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PRACTICAL TIPS TO STREAMLINE DISPUTE RESOLUTION PROCESS FROM AN EARLY STAGE

By WongPartnership and Makes & Partners, member firms of WPG, a regional law network.

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Indonesia: Practical Tips to Streamline Dispute Resolution Process from an Early Stage

There is a common perception that Indonesia's dispute resolution environment is complex and challenging. In the World Justice Project Rule of Law Index 2019[1], which ranks jurisdictions on various aspects of their legal and regulatory framework, Indonesia is ranked 62 out of 126 jurisdictions. However, for the "*Civil Justice*" category, which concerns, among others, the enforcement of civil and commercial claims, Indonesia was placed 102 out of 126 jurisdictions.

President Joko "Jokowi" Widodo had set a target for Indonesia to be in the top 40 countries in the World Bank's Ease of Doing Business Index under his watch[2]. After moving up from 114th place in 2014 (when President Jokowi took office) to 72nd place in 2017, Indonesia has since slid back one place to 73rd in 2018. The improvements in Indonesia's ranking have generally been attributable to the new rules that, among others, allow for greater ease in starting a business in Indonesia, registering property and obtaining credit. However, reforms in certain areas, including in enforcement of contracts and resolving insolvencies, have not been fully implemented yet.

While it is expected that such reforms will be forthcoming in the near future, in the current environment, it is crucial for parties to understand the strategic factors which will impact them in the event of a dispute and build safeguards into the contractual mechanisms, even from the early stages in drafting the contract.

International Arbitration as the Dispute Resolution Mechanism

International arbitration has been the preferred mode of dispute resolution for parties in Indonesia-related contracts for the simple reason that it allows parties to resolve disputes in a neutral and recognised international forum outside of Indonesia. However, there are other strategic factors which parties should be aware of when choosing international arbitration as the mode of dispute resolution.

Advantages of international arbitration

The most significant advantage of international arbitration is that it allows the dispute to be resolved in a neutral forum with established procedures and rules to maintain fairness and impartiality. Furthermore, parties have the freedom to customise and determine their preferred dispute resolution process. Parties are able to, among others, choose the procedural rules that will apply in the arbitration, the seat and place of arbitration, the language of the arbitration and the arbitrators who will hear the dispute. The increasing popularity of arbitrations administered by institutions such as the Singapore International Arbitration Centre ("**SIAC**"), the International Chamber of Commerce's International Court of Arbitration ("**ICC**") or the London Court of International Arbitration ("**LCIA**") has

[1] See World Justice Project Rule of Law Index 2019 (https://worldjusticeproject.org/sites/default/files/documents/WJP-ROLI-2019-Single%20Page%20View-Reduced_0.pdf).
[2] See *Indonesian Slips a Notch in 2019 Ease of Doing Business Ranking*, Jakarta Globe, 1 November 2018 (https://jakartaglobe.id/context/indonesia-slips-a-notch-in-2019-ease-of-doing-business-ranking).

resulted in the issuance of a number of guidelines on the application of the procedural rules at these institutions which allows for greater certainty in the conduct of the arbitration and the application of the procedural rules. We will further elaborate below, the points which parties should consider when customising their dispute resolution mechanism at the contract-drafting stage.

Secondly, it is well-known that since Indonesia is a signatory to the United Nations Convention on the Recognition and Enforcement of Foreign Arbitral Awards (New York, 10 June 1958) ("**New York Convention**"), an arbitral award from other signatories to the New York Convention will be recognised and enforced in Indonesia. For example, an arbitral award in a Singapore-seated arbitration is automatically registrable and enforceable as a court judgment in Indonesia. That being said, there may still be practical difficulties in enforcing an international arbitral award in Indonesia, as will be elaborated upon further below.

Thirdly, the New York Convention allows for the recognition and enforcement of arbitral awards in other jurisdictions which are also signatories to the New York Convention and this is a significant because the debtor under the arbitral award may have assets in those jurisdictions. Depending on the jurisdiction, it may be possible to quickly and expediently move to enforce against those assets in the event of a successful arbitration, thus circumventing the need to enforce in Indonesia or the home jurisdictions of the contracting parties. The challenge however, is for the party seeking enforcement to identify assets belonging to the debtor under the arbitral award. Such challenge can be minimised if information on these assets is obtained prior to the execution of the contract, and if possible, by taking security over such assets (as will be elaborated further below).

