

# INTERPRETING DISPUTE RESOLUTION CLAUSES

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**Abstract**—In Indonesia, courts have ruled that the presence of an alternative dispute resolution (ADR) clause denies them jurisdiction to rule on issues arising from the contract, even if the ADR clause only purports to cover particular disputes or terms and the issue before the court falls outside of the ADR clause. To explore and analyse why this is the case, the laws surrounding such clauses, especially arbitration clauses, will be analysed in the Indonesian context and then compared to the approach of other nations. The cases of *Banker Trust Company & Banker Trust International v PT. Mayora Indah, Tbk*, and *PT Buahan v PT Bali Leisure* will be used as case study for the Indonesian approach. It will be demonstrated that the absolute coverage that Indonesian courts believe ADR clauses have leads to problems where causes of action fail to be dealt with by either ADR or by litigation.

**Keywords**—ADR; arbitration; litigation

## I. INTRODUCTION

When a contract has been breached or its terms give rise to a dispute, the Indonesian legal system has often proved uncertain, with widespread corruption in the court system contributing to legal uncertainty [1]. In addition, foreign companies are often unfamiliar with Indonesian civil procedure and wary of the costs of employing lawyers and filing lawsuits in Indonesia; therefore they seek the legal certainty, and other benefits, of employing alternative dispute resolution clauses in their joint venture agreements.

These clauses seek to bind companies to undergo alternative dispute resolution, most often in the form of mediation or arbitration, and if upheld these clauses can prevent companies from suing in courts without first attempting to resolve their disputes through the outlined dispute resolution mechanism [2].

However, issues arise in Indonesia on a number of grounds. Firstly, dispute resolution clauses are often added in as an afterthought and as such tend to be poorly drafted, and have not been thoroughly tested in Indonesian courts; secondly, even if well drafted, an Indonesian court may not accept the enforceability of such a clause and allow a suit in non-compliance with the alternative dispute resolution clause to proceed. It is these two issues that are the subject of this paper, and in addition this paper also seeks to advise on the

best way to draft a binding alternative dispute resolution clause that will be effective in an Indonesian court of law.

### A. What Dispute Resolution Clauses Are and Why They Are Useful

At law, parties in a contract are obligated to carry out the contractual terms in good faith, but in practice, disputes can arise. To resolve disputes there are two broad methods:

1. Through court litigation.
2. Through alternative dispute resolution.

Alternative dispute resolution can be broken down into five separate different methods[3]:

1. Consultation
2. Negotiation
3. Mediation
4. Conciliation
5. Arbitration

Some advantages of alternative dispute resolution mechanisms, especially when compared to court litigation, are:

- The non-judicial nature of the settlement process allows parties to negotiate interests instead of legal rights;
- The flexible nature of such mechanisms can accommodate the needs of the disputing parties whereas Indonesian legal procedure can be overly formal and rigid;
- The relative speed that dispute resolution mechanisms can offer, especially if a deadline is incorporated to drive the parties to a resolution can be significantly faster than resolving disputes through litigation which can take months or years to arrive at a decision;
- The cost of alternative dispute resolution mechanisms is again significantly lower than litigation due to quicker resolution of disputes and avoiding the need to pay court fees;

- As the parties are actively involved in the creation of the settlement, they are more likely to comply with the settlement;
- The parties are more likely to be able to continue a business relationship after completing a dispute resolution settlement as they have not entered a long and often bitter litigation process with the best outcome in terms of their interests even if they have not enforced their legal rights.

#### *B. Legal Basis of Alternative Dispute Resolution Mechanisms*

There is a comprehensive international system of treaties and laws that seek to recognise and enforce differing dispute resolution mechanisms, with the most thorough being arbitration. Arbitration awards are recognised worldwide with 137 nations recognising arbitration awards. In contrast to court decisions, arbitration awards are much more transferable and their widespread recognition can make arbitration awards more easily enforceable. Indonesia has ratified and recognises in its own legal framework, the New York Convention, and the ICSID.[3]

The New York Convention has 156 parties, including Indonesia and Australia. In Indonesia, the New York Convention was ratified by the Indonesian government through Presidential Decree no. 34 of 1981, dated August 5, 1981. Thus, for any international arbitration decision which was decided by international arbitration institution outside the jurisdiction of Indonesia, acknowledgment and execution can be carried out with regard to the principle of reciprocity (hereafter 'reciprocity').

The Republic of Indonesia ratified the ICSID (International Centre for Settlement of Investment Disputes) convention through Law No. 5 Year 1968. Therefore, based on Law No. 5 1968 foreign arbitral awards can be implemented in Indonesia with written permission from the Supreme Court. The Supreme Court can only reject the arbitration decision of the Washington Convention if there are aspects to the decision deemed 'contrary to public order'.

