COMPARISON BETWEEN CONSTRUCTION CONTRACT USED FOR
GOVERNMENT PROJECTS IN INDONESIA AND MALAYSIA

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COMPARISON BETWEEN CONSTRUCTION CONTRACT USED FOR GOVERNMENT PROJECTS IN INDONESIA AND MALAYSIA

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DEDICATION

“To my beloved wife, son, mother, and father”
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ABSTRACT

Standard forms of contract have been used widely in construction industry in the world. PWD 203A (Rev.2007) is one of Malaysian standard forms of construction contract for building and civil projects for public work. In contrast Indonesia still do not have a standard form of construction contract unless for government project where a regulation for Standards and Guidelines for the Procurement of Construction Services which was published by Ministry of Public Work of Indonesia (Permen No.43/2007) that has been in use. The important thing is that the standard form of contract are drafted based on its construction practices, circumstances, nature of politic and culture of the society. It is presumed that there are some similarities and differences of its provisions, term and conditions since Malaysia and Indonesia have similar cultural roots while having a different legal basis. The main objective of this research is to compare the PWD 203A (Rev.2007) and the Permen No.43/2007 and find out how far the similarities and differences on the terms and conditions of the both forms. Hopefully in the future can be used to develop and improve the current standard of government’s contract for construction industry as well as to identify the disputes earlier and minimize it. The focus on the comparative study is on the selected clauses which are considered as dispute area in construction industry i.e., Payment to Contractor, Variation, Delay and Extension of Time, Dispute Resolution, Termination of Contract and Contractor. This is a descriptive study which is combine literature analysis and interview techniques. The research found that in general there are more similarities than differences between the two forms. The system of administration of contract between PWD 203A (Rev. 2007) and Permen No.43/2007 is significantly different. Under PWD 203A (Rev.2007), Advance Payment not expressly stated and there is no remedies for late payment by the employer as well as Pemen No.43/2007. PWD 203A (Rev.2007) also provide detail procedure in dispute resolution than Permen No.43/2007. Moreover PWD 203A (Rev.2007) does not provide clause for determination of contractor own employment due to default by the employer. In general the Permen No. 43/2007 provides flexibility to the contract administrator in the management of the contract. Upon the analysis of selected clauses, there are some provisions that can be used to develop and improve the current regulation for standards form of contract or to draft the standard form of contract in Indonesia.
ABSTRAK

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CHAPTER 1

1INTRODUCTION

1.1 Background of the Study

Contract is a form of bond that we often encounter in everyday activities. In the construction industry, contracts are a vital component in supporting the operational activities. Almost all constructions involve a contract between employers, consultants, contractors, suppliers and buyers of the construction industry.

Contract can be defined in many ways. Section 2(h) of the Contract Act 1950 defined contract as ‘an agreement enforceable by law is a contract’. Smith & Chappell (1985) defined contract as “a legally binding agreement”. A contract is a legally binding agreement between the parties involved in the agreement to fulfil all the terms and conditions outlined in the agreement.

Construction contracts are basically different from major service contracts. Like all contracts, construction contracts are about the prior allocation of risk. Windward (1991) drew attention to the construction industry’s need to make a profit on the employment of capital: “If risk is an essential ingredient of the system which generates your profit, it is inevitable that there must be a structure for resolving disputes. It brings the relationship of the disputants back into balance so that life can resume its normal course.”

In construction contract, there are varieties of risks and factors that can have effects on the progress of the work. Therefore, risks should be managed. Identifying
and controlling the risks earlier and to avoid and minimize the risks which may arise in a contract is important. Due of the large sums of money are involved in the construction industry, it is significant that the contractual arrangement should always be formal and legal from the start of the project.