Disadvantages of international arbitration

There are also significant disadvantages of Indonesia-related arbitration that need to be highlighted.

First, the duration and costs typically associated with an arbitration are normally longer and higher respectively compared to domestic litigation before the national courts. It is not uncommon for arbitration proceedings to take up to 1-2 year(s) from the commencement until the issuance of a final award, particularly for a high-value dispute where complex issues of law may be raised. For instance, the median duration of an SIAC arbitration is 11.7 months[3] and the median duration of an LCIA arbitration is 16 months.[4] Parties should also expect to incur costs (comprising fees of the arbitral institution and tribunal) of around US$29,567 (median) in an SIAC arbitration[5] and US$97,000 (median) in an LCIA arbitration[6], depending on the complexity, the length of the proceedings and the number of arbitrators involved. However, it is important to note that these costs make up only a small percentage of the total costs parties will incur in an arbitration as parties will also have to incur the costs of engaging legal counsel and expert witnesses, which make up the bulk of costs incurred.

Secondly, notwithstanding the New York Convention, there may still be practical difficulties in enforcing international arbitral awards in Indonesia. This can be illustrated by the case of *Astro Nusantara International BV and others v PT Ayunda Primamitra and others (2009)* which concerned a dispute

[3] See "*SIAC Releases Costs and Duration Study*", 10 October 2016.
[4] See "*LCIA Releases Updated Costs and Duration Analysis*", 3 October 2017.
[5] See "*SIAC Releases Costs and Duration Study*", 10 October 2016.
[6] See "*LCIA Releases Updated Costs and Duration Analysis*", 3 October 2017.

over a failed satellite television joint venture. In that case, the Astro Group commenced a Singapore-seated arbitration against the Lippo Group for claims arising from the joint venture between the parties. After obtaining a favourable arbitral award at the SIAC, the Astro Group sought to enforce the award in Indonesia. However, the Central Jakarta District Court and subsequently the Indonesian Supreme Court refused to enforce the award on public policy grounds.[7]

Even if the Indonesian courts recognise and allow enforcement of the arbitral award in Indonesia, parties often face practical difficulties in identifying assets of the debtor under the arbitral award and taking possession of these assets.

Practical Tips

- It is still advantageous for parties to incorporate an arbitration clause providing for international arbitration seated in a country that is a signatory to the New York Convention, such as Singapore, Hong Kong, the United Kingdom or the United States of America. This ensures fairness in having the arbitration seated in a neutral State, and also efficiency in enforcement by virtue of the New York Convention.
- Parties can also minimise the potential difficulties in enforcing against the other party's assets by identifying those assets (particularly assets located in a signatory state to the New York Convention outside Indonesia) at the contract-drafting stage, and if possible, by obtaining security or restrictive covenants over those assets.
- Parties can also minimise the time (and cost) taken for the dispute resolution process by incorporating certain mechanisms into the contract. For example:
  - Relationships between the parties (and in particular, the principals of the parties) are often regarded as paramount in Indonesia. If a disagreement or dispute arises, Indonesian parties would often prefer to discuss in an amicable and informal setting, and attempt to reach a settlement before referring the dispute to an arbitration. The dispute resolution mechanism can be multi-tiered to incorporate a procedure for parties to, for example, mediate between the principals of the parties, before an arbitration can be commenced. However, it is important that the parameters of such pre-arbitration mechanisms (such as the means by which a mediation can be started, the number of mediation sessions and the duration of that mediation before parties can refer the dispute to an arbitration) be set out clearly, in order to prevent uncertainty or delay in referring the dispute to arbitration should such parties fail to reach a settlement.
  - Parties can also agree to an expedited procedure for the arbitration right at the outset, or at least choose the arbitral rules which will provide them the option of proceeding under the expedited procedure if necessary. For example, the SIAC and ICC Rules of Arbitration provide for expedited procedures which may apply in certain situations. Rule 5 of the SIAC Rules 2016 allows a party to apply for the proceedings to be conducted pursuant to the expedited procedure if the amount in dispute does not exceed S$6m, if parties so agree or in cases of exceptional urgency. Article 30 of the ICC Rules of Arbitration provides that the expedited procedure automatically applies if the amount in dispute does not exceed US$2m or if parties so agree.

