

## ***Enforcement of Arbitral Awards in Indonesia & Other Issues of Judicial Involvement in Arbitration<sup>1</sup>***

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### **I. BACKGROUND**

When Indonesia attained independence, in 1945, the then governing Dutch laws remained in force until such time as new laws would be promulgated to replace them. Thus Indonesia remains a civil law jurisdiction, with Dutch law as the underlying basis. Arbitration in Indonesia dates back to the mid-19th Century Dutch Code of Civil Procedure, *Burgelijke Reglement of de Rechtsvordering* (generally known as the “RV”)<sup>2</sup> coupled with the general freedom of contract provisions in the Indonesian Civil Code.

Until 1981, when Indonesia ratified the 1958 United Nations Convention on the Recognition and Enforcement of Foreign Arbitral Awards (the “New York Convention”)<sup>3</sup>, enforcement of any arbitral award was handled in the same manner as enforcement of a final and binding court judgement. However, since Article 463 of the RV provides that, except for general average awards, judgments of foreign courts cannot be enforced in Indonesia, it had previously been assumed that the same applied to foreign-rendered arbitration awards and thus these could not be enforced in Indonesia.

Even after ratification of the New York Convention, a further nine years passed before implementing regulations were promulgated, through Supreme Court Regulation No. 1 of 1990, and in the meantime the courts remained reluctant to enforce foreign-rendered awards, even though such a position was in violation of

<sup>1</sup> This paper is an updated version of the paper presented by this writer at The Inaugural International Conference on Arbitration of the Malaysia Branch of the Chartered Institute of Arbitrators in Kuala Lumpur on 1 March, 2003.

<sup>2</sup> State Gazette No. 52 of 1847, junct. No. 63 of 1849 (Arbitration was covered in Articles 615 through 651 of Title I).

<sup>3</sup> By Presidential Decree No 34 of 1981, published in the State Gazette (Berita Negara) of 1981, as No. 40, of 5 August, 1981.

Article III of the New York Convention, which provides that every contracting state must recognise and enforce awards rendered in other contracting states without imposing substantially more onerous conditions than are imposed upon recognition or enforcement of domestic awards.

The confusion was understandable, however. Since registration and application for enforcement of domestic-rendered awards was to be made in the District Court (*Pengadilan Negeri*) in the district in which the award is rendered<sup>4</sup>, the members of the Supreme Court could not agree as to which court one would apply for enforcement of a foreign-rendered award, there being no District Court in which to register, nor which would have had jurisdiction to grant enforcement of, an award rendered outside of the jurisdiction of any domestic court. Some judges therefore believed that application should be made directly to the Supreme Court; others that the awards should be “self-executing”; and still others that a single District Court should be designated to take jurisdiction over New York Convention enforcement applications.

Finally, Supreme Court Regulation No. 1 of 1990 set out the necessary implementing regulations for enforcement of arbitral awards rendered in a country which, together with Indonesia, is party to an international convention regarding implementation of foreign arbitral awards. The District Court of Central Jakarta (*Pengadilan Negeri Jakarta Pusat*) was designated as the venue to which application for enforcement thereof was to be made. The Chairman of that court was then allotted 14 days in which to transmit the request file to the Supreme Court, which was the sole court with jurisdiction to issue *exequatur*, the enforcement order, in cases of foreign-rendered awards.

Once the order of *exequatur* was granted, the same was to be sent back down to the Chairman of the District Court of Central Jakarta for implementation. If execution was to be effected in a different district (i.e. that of the domicile of the losing party), the Central Jakarta court was to transfer the order to the appropriate District Court for implementation. Execution was effected on property and possessions of the losing party in accordance with the normal provisions of the RV relating to execution of court judgements.

<sup>4</sup> Article 634 of the RV, now repealed by the new Arbitration Law, Law No. 30 of 1999.

Regulation 1 of 1990, however, did not set any time limit within which the Supreme Court was required to rule on these applications and, for the most part, they were simply docketed into the Supreme Court's normal case-load. The initial nine applications, those filed between 1991 and mid-1993, were acted upon with reasonable promptness - some in less than six months. No such orders were issued after mid-1994, however, either of *exequatur* or rejection thereof, and thus the remaining seven applications filed prior to August, 1999 may still be pending.

## **II. NEW ARBITRATION LAW**

On 12 August, 1999, Indonesia promulgated its new, and in fact its first comprehensive, Arbitration Law, Law No. 30 of 1999 (the "New Law"). The New Law, which concerns both Arbitration and Alternative Dispute Resolution, went into effect immediately upon promulgation and rescinded and superseded Articles 615 - 651 of the RV, those previously covering arbitration. Although the New Law does not also specifically rescind the provisions of Supreme Court Regulation 1 of 1990, a law is superior to a regulation in the legal hierarchy and thus to the extent that the two are inconsistent the provisions of the New Law will prevail.

### ***Domestic Awards***

The New Law codifies and confirms that Indonesia takes the territorial position on characterisation of arbitrations, as also set out in Supreme Court Regulation No. 1 of 1990, defining international awards as those rendered in arbitrations with the venue, or seat, outside of Indonesia and domestic awards as those rendered in any arbitration held within the bounds of the nation's archipelagic jurisdiction. Domestic awards must be registered with the clerk of the District Court "*having jurisdiction over the respondent*"<sup>5</sup>, which would be that court sitting in the district in which the losing party is domiciled or maintains assets, within 30 days of rendering.<sup>6</sup> Failure to so register will render the award unenforceable.

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<sup>5</sup> Article 1 (4), New Law

<sup>6</sup> Article 59 (1) , New Law.

The enforcement procedure for domestic awards allows the appropriate District Court to issue an order of execution directly if the losing party does not, after being duly summoned and so requested by the court, satisfy the award. Although no appeal is available, the losing party does have the opportunity to contest execution, both at the hearing and also after issuance of any execution order, by filing a separate contest. Although the District Court may not review the reasoning in the award itself<sup>7</sup>, it may only execute the award if both the nature of the dispute and the agreement to arbitrate meet the requirements set out in the New Law<sup>8</sup> (the dispute must be commercial in nature and within the authority of the parties to settle, and the arbitration clause must be contained in a signed writing) and if the award is not in conflict with public morality and order<sup>9</sup>. There is no recourse against rejection by the court of execution<sup>10</sup>.

### **Some data on enforcement of domestic awards**

It should be noted here that, Indonesia being a Civil Law jurisdiction, her courts are not required to follow precedent and consequently very few cases are reported. This lack of reported information, coupled with the fact that both registration and enforcement of domestic awards is effected in the District Court in the domicile of the losing party, and since there are 292 judicial districts spread throughout the archipelago, it is almost impossible to obtain full data on enforcement of domestic awards, except with respect to cases sufficiently notorious to raise a stir in legal or business circles or warrant comment in the press. However, some years ago, while the provisions of the RV still governed arbitration, this writer conducted a survey of most of the leading practitioners in the field to determine the approximate success rate for enforcement of domestic awards. With only one exception<sup>11</sup>, which was later reversed on appeal, all responses indicated that domestic awards were being executed by the District Courts as a matter of course and without any difficulty.

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<sup>7</sup> Article 62 (4), New Law.

<sup>8</sup> Articles 4 and 5, New Law.

<sup>9</sup> Article 62 (2), New Law.

<sup>10</sup> Article 63 (3), New Law.

<sup>11</sup> PANIN INTERNATIONAL CREDIT VS. P.T. GEMAWIDIA STATINDO KOMPUTOR, case before the District Court of Central Jakarta, May, 1997, discussed later in this paper.

The New Law has not altered procedures for enforcement of domestic awards in any material way, and there is thus still no effective means to assess all data on domestic enforcement. There have unfortunately been a few cases of domestic awards being annulled by the local district courts since the inception of the New Law, and these are discussed later in this paper.

### **International Awards**

Consistent with Supreme Court Regulation No. 1 of 1990, Article 1 (9) of the New Law defines international arbitral awards as: “ . . . awards handed down by an arbitration institution or individual arbitrator(s) outside the jurisdiction of the Republic of Indonesia, or an award by an arbitration institution or individual arbitrators(s) which under the provisions of Indonesian law are deemed to be International arbitration awards” As there has been no legislation, nor Supreme Court ruling, to the contrary, an award rendered in an arbitration with venue within Indonesia will be domestic, without exception. Thus, regardless of the nationality of the parties, only awards rendered in arbitral references with the venue outside of Indonesia are considered as international, or foreign, awards, and the procedure for enforcement of such an award differs slightly from that of domestically-rendered awards.