According to Web Finance (2011), construction contract can be defined as ‘formal agreement for construction, alteration, or repair of buildings or structures (bridges, dams, facilities, roads, tanks, etc.).’ Types of construction contract are varied. Generally, the choice of contract form is based on pricing, the nature of the project and the contract strategy that best meets the project objectives. The various types of construction contracts offer different ways of handling pricing, risk transfer, responsibility for performance, cost certainty and complexity. It is important that parties in the contract must fully understand the contract including their rights and obligations under them.

In Malaysia, there are several standard forms of contract being used in the construction industry. Professional institutions have issued some of them such as ‘Pertubuhan Arkitek Malaysia (PAM)’, ‘Institution of Engineers Malaysia (IEM)’ and ‘Construction Industry Development Board (CIDB)’ that are usually used for private project. While, the Public Work Department (PWD) have drafted and published the standard form of contract for the public sector.

On the other hand, Indonesia has no standard form of contract as Malaysia. Private sector project or project funded by foreign loans such ‘ADB (Asian Development Bank)’, ‘IBRD (International Bank for Reconstruction and Development)’ or other body have adopted some of international standard form such as FIDIC (Federation Internationale Des Ingenieurs-Conseils), AIA (American Institute of Architects), even JCT (Joint Contract Tribunals) to be used as the standard form of contract. For project funded by the government in Indonesia, beside the contract agreement, the provisions of construction contract are formulated by the Minister of Public Work regulation (Peraturan Menteri) on the Standards and Guidelines for the Procurement of Construction Services. The Public Work regulation governs from the procurement procedure until the implementation of construction project which is explained in general conditions and particular
conditions of contract. Nowadays the Minister Regulation being used is No. 43/2007 (Permen PU No. 43 Tahun 2007). Consequently the provisions of contract are drafted in appropriate with Indonesian law, culture and society and environmental.

Construction industry is not far from disputes that may be arise during construction period. The success of a project cannot be separated from the cooperation from parties involved i.e. the employer, the engineer and the contractor. According to the research result of Asniah (2007), the disputes causes in Malaysian construction industry consist of payment which is contribute 51%, followed by delay in completion (19%), termination (18%), variations (13%), damages (11%), performance bond (8%), defaults (8%) and defect (1%).

Meanwhile, Sumaryanto (2010), head of BP konstruksi stated that approximately 47% of disputes that were resolved in Badan Arbitrasi Nasional Indonesia (BANI) are from construction industry, which is caused by the absence of uniformity in the standard form of contract which are used as guideline by consultant, contractor and employer. Moreover, difference of interpretation of contract clauses frequently occurs due to lack of ability to analyze its provisions. Furthermore, Djoko Kirmanto (2010) commented that the understanding of contract between employer and contractor must be enhanced to increase synergy and give the same understanding of the contract clauses. Therefore, a standard form of contract is required in Indonesian construction industry to reduce disputes and claim, because of frequent usage of the same forms of contract will lead the parties to be more familiar and have more understanding in the interpretation of the clauses.

1.2 Statement of Problem

As highlighted earlier, there are several types of standard forms of construction contract being used in Malaysia. On the other hand Indonesia has no standard form of construction contract until today. Especially for government project there is a regulation for Standards and Guidelines for the Procurement of Construction Services published by Ministry of Public Work of Indonesia.
Sumaryanto (2010) stated that, quite a number of Indonesian construction disputes are resolved in arbitration due to lack of understanding of the parties of the construction contracts. Moreover, lack of uniformity of contract forms caused obstacles that often lead to differences of interpretation of different contracts. Additionally Nela et al (2007) defined the crucial factor in construction industry are caused by late payment, delay on delivery product, different interpretation of contract document, technical and managerial insufficiency of parties, change on design and undercapitalize. Furthermore, in order to assist the potential market of construction industry in Indonesia, a standard form of contract will be required so to be used. That the parties involved have better understanding to the contract which will be entered.