[7] See the Central Jakarta District Court Decision No. 05/ PDT/ARB-INT/2009/PN JKT. PST and the Supreme Court Decision No 877 K/ Pdt.Sus/2012.

Ensuring a Comprehensive Security Package or Restrictive Covenants over Available Assets

In the event that the transaction between the parties involves the provision of credit, it is customary for the lender to seek a comprehensive security package and/or restrictive covenants over the debtor's assets to mitigate against the risks of being unable to enforce or to prove the debt against the debtor.

Advantage of seeking a comprehensive security package

If a dispute does arise, the availability of a comprehensive security package, including or alternatively, restrictive covenants, will strengthen the lender's position at the negotiating table, particularly if personal and/or corporate guarantees by the debtor's principals are provided. Ideally, the security package should encompass the debtor's assets in Indonesia and abroad, so that the lender will not be limited to seeking the enforcement of assets in Indonesia, but would also be able to ring-fence an effective enforcement action outside Indonesia. This would also ensure that any successful judgment obtained by the lender will not be rendered moot by any dissipation of assets by the debtor outside of Indonesia.

Even if the debtor only grants security over its assets in Indonesia, the lender would technically still be in a position to obtain quick recourse against the debtor's assets. Under Indonesia law, the lender may choose to enforce the security directly by way of a public auction upon the occurrence of an event of default without resorting to the Indonesian courts, and apply the proceeds from such enforcement as a repayment of the outstanding loan.

Potential difficulties in enforcing security over assets in Indonesia

However, should the lender choose to enforce against the security directly (as mentioned above) without obtaining an order from the Indonesian courts to do so, it is common for a disgruntled debtor to challenge the said enforcement in the Indonesian courts. To stave off such possible challenges, the lender should ideally and pre-emptively obtain a court order granting the enforcement of the security through a public auction,[8] but this in turn will increase the time and costs spent by the lender.

[8] The relevant general procedures are as follows: (a) the creditor must submit an application for enforcement of the security over the relevant assets at the District Court having jurisdiction over the assets; (b) the Court will issue an order for the debtor (or the obligor under the relevant security agreement as the case may be) to voluntarily carry out the enforcement of the security within the period set out in the order. If the debtor (or the obligor) fails to do so, the creditor must submit to the Court and the Court will thereafter issue a *Fiat Executie*; (c) upon the creditor's application, the Court will then issue an order for the enforcement of the security through a public auction and instruct the bailiff seize the relevant assets; and (d) finally, the creditor must make an application to the Auction Office to carry out the auction. In addition to proceeding by way of a public auction, the creditor may also choose to sell the assets subject to the security through a private sale in accordance with applicable laws and regulations.

Practical Tips:

- At the outset when parties are negotiating the relevant contracts, it is recommended that the lender seeks a list of assets owned by the debtor that can be secured against the debt. Even if the transaction does not involve a debt that would allow for the calling of security, or if for any reason security over the debtor's assets is not provided, it would still be highly beneficial if information on the debtor's assets (within Indonesia and abroad) is provided, for instance, to aid enforcement of any monetary judgment or award against the debtor in the future.
- It would also be beneficial from an evidentiary perspective for the lender to obtain a notarised deed of indebtedness from the debtor stating that the debtor acknowledges all of its indebtedness right at the outset. In the event of a dispute, this would strengthen the lender's position in proving the existence and quantum of the debt should the debtor subsequently challenge the existence and quantum of the debt.