For the most part the requirements of the New Law for enforcement of a foreign award mirror those of Supreme Court Regulation No. 1/1990, with one significant exception. Unless the Republic of Indonesia itself is a party to the arbitrated dispute, applications for enforcement are no longer required to be submitted to the Supreme Court at all. The New Law vests in the District Court of Central Jakarta (*Pengadilan Negeri Jakarta Pusat*) the jurisdiction to issue orders of *exequatur* to enforce international arbitral awards, as well as to execute such domestic awards as are rendered within its normal jurisdiction - central Jakarta. Although no time limit for issuance of *exequatur* on international awards is expressed in the New Law, in the past applications to most District Courts for execution of domestic awards has normally engendered not more than six months, despite the absence of a time limit. Since the promulgation of the New Law, the District Court of Central Jakarta has acted upon every application for enforcement of foreign awards even more promptly than it had acted on applications for enforcement of domestic awards in the past, in some cases issuing *exequatur* within less than a month of request therefor.

Note, however, that the applications for *exequatur* which had been submitted to the Supreme Court prior to promulgation of the New Law and had not been acted upon were not automatically transferred to the District Court of Central Jakarta. Any party awaiting an *exequatur* order with respect to any of those seven applications filed prior to August, 1999 and not yet acted upon will need to make special application to have the file transferred from the Supreme Court to the District Court of Central Jakarta.

**Procedure for enforcement of international awards:** Similar to Supreme Court Regulation No 1 of 1990, the New Law requires that applications for enforcement of a foreign-rendered award attach:

- (i) the original award, or a certified copy thereof, together with an official translation thereof;
- (ii) the original or a certified copy of the agreement forming the basis of the award, together with an official translation thereof; and
- (iii) a statement from the Indonesian diplomatic mission in the jurisdiction in which the award was rendered to the effect that such country has diplomatic relations with Indonesia and that Indonesia and such country are contracting states to an international convention regarding implementation of foreign arbitral awards<sup>12</sup>.

### **Appeals, Annulment**

Rejection of *exequatur* for a foreign award can be appealed to the Supreme Court, which must decide upon the appeal within 90 days of application therefor.<sup>13</sup> Issuance of *exequatur*, however, is not subject to appeal<sup>14</sup>. Nor may a decision of the Supreme Court either issuing or rejecting *exequatur* where the Government of

<sup>12</sup> It is implicit that awards rendered in states that are not party to the New York Convention (or other such conventions, such as the ICSID, Washington convention, to which Indonesia is also a party) will not be enforced in Indonesia.

<sup>13</sup> Article 68, New Law.

<sup>14</sup> See Article 68 (1) & (2), New Law.

Indonesia is a party be appealed<sup>15</sup>. Decisions of the Supreme Court are final and binding and may be executed upon application to the District Court having jurisdiction over the losing party, in the same manner as are domestic awards.

Although there is no appeal from an arbitral award, application may be made to the applicable District Court to annul either a domestic or an international award, but on grounds even more limited than those provided in the New York Convention. Such grounds generally involve only the withholding of decisive documentation, forgery or fraud.<sup>16</sup> Application for such annulment must be submitted within 30 days of registration of the award<sup>17</sup>, and a decision must be made upon such application within 30 days of submission thereof. Appeal may be made to the Supreme Court against any such decision, and the Law requires the Supreme Court to decide upon such appeal within 30 days of application<sup>18</sup>.

#### **Enforcement Record - International Awards**

Of the nine applications which were acted upon prior to the enactment of the New Law, all but three were granted *exequatur*. One was withdrawn (presumably settled) before any action could be taken; one was sent back down to the District Court because it was not an international award, having been rendered in Indonesia; and only one was rejected - on the grounds that the instrument containing the arbitration clause had not been executed by the parties to the reference.

Unfortunately, despite issuance by the Supreme Court of *exequatur* for the very first application made, under Supreme Court Regulation 1 of 1990, the matter was subsequently taken up in the courts with the result that the award could not be executed. This notorious case<sup>19</sup>, which gave Indonesia its most unfortunate reputation with regards arbitration, is discussed later in this paper.

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15 Article 68 (4), New Law.

16 Article 70, New Law.

17 Article 71, New Law.

18 Article 72, New Law.

19 ED&F Man (Sugar) Limited v. Yani Haryanto.

Since the enactment of the New Law (August, 1999) there have been sixteen foreign-rendered arbitral awards registered with the District Court of Central Jakarta, and judicial enforcement has been sought with respect only to nine of these, as at mid-February, 2005. Of these nine, *exequatur* was issued quite promptly for five. Four related cases, were granted cassation (appeal) to the Supreme Court, and later judicial review by that court, with the final outcome still pending. Of the five awards for which *exequatur* was issued, a contest was lodged with respect to one, at least one award has already been satisfied through court-ordered auction of assets of the losing party and the others seem to have been satisfied voluntarily by the parties because there was no further court involvement after judicial reminders were issued to the losing parties. One award was never registered by the successful party, but the losing party subsequently deemed it necessary to register the award itself in order to seek annulment thereof, which annulment was granted by the District Court of Central Jakarta<sup>20</sup>. This case is discussed later in this paper.

### III. JUDICIAL INVOLVEMENT IN ARBITRATION

Article 1338 of the Indonesian Civil Code provides that a contract validly entered into has the force of law as between the parties thereto. Validity depends upon satisfying the requirements of Article 1320 which include, among other things, that the parties must be legally competent to enter into an agreement; the contractual terms must be clear and certain; the parties have agreed to such terms voluntarily and the contract may not be for a purpose contrary to law or public policy. Thus a clear arbitration clause in a valid underlying commercial agreement should be binding upon the parties.

Articles 3 and 11 of the New Law mandate that where the parties to a validly entered into contract have designated arbitration as the means of resolution of any disputes arising out of and/or in connection with that contract, the court does not have, and may not take, jurisdiction to hear any case within the scope of the parties' agreement to arbitrate. Article 3 provides:

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<sup>20</sup> Perusahaan Pertambangan Minyak dan Gas Bumi Negara ("Pertamina") v. Karaha Bodas Company, LLC. (and PT. Perusahaan Listrik Negara [Persero]); decision of the District Court of Central Jakarta No. 86/PDT.G/2002/PN.JKT.PST.



*The District Court shall have no jurisdiction to try disputes between parties bound by an arbitration agreement.*

**and Article 11:**

- (1) *The existence of a written arbitration agreement shall eliminate the right of the parties to seek resolution of the dispute or difference of opinion contained in the agreement through the District Court.*
- (2) *The District Court shall refuse and not interfere in settlement of any dispute which has been determined by arbitration except in particular cases determined in this Act<sup>21</sup>.*

The “. . . particular cases determined in. . . ” the New Law, referred to above, restrict the role of the judiciary to: (i) selection and dismissal of arbitrators where the parties are unable to agree and have failed to designate another appointing authority or institutional rules which provide otherwise<sup>22</sup>; and (ii) enforcement of awards<sup>23</sup>. The New Law does not go the extra step and specifically provide that when faced with a dispute under a contract containing an arbitration clause the court is required to stay any court proceedings and/or refer the parties to arbitration, as is called for under the UNCITRAL Model Law<sup>24</sup>. The New Law is not based upon the Model Law, although a few provisions may have been adopted therefrom.

The same principle prevailed under the prior legislation, although not codified in such clear language. In most cases known to have come before the Indonesian courts, such courts have upheld this principle and have declined jurisdiction. There were, however, two instances under the prior regulatory regime (one international and one domestic), and at two under the new Arbitration Law (likewise one

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21 There is no official English translation of the New Law. All translations contained herein are from an unofficial translation of the New Law prepared by the writer and included in several texts on Arbitration in Asia published in the English Language.

22 Articles 11,14,15,19,23-25 and 75 (2), New Law.

23 Articles 61 - 72, New Law.

24 UNCITRAL Model Law on International Commercial Arbitration ( the “Model Law”) adopted by the United Nations Commission on International Trade Law on 21 June 1985. The reference in the text is to Article 8 (1). Indonesia has not adopted the Model Law, nor is Indonesia’s New Law based thereupon.

domestic and one international), in which courts have accepted jurisdiction despite the clear agreement by the parties to arbitrate. These cases have not been entirely transparent. One was reversed on appeal, another settled before an appeal could be made and a final decision on a third is still pending. It is nonetheless these few aberrant cases, and a few others in which arbitral awards were annulled by the courts, that received wide publicity which at first created and have subsequently exacerbated Indonesia's unfortunate international reputation with regards to arbitration.