#### *C. Indonesian Legal Basis*

In Indonesia, the legal basis for arbitration and alternative dispute resolution stipulated in Law No. 30 of 1999 on arbitration and alternative dispute resolution (UUAPS). With the enactment of this UUAPS the position and authority of arbitration in Indonesia is increasingly obvious. UUAPS provide some regulation of peaceful dispute resolution options that can be taken by the parties to finalizing the civil disputes through several means such as negotiation, conciliation, mediation, or expert judgment.

#### *D. Problems Arising from Dispute Resolution Clauses*

The problems that are often found in the implementation of the contents of the investment agreement is vagueness of the norm in clause contained in the investment agreements.

The opaqueness occurs because the words contained in the agreement result in ambiguity. This has implications for:

- Weak implementation of the agreement (poor drafting)
- The validity of the dispute resolution clause in the investment agreement (in relation to the jurisdiction of the alternative dispute resolution) (legal validity of dispute resolution clause)
- Legal certainty an agreement so as to cause damage to the parties concerned (legal uncertainty)

More specifically, where the clause fails to cover the entire agreement, Indonesian courts have declined to produce remedies to correct deficient clauses, choosing instead to declare that they lack jurisdiction.

#### E. Interpreting Arbitration and ADR Clauses

Interpreting clauses according to Indonesian Law (Civil Code) some guidance in the interpretation of the contract was formulated in the book of the Undang-undang Hukum Perdata (KUHPerd), the third book The Fourth Part of Section 1342 to 1351. Article 1342 of the Civil Code determine "if the words of a legal agreement are stated clearly, it is not permitted to deviate there from by way of".

This provision is the legal force in Indonesia for the literal method of interpretation, where only the meaning of the words are used for interpretation. These sections also stipulate that where clauses in a legal agreement are ambiguous, reference can be had to the intent and purpose of the parties of the legal agreement.

Article 1343 of the Civil Code states "if the words of a clause can be given various interpretations, it must be investigated intention of both parties to make the clause [Ambiguity is a type of uncertainty of meaning in the which Several Interpretations are plausible [1]. Thus Spake It is an attribute of any idea or statement Whose intended meaning can not be definitively resolved According to a rule or process with a finite number of steps. (The ambi- part of the name Reflects an idea of "two" as in two meanings).

## II. RESEARCH METHOD

The approach to legal research adopted by the paper is normative legal and political research, through a reading and analysis of several cases and surrounding literature on cases where ambiguous dispute resolution clauses have played major roles in disputes.

## III. RESULT AND DISCUSSION

#### A. How are ADR Clauses Interpreted in Indonesia

In Indonesia the ADR clause interpretation process is often artificially shortened to identifying whether it exists, as Indonesian law on arbitration states that where an arbitration clause exists, Indonesian courts are only able to intervene in specific circumstances.

### *1. Indonesian Cases*

The case *PT. Buahan and Bali Leisure* in case No. 733 / Rev. G / 2013 / PN.Dps. about the lawsuit defaults by PT. Buahan of the PT. Bali Leisure. This case is a case of a lease agreement brought by PT. Buahan as against PT. Bali Leisure. While the parties named their agreement a lease agreement the content of the lease agreement was about investment and took the form of a contract.[4]

The lease agreement between PT. Buahan and Bali Leisure had standard clauses which are generally contained in investment agreements. Article 14.1 of the relevant contract on arbitration reads:

*Any disputes between the parties arising out of this agreement or any of the related agreement can not first be settled by the president directors of the lessor and the lessee within 90 days of either party requesting in writing a meeting to settle the relevant dispute, shall be submitted to binding arbitration in Singapore at the Singapore Arbitration Center (SIAC)*

Article 17 paragraph 17.1 on the Law Applicable / Applicable law in the contract specifies that "This agreement will be governed and construed in accordance with the laws of the Republic of Indonesia."

The definition of default was contained in the provisions of Article 13 paragraph 13.1 which specifies that:

*For the purpose of this agreement, Event of Default means any one or more of the following events or any event or circumstance which, with the giving of any notice by any party (hereinafter shall be referred to as Non-defaulting Party and / or the lapse of any period of time and / or the non-fulfillment of the requirements could another Become following one of these events (Whether within or beyond the control of either party (hereinafter shall be referred to as the defaulting party to this agreement ...*

Ambiguous clauses in this agreement are less clear than its desired jurisdiction of arbitration the parties. The arbitration clause contained in Article 14 of the lease agreement specifies that any dispute or difference of opinion arising from the agreement is the jurisdiction of SIAC. However the clause did not cover the case of default and so SIAC has no jurisdiction on matters of default within the contract.