Commencing a *Penundaan Kewajiban Pembayaran Utang* ("PKPU" or a postponement of debt payment obligation) proceeding

In general, the PKPU is a formal debt restructuring process which provides for a moratorium against enforcement of claims against a debtor, who is unable, or anticipates that it will be unable, to pay its debts as and when they fall due, which allows the debtor the opportunity to negotiate and agree to a composition plan with its creditors. A PKPU proceeding is often regarded as an effective way to exert pressure on an errant debtor to pay the debt.

Advantage of commencing a PKPU proceeding

The PKPU imposes a time constraint of 270 days from the grant of a temporary PKPU order[9] during which a composition plan must be agreed or ratified by the Indonesian courts or else the debtor company will automatically become bankrupt. Given this time constraint and the potentially devastating consequence of immediate bankruptcy if a composition plan is not agreed or not ratified by the Court, the PKPU is a powerful method to apply pressure or to prevent a debtor from delaying the repayment process.

Difficulties in commencing a PKPU proceeding

Two procedural hurdles must be met before a PKPU proceeding may be commenced: (a) at least **two** petitioning creditors whose claims are due and payable will have to apply; and (b) the debt must be capable of **simple proof**. These requirements may pose a challenge to lenders with complex debt instruments or other financial instruments. Various arguments have been successfully advanced by the debtors to avoid PKPU, including (i) that the lenders have no locus standi to bring a PKPU proceeding

[9] Once a PKPU application is filed, the Court will issue a temporary PKPU order within 20 days (3 days in the case of a voluntary PKPU) of filing. A temporary PKPU order lasts for 45 days. At the same time, the Court will also appoint a supervisory judge to supervise the PKPU process and an administrator who will, jointly with the debtor, manage the debtor's affairs and assets while the PKPU process is afoot. The debtor then has 270 days after the issuance of the temporary PKPU order to propose a composition plan and to seek approval of its proposed plan from the creditors and the court.

as they are not the relevant creditors under the contract[10]; or (ii) that the debts are difficult to be proven so the creditors need to settle such debts in the District Court.[11] Alternatively, the debtors may also argue that proper authorisation to execute the debt instrument has not been obtained or that the agreement was illegal.

Practical Tips:

- In negotiating and drafting the relevant contract, it is important to bear in mind the procedural requirements to bring a PKPU proceeding against a debtor. In particular, it would be useful for the lender to be aware of the identities of the debtor's other creditors in order to meet the requirements of 2 creditors required to bring a PKPU petition.
- It is equally important to ensure that simple and clear proof of the debt, its disbursement and the breach of the contract are available. In this regard, the presence of the notarised deed of indebtedness from the debtor would also be useful to prove the existence of the debt.

Further considerations

Commencing a suit in Indonesia could potentially become a tricky minefield given the various strategic factors at play. It is common for Indonesia-related disputes to involve **civil suits in the Indonesian courts** notwithstanding the presence of a binding arbitration clause between the parties. It is also common for **criminal allegations and police reports** to be filed against the principals and/or employees of the parties, which may make it difficult for such individuals to enter or exit Indonesia.

Even before any disputes potentially arise, strategic decisions which consider the available options should a dispute arise will have to be made when drafting and negotiating Indonesia-related contracts, and thus, it is important to engage both transactional and disputes counsel who are able to provide insights into Indonesia's legal landscapes at the outset. When such disputes do arise, strategic and customised advice from legal advisors who understand the nuances of Indonesia's legal environment becomes all the more critical. Given the different circumstances in each case, such strategic advice would have to take into account the myriad factors at play in order to yield a successful result.

[10] See for instance PKPU Case No. 68/Pdt.Sus-PKPU/2018/PN Niaga Jkt Pst between PT Relys Trans Logistic and PT Imperia Cipta Kreasi versus PT Mahkota Sentosa Utama (also known as Meikarta case).
[11] See for instance PKPU Case No. 131/Pdt.Sus-PKPU/2018/PN Niaga Jkt Pst between Molucca Holding S.a.r.l versus PT Pelita Cengkareng Paper.

Should you require any strategic or legal advice on structuring a transaction or a dispute resolution / enforcement action involving Indonesian elements, you may wish to contact the following persons:

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