



Navigating the Principles of Good Faith under Indonesian and Dutch Law

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The shared history between the Netherlands and Indonesia has given rise to extensive Dutch influence on the Indonesian legal system, including on the governance of civil and commercial matters through the adoption in 1847 in Dutch-held Indonesia of the 1830 Civil Code of the Netherlands (the *Burgerlijk Wetboek* or the “**BW**”). Since Indonesia gained its independence in 1945, the development of civil and commercial law in both countries has diverged as each country has developed its own case laws and jurisprudence. It should also be noted that the BW, as issued in 1830, has largely remained in force in Indonesia and is now referred to as the Indonesian Civil Code or “**ICC**”, whereas the Netherlands substantively reformed the BW in 1992.

This article is part of a series of publications aimed at discussing the distinctions between the key contractual law features and the principles under the BW developed under the Indonesian and Dutch legal frameworks, exploring also how such principles are applied in a commercial context. In this article, we will analyse how the principle of “good faith” is applied in both jurisdictions as well as the key concerns in navigating the issue within each jurisdiction.

1. The principle of good faith

Indonesia

Many jurisdictions of both civil and common law traditions have long recognised an obligation to act in “good faith” when concluding or performing contracts. Indonesia is no exception in this regard as one of the fundamental principles in the ICC is that parties to a contract must perform their obligations under such a contract in “good faith”. The ICC (and Indonesian contractual law as a whole) does not recognise a universal definition of “good faith” and the assessment of (i) whether such a principle has been satisfied in respect of any individual contract as well as (ii) the consequences arising from the satisfaction or violation of such a principle are generally carried out on a case-by-case basis by holistically analysing each situation through the use of a combination of ICC textual provisions, case laws and jurisprudence.

That being said, there are generally two widely-accepted legal tests that are often used by Indonesian judges to determine whether the obligation to perform a contract in “good faith” has been satisfied in any given case, each commonly referred to as the “subjective test” and the “objective test”.

(a) Subjective test

One of the legal tests consistently applied by Indonesian judges and supported by legal scholars to assess the existence of “good faith” in the making or performance of a contract is the “subjective test”. This test is typically applied in cases involving disputed ownership of land and it involves assessing whether a purchaser (i) has acted in a manner that demonstrates “honesty or sincerity” and (ii) has observed the applicable laws (ie, has acted in “good faith”). Purchasers that are proven to have acted in “good faith” in their acquisition of the relevant plot of land are typically afforded affirmation of their ownership of the land by Indonesian courts.

Such a principle is also manifested in Circular Letter No. 4 of 2016 (“**Circular Letter 4/2016**”), issued by the Indonesian Supreme Court, which contains a guideline for judges for determining whether or not a purchaser of a plot of land has acted in “good faith”. Circular Letter 4/2016 indicates that a buyer is considered to have acted in “good faith” if they (i) have observed the applicable laws and regulations in carrying out the transaction and (ii) have demonstrated a degree of care in the carrying out of due diligence on the land in question.

As a further illustration of this, in 2010, the Indonesian Supreme Court issued Decision No. 2318.K/Pdt/2009 where it dealt with a land ownership dispute between two parties. The court ultimately assigned ownership of the land to the defendant on the basis that the latter had acted in “good faith” when purchasing the plot of land by carrying out the purchase in accordance with the applicable laws and requirements.

More recently, the Constitutional Court issued Decision No. 83/PUU-XXII/2024 (“**Decision 83**”). This ruling dealt with the constitutionality of a long-standing legal provision concerning insurance contracts¹. Notably, in its reasoning, the court affirmed that parties to a contract have a duty to exhibit “subjective good faith” by acting with honesty and transparency, being attentive to each other, and refraining from causing harm to the other party. While the court does not touch on the range of conducts that indicate a lack of subjective good faith, omitting or concealing information crucial to the contract from the other party can be construed as a conduct that exhibits lack of good faith. The ruling underscores the significance not only of the content of the contract but also of the parties’ conduct before and during its inception.

(b) Objective test

The other legal test commonly applied by Indonesian judges to determine whether the conclusion or performance of a contract has satisfied the “good faith” principle is the “objective test”. Through this test, judges will consider whether the implementation of the terms of a contract would be contrary to “appropriateness and fairness”. Unlike the subjective test, which primarily applies to land transactions, the objective test applies to all contracts in general (such as facility agreements and service agreements). The focus of the objective test is to ensure that no “inappropriate or unfair” terms are included and/or enforced in Indonesia.