### *2. The Statutory Oust*

In the Indonesian legal system, the relevant regulation on alternative dispute resolution and arbitration can be found in Law No. 30 of 1999 on Arbitration and Alternative Dispute Resolution (AAPS Act). It determines that "arbitration is the way of the settlement of civil disputes outside the public courts based on the arbitration agreement made in writing by the parties to the dispute".

The arbitration clause is itself separable from the contract and the arbitration clause itself can be considered a separate agreement. Arbitration clauses can stand alone or separated from the principal agreement. The arbitration clause should be

prepared accurately and carefully to be binding. Ordinarily the aim is to avoid an ambiguous arbitration clause to avoid a situation which would allow a party to bring their case to court if the ADR process looks to produce an unfavorable result.

According Priyatna Abdurrasyid, chairman of the Indonesian National Arbitration Board (BANI), when a contractual law case is filed it is first checked whether or not there is an arbitration clause in the contract, then the validity of the arbitration clause will determine whether a dispute would be resolved through arbitration.

### *3. To What Extent are Indonesian ADR Clauses Ambiguous?*

One of the cases referenced in this article is *Bankers Trust, Banker trust international vs. PT. Mayora Indah Tbk* [5]. The other is the case of *PT. Buahan vs PT. Bali Leisure* that the agreement included an arbitration clause but separates the notion of default and disputes. Although UNCITRAL has provided a standard arbitration clause "any disputes, conflicts or claims that occur or in connection with this agreement or the breach, termination, legitimate or not an agreement will be settled by arbitration" contracting parties are free to separate issues when modifying the standard clause for their own use. For example if the parties separate understanding between default and dispute settlement case than defaults can not be done through the arbitration mechanism.

In addition to the terms of the interpretation, the arbitration clause shall also include the object of the dispute can be resolved through arbitration. Because Indonesia is based on a legal basis, Article 5 of Law Arbitration, disputes can only be resolved through arbitration in trade disputes and the rights under the laws and regulations are fully controlled by the parties to the dispute. In some cases in the Commercial Court, arises the issue of arbitration authority in handling bankruptcy cases. Until now there are two different opinions among the judges of the Commercial Court and the Supreme Court. The first opinion says that the arbitration clause is absolute. Thus, the Commercial Court should declare that it lacks jurisdiction to examine the dispute in the arbitration clause contained therein. This is based on the assumption that the procedural law applicable to the Commercial Court is the Indonesian procedural code, or HIR. This opinion is shared by judges of the Commercial Court as in the case of *PT Enindo vs. PT Putra Putri Fortuna Windu*. However, the Supreme Court found the arbitration clause in a treaty does not in itself lead to the Commercial Court in the matter of bankruptcy was not authorized trial. In this case the bankruptcy case specifically regulated in Law No. 4 of 1998 on Bankruptcy. The Commercial Court opinion is more acceptable as it is not contrary to article 3 of the Arbitration Act. However more importantly, both Courts should examine the relevant clauses before declaring that they lack jurisdiction. The Court should ask if the issues in dispute were included in the arbitration clause. Upon construction of the clause if the matter at dispute is included in the ADR clause then the issue should proceed under ADR and the relevant declaration made, otherwise the court should proceed to rule on the issue.

So that a clause on arbitration or alternative dispute resolution out of court can be said to contain vague norm if the clause does not specify in detail what the authority / jurisdiction of arbitral dispute resolution institutions.

#### *4. How do Indonesian Courts Interpret Ambiguous ADR Clauses?*

In accordance with article 11 paragraph 2 of AAPS determine “the District Court must reject and will not intervene in a dispute that has been established through arbitration, except in certain cases specified in this Act [Pengadilan Negeri wajib menolak dan tidak akan campur tangan di dalam suatu penyelesaian sengketa yang telah ditetapkan melalui arbitrase, kecuali dalam hal-hal tertentu yang ditetapkan dalam Undang-undang ini]”. It can be seen that, all disputes between the parties to a contract with a specified arbitration clause shall be settled by arbitration and either party can not take the case to the District Court.

In reality, the District Court has rejected cases brought before it if a contract has an arbitration clause. This has proven problematic where the ADR clause does not cover all causes of action arising from the contract. In the case of *PT. Buahan v PT. Bali Leisure*, the contract treated disputes and defaults differently. The general court actually has the authority to investigate and adjudicate cases of default because the jurisdiction of arbitration in accordance with the agreement between PT. Buahan and PT. Bali Leisure was merely dispute or difference of opinion.

In addition to the case between PT. Buahan and Bali Leisure, there is also the case between *Banker Trust Company & Banker Trust International v PT. Mayora Indah, Tbk*, where the parties has arbitration clauses in the agreement but Indonesian court allowed themselves to examine and prosecute the case as it in case no. 46/Pdt.G/1999 dated December 9th 1999 where *PT. Mayora* won by Indonesian court decision.