Let us now examine some of these notorious cases.

#### **IV. CASES REGARDING ARBITRATION DECIDED UNDER THE PRIOR LEGISLATIVE REGIME:**

**1. E.D. & F. Man (Sugar) Ltd . vs. Yani Haryanto.** (International arbitration, venue in London.)

The first order of *exequatur* issued by the Supreme Court (in 1991, under Supreme Court Regulation No. 1 of 1990) involved a long series of arbitral references and court applications. The subject matter of the dispute was a contract for provision of sugar by E.D. Man (Sugar) Ltd. (the Seller) to Yani Haryanto (the Buyer), FOB a port in Indonesia. As it happened, at the time only the Government Logistics Bureau ("BULOG") was permitted to import, or authorise the import of, of certain staples, including sugar, and no such authorisation had been obtained by the Buyer. Between contracting and intended delivery date, the market price of sugar declined substantially. The Buyer did not perform, failing to provide the necessary Letters of Credit, and subsequently cancelled the contract. As the initial purchase contract called for arbitration in London, the Seller commenced arbitration, obtaining an award against the Buyer for breach of contract. The Buyer then filed a suit in the High Court of London seeking a declaration that the contract was null and void as being contrary to law and public policy, since no permit had been issued by BULOG to import the sugar. The parties subsequently reached a settlement agreement whereby the Buyer was to pay to the Seller a reduced compensation in installments, also calling for arbitration in London in case of any disputes. After meeting its obligation with regard to the first installment, the Buyer defaulted on subsequent

installments and the Seller again brought arbitration in London, once again prevailing and obtaining an award against the Buyer. The Buyer did not satisfy the award but instead brought an action in the District Court of Central Jakarta seeking annulment of the original contract on the basis that it was invalid *ab initio*, being in violation of the law and public policy, and therefore the arbitration clause was also invalid.

This position was not without some logic, since the Indonesian Civil Code provides that if a contract is defective due to ambiguity about the subject matter or illegal cause, the contract is null and void *ab initio*, and the court must, *ex officio*, so declare. (This is in contrast to a situation in which the defect is in capacity of a party or coercion in the entering into the contact, in which case the same is only voidable and annulment of the contract must be sought before the courts, but any such annulment would not nullify an agreement to arbitrate contained in the underlying contract<sup>25</sup>). The court apparently followed this logic, despite the fact that it was the Buyer that violated the provisions of law and also that at this stage the parties were in dispute not over the original sale contract but the subsequent settlement agreement. The settlement agreement was declared null and void by the District Court, and its decision was confirmed at the high court level. The Seller further appealed to the Supreme Court, and also brought action against the Buyer in the District Court for breach of its obligation to make payments under the settlement agreement.

Before the Supreme Court had rendered a decision in these appeals, the same court issued the order of *exequatur* to enforce the London arbitral award against the Buyer. But the Seller was unable to execute because of the appeals still pending. Finally the Supreme Court found for the Buyer in both applications and therefore nullified its *exequatur* order on the basis that it had now found that the original contract was null and void and therefore so was the arbitration clause<sup>26</sup>.

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<sup>25</sup> Article 10 (h), New Law.

<sup>26</sup> See also, inter alia: Arbitration in Indonesia, THE ICC INTERNATIONAL COURT OF ARBITRATION BULLETIN, ICC Publishing S. A., Paris, France, (November 1998); Arbitration Procedures in Indonesia, ARBITRATION PROCEDURES IN ASIA, Sweet & Maxwell, London, U.K., (1999, Revised in 2001 edition); Enforcement of Arbitral Awards in Indonesia, INTERNATIONAL ARBITRATION LAW REVIEW, Vol. 3 Issue 6, Sweet & Maxwell, London. (December 2000); Arbitration in Indonesia, ARBITRATION IN ASIA, , Edited by Michael Moser, Butterworths Asia, Hong Kong

If one accepts that the underlying contract was null and void, given the state of the law, the decision could be considered tenable with respect to the award rendered on the original contract. However the same defects do not apply to the settlement agreement, which was clear, voluntarily entered into and not contrary to public policy, and any award rendered thereunder should have been enforced. Whether this notorious decision was a product of undue influence, or only lack of understanding of the arbitral concept on the part of the court, has never been determined. In any case, it was not an auspicious beginning for enforcement of arbitral awards in Indonesia.

Nonetheless, as mentioned above, in subsequent years, until the enactment of the New Law nine years later, there was only one application for enforcement of a foreign-rendered award that was rejected by the Supreme Court, and that one on the ground that the parties had not executed the agreement to arbitrate.

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There was, under the previous legislative regime, one domestic arbitration, relating to an almost equally complex dispute, in which the courts intervened, on very tenuous grounds. Although this case was later reversed on appeal, it merits mention, as it caused a considerable stir at the time.

## **2. Panin International Credit vs. P.T. Gemawidia Statindo Komputor<sup>27</sup>** (Domestic arbitration, venue in Jakarta)

An Indonesian company (“PT”), provided computer hardware to an Indonesian bank (“Bank”) pursuant to a contract (“A”) calling for disputes to be settled by

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(January, 2001). All of above notes were prepared by the writer hereof. See also Gautama, Sudargo; Indonesia National Report, INTERNATIONAL HANDBOOK ON COMMERCIAL ARBITRATION, edited by A.J. van den Berg, ICCA/Kluwer, Deventer; 1994 and subsequent editions (Prof. Gautama acted as counsel for Haryanto in this matter); and Budijaja, Tony, Public Policy as Grounds for Refusal of Recognition and Enforcement of Foreign Arbitral Awards in Indonesia, INTERPACIFIC BAR ASSOCIATION JOURNAL, September, 2001.

<sup>27</sup> Decision of the District Court of Central Jakarta (Pengadilan Negeri Jakarta Pusat) May, 1997. For more information on this case, see this writer’s summary in INTERNATIONAL ARBITRATION LAW REVIEW, Issue No. 3 of 1998, April, 1998, Sweet & Maxwell, London.

arbitration in Indonesia under Indonesian law. PT, and a Singapore services company (“SinCo”), also entered into a service contract (“B”) with Bank, governed by Singapore law and calling for disputes to be resolved by arbitration in Singapore.

In early 1996, PT. brought an arbitral reference before the Indonesian local arbitration institution, *Badan Arbitrase Nasional Indonesia* (“BANI”), against Bank for failure to pay for the hardware under contract A. Bank counterclaimed requesting BANI to order PT to remove the hardware on the grounds that there was a default in service under contract B, also requesting that SinCo be interpleaded. The arbitral board refused to interplead SinCo because contract B called for Singapore arbitration and law; said it could not consider contract B; and ordered Bank to pay the outstanding amount to PT. On the counterclaim, the board nonetheless found there may have been default in the service and thus ordered PT to pay some compensation to Bank.

Bank brought an action in the District Court of Central Jakarta, against BANI as first defendant and PT as second defendant, to have the award set aside, claiming the award was legally defective. The District Court ruled in favor of Bank and declared the award null and void based upon the then prevailing provisions of the RV, specifically, Article 643 (4), (5) and (6) , which provided that:

*Article 643: An arbitral award not subject to appeal may be challenged as being null and void upon the following grounds:*

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- (4) *If the award covers matters not claimed or if the award grants an amount in excess of the amounts claimed. (Compensation for default in service, although note that in their counterclaim Bank asked that the panel make a fair and equitable award if they would not order the equipment to be removed.)*
- (5) *If the award contains contradictory holdings (The arbitrators refused to allow the interpleader under, nor would consider, contract B, and yet mentioned it somewhere in the award. This may be inconsistent in a minor way but can hardly be considered contradictory).*

- (6) *If the arbitrators have omitted to rule upon one or more matters which, according to the agreement, were submitted for their decision (Presumably the refusal to deal with the default in service under contract B, although note that there was no claim made by PT for payment for such service).*

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What was most irregular in this case was that rather than awaiting the application for execution and contesting that, which would have been the proper procedure, Bank sued the arbitral body, BANI, itself. No precedent for this is known and, despite the confusion when judgement was rendered against BANI, clearly the Supreme Court recognised the impropriety and reversed on appeal.

