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The Enforcement and Annulment of International Arbitration Awards in Indonesia

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THE ENFORCEMENT AND ANNULMENT OF INTERNATIONAL ARBITRATION AWARDS IN INDONESIA

NOAH RUBINS*

INTRODUCTION	359
I. INDONESIA'S LEGISLATION ON ARBITRATION	364
A. INDONESIA'S ARBITRATION TRADITIONS.....	364
B. PAST PROBLEMS OF ENFORCEMENT	366
C. LAW No. 30 OF 1999.....	369
II. KARAH BODAS V. PERTAMINA.....	373
A. THE KARAH BODAS PROJECT	373
B. ARBITRATION PROCEEDINGS	377
C. LEGAL PROCEEDINGS.....	377
III. FLAWS IN THE INDONESIAN "ANNULMENT"	384
A. INDONESIA WAS NOT A "COMPETENT AUTHORITY" TO VACATE THE SWISS ARBITRAL AWARD	385
B. THE INDONESIAN "ANNULMENT" VIOLATED LAW No. 30....	392
IV. RECENT INDONESIAN CASES	398
CONCLUSION	400

INTRODUCTION

Most practicing arbitration lawyers have rarely had the occasion to seek enforcement of an international arbitration award through national courts. Statistics indicate that the vast majority of defeated companies comply with the terms of international arbitral awards

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against them or settle soon after the award is rendered.¹ The United Nations Convention on the Recognition and Enforcement of Foreign Arbitral Awards (the “New York Convention” or the “Convention”) contributes to this compliance by obligating member nations to enforce awards rendered outside their territory, as long as they meet certain requirements (generally procedural in nature).² The New York Convention, currently with over 130 member nations, has become one of the most widely-ratified treaties in the world.³ Such breadth ensures, with relative certainty, that the losing party to arbitration will sooner or later have its assets rooted out by the victor, identified in some corner of the world subject to the strictures of the New York Convention and seized through a swift proceeding that is extremely difficult to deflect.

Enforcing arbitration awards under the Convention, however, necessarily implicates domestic courts.⁴ National courts become

1. See ALAN REDFERN & MARTIN HUNTER, LAW AND PRACTICE OF INTERNATIONAL COMMERCIAL ARBITRATION 443 *3d ed. 1999) (a successful party in an international commercial arbitration proceeding expects that the award will be carried out in a reasonable time, and observing that statistics imply most awards are in fact carried out voluntarily). However, statistics on this topic are hard to obtain because arbitration is confidential and because the arbitral tribunal does not assist in enforcing the decision. *Id.*

2. See United Nations Convention on the Recognition and Enforcement of Foreign Arbitral Awards, June 10, 1958, art. 1, 330 U.N.T.S. 38, reprinted in International Handbook on Commercial Arbitration, Supp. 29 (J. Paulsson ed., 1999) [hereinafter New York Convention] (each Contracting State must recognize arbitral awards as binding and enforceable, as long as the awards meet certain procedural requirements).

3. See *Status of Conventions and Model Laws*, sec. I.9, United Nations Commission on International Trade Law (“UNCITRAL”) [hereinafter *Status of Conventions*] (identifying in chart form the 134 Member States, together with when they signed, ratified, and put the Convention into force), at www.uncitral.org/english/status/status-e.htm (last visited Feb. 21, 2005).

4. Cf. Convention on the Settlement of Investment Disputes between States and Nationals of Other States, Aug. 27, 1965, art. 54, 17 U.S.T. 1270, 29 [hereinafter Washington Convention] (unlike the New York Convention’s enforcement provisions, the Washington Convention employs direct implementation of investment arbitration awards rendered under the Convention). See *Liberian Eastern Timber Corp. v. Liberia*, 650 F. Supp. 73, 76 (S.D.N.Y. 1986) (maintaining that Contracting States shall recognize as binding any awards rendered under the Washington Convention); see also Aron Broches, *Cour de*

involved most commonly at one of three stages of the arbitration process: at the outset of the dispute, to enforce the agreement to arbitrate; during the arbitration proceedings, through requests for interim measures or assistance with evidence-gathering; and after the close of arbitration to either enforce or annul the final award.⁵ Court intervention is necessary to some degree to avoid abuse and injustice, but courts that are too invasive frustrate the parties' will and hamper international commerce.⁶ While recognition of international arbitration awards pursuant to the New York Convention has generally been uniform worldwide, a few recent cases demonstrate that national courts still retain the power to sabotage enforcement despite the Convention's requirements.⁷ These cases could erode confidence in the international arbitral process, raising doubts as to the advantages of resolving international commercial disputes through arbitration.⁸