In this study, the clauses in the construction contract issued by Indonesian government (Permen No. 43/2007: Book1) and the Malaysian government standard form of contract (PWD 203A Rev. 2007) will be analysed to identify the differences and similarities. Indonesia and Malaysia are countries with similar cultural roots but have different legal systems. It is presumed that there are some differences of its provisions, term and conditions. Thus this will lead us to the issue of the differences and similarities between both terms and conditions of construction contract of two countries and whether the differences and similarities can develop and improve the existing Indonesian contract and encourage the scenario of drafting the standard form of contract for Indonesian construction industry.

Some clauses of construction contract, which are considered as key points in the construction disputes were chosen to be analysed in detail. The chosen clauses are payment to the contractor, variation, delay and extension of time, dispute resolution and termination of contract and contractor employment. Hopefully the findings can enhance the understanding on the construction contract to improve the provisions and can be used as a starting point to draft a standard form of contract for Indonesian construction industry. This is necessary in order to avoid more disputes and delay on completion of the projects in Indonesia.
1.3 Previous Study

There is no research in the internet or library that had discussed this topic. However, there are some study that has been done to review the contract from other countries.

1.4 Objective of the Study

The objective of the study is:

- To compare the terms and conditions of the construction contract for government projects used between Indonesia and Malaysia.

1.5 Scope of the Study

This study is limited to the terms and conditions of PWD 203A (Rev. 2007) and the general condition of Permen No.43/2007, which is considered as area of disputes in the construction industry. These clauses are as follows:

1. Payment to Contractor.
2. Variation.
3. Delay and Extension of Time.
4. Dispute Resolution.
5. Termination of Contract and Contractor Employment.
1.6 Importance of the Study

The selected clauses are considered as dispute area in construction industry. Hopefully this study will enhanced the understanding of contracting parties who are involved in construction industry. This study can be used to improve and to develop the current standard of government’s contract for construction industry as well as to identify the disputes earlier and minimize it. Furthermore, it is hope that the result of this study can be used as pre-study or starting point to draft standard form of contract in Indonesia.

1.7 Research Methodology

The following is an explanation to the research process that has been adopted to be used to this research (see Figure 1.1):

1.7.1 Development of Research Proposal

In the initial stage, the method used is discussion with experts and literature review on the scope of study. A research outline will be prepared in order to identify what kind of data is needed including its source.

1.7.2 Data Collection

After determining and settling the objectives and the scope of the study, the next step is data collection by gathering some information obtained from books, journals, papers, others researchs, contract documentary from Malaysia and Indonesia, newspapers, and on line
references such as lexis nexis contract documentary from Malaysia and Indonesia.

1.7.3 Data Analysis

The third stage involves data arrangement, analysis and interpretation. This process is to convert and analyse the collected data to information which is useful for the research purpose. This study is carried out through the combination of literature analysis / documentary study and interviews technique. The outcome of this stage tends to streamline the process of the research writing.

1.7.4 Writing Up

In the last stage of the research process mainly involves writing up and checking of the writing.
Figure 1.1 - Research Process and Method of Approach
1.8 Organization of Thesis

This study comprised of five chapters as stated below:

❖ Chapter 1 : Introduction

   This chapter will be explained the background of study, statement of problem, objective of study, limitation of study, importance of study, and research methodology.

❖ Chapter 2 : Standard Forms of Contract

   This chapter discussed the definition of standard form of contract, advantages and disadvantages of using standard form of contract in construction industry and the construction contract in Malaysia and Indonesia.

❖ Chapter 3 : General Comparison of the PWD 203A (Rev.2007) and the Permen No.43/2007

   This chapter discuss general comparison of terms and conditions between PWD 203A (Rev. 2007) and Permen No.43/2007.

❖ Chapter 4 : Analysis of Selected Clauses

   This chapter will discuss the detail analysis of selected clauses of Permen No. 43 Tahun 2007 and PWD 203A (Rev. 2007).
Chapter 5 : Conclusion and Recommendation

The last chapter of this thesis will discuss the result of the analysis and suggestion for further study.
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