## **V. CASES DECIDED UNDER THE NEW ARBITRATION LAW**

### **Cases relating to Domestic Arbitrations:**

3. **PT Perusahaan Dagang Tempo v. PT Roche Indonesia**<sup>28</sup> (Domestic court case. Had there been arbitration the venue would have been Jakarta.)

Pursuant to a series of Distribution Agreements, the most recent extension of which was dated 9 December, 1996 (the “Agreement”), P.T. Perusahaan Dagang Tempo (“Distributor”) acted as sole distributor of (i) over the counter (“OTC”), and (ii) prescription (“Rx”) products of P.T. Roche Indonesia (“Principal”), a subsidiary of the Swiss pharmaceutical firm. The Agreement contained a provision allowing termination on six months notice. On 31 August 1999, Principal sent written notice to Distributor terminating the distribution of OTC products, effective as at February 29, 2000. No breach of contract was claimed by Principal against Distributor.

The dispute resolution clause in the Agreement provided, in part:

*“In the event of any dispute arising among the parties in relation to, or in connection with this Agreement or a breach thereof which cannot be settled amicably shall be finally settled by arbitration to be conducted in the English*

<sup>28</sup> Decision of the District Court of South Jakarta (Pengadilan Negeri Jakarta Selatan) No. 454/Pdt.G/1999/PN.Jak.Sel, 30 May, 2000. For more information on this case, see this writer’s summary in INTERNATIONAL ARBITRATION LAW REVIEW, Issue No. 3 of 2000, Sweet & Maxwell, London.

*language and to be held in Jakarta under the Rules of Arbitration of the Badan Arbitrase Nasional Indonesia (“BANI - Indonesian National Board of Arbitration) in respect of such dispute by a panel comprised of 3 (three) persons appointed in the manner referred to below.”*

Despite the arbitration clause in the Agreement, Distributor brought action before the District Court of South Jakarta (*Pengadilan Negeri Jakarta Selatan*), asserting that Principal could not terminate the Agreement without prior consent of the other party and also because it was clear that Distributor had not breached the Agreement. Principal opposed the lawsuit, claiming that the court did not have jurisdiction to hear any such dispute, as the forum for resolution of disputes designated in the Agreement is arbitration in Jakarta before BANI, and further asserted that the Agreement provided that either party may terminate part of all of the Agreement upon 6 months prior written notice even in the absence of any breach of contract. This case was brought after the New Law was already in effect, which Law, as mentioned above, clearly provides that if parties have designated that their disputes are to be settled by arbitration, the District Courts have no jurisdiction to hear such disputes.

The Court rejected Principal’s jurisdictional objection, accepted jurisdiction, froze Principal’s assets, and finally ruled in favor of Distributor, awarding them considerable damages on the grounds that the partial termination was an “act of tort” which is not arbitrable but falls under the jurisdiction of the District Court to decide. The court further held that arbitrators may only resolve disputes relating to technical and business matters and, because the dispute related to a tort matter, a legal resolution must be settled by the Court - in effect holding that only the Court and not any arbitral panel had jurisdiction over the dispute, despite the unequivocal arbitration clause.

The District Court of South Jakarta in this instance appears to have created a new differentiation between disputes occurring from “legal relations” as opposed to those relating to “technical and business matters” and characterised what was clearly a commercial dispute as a tort claim in order to justify accepting jurisdiction, in direct contradiction to Articles 3 and 11 of the New Law, quoted above. Again, we wonder whether this aberration was a result of the court’s inadequate understanding of the basis and ramifications of arbitration and the intent of the New Law, or of “improper influences” upon the court. In this case the latter is strongly suspected.

Before Principal could lodge its appeal, the parties managed to reach a negotiated settlement, so that the matter was never considered by the Supreme Court. This is unfortunate because it is generally assumed that the Supreme Court would have reversed, as they did in the Panin Bank case, giving strength to the intended force and effect of the New Law.

**4. PT. Krakatau Steel v. International Piping Product, Inc.<sup>29</sup> (Domestic Arbitration, venue Jakarta)**

PT. Krakatau Steel (“Buyer”) and International Piping Product, Inc (“Seller”) entered into a Sales and Purchase Agreement (the “Agreement”) for the sale and purchase of Grade 8R Steel Billet. The goods were shipped before the issuance of the requisite Letter of Credit. Buyer refused to accept the shipment and notified the seller that it had wished to purchase a different specification: not 8R but 8A, which had initially been requested in a letter from Buyer to Seller a month prior to execution of the Agreement, and unilaterally nullified the Agreement.

The parties were unable to settle their dispute amicably and thus, pursuant to the dispute resolution clause in the Agreement, Seller initiated *ad hoc* arbitration in Jakarta, under UNCITRAL rules, claiming that Buyer had breached the Agreement and requesting compensation for its (Seller’s) losses.

In the arbitration hearings, held during the first half of 2001, in defense of Seller’s claim, Buyer contended that: (i) certain documents preceding the execution of the Agreement contained forged signatures thereby rendering the the Agreement null and void; (ii) the Agreement was negotiated in a misleading manner, in bad faith and constituted fraud with respect to the specification of the goods, rendering the Agreement null and void; and (iii) Buyer did not receive the Bill of Lading and therefore had no legal obligation to receive or accept the goods.

On these three points, in its award, the tribunal found as follows:

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<sup>29</sup> Decision of the District Court of South Jakarta No.282/Pd,P/2002/PN Jak.Sel .



(i) Although there were apparent differences in the signatures of Seller's director on various letters, the signatory himself confirmed to the tribunal that he had signed all of the questioned documents, and therefore there was no forgery. In any case the signatures in question were not those on the Agreement itself, which formed the basis of the claim, but on other, ancillary, documentation which were not material to the determination of the award;

(ii) It was Buyer that had drawn up the Agreement and was the first party to sign it. Once executed by both parties, this Agreement, calling for 8R specifications, superseded any previous letter of enquiry. The Agreement, as executed, met all requirements for a binding contract and therefore was binding upon both parties.

(iii) The Buyer had not issued its letter of credit, refused to accept the shipping documents and refused to accept the freight on arrival, thereby breaching the Agreement, and thus was not entitled to receive the Bill of Lading. This defense was therefore gratuitous.

The arbitral tribunal therefore found in favor of Seller.

The Buyer filed an application for annulment of the award in the South Jakarta District Court pursuant to Article 70 of the New Law, which provides:

*An application to annul an arbitration award may be made if any of the following conditions are alleged to exist:*

- (a) *letters or documents submitted in the hearings are acknowledged to be false or forged or are declared to be forgeries after the award has been rendered;*
- (b) *after the award has been rendered documents are found which are decisive in nature and which were deliberately concealed by the opposing party; or*
- (c) *the award was rendered as a result of fraud committed by one of the parties to the dispute.*

The elucidation to Article 70 states:

*"...the annulment petition reasons as mentioned in this article shall be proven with a court decision. If a court states that the reasons are proven or unproven, then this court decision may be applied as a ground for a judge to grant or reject the petition."*

In its application, Buyer again contended: (1) the signature of Seller's director in all documents supporting the Agreement was false or presumed false; (2) Seller had hidden the shipping documents (B/L, Certificate of Weight, etc.); and (3) the Agreement negotiation was fraudulent with respect to the specifications.

In reply, Seller contended: (1) Buyer's application did not satisfy Article 70 because no court decision nor police report had been issued in support of its claim of forgery; and in any case the tribunal had examined the evidences presented and had concluded that there was no forgery; nor was there fraud in the negotiations; (2) there was no new evidence submitted to the court supporting Buyer's contentions, in particular that any documents were hidden by Seller; and (3) the facts regarding forgery and fraudulent negotiation process had been examined by the arbitral tribunal and thus the district court had no power to re-examine these.

The South Jakarta District Court granted Buyer's petition and annulled the award. This decision was based primarily on the following reasoning: (1) that the elucidation of Article 70 is not binding, but only advisory and thus the court may, and did, find the signatures in question as forgeries, (despite the confirmation by the signatory that they were genuine); (2) that Seller was obliged to deliver the shipping documents, but this was not done, therefore Seller had hidden such documents; and (3) that Buyer intended to buy 8A specifications, as per its initial letter, but the Agreement stated 8R specifications, and therefore there was fraud committed by Seller.