Historically, Indonesian courts have engendered little confidence among foreign investors that the dispute resolution systems they and their Indonesian partners devise in their contracts will be given full

Cassation 11 juin 1991 Société SOABI v. État du Sénégal, REVIEW DE L'ARBITRAGE 637, 637-38 (1991) (the Washington Convention limits the power of judges in each Contracting State to control the arbitration award).

5. See Mark Kantor, *Local Court Intervention in International Arbitration*, 1 OIL, GAS AND ENERGY LAW INTELLIGENCE 2, March 2003 (discussing how recent rulings in domestic courts demonstrate local project participants' and government agencies' ability to usurp arbitrators' authority by seeking court invalidation of underlying contracts).

6. See *id.* (while courts base their interventions on widely supported legal doctrines, international project participants may fear the prospect of local court action, as hard assets and contract rights may be "held hostage" to compliance).

7. See generally William A. Isaacson, *Enforcement Difficulties are Increasing*, 25 NAT'L LAW L.J. 89 (2002) (discussing how the New York Convention binds countries all over the world to enforce foreign arbitral awards although recent enforcement difficulties have undermined uniform application).

8. See Nicholas Stone, *Indonesia: Arbitrating Indonesian Disputes*, INDONESIA ACADEMIC ENHANCEMENT PROGRAM, Oct. 25, 2001 (the efficiency and reliability of the arbitration process depends in part on "the extent of support and recognition that it receives in the laws of the place where the arbitration is proceeding, or where an award is to be enforced"), at <http://www.east.asu.edu/msabr/research/indonesia/iradru/stone.htm> (last visited Feb. 21, 2005).

effect when a conflict ultimately arises.⁹ It is well-known that local courts frequently penetrate the arbitral process—adjudicating cases subject to arbitration agreements, enjoining ongoing proceedings, and reopening the merits of final awards.¹⁰

Indonesia passed a new arbitration law in 1999, inspiring a great deal of optimism.¹¹ On its face, the new law offered predictability and harmonization with global standards, which could have helped draw indispensable foreign capital back to the country after the 1997-1998 financial crisis.¹² To date, however, the implementation record of the 1999 legislation has been sobering.¹³

The case of *Karaha Bodas Company LLC (“KBC”) v. Perusahaan Pertambangan Minyak Dan gas Bumi Negara (“Pertamina”)* is sadly emblematic of the continuing problems in enforcing arbitral agreements and awards. After an ICC tribunal ordered Pertamina to pay \$261 million to Karaha Bodas Company LLC as compensation for canceling a power project in 1998, in the wake of the Asian financial crisis, Pertamina refused to comply.¹⁴ Pertamina sought to annul the award in Switzerland, the arbitration’s venue.¹⁵ The Swiss court rejected Pertamina’s application twice, without ever reaching the merits.¹⁶ When KBC began to enforce the award by seizing assets in the United States, Hong Kong, Singapore, and Canada, Pertamina

9. *See id.* (underlining the Dutch Colonial Code’s inadequacy in preventing courts from interfering with arbitration processes). Until recently, the Dutch Colonial Code governed the arbitration process in Indonesia. *Id.*

10. *Id.*

11. *See id.* (noting that the new Indonesian law on arbitration was designed to stop judicial interference; in fact the law clearly states that the District Court has no authority in disputes involving arbitration agreements).

12. *See generally id.* (explaining the impetus for the new law and some of its features).

13. *See id.* (suggesting that recent actions prove the courts will still interfere in some arbitration processes, despite the new law).

14. *See generally* *Karaha Bodas Co. v. Perusahaan Pertambangan Minyak Dan Gas Bumi Negara*, 335 F.3d 357, 360-63 (5th Cir. 2003) [hereinafter *Karaha Bodas I*].