A provision related to this issue that is worth discussing is Article 1339 of the ICC, which provides that an agreement is not only binding on the matters expressly agreed to by the parties in such an agreement, but also, due to the nature of the agreement, must also be legally binding on the parties based on the principles of fairness, customs/common practice and applicable laws. While this is similar to the concept of an “objective test”, as discussed in the preceding paragraph, the key difference is that this provision contemplates the rights and obligations that exist in addition to what is agreed as opposed to whether the terms of a contract are sufficiently appropriate and fair to be deemed to have been made in “good faith”. Therefore, when considering the terms of a contract, Indonesian judges will typically not only assess whether such terms are sufficiently appropriate and fair, but may also infer additional rights and obligations on the parties that are not expressly governed in the contract based on the principles of fairness, common practice and applicable laws.

As an illustration, in 2020, the Pasir Pengaraian District Court issued a decision concerning a dispute between the borrower and the lender in a loan agreement with monthly interest rates ranging from 15% to 20%. The borrower had failed to make several scheduled repayments and this prompted the lender to file a claim to the court seeking damages amounting to the outstanding payments. While the court ordered the borrower to make the loan repayment to the lender, it unilaterally reduced the interest rate applicable to the loan to 1%², thereby reducing the amount payable by the borrower. The court’s reasoning was that the initial interest rates of 15% to 20% were unusually high, making it inappropriate, unfair and overly onerous to be imposed on the borrower. The court viewed that a party acting in “good faith” should not seek to implement such an exorbitant interest rate and it considered that, notwithstanding the borrower having entered into the agreement, the fact that the lender sought to impose such overly onerous terms upon the borrower demonstrated that it had not acted in “good faith”.

In Decision 83, the Constitutional Court also touched upon the concept of objective good faith, where the court affirmed it as a fundamental pillar of the principle of good faith in its entirety (alongside subjective good faith). Consistent with our discussion above, the court clarified that the principle of objective good faith requires the terms of a contract to reflect norms of “decency, propriety, and morality”. In practice, this standard ensures that the contract does not contain any terms that are inappropriate, indecent, or unfair.

In other words, in order to satisfy the objective test to determine the existence of “good faith”, a contract should not contain any unusually onerous or unfair terms and parties to a contract should be aware of the prevailing market practices for the relevant transaction to avoid such a pitfall.

1 Decision 83 was issued to deal with a challenge to the constitutionality of Article 251 of the Indonesian Commercial Code, which allowed insurers to, unilaterally and without a court judgement, terminate an insurance policy if the insured did not disclose material information during the policy’s inception. The Constitutional Court adjusted this provision so that insurance providers can only terminate an insurance policy with the consent of the insured or a court judgement (even if the insured failed to disclose material information when entering into the policy).

2 It is a slightly unusual practice for Indonesian courts to unilaterally alter the interest rate in a loan agreement without the consent of the parties, especially since the initial interest rate was negotiated and agreed to by the parties. However, the key emphasis here is that the court views that the imposition of an unusually high interest rate is inconsistent with the principle of “good faith” where the provisions of a contract must adhere to the reasonableness and fairness standard.

The Netherlands

Under Dutch law, the starting point for contractual interpretation is an analysis of the parties' common intention, which involves and is influenced by any and all circumstances of the case that the court considers to be relevant. The principles governing interpretation can, in turn, be derived from both (i) Dutch statutory provisions as well as (ii) settled case law. When it comes to the Dutch statutory provisions, three provisions of the BW are most relevant in the context of contractual interpretation: Articles 3:33, 3:35 and 6:248. As will be explained further below, the first and second provisions generally relate to "subjective good faith" (focusing specifically on subjective party intentions), while the "reasonable and fairness" standard in the third provision relates to "objective good faith" (ie, what the objective standard of reasonableness and fairness requires in a given situation).

Subjective good faith

The first provision and second provision, the often-paired Articles 3:33 and 3:35 of the BW, embody the so-called "doctrine of will and reliance" (in Dutch: *wilsvertrouwensleer*). On the one hand, the law provides that any party's action intended to have legal effect can only have such an effect if there is a will (or "intention") to that end, which is expressed through a certain representation or statement. On the other hand, if a party has interpreted another party's statement or conduct, in accordance with the meaning that it could reasonably attribute to it under the given circumstances, as a declaration of a certain intent directed to it by the other party, this other party cannot invoke that there was no will consistent with this declaration. More simply put, the absence of intention in one party's declaration cannot be used against the other party if the latter reasonably interpreted the declaration as having a specific meaning.

