) maintained that a contract was an agreement (usually made between two or more parties) giving rise to obligations on the part of both persons which were enforced or recognized by law. While Fisher and Greenwood (2011) defined a contract as a “legally enforceable agreement”, Gibson (2005) specified that a contract was an agreement (or a set of promises) between two or more parties under which legal rights and obligations were created and enforceable. The element of agreement is of crucial importance because it distinguishes contracts from other forms of obligation,

notably tortious ones (Gibson, 2005). According to *Smith v. Hughes* (1871), if, whatever a man’s real intention may be, he so conducts himself that a reasonable man would believe that he was assenting to the terms proposed by the other party, and that other party upon that belief enters into the contract with him, the man thus conducting himself would be equally bound as if he had intended to agree to the other party’s terms.

A test needed for whether an agreement has been reached is an objective one. Hough and Kuhnel-Fitchen (2014) further argued that the subjective intentions of the parties were not relevant. According to Fisher and Greenwood (2011), the elements of agreement must be qualified. Ideally, the agreement shall involve intense haggling, give and take between parties, and ultimate consensus (Young, 2010). In this context, it is essential to distinguish the notions of agreement from the contract. Arjunan and Baksh (2008) maintained that although “agreement is an integral part of a contract, it is not, by itself, sufficient and would fall short of a contract.” To be a contract, an agreement must satisfy other elements. For example, s.10 (1) of the *Malaysian Contract Act 1950*, states that “all agreements are contracts if they are made by the free consent of the parties competent to contract, for a lawful consideration and with a lawful object, and are not hereby expressly declared to be void.”

Generally, a businessman entering into a contract or an international commercial transaction is interested in drafting a private

agreement that will satisfy both parties and will be performed as drafted. The parties sign the contract because they wish to transact business, and they will agree to the contract in good faith. Good faith “emphasizes faithfulness to an agreed common purpose and consistency with the justified expectations of the other party...” (Garner, Garner, Jackson, McDaniel, & Newman, 2009).

Connor, as cited in Mitchell (2008), stated that good faith was a basic principle of civil law, canon law and international law, which, was rooted in Roman law (*bonafides*), which is associated with trustworthiness, conscientiousness, and honourable conduct, and which is its most direct ancestor. It describes a significant general principle of law that refers to private contracts, one that underlies the entire system of contract-based relations between private parties. In the Indonesian context, Article 1338 para. 3 ICC states that a contract must be performed in good faith. This is related to the general principle of correct behaviour in commercial practice. The essence of good faith is honesty, which is a subjective state of mind, but the principle can also incorporate notions of fairness and reasonableness, both of which concern an objective state of affairs.

The good faith principle related to the *pacta sunt servanda* principle states that the parties are bound by the contract that they have signed. According to one definition, this Latin phrase translates roughly as “agreements must be observed” (Garner et

al., 2009). In essence, this principle stresses that the contract, more precisely its clauses, are law between the parties, and implies that nonfulfillment of respective obligations constitutes a breach of contract.

Theoretically, the validity of an international commercial contract is based on the principle of freedom of contract, which is of paramount importance in the context of international trade. The binding character of the contract obviously presupposes that an agreement has actually been concluded by the parties and that the agreement reached is not affected by any grounds for invalidity. In drafting a contract, one must be sensitive to the difference between an international contract and contracts that are to be enacted domestically. It is a mistake to assume that there are no differences between the two. In contrast to purely domestic transactions, the language differences between the parties to international contracts often demand that the parties agree to a single, official language for the contract, even if the document is translated into other languages for the convenience of the parties. Indeed, a contract is a purely private commercial agreement between parties. The parties can negotiate almost everything and include what they wish into a contract, including a requirement about the contract’s official language. In bilingual contracts, the parties thereto may consent on the governing language of the contract, thereby exercising their freedom of contract, and simultaneously established clarity in the contract as well because the governing language shall prevail and take

precedence over the other language version. In the case concerned, a bilingual contract would also avoid the contract contradicting with Act 24/2009 because it would not have been written exclusively in English.

### **Legal Uncertainty of the Implementation of Act 24/2009**

International contracts have become an indispensable means of exchanging goods and services in today's international trading system. Transnational economic transactions between individuals include both business and legal risks. International trade requires not only a trusting business relationship between parties but also legal certainty about the application of international contracts to certain countries. On the latter topic, Neuhaus (1963) expressed the view that the promotion of legal certainty, with a view to eliminating the legal risks of business and other transactions by making them clearly predictable, was considered more important than the struggle for justice and equity, which were generally not considered endangered.