15. *Id.* at 361. Pertamina appealed to the Supreme Court of Switzerland to have the award annulled. *Id.*

16. *Id.* at 361 n.9.

turned to its home courts in Indonesia. The state-owned oil giant petitioned the Jakarta Central District Court to annul the award under Indonesian law.¹⁷ In the *Karaha Bodas* case, the central problems of the old arbitration legislation arose once again—Indonesian courts asserted jurisdiction over an arbitration the parties had explicitly sought to isolate from its power, and then annulled an award on unpredictable and unprincipled grounds.¹⁸ Indonesia's reputation in the international community, not only as a participant in the arbitration regime, but also as a locale for foreign investment, will likely decline further in light of the *Karaha Bodas* vacatur.¹⁹ How could the adoption of a reasonably modern arbitration law have made so little difference to the Indonesian court? Answering this is important because the success of international commercial arbitration as a system depends in large part on predictability at the enforcement stage.²⁰

This article explains why the Jakarta Central District Court's *Karaha Bodas* award of vacatur violated the spirit and letter of the New York Convention, and how, in the end, that court's decision will have little effect outside of Indonesia. Part II provides an overview of past and current Indonesian arbitral law.²¹ Part III presents the facts of the *Karaha Bodas* case and the contours of the related enforcement litigation.²² Next, Part IV examines the

17. *Id.* at 361.

18. Stone, *supra* note 8. This decision contradicts the international view that arbitration clauses are separate from the contract and therefore binding, even if the contract is invalid. *Id.*

19. See, e.g., U.S. DEPT. OF STATE, BACKGROUND NOTE: INDONESIA (Aug. 2004) (noting that Indonesia has made significant changes to its regulatory framework since the late 1980s in an effort to encourage economic growth, which was previously financed largely through both domestic and foreign private investments), at <http://www.state.gov/r/pa/ei/bgn/2748.htm> (last visited Feb. 21, 2005); see also Stone, *supra* note 8 (the *Karaha Bodas* decision was a discouraging first test for the new law because the court refused to follow the accepted international view on arbitration).

20. See *id.* (noting that the reason arbitration is usually more preferable than the courts is because the courts are unpredictable and generally lack the expertise needed to correctly decide the case).

21. See *infra* notes 25-79 and accompanying text.

22. See *infra* notes 80-154 and accompanying text.

procedure for enforcement actions under the New York Convention and its relationship to enforcement and annulment proceedings under Indonesian arbitral law.²³ Finally, Part V explores the reasons for the 1999 law's failure and suggests ways in which it could be improved.²⁴

I. INDONESIA'S LEGISLATION ON ARBITRATION

A. INDONESIA'S ARBITRATION TRADITIONS

The principal sources of commercial arbitration law in Indonesia are traditional norms known as the *pancasila*, the colonial Code of Civil Procedure, the Indonesian Civil Code, and, most recently, Law No. 30 of 1999.²⁵ Historically, each of these sources' peculiarities, and their occasionally conflicting demands, have hobbled the development of clear and predictable rules concerning enforcement of foreign awards in Indonesia.²⁶

Traditionally, Indonesian society is somewhat "non-litigious;" Indonesians are thought to prefer amicable dispute settlement through negotiation, and value greatly the preservation of commercial relationships.²⁷ This consensual approach finds inspiration in the *pancasila* (the "five pillars"), an influential body of traditional philosophy that calls for avoiding confrontation whenever possible.²⁸ From a legal standpoint, those legal scholars and judges

23. See *infra* notes 156-247 and accompanying text.

24. See *infra* notes 248-253 and accompanying text.

25. Asia-Pacific Economic Cooperation ("APEC"), *A Guide to Arbitration and ADR in APEC Member Economies (Indonesia)* [hereinafter *APEC Guide to Arbitration*], at <http://www.arbitration.co.nz> (last visited Feb. 21, 2005).

26. See Karen Mills, *Enforcement of Arbitral Awards in Indonesia*, 6 INT'L ARB. L.R. 192, 193 (2000) (although the Indonesian Civil Code provided that foreign judgments—which most commentators agree include arbitration awards—cannot be enforced, the New York Convention, which Indonesia has ratified, specifically called for enforcing such foreign awards).