In essence, then, when interpreting a contract, Dutch courts will consider the parties' original intentions. However, parties cannot successfully argue that they did not have the intention to be bound to a certain agreement if their conduct and/or declaration could reasonably be interpreted by the other party as an expression of their willingness to be bound.

Objective good faith

The third provision that we need to flag in this context is Article 6:248 of the BW, the first paragraph of which provides that *"[a]n agreement not only has the legal consequences agreed to by the parties, but also those which, according to the nature of the agreement, apply by virtue of law, usage or the standards of reasonableness and fairness"*. As mentioned above, the reasonableness and fairness standard in this provision is sometimes also referred to as "objective good faith". This provision does not necessarily contemplate the interpretation of contracts as such, but, rather, is focused more on what rights and obligations exist in addition to what is agreed (and interpreted). Thus, if parties left a gap in the contract, a court may supplement the gap as long as it is done along the lines provided by the contract and by applying the standard of reasonableness and fairness. However, this does not mean that, in interpreting contracts, the standard of reasonableness and fairness does not play a role (as will be discussed in section 2 below). Furthermore, unlike the "Objective Test" provided under Indonesian law, Article 6:248(1) of the BW does not provide judges with the authority to unilaterally modify the terms of a contract for the sake of reasonableness and fairness but is rather aimed at providing judges with the necessary tools to fill gaps within a contract.

The second paragraph of Article 6:248 of the BW is also an expression of "objective good faith". More specifically, it provides that *"[a] rule binding upon the parties as a result of the agreement shall not apply to the extent that, in the given circumstances, this would be unacceptable according to standards of reasonableness and fairness"*. For a party to successfully argue that they should not be held to an agreement on the basis of "good faith", they must thus be able to argue that the other party's conduct is, by the standard of reasonableness and fairness, *unacceptable*. This is a high standard, to which Dutch courts take a restrictive approach.

2. Case study

Indonesia

A notable Indonesian arbitration case where the principle of “good faith” sat at the core of the dispute and was therefore addressed extensively was *Himpurna California Energy Ltd. (“Himpurna”) v PT Perusahaan Listrik Negara (Persero) (“PLN”)*. Himpurna and PLN had entered into an Energy Sales Contract (“ESC”) in 1994 where PLN had agreed to purchase a certain volume of energy from Himpurna on a regular basis. However, in 1997, PLN’s financial position was greatly affected by the Asian financial crisis which resulted in PLN being unable to fulfil its minimum required purchase quantity from Himpurna under the ESC. This prompted Himpurna to initiate an arbitral proceeding against PLN for breach of contract with an ad hoc tribunal in Jakarta.

PLN argued that the economic downturn materially impacted PLN’s financial capability to purchase electricity from Himpurna, rendering the terms of the ESC overly onerous for PLN. It further argued that, as a demonstration of its “good faith”, Himpurna should seek to renegotiate the terms of the agreement and refrain from seeking enforcement of the existing terms as it would be neither appropriate nor fair for Himpurna to seek the full performance of the contract in such a situation. In other words, PLN sought to convince the tribunal to apply the “objective test” in this case and conclude that the terms of the contract were not “appropriate or fair” and would be overly onerous to be imposed on PLN during the economic situation and that, as a result, PLN should not be compelled to fully perform the contract.

However, the tribunal rejected this argument for several reasons. First, the tribunal considered that Himpurna’s correspondence with PLN and various Ministers of Indonesia indicated that PLN was aware of its obligations to fully perform the contract. Second, PLN’s willingness to use US Dollars to calculate the energy purchase price in the contract shows that the parties unambiguously allocated the risk of a potential depreciation of the Rupiah to PLN. For these reasons, the tribunal determined that PLN’s insistence that Himpurna was under a “good faith” obligation to renegotiate the terms of the contract was made in bad faith as PLN had demonstrated a degree of awareness that it was under an obligation to fully perform the contract. On 4 May 1999, the arbitral tribunal issued an award in favour of Himpurna and ordered PLN to pay US\$391,711,652 to Himpurna in damages and proceeding costs. This demonstrates that, although the “good faith” principle requires parties to refrain from including unreasonably onerous provisions in a contract, there is an underlying expectation under Indonesian law that, even in extraordinary circumstances, parties to a contract should work towards implementing the original provisions of the contract and avoid contesting the validity of a provision merely as a means to circumvent its contractual obligations.