It is clear that the court erred in interpreting the elucidation of Article 70 of the New Law. Elucidations officially issued with laws must be taken together with the language of the laws, as they are considered an integral a part thereof. The court did not address the issue of whether the court hearing the annulment application has the power to decide whether a document is false or whether there is a fraud. A reasonable reading of the elucidation of Article 70 would surely be that the annulment petition itself must be based upon, and attach, the decision of another court, more likely in a criminal action, that a fraud or forgery had taken place, which determination would have to have been made after the award had been issued but before the annulment petition is submitted. Furthermore, the court did not actually declare the documents forgeries, but only that they were presumed to be

forgeries (whereas the tribunal had examined the question and found to the contrary). But more importantly, even had the documents in question actually been forged, they would not materially have affected the award because they preceded the Agreement and were not the basis of the claim. No allegation of forgery was made with respect to the Agreement itself. The court did not even examine the issue of whether the alleged forged documents were material to the outcome.

The court also erred in its finding “decisive documents hidden by Seller” and “fraudulent negotiation process.” The New Law requires new evidence to be submitted on these points by the party seeking to annul the award. No such new evidence was submitted, and in fact both of these issues had been examined by the tribunal and such examinations were considered in the award rendered. In effect the court improperly re-examined the material findings of fact by the tribunal, which is contrary to both the intent and spirit of the New Law. Article 62 (4) of the New Law provides:

*The Chief Judge of the District Court shall not examine the substantive reasons or considerations upon which the arbitration award was based.*

Finally, the court simply annulled the award without any further determination of how the dispute is to be resolved. This is contrary to Article 72 (2) of the New Law, which states:

*If the application . . . (for annulment). . . is granted the Chief Judge of the District Court shall determine further the consequences of the annulment of the whole, or a part, of the arbitration award.*

The Seller appealed to the Supreme Court. which reversed the decision of the District Court..

**5. PT. Pura Barutama v. Perum Percetakan Uang R.I. (“PERURI”)<sup>30</sup> (Domestic arbitration, administered by BANI, venue: Jakarta)**

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<sup>30</sup> Decision of the District Court of Kudus, Central Java, No. 30/Pdt.P/2002/PN.KDS.

PERURI (“Buyer”) is a state-owned entity with the authority to source and supply secure paper and to undertake the printing of such notes for Bank Indonesia (Indonesia’s Central Bank). In practice, as well as under the relevant legislation, both entities (the Buyer and Bank Indonesia) have complementary and mutual functions and roles with regard matters of Indonesia’s currency. Buyer contracted with a Kudus, Central Java, based supplier, PT. Pura Barutama (“Seller”) for the supply of paper designed for printing by Buyer of Rp. 1,000 and Rp. 5,000 notes. In compliance with their standard practice, Buyer paid Seller for the full order in advance of shipment. After delivery of the first shipment, the Buyer commenced use of the paper and discovered it defective and unfit for the intended purpose. Buyer notified Seller and allowed a second shipment to enable Seller to improve the quality, but the paper in the second shipment was also defective.

The parties were unable to reach an amicable settlement on the matter and Buyer commenced arbitration before BANI in accordance with the arbitration clause in the sales contract, claiming that the paper was defective, unfit for its intended purpose and, due to the secure nature of the intended application, could jeopardise the economy if used.

The BANI tribunal, consisting of three arbitrators including the Chairman of BANI, who was appointed by claimant (Buyer), found for Buyer and issued its award ordering Seller to refund the deposit and pay the costs of the arbitration. The award was registered with the District Court of Kudus and Buyer applied to such court for an order of execution against Seller. Seller in turn applied to the same court to decline execution and for annulment of the award. The grounds for the application for annulment were purportedly based upon Article 70 of the New Law, quoted in the previous case summary, although the claims of Seller went far beyond the limited grounds set out in Article 70 and spoke of the merits of the case, and matters already considered and ruled upon by the arbitrators.

The Kudus court found, among other things, that: (i) insufficient documentation was shown of the authority of Buyer from Bank Indonesia to bring the arbitration (even though the agreement of purchase was between Buyer and Seller only), and that documents which Seller claimed should have been submitted bearing on the defects of the paper were not submitted by Buyer, and on those bases held that decisive documents were deliberately concealed by Buyer, so as to satisfy the Article 70 (b) of

the New Law, thereby allowing the court to annul; and (ii) one of the arbitrators, in fact the Chair of BANI, had a relationship with Buyer and therefore was not independent. This latter claim, which had already been considered in the arbitration, was based on an invitation list for a meeting relating to supply of paper to Buyer on which list the name of that arbitrator appeared as a possible consultant attendee, the court determining that failure of the tribunal to recuse that arbitrator, and also some matters relating to evidences, constituted fraud as meant under Article 70 (c), thereby allowed the court to annul the award.

The Kudus court therefore rejected execution of the award and declared the award annulled. The court further interpreted Article 72 (2) of the New Law as giving it the authority to constitute an entirely new arbitral tribunal to hear the case again in Kudus (thereby disregarding the agreement of the parties to BANI arbitration in Jakarta) and the court decision names new arbitrators and directs them to re-hear the case in Kudus.

Article 72 (2) states as follows:

*If the application as contemplated in paragraph (1) above (for annulment) is granted the Chief Judge of the District Court shall determine further the consequences of the annulment of the whole, or a part, of the arbitration award.*

The Elucidation to Article 72 (2) states:

*The Chairman of the District Court is authorized to examine any indictment of annulment if asked by parties, and regulate the consequences of the annulment of the whole or part of an arbitration decision.*

*The Chairman of the District Court may, after reading out the annulment, decide that the same arbitrators or other arbitrations will re-examine the relevant dispute or determine that the dispute is no longer possible to settle through arbitration*

It is not clear whether this intends to give the court the authority to constitute a new and different tribunal and appoint arbitrators on its own volition, but if it does it would run counter to the very consensual basis of arbitration.

Some of the court's determinations might have been valid points for adjudication in the arbitration itself, but it is clear that the court does not have the jurisdiction to revisit the merits of the case. As in the Krakatau Steel case, discussed under No. 4, above, the court seems to have gone through considerable contortions to enable it to characterise substantive issues as fraud or concealment of documentation in order to give itself the power to annul.

The Buyer has appealed to the Supreme Court but no decision has, as at time of writing, been issued. It is hoped that that court will clarify the ambiguous language of the above-quoted elucidation let it open the door to court-constituted arbitral tribunals throughout the archipelago.

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One further set of domestic arbitrations merits mention here, although there was no attempt either to enforce or to annul these awards. Rather, an essential party to the underlying agreement, and to the project the basis of the dispute, was not joined in the arbitration and, that party sustaining substantial losses as a result of the award, sought and obtained a temporary injunction against further action on the award pending adjudication of its own interests. The tribunal violated these injunctions and moved the venue of the second tranche of arbitrations outside of the designated seat in order to do so. Considerable backlash resulted and awards were rendered what were clearly invalid under the governing law as well as violating principles of natural justice, which awards have had ramifications well beyond these arbitrations themselves.

**6. Pertamina vs. Patuha Power Ltd., Perusahaan Listrik Negara ("PLN") and the Minister of Finance of the Republic of Indonesia<sup>31</sup>; and Pertamina vs. Himpurna California Energy Ltd., Perusahaan Listrik Negara ("PLN") and the Minister of Finance of the Republic of Indonesia<sup>32</sup> (Relating to Domestic *ad hoc* arbitrations applying UNCITRAL rules - venue Jakarta.)**

These are probably the most widely misunderstood of all of Indonesia's notorious cases, primarily because of the plethora of press reports prepared and widely disseminated by the Claimants in the original arbitral references (First Defendants in

<sup>31</sup> Decision of the District Court of Central Jakarta , No. 271/PDT..G/1999/PN.JKT. PST

<sup>32</sup> Decision of the District Court of Central Jakarta , No. 272/PDT..G/1999/PN.JKT. PST

these court applications) and by their various counsel and expert witnesses, with no counterbalancing coverage having been afforded the Indonesian parties or truly independent scholars<sup>33</sup>.

The basis of these court applications was a series of arbitral references brought by two special purpose Bermuda subsidiaries of subsidiaries of a US-based energy company (collectively referred to herein as “Claimants”) against the Indonesian state-owned electric company (“PLN”) under certain Energy Sales Contracts (“ESC”)s among each of the Claimants, the Indonesian state-owned oil company (“Pertamina”) and PLN; and against the Minister of Finance (“MOF”) of the Republic of Indonesia under certain comfort letters subsequently issued by the MOF at the request of the Claimants to assist in Claimants obtaining onward financing for the subject projects.