The provisions of Act 24/2009 in essence confirmed that the Indonesian language functions as an official language for transactions and commercial documents. The District Court had confirmed and judged pretty much similar with the Act 24/2009 provisions, or in other words, the Courts have decided the case normatively as is stated in the Act 24/2009. The justification for the use of the Indonesian language is that it underscores Indonesian unity and the nation's identity and existence, as it has become a symbol of the sovereignty

and dignity of Indonesia as mandated by the Constitution. The Act further states that if agreements and contracts are executed in multiple languages, i.e., the Indonesian language, the national language of the foreign party and/or the English language, each version is equally original. No sanctions exist for violations to the obligation to use the Indonesian language. The government has issued Government Regulation 57/2014 as ancillary to Act 24/2009. Unfortunately, as this Regulation does not contain provisions on contractual languages, the problems surrounding international commercial contracts where Indonesian parties are involved remain unresolved and may create legal uncertainty.

One should bear in mind that it has long been the way for the Indonesian government to encourage investor-friendly law-making to promote foreign investment. Indeed, the government has taken significant steps to improve Indonesia's business environment, such as reducing corporation taxes, simplifying its licensing processes, and amending laws to give foreign companies greater protection. It is probable that Act 24/2009 has created legal uncertainty, especially in the international business community. Consequently, Indonesia may continue to feature prominently in future complexities, as in 2015 it was ranked as the second most complex place for business compliance in the world (Mondaq, 2016). Thus, it is a matter of some urgency for Indonesia to promote legal certainty by eliminating the legal risks surrounding business by making them clearly predictable.

**Language As A Cultural Element in An International Contract**

Common problems in the process of contract drafting for international contracts are related to the cultural and linguistic aspects of the states or parties. The role of the contract can be viewed differently in different cultures. The parties should be very cautious of the pitfalls and dangers of negotiating and drafting contracts involving cultural and linguistic matters. Language differences can cause serious problems of interpretation (Fox, 1992). DeLaume, in his book *Transnational Contracts*, identified some French words which were similar to English but had different meanings in English (as cited in Fox, 1992), as shown in Table 1.

Table 1  
*Words and different meanings*

English	French
Compromise	Transaction
Agreement to arbitrate	Compromise
Execution	Signature
Performance	Execution

Source: Fox, 1992

The examples above show that problems may arise even in cultural systems where languages are somewhat similar and have common roots. This translation problem would also be far more serious for the countries with vast differences in culture, legal systems and language. Thus Fox (1992) maintained that for a contract between two parties who spoke different languages, it was generally conceded that an international commercial contract should

have an official language as well as be translated into the languages of the various contracting parties.

In a dual-language contract, the parties should decide which of the two languages will predominate. If neither party states which one predominates, in practice the foreign language version will normally prevail in a local court, which will apply local law if different interpretation criteria or discrepancies arise. Thus, both parties should always be aware of what the foreign language contract says. To prevent conflict between the two languages, it is essential to consider which will have priority; hence the agreement must be extremely clear. For dual language contracts, an IACCM research paper (Cilotta, 2014, para. 25) proposed that the parties should state that the original version is in a certain language (e.g., English) and that if a conflict or discrepancy occurs between the languages, one language shall prevail and take precedence over the other. Cilotta (2014) suggested the following example of a clause in a contract:

This agreement is in both languages, English and Spanish. In the event of any inconsistency, the English version is the original language and the Spanish version is a translation for information purposes only. In case of conflict, the English version will prevail and will therefore be the binding version for both parties (para. 27).

The requirement of the Indonesian language in international commercial contracts from an international law perspective



The BPKL challenged the validity of the contract based on its language. It should be noted that freedom of contract is a solemn principle in drawing up international commercial contracts and includes freedom to choose language. However, the Court was of the opinion that the absence of the Indonesian version of the contract violated Article 31 of Act 24/2009, which resulted in the contract having an illegal cause; thus, the contract was deemed null and void, as it contravenes Article 1335 of ICC, which states that an agreement which has been made for a false or forbidden reason shall have no effect. Those who entered into agreements involving Indonesian parties after 9 July 2009 should take the Court's decision into account. This potentially affects not only Indonesian law-governed contracts but also all contracts regardless of the governing law of the contract. This may lead some to consider Indonesia not an investor-friendly region for foreign lenders and financiers, especially given the difficulties involved in translating contractual terms, let alone into the Indonesian language.