The Netherlands

Over the years, the Dutch Supreme Court has developed a unique canon of contractual interpretation that has its genesis with the *Haviltex* judgment issued by the Dutch Supreme Court on 13 March 1981. In the *Haviltex* case, which builds on the system of Articles 3:33 and 3:35 of the BW, the Dutch Supreme Court ruled that contract interpretation went beyond a purely linguistic interpretation of the relevant provisions. Instead, interpretation thereof depended on the meaning that parties in the given circumstances could both reasonably mutually ascribe to these provisions and on what they could reasonably expect from one another on this matter. Relevant circumstances also include the social circles the parties belong to and what legal knowledge can be expected from such parties. Subsequently, in the matter of *DSM v Fox*, the Dutch Supreme Court decided that all circumstances of a specific case, assessed in accordance with the standard of reasonableness and fairness, are of decisive meaning when interpreting a written contract. This is not to say, however, that the wording of a contract is meaningless in its interpretation. Quite the contrary: there are many cases where significant weight is attached thereto, also where both parties are professional or commercial in nature.

In any event, the significant role of the *Haviltex* standard set out by the Dutch Supreme Court in contract interpretation under Dutch law has triggered a discussion as to whether the parties are able to “contract out” of this standard. Put differently, can the parties contractually agree that the literal meaning of the contract (and not its context) should prevail?

A recent decision of the Dutch Supreme Court has reintroduced this discussion. The case related to the preamble of a settlement agreement between former spouses that included an express deviation from the *Haviltex* standard that required the “competent court” to interpret the agreement on a solely grammatical basis: “*the competent court shall interpret and apply the provisions as contained in the present agreement solely grammatically*”. Pursuant to the text of the provision that had to be interpreted, the spousal support had to be paid until “*the wife reached the retirement age, ie, 24 May 2021*”. In reality, however, that retirement age would only be reached on 24 May 2022, which was a full year later.

The district court, deviating from the literal text of the agreement, held that the obligation to pay spousal support continued until 24 May 2022. The Court of Appeal, however, departed from the lower court’s decision and rejected the extension of spousal support on the ground that the parties had explicitly excluded the *Haviltex* standard. According to the Court of Appeal, the end date of the spousal support in the settlement agreement itself was not open to multiple interpretations, while the words “retirement age” used therein were. In view of the agreed-upon exclusion of the *Haviltex* standard, its application was not permitted to assess these multiple interpretations. The Court of Appeal therefore held that the end date of the spousal support was 24 May 2021.

The Court of Appeal’s judgment was upheld by the Dutch Supreme Court. However, the relevant interpretation clause was not complained against, and consequently it was not subject to the Dutch Supreme Court’s review. It is therefore yet to be seen what the consequences of this decision will be.

3. Key takeaways

Indonesia

Businesses should generally consider the following issues when entering into and/or performing an agreement in Indonesia:

- (a) Ensure that their actions, throughout the conclusion and performance of an agreement, are in line with the applicable laws and does not demonstrate a lack of sincere intention to enter into the contract in good faith (eg, by refraining from concealing or omitting crucial information when negotiating a contract).
- (b) Consider the potential situations where their performance of a contract could potentially be hampered or delayed (eg, by an economic downturn or a pandemic) and whether it would make sense to include provisions allowing the parties to adjust the terms of the agreement or invoke *force majeure* or hardship in such instances.
- (c) Consider whether any of the proposed terms of an agreement could be construed as “inappropriate or unfair” in Indonesia, given that Indonesian judges may not look at onerous terms favourably.
- (d) In any situation involving a potential or actual dispute, prior to making any statements or committing any actions that are contrary to contractual terms, consider whether such actions or statements could be construed as a demonstration of a lack of “good faith” (eg, showcasing a breach of contract while at the same time refusing to perform its obligations under an agreement). This means that the expectation under “good faith” principles is for the parties to implement the contractual obligations. If there are situations which would prevent a party from performing their contractual obligations, such party should notify the other party, as soon as practicable, of the situations, and find a mutually acceptable solution to implement the contract pursuant to the parties’ original intention, for which the contract was entered into, as soon as the issues have been mitigated.

The Netherlands

Businesses should generally consider the following issues when entering into an agreement governed by Dutch law:

- (a) Consider whether the proposed terms of an agreement accurately reflect the parties’ intentions, as the wording of a contract will still be afforded significant weight.
- (b) Ensure that, to the extent practicable, the intention and expectations of the parties in respect of the contract are well-documented and expressed.
- (c) Consider inserting an “interpretation clause” governing the intended rules and principles that will be used to interpret the provisions of the contract, while keeping in mind that the effects thereof are not yet settled under Dutch (case) law.

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