In a case of ambiguity, an extended exercise of interpretation of clauses with reference to outside material is allowed by Indonesian civil code. It is written in article no. 1342-1351. Extrinsic and purposive interpretation of clauses in a contract is only allowed when the contract contains ambiguous sentences, or the clauses are not well understood.

#### *B. How Are Ambiguous ADR Clauses Interpreted Internationally*

Internationally, there are a number of different approaches to interpreting vague and ambiguous arbitration and dispute resolution clauses. Common law countries have some form of ‘uncertainty principle’, by which any contractual term which is ambiguous or vague can be declared void by a court for uncertainty.

##### *1. Under Common Law*

In common law nations, case law has developed a set of sophisticated principles by which contractual terms including ADR clauses can be tested for certainty. The uncertainty rule also provides an example of the general common law approach to clauses which specify alternative mechanisms to litigation to resolve disputes and breaches. English law

specifically recognises that contracting parties are able to agree to be bound by an external resolution mechanism but the courts still retain their jurisdiction to determine and enforce the contract. The ADR clause can only act as a precondition to litigation and with such a term the courts will attempt to funnel disputing parties through their chosen mechanism.

The principle is found in the English case of *Scott v Avery*, and the English have passed on the principle to other common law nations. In legal systems outside of the English heritage of legal systems, ADR has taken longer to find its place in the legal system [6], but even so ADR clauses are common around the world.

#### *2. Where a Clause has been Drafted to only Cover Certain Types of Disputes*

In the English case of *Ashville Investments v Elmer Contractors* [5], and in the *Fiona Trust Case*, the court took a broad policy approach, electing to broaden the scope of the dispute resolution clause in both cases. In both cases issues falling outside the scope of the arbitration clause were ruled to be covered as the English courts have taken a policy approach. Most telling is Bingham LJ in Ashville, who state that he would be reluctant to interpret ADR clauses to result in “two sets of proceedings”. In *Fiona Trust* Lord Hoffman stated that in his view the relevant clauses should be construed with the presumption that they intend all their disputes to be heard in the same arena, unless the presumption is rebutted by clear language. Lord Hoffman cut short his analysis of the case law by stating that he shared the opinion of Long more LJ by wanting to ‘draw a line’ under the authorities on the topic, empowered s7 of the *Arbitration Act 1996* (UK), to give a broader and more presumptive reading into arbitration and ADR clauses. This represents a break from *Scott v Avery* which itself was revolutionary when the House of Lords ruled that a pre litigation arbitration clause was grounds for staying a cause of action. The net result is that in the UK the courts start with a pragmatic presumption to give effect to arbitration clauses as long as other principles of contract law including certainty are met.

#### *3. The Crucial Difference: Treatment of Jurisdiction*

The difference between the English and Indonesian approaches are the way they treat jurisdiction. The English courts have started in *Scott v Avery* from a position where they hold jurisdiction and the starting point was that the court always had jurisdiction. Pre Litigation ADR clauses did not oust the court’s jurisdiction but represented a condition prior to litigation [7]. In Indonesia article 11.2 of the UUAP specifically rejects the court’s jurisdiction to hear causes of action which are subject to arbitration clauses except in some exceptions. In other words the starting point is that Indonesian courts lack jurisdiction. For Indonesian courts this has meant that courts have outright abandoned cases over contracts with ADR clauses, even if the ADR clause itself is defective. The net result is that English courts undergo an exercise of interpreting arbitration and ADR clauses which Indonesian courts refrain from doing.

#### IV. CONCLUSION

While the legal reasoning for the failure of Indonesian courts to intervene in contractual causes of action involving incomplete ADR clauses has been explored in this paper the policy reasons have not. The reliance on article 11.2 of the Arbitration Act and the broad construction given to it and to ADR clauses by Indonesian courts has continued since the introduction of Arbitration Act and the case of *PT. Buahan and PT. Bali Leisure* is an ongoing one. Future study into why the Indonesian legal system has allowed this unsatisfactory situation of allowing incomplete ADR clauses to waive all causes of action could reveal and help to rectify problems in Indonesian investment and contract law. As shown in the cases above, there are examples of cases where ADR clauses have been interpreted to cover more than their purported scope. In English law this has seen the court send parties back to arbitration over issues which were not covered by their ADR clause. In Indonesia the result was legal limbo as the courts merely declared themselves unable to rule on matters within a contract due to the presence of the ADR clause. The Indonesian law referenced in support of such a position excludes courts the ability to make orders and from the cases Indonesian courts have constructed the legislation to exclude even hearing matters at length.

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