The contractual parties should take firm precautions, at least three steps, to prevent any possibility of a void contract. First, the contract should be drafted as a dual-language agreement in both English and Indonesian, regardless of the governing law. Second, the parties should have an agreed-upon clause in the contract stating that an Indonesian translation will form an integral part of that contract. Third, the parties should be careful with their wishes that place the contract to contradict with the law. In essence, the

parties to the contract make the law for themselves; so long as they do not infringe on some legal prohibition, they can make whatever rules they wish with respect to the subject matter of their agreement, and the law will uphold their decisions (Young, 2010). The role of the courts is to identify and enforce the contractual will of the parties and to intervene as little as possible with respect to bargains freely made by competent adults.

This concerning issue requires an adequate response from the government, as Indonesia is moving towards a liberalized trade arena and has agreed to some commitments within Association of Southeast Asian Nations (ASEAN) by establishing the ASEAN Community 2015 (AC 2015) that comprises of the ASEAN Political Security Community (APSC), the ASEAN Economic Community (AEC) and the ASEAN Socio-Cultural Community (ASCC). In this context, ASEAN aims to establish a region as a single-market and production base, providing economic cross-border liberalization via a free flow of goods, services, foreign direct investment (FDI), skilled labour and freer flow of capital. Pelkmans (2016) observed that

The very purpose of the ASEAN Economic Community (AEC) is to attract more foreign direct investment (FDI), to increase local value-added in global value chains, and to generate additional prosperity by moving up the ladder of dynamic comparative advantage and quality in a fiercely competitive setting in East Asia and beyond (p. 12).

ASEAN Blueprint 2025 provides broad direction through strategic measures for ASEAN from 2016 to 2025. It aims to have an ASEAN by 2025 that is “highly integrated and cohesive, competitive, innovative and dynamic; ... people-oriented, people-centred community, integrated with the global economy”. The establishment of the AC 2015 aims to create a competitive, people-oriented arena which will be integrated with the global economy by 2025. Beyond 2015, as the effect of the implementation of the AEC in the Member States regions, as one community, for the next ten years, more businesses and individuals are expected to participate in, and benefit from ASEAN regional economic integration.

FDI will also divert to the ASEAN competitive integrated market as it offers good reasons for home-grown businesses to expand their market reach. Since ASEAN is a well-positioned region at the centre of the global production network, ASEAN has diverse strength and potential to integrate into the global chain. ASEAN remains a major destination of global FDI receiving around 16 percent of the world FDI among developing economics with total FDI flow of US\$120 billion in 2015 (ASEAN and UNCTAD, 2016). In this context, Indonesia has to take these opportunities to be active in investing and expanding in other Member States’ various industries, and vice versa. In other words, as a competitive region, Indonesia should prepare its entire legal infrastructure, including its regulations, to be a business-friendly environment in this globalized trade liberation era. It is urgent

for Indonesia to be prepared, as Mugijayani and Kartika (2012) have noted, because the major players of the AEC will be large companies, foreign companies, and foreign affiliates whose activities are related to export-import, or local companies involved in international production networks. International transactions will observe distinctive increase in growth compared to previous years as the number of international contracts rise as the result of the continuously expanding Indonesian market as a part of the AEC integrated market.

Furthermore, the AEC Blueprint 2025 aims to “foster robust productivity growth ... designed for commercial application to increase ASEAN’s competitive edge in moving the region up the global value chains (GVCs) into higher technology and knowledge-intensive manufacturing and services industries” (ASEAN, 2015). Thus, participation from international commercial parties is a significant factor for ASEAN economic growth. The government should make efforts to attract foreign investors to transact business in Indonesia. According to the annual report of the Global Benchmark Complexity Index by the TMF Group, which ranks 95 countries based on regulatory and compliance regimes, Indonesia was ranked the second most complex place for multinationals to remain compliant with corporate regulations and legislation during 2015. Furthermore, Indonesia has been included in the Index’s top 10 most complex countries for three years running, and has moved up from seventh to second place.

## CONCLUSIONS

The NINE AM case is the first to concern Indonesian as the mandatory language of international commercial contracts in Indonesia. The Court's decision was final and binding following the Supreme Court decision. The English-only version of the international commercial contract is null and void because it contravenes Article 31 of Act 24/2009. This has provoked controversial debate in Indonesia, especially within the international commercial community. The Court's decision is not timely, as the Indonesian government is currently in the middle of economic agreement commitments with ASEAN, which needs an investor-friendly economy for the domestic market.