The ESCs were tri-partite contracts pursuant to which the Claimants were to build own and operate private geothermal power plants in various parts of Indonesia and sell the power to Pertamina, which would then re-sell to PLN for distribution to the public. The Claimants were to invoice Pertamina and Pertamina would invoice PLN. Payment was to be made by PLN to Pertamina and then Pertamina was to pay the Claimants, who would then return to Pertamina an amount as commission. Pursuant to the ESCs, Pertamina was to instruct PLN to make payment directly to the trustee for Claimant’s lenders if so requested by the Claimants. That was the only direct right/obligation between PLN and Claimants; Pertamina sat as intermediary with regard all others.

The contracts were governed by Indonesian law and contained an arbitration clause which provided that any dispute between PLN on the one hand and Pertamina and/or the Claimant on the other, that could not be settled amicably were to be referred to arbitration in Jakarta under UNCITRAL rules. The clause went on to state that Pertamina was entitled to give power of attorney to the Claimant to act as Pertamina’s proxy to settle any such disputes.

<sup>33</sup> It is most unfortunate that in the international legal press only one-sided accounts of these cases have been published. It is also unfortunate that when the writer prepared and submitted several responses to put the other side of the case, the two principal journals concerned would not publish them. It appeared that the article in one of them, the Swiss Arbitration Association Bulletin, was published "anonymously" by one of the editors who had also acted as an expert witness for the Claimants in the arbitration (first Defendants in the court applications).

In addition to the ESCs, the Claimants were also parties to certain Joint Operating Agreements (“JOC”s) with Pertamina, pursuant to which Pertamina appointed the Claimants as their contractors for the purpose of exploration and extraction of the geothermal resources in certain areas over which Pertamina had exploration and exploitation rights. These are what is known as “upstream” contracts (relating to extraction of an energy resource), whereas the ESCs are “downstream” contracts (relating to sales of the power generated). Because geothermal energy - steam - cannot be transported, but must be utilised where extracted, these contracts were inexorably linked. The JOCs gave the Claimants the right to use the facilities already constructed by Pertamina, in return for certain rental payments to be made to Pertamina, and also the right to receive from the Claimants a 3% commission on all sales of power eventually made from the product of the resource. They further provided that at the expiration of the contracts, and of the ESCs contemplated therein, all facilities constructed by the Claimant on the properties would be transferred back to and become the sole property of Pertamina. The JOCs were also governed by Indonesian law and contained similar arbitration clauses to the effect that any dispute between a Claimant and Pertamina would be settled by arbitration in Jakarta under UNCITRAL Rules.

Claimants brought arbitration against PLN under the ESCs, claiming failure of PLN to pay for energy proffered<sup>34</sup>. Pertamina was not joined as a party, nor did Claimants provide powers of attorney from Pertamina to bring these actions on their behalf. Under Indonesian law and practice any action under a multi-party contract can only proceed if all parties are joined and have an opportunity to be heard. The Tribunal nonetheless refused PLN’s insistence that Pertamina be joined, ignoring the respondents’ jurisdictional objection and stating that Pertamina was not a necessary party, despite the fact that every right and obligation of each of PLN and the Claimants were with Pertamina, there being no direct obligation of PLN to the Claimants, nor vice versa. This was not an insignificant formality. It was through Pertamina that Claimants had secured the projects and the participation of PLN, bypassing the strict requirement of both law and public policy that such contracts be awarded through transparent tender procedures<sup>35</sup>.

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<sup>34</sup> Note that Claimant’s plants had not yet passed commissioning tests, nor had Claimants yet applied for operating licenses, when their invoices were issued.

<sup>35</sup> Indeed there were serious Foreign Corrupt Practices Act issues involved which have



Awards were rendered against PLN, cancelling the ESCs, ordering PLN to pay compensation to the Claimants for its full costs plus 42 years of anticipated profits, and ordering the Claimants to transfer all of their facilities already built on site to PLN.

The awards specifically stated that Pertamina's interests were not affected thereby. However the fact was that all of Pertamina's rights under not only the ESCs, but also those under the JOCs, were entirely extinguished by the awards. Were the awards to be enforced, Pertamina would lose not only its right to rents and commissions from the projects, but also its ownership of the land and facilities to which it was entitled.

Claimants did not attempt to enforce the awards against PLN in the Indonesian courts, but immediately commenced a second set of arbitral references against the MOF under the comfort letters, claiming that these were guarantees of PLN's obligations and that therefore the government itself was responsible to satisfy the awards.

When Pertamina become aware of these awards and the effect such awards had upon its interests, seeing that they had no recourse in the arbitrations, which were already completed, nor the opportunity to interplead in contest of enforcement by the courts since no application for enforcement had been made, Pertamina brought an action in the District Court of Central Jakarta to defend its rights. In conjunction with such action, Pertamina applied to the court for a temporary injunction to stay enforcement of the awards, both by the Indonesian courts and through the second arbitral references, pending determination of its such rights. The court, in a very comprehensive set of decisions, granted to Pertamina a temporary injunction, suspending any further arbitration proceedings among the parties pending the outcome of Pertamina's case.

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never been properly addressed by the United States Justice Department. Aside from the failure to tender for these projects, the Claimant companies had as minority shareholders relatives of high government officials, whose shares were issued without compensation and who were awarded other lucrative sub-contracts to the projects.

Rather than await the court's decision on Pertamina's claim, the Tribunal constituted to hear Claimants' claims against the MOF (which consisted of the same Chair and Claimant-appointed arbitrator, but a different Respondant-appointed arbitrator) intentionally violated the injunction and, ignoring the fact that these were domestic arbitrations with the venue in Jakarta, moved the venue to the Netherlands, scheduling an early hearing on the merits, despite Respondant's inability to appear lest it violate the injunction of the court of its own country<sup>36</sup>.

The Central Jakarta District Court issued a further directive addressed to the arbitrators, reminding them of the injunction and advising that they, too, were included within its scope. Upon receipt of this notice, on the eve of the scheduled hearing in Holland, the Respondant's party-appointed arbitrator, an Indonesian national and former official of the Attorney General's office, opted not to appear at the hearing but rather to respect the injunction, and returned to Jakarta. The hearing proceeded nonetheless, with only Claimant appearing before a truncated tribunal, consisting of the Chair and Claimant's party-appointed arbitrator, in which hearing the latter arbitrator appeared as witness before himself and the Chair claiming that Respondant's party-appointed arbitrator had been "kidnapped", despite a letter from that Respondant's party-appointed arbitrator stating otherwise and attaching a copy of the court's reminder of the injunction.

This truncated Tribunal, sitting outside of the agreed-upon venue and in violation of the order of the court having jurisdiction over the reference, proceeded nonetheless, in the absence of both the Respondant and its party-appointed arbitrator, to issue final default awards in favor of the Claimants.

Article 44 of the New Law provides:

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<sup>36</sup> It should be noted that, at the time the Tribunal scheduled this questionable hearing, a challenge for recusal of the Chair was pending, on the grounds of conflict of interest. The firm of which the Chair is a partner represented another company in a somewhat similar position to Claimants, which company was in the process of preparing to bring arbitration against the same Respondants in these references. The Chair had been asked to recuse himself from the second set of arbitrations, but had refused. An application was then made to ICSID, which had thus far declined to address the matter, and the challenge was still pending when the Tribunal decided to proceed nonetheless, and it was still pending when the awards were issued

- (1) *If on the day determined pursuant to Article 40 paragraph (2)<sup>37</sup>, the respondant for no good reason does not appear, but has been duly summoned, the arbitrator or arbitration tribunal shall immediately summon the respondant again.*
- (2) *If the respondant for no good reason still does not appear at the hearing, within ten (10) days after receipt by it of the second summons, the hearing shall continue without the presence of the respondant and the claimant's claim shall be granted as a whole, unless the claim is unfounded or contrary to law.*

Ignoring this clear requirement of the governing law, the Tribunal, sitting in Holland, did not attempt to summon the Respondant again, but issued a final award after only a single hearing, from which the Respondant was enjoined to appear, having already so advised the Tribunal. Curiously, the awards did not specify the place at which they were rendered, one of the requirements for a valid award as set out in Article 54 of the New Law. Clearly these awards were invalid under the governing law and could not have been enforced. Claimants, presumably, were well aware of this defect, as they did not make any attempt to enforce these awards, just as they had never applied to enforce the awards against PLN. Instead they pressured the US Congress to force the Overseas Private Investment Corporation ("OPIC"), with which agency the Claimants had placed political risk insurance, to pay the insurance proceeds to the Claimants, despite the normal conditions for such payment requiring insureds to exhaust all remedies against the subject government before making a claim on the political risk insurance.