27. See *id.* at 195 (in Indonesia, confrontation is usually avoided; but when commercial disputes do arise, they are typically simple matters that parties can settle through negotiation).

28. See C.G. de Souza and M.A. Karolewski, *Dispute Resolution in Indonesia* 1 (identifying five sources upon which Indonesian law is based), at

who closely adhere to *pancasila* promote such alternative dispute resolution (“ADR”) forms as mediation and conciliation or consensus building, rather than arbitration—the more adversarial approach.²⁹

Until 1999, Indonesia’s arbitration legislation was a jumble of provisions dating back to the colonial period and based squarely on early twentieth-century Dutch models.³⁰ The Indonesian Constitution of 1945 stipulated that the laws of the Netherlands would remain valid so long as they did not contradict the Constitution, or until they were superseded by new local laws.³¹ Articles 615-651 (Title I) of the Dutch colonial Code of Civil Procedure, together with the general freedom of contract provisions of the Indonesian Civil Code, formed the legislative basis for arbitration in Indonesia.³²

This legal framework had important shortcomings. The civil procedure rules contained no express arbitration rules, so Articles 615-651 of the Code provided legitimacy to arbitration only implicitly.³³ Further, there was no clear mandate for recognizing and

<http://www.geocities.com/karolewski/indo.pdf> (last visited Feb. 21, 2005).

29. See APEC *Guide to Arbitration*, *supra* note 25 (explaining that the philosophy of *pancasila* favors non-confrontational and consensual settlement of disputes, such as alternative dispute resolution).

30. See Sudargo Gautama, *Indonesia*, INTERNATIONAL HANDBOOK ON COMMERCIAL ARBITRATION, Supp. 26 at 1 (Paulsson ed., 1998) (discussing how Indonesian regulations on arbitration, as of 1998, were based on articles introduced for “Europeans” and “foreign Oriental Chinese” under the Constitution of the Netherlands).

31. See Mills, *supra* note 26, at 106 (suggesting that Dutch laws are not necessarily binding but at least serve as guidance to judges).

32. See *id.* (explaining that by combining the two Codes, the basis for arbitration in Indonesia was formed before Indonesia existed as a nation, and that this foundation was preserved when the new Indonesian Constitution was written).

33. See Mulyana & Jan K. Schaefer, *Indonesia’s New Framework for International Arbitration: A Critical Assessment of The Law And Its Application By The Courts*, 17 MEALEY’S INT’L ARB. REP. 39, 40 (2002) [hereinafter Mulyana & Schaefer, *Critical Assessment*] (although Indonesia abandoned the Civil Code after its independence from the Netherlands, Articles 615-651 still governed the arbitration process *de facto* because the new procedural rules did not address the issue).

enforcing domestic arbitral awards, let alone foreign ones.³⁴ These deficiencies caused some foreign businesses to question the legal security of their investments in Indonesia.³⁵

B. PAST PROBLEMS OF ENFORCEMENT

Indonesia's antiquated arbitration legislation led to decades of problems in enforcing foreign decisions.³⁶ This legacy is due chiefly to an article of the Dutch Civil Code stating that judgments of foreign courts may not be recognized in local courts.³⁷ In the absence of any express law on arbitration, Indonesian courts interpreted the Civil Code instruction as extending equally to foreign arbitral awards.³⁸ The government did not address this dilemma until 1981, when Indonesia acceded to the New York Convention.³⁹ Clearly, the

34. See *id.* (observing that the colonial arbitration law did not address a range of issues often arising during arbitration proceedings, leading to scrutiny by foreign investors).

35. See Ricardo Simanjuntak, *Legal Practitioners and Business Perspectives on Business Contract Enforceability* (June 13, 2002) (recalling that recent conflicts between foreign investors, state-owned companies and Indonesian businesspeople have led foreign investors to question whether their investments will be respected and protected by Indonesian law) (unpublished paper presented in the Seminar on the Enforceability of Business Contracts in Indonesia, on file with the *American University International Law Review*).

36. Mills, *supra* note 26, at 106. For at least ten years after Indonesia signed the New York Convention in 1981, courts remained reluctant to enforce foreign awards. *Id.*

37. See BURGELIJKE REGLEMENT OF DE RECHTSVORDERING [hereinafter RV] art. 