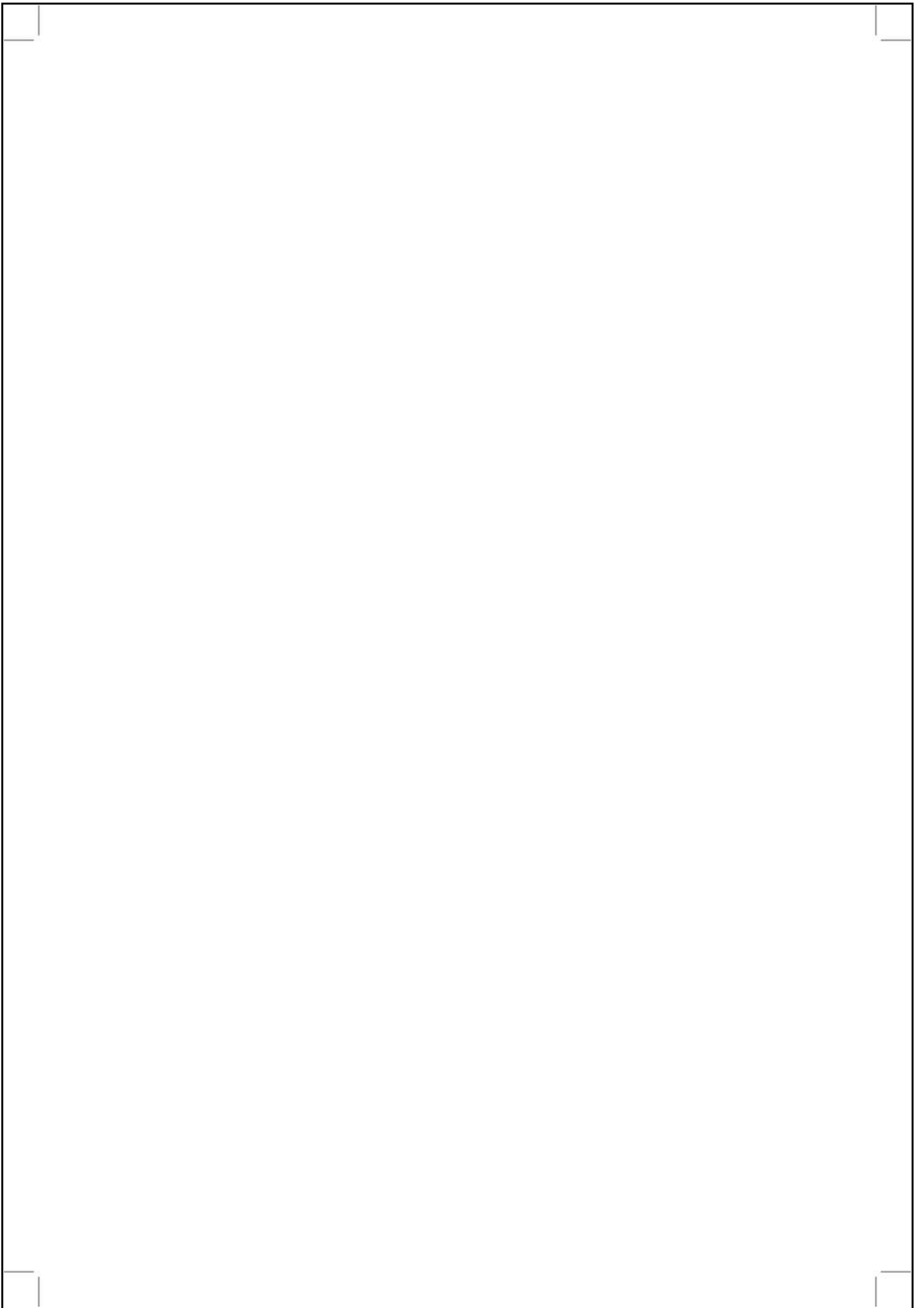
In ensuring legal certainty and preventing undesirable dispute it offers a viable solution for foreign investors engaging with local parties to establish their businesses in Indonesia, in which every contract with Indonesian entities or individuals is in both Indonesian and English or another foreign language. In this respect, the foreign language version would be deemed the predominant version and would prevail in case of contradictions. Furthermore, the Indonesian version ensures that the Indonesian party understands the contract and also fulfils the requirements of Article 31 of Act 24/2009. The contracting parties should follow this fairly practical solution because Government Regulation 57/2014 provides no details on fulfilling the obligation to use Indonesian in a contract with Indonesian parties. Another

implementing regulation focusing on dual-language contracts should be issued, as this would reassure existing investors and prevent further confusion in the future, as well as safeguard investors' trust that the business and cooperation they will establish in Indonesia will not be ruined by mere formalities.

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