Under such pressure, OPIC anticipated payment of the claim. And OPIC, too, must have been aware of the invalidity of the awards to which it had been subrogated, for it also did not make any attempt to enforce these awards - in any jurisdiction - but rather proceeded to use diplomatic and political channels to pressure the Indonesian Government to agree to reimbursement, still without seeking legal clarification nor relief anywhere.

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<sup>37</sup> Date set for hearing on not less than 14 days written notice to the parties.

## **Cases under the New Law Relating to International Arbitrations**

**7. Bankers Trust Company & Bankers Trust International vs. PT. Jakarta International Hotels and Development, Tbk, and Bankers Trust Company & Bankers Trust International vs. PT. Mayora Indah.** (International arbitration - venue London)<sup>38</sup>

Once again, the first applications for *exequatur* under new legislation, this time under the New Law, have brought further embarrassment to Indonesia's reputation in the world of arbitration. But it should be noted that these are the only applications for enforcement of international awards that have been rejected by the court since the promulgation of the New Law. These cases had actually been arbitrated, and the awards rendered, prior to August 1999 but, as they had not been enforced by such time, became subject to the new Law with respect enforcement.<sup>39</sup>

These two cases, each involving two awards, are virtually identical and for purposes of this paper are dealt with together. They involve derivative trading in exchange and interest rate swap agreements between the Bank and the Customers under International Swaps and Derivatives Association ("ISDA") Master Agreements. Each ISDA Agreement, by its terms, included an attached Schedule setting out the standard terms and conditions, including an arbitration clause, which are specifically incorporated into the agreement by reference.

The derivative agreements were entered into between the Bank and above-named Customers in 1995, prior to the Asian economic crisis of 1997 - 1998 which brought the value of Indonesia's currency, the Rupiah, down to between 15% and 25% of its former value. Customers subsequently defaulted in their obligations to make

<sup>38</sup> Decision of the District Court of South Jakarta (Pengadilan Negeri Jakarta Selatan) No. 454/Pdt.G/1999/PN.Jak.Sel, 30 May, 2000; and applications for Exequatur of international arbitrations No. 001/Pdt/Arb.Int/1999 with respect to LCIA award No. 8199 of 18 June, 1999; and No. 004/Pdt/Arb.Int/1999 with respect to LCIA award No. 9128 of 19 October, 1999. For a more detailed discussion of the Mayora Indah case, see Budijaja, Tony, Public Policy as Grounds for Refusal of Recognition and Enforcement of Foreign Arbitral Awards in Indonesia, INTERPACIFIC BAR ASSOCIATION JOURNAL, September, 2001. (Mr. Budijaja's firm represented Bankers' Trust in this matter.)

<sup>39</sup> See Transitional Provisions, Article 80 of the New Law.

payments under the swap agreements. While the matter was under negotiation, Customers brought action in the South Jakarta District Court seeking annulment of the ISDA agreements on the grounds that they were contrary to public policy (presumably claiming that swap trading was, in effect, gambling, which is strictly prohibited in Indonesia) and further that entering into such agreements was beyond the powers of the Customer's corporate authority. The Bank, in turn, brought arbitration references against the Customers before LCIA in London in accordance with the arbitration clause contained in the Schedule to the ISDA agreements.

LCIA issued awards in favor of the Bank, which awards were registered with the District Court of Central Jakarta for execution. Meanwhile the South Jakarta District Court found in favor of the Customers. To the Bank's argument that the Court did not have jurisdiction because the parties had agreed that all disputes would be settled by arbitration, the court found that the arbitration agreement in the Schedule was not incorporated into the ISDA agreements and was therefore not binding upon the Customers. This finding was exactly opposite to the finding of the LCIA that the Schedule formed an integral part of the ISDA agreements and thus the parties had in fact agreed to arbitration.

The Bank appealed the decision of the South Jakarta District Court and at the same time requested the Central Jakarta District Court to enforce the LCIA awards. The judgement of the South Jakarta court was not final and binding until all appeal routes are exhausted, whereas an arbitral award is final and binding and all that is left to the court is to enforce it, but not to review it. Nonetheless, faced with contradictory rulings by the South Jakarta District Court and the LCIA, the Central Jakarta District Court was unwilling to enforce the final and binding arbitral awards so long as there was a contradictory ruling of the court that had not gone through the full judicial appeal process.

The Bank sought *Cassation* (a form of appeal) from the Supreme Court, requesting it to rule that the arbitral awards must be enforced in accordance with the New Law, but the request was denied and the Supreme Court would not hear the matter and declared that execution would be suspended while the court decisions were still pending. The Bank has sought judicial review by the Supreme Court, the final recourse of Indonesia's judicial system, and, despite considerable time having elapsed, such applications remain pending, so that the final outcome of this matter is not yet determined.

The public policy argument is an interesting one here. Surely no contract of gambling can be enforced in Indonesia and, in accordance with the Civil Code, as mentioned above, were the ISDA agreements determined to be one of gambling, being for an illegal purpose they would be null and void *ab initio*, and along with them the arbitration clause. Note, however, that the ISDA agreements were, by their terms as set out in the Schedule, governed by English law.

The argument that entering into the swap contracts was above the corporate powers of the Customer goes to capacity of the parties and, as mentioned earlier, Indonesian law and practice hold that where a party does not have legal capacity the contract may be annulled by a court upon application, but is not automatically deemed invalid *ab initio*. The New Law provides that any such annulment would not affect the validity of an arbitration clause, which clearly the parties do have capacity to agree upon, and thus the court does not have jurisdiction to hear any dispute under that contract. An application for nullification would therefore have to be decided by the arbitral tribunal and not the court. This would mean that the issue as to whether the parties had in fact agreed to arbitration should also be a matter for the arbitral tribunal to decide.

The above summary has simplified the issues and it may be noted that there were criminal charges filed in both directions as well, which the writer does not deem relevant for purposes of this paper. As this case has not as yet been finalised, we must reserve judgement and hope that the Supreme Court is able to rectify this once again embarrassing situation.

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The case relating to an international award which has received the most attention in the past year or so was that of a foreign-held arbitration in which the award, rendered against two Indonesian state-owned entities, was not registered by the successful claimant nor did such claimant attempt to enforce the award in Indonesia. As there were serious procedural irregularities, however, one of the Respondants sought to have the award annulled in the District Court of Central Jakarta, its domicile. In order to do so, in a rather unusual move, that Respondant itself registered the award with the court.

**8. Perusahaan Pertambangan Minyak dan Gas Bumi Negara (“Pertamina”) v. Karaha Bodas Company, LLC. and PT Perusahaan Listrik Negara [Persero] (“PLN”)** <sup>40</sup> (Relating to international *ad hoc* arbitration under UNCITRAL rules, venue: Geneva.)

This was the the second set of arbitrations<sup>41</sup> brought by foreign private power producers against the state owned electricity company (PLN) and, in this case, also against the state oil company, Pertamina, after the onset of the economic crisis of 1997/1998, following suspension of certain of such projects on the insistence of the IMF. The claimant entered into a Joint Operating Contract (“JOC”) with Pertamina and an Energy Sales Contract (“ESC”) with both Pertamina and PLN. It claimed in the arbitration that it had also received a “comfort” letter from the Minister of Finance, except that no such letter had ever been executed by the Minister and the unsigned draft submitted by claimant was rejected by the tribunal.

Claimant brought one single arbitration under three distinct instruments, each of which had its own arbitration clause calling for *ad hoc* arbitration in Geneva applying UNCITRAL rules, against the parties to the three instruments (Pertamina alone in the case of the JOC, PLN and Pertamina in the case of the ESC and the Minister of Finance under the alleged comfort letter). There had been no consent to consolidate and before the three Indonesian party respondents had had an opportunity to contest jurisdiction, or even figure out which party or parties were to appoint an arbitrator or arbitrators after each received a similar notice of arbitration, the claimant caused ICSID to appoint a single arbitrator, unknown to any of the respondents, as party-appointed for all three. Thus none of the Indonesian parties had the opportunity to participate in the designation of the tribunal. This tribunal, after releasing the Minister of Finance from the reference on the basis that no comfort letter had in fact been executed, then awarded substantial damages to the claimant against Pertamina and PLN, covering not only costs alleged to have been expended but also interest thereon and onward profitability for the 30+ years expected life of the contract, despite the fact that no power plant had as yet been

<sup>40</sup> Decision of the District Court of Central Jakarta No. 86/PDT.G/2002/PN.JKT.PST.

<sup>41</sup> The first set were domestic arbitrations and the court involvement portion is discussed above as case no. 6.

constructed, nor had the claimants as yet made, nor even obtained financing for, its promised investment. In effect, the award was based on an “expropriation” calculation, rather than damages for breach of Contract, which latter was the basis of the dispute submitted to arbitration, and thus it would appear that the Tribunal greatly exceeded their jurisdiction.

The calculation of damages was based upon that applied by the tribunal in the previous set of private power arbitrations<sup>42</sup>, despite that fact that the awards in those cases were confidential and this tribunal had no right even to view, let alone follow them. In fact the awards upon which these calculations were based were fatally flawed under the New Law and no attempt had, nor has to date, ever been made to seek enforcement thereof either in Indonesia nor anywhere else. As in the previous private power arbitrations, this tribunal declined to consider either the fact that the claimants had not performed their own obligations or the question of validity of the underlying contracts, which were not tendered as required by governing law and were assumed to have been granted through corruption collusion and nepotism (known in Indonesia as “KKN”).

In this case, the claimant neither registered nor sought to enforce the award in Indonesia, but immediately sought enforcement against state assets being held in several other jurisdictions, primarily in the U.S. but also in Canada, Hong Kong and elsewhere. The U.S. courts found that approximately 5% of these assets belonged to Pertamina and that these could be attached for satisfaction of the award. The US District Court for the Southern District of Texas also issued contempt orders against Pertamina for seeking annulment in the Indonesian court.

Pertamina had lodged a contest against the award in the Swiss courts right after the award was rendered. However, Pertamina’s application court fee was held up in the Swiss banking system for several days with the result that it was received by the court one day late and as a result the Swiss court refused to entertain Pertamina’s application and would not review the award. Pertamina therefore brought an action in the District Court of Central Jakarta to annul the award and was successful. The Indonesian court based its decision upon principles set out in both the New York Convention and in the New (Arbitration) Law, as the agreements in dispute

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<sup>42</sup> Those to which case no. 6, described above, relates.



provided Indonesian as the governing law. This was a well reasoned decision, in contrast to a number of the others discussed above, and disclosed a number of the procedural and substantive errors in the award, not the least of which a violation of natural justice, in that the claims under two distinct contracts (one bilateral and the other tri-partite<sup>43</sup>), as well as an alleged third with the Government itself, which the arbitrators had already deemed to be a fraudulent claim, as no such agreement had ever existed. These three claims were consolidated and a single arbitrator appointed on behalf of all Indonesian parties without their knowledge or consent. The court also found fraud in the calculation of the damages sought and awarded, a matter that the tribunal failed to consider. Nor had the Tribunal taken into account the U.S. \$ 75,000,000.00 insurance proceeds already received, which the claimant refused to disclose in the arbitration. The claimant (first defendant in the court action) appealed, but before the appeal could be heard, the case was entirely withdrawn under intense US political pressure

Unfortunately, as in the case of the CalEnergy arbitrations, failure of the Indonesian parties to make the content of the Karaha Bodas court decision known or otherwise publicise the Indonesian side of the story has allowed the foreign claimant and their public relations firms to conduct a widespread lobbying and media campaign to further damage Indonesia's already shaky reputation with regards arbitration and attempt to discourage foreign investment in Indonesia generally. The claimant announced it has appealed the Jakarta court decision, although recent press coverage reports that the matter has now been settled<sup>44</sup>. The ultimate result of the appeal, as well as the fate of the contempt order and the attachment actions in the U.S., Hong Kong and elsewhere, remain uncertain as of time of writing.

## **VI COMMENTARY**

The question of judicial involvement in arbitration may not always be as clear cut in *third-world* jurisdictions as it is in more developed, western countries.

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<sup>43</sup> Not to mention the third which was claimed to have been executed by an entirely different third party, later found not to have been so executed, as mentioned above.

<sup>44</sup> See Tempo magazine, 31 December, 2002.

Certainly where parties have deliberately agreed to vest the power in an arbitral tribunal to adjudicate their disputes, that agreement must be honored, within the confines of the other elements agreed to by the parties: the governing law and their other contractual provisions, and also against the cultural background of the place of subject matter of the dispute and the venue for such arbitration.

Arbitration is still finding its way in many developing countries, and we can see that sometimes the result involves unjust or improper court decisions and/or arbitral awards. Education of judges as well as prospective arbitrators is sorely needed in such jurisdictions but what is normally dealt out is only harsh and arrogant criticism without any attempt to rectify the situation.

There is a growing trend of western arbitrators to consider that international arbitration stands above the law of any individual jurisdiction, and that such arbitrators are more powerful than the governments and courts of the jurisdictions in which they operate, and thereby qualified to make awards unencumbered by local laws, policies, politics and customs. But arbitrators are only human beings. We must not forget that we, too, are fallible and not allow the position of power granted to us as arbitrators to create in us such arrogance as to eclipse the fact that we are still subject to the laws of the lands in which we operate. We may not agree with some of the laws of developing countries, but let us not forget that it is the very laws of each county which allows the parties to opt out of the jurisdiction of its courts and give that jurisdiction to private commercial adjudicators. But it still remains the duty of the courts to ensure that the laws of their land are not breached and that their citizens are protected against consequences of failure of others to comply with their laws.

In institutional arbitration, such as under the ICC or other administering bodies, awards of the arbitrators are reviewed before issuance to ensure that they are not so defective as to completely ignore or contravene the laws under which they are governed, or to violate precepts of natural justice. *Ad hoc* arbitrations have no such stop-gap, and thus it is only in the court in which enforcement is sought that compliance with the governing law can be monitored. That is the duty of the court. Indeed there are courts which have exceeded the scope of that duty, either out of ignorance or improper influences. Just as there are arbitrators who exceed the scope of their mandate. But in the majority of instances, in both cases, the system

runs properly. It is only the improprieties, or questionable cases, that become known and discussed in print or in conferences such as these and give the courts and/or arbitration a bad name.

There is no question that one of Indonesia's largest problems is its judicial system. Fortunately, with the New Law, an attempt is being made to improve the situation with respect to arbitration and to encourage disputes to be settled in that way, in order to reduce the ability of the courts to interfere in due legal process. And, for the most part, with notable exceptions such as those mentioned earlier, the courts are trying to do this. After all, it is really only the first, related, set of applications for enforcement of international awards that have met with irrational judicial interference. All applications made thereafter have thus far been enforced promptly. So, let us not give up hope. And let us not lose perspective. Arbitrators are not infallible any more than are judges. There are some situations in which judicial involvement is necessary and beneficial.

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### **Biographical Note**

*Karen Mills, a member of the Bar of the State of New York, U.S.A., has practiced in Indonesia for over 20 years and is one of the founders of the KarimSyah (formerly Karim Sani) Law Firm in Jakarta. Ms. Mills is a Chartered Arbitrator and Fellow of the Chartered Institute of Arbitrators as well as of the Singapore and Hong Kong Institutes and acts as special advisor to the Board of Indonesia's arbitral institution, BANI. Ms. Mills writes, speaks and teaches extensively on arbitration and other forms of dispute resolution, as well as on tax structures, e-commerce, oil & gas and energy law, financing and other transactional matters. Ms. Mills is on the panel of many arbitral institutions, often sits as arbitrator in international disputes and is also a skilled mediator. She has been a member of the International Bar Association since 1984, serving on SBL Committees A and D, the Asia Pacific Forum and the Section on Energy and Natural Resources Law, and is also a member of the IBPA (currently co-chairing the Program Committee for their forthcoming Annual Meeting in Bali), the NYSBA and a number of other professional organisations, including the Indonesian branch of the International Fiscal Association, for which she served as Vice Chair from 1996 - 2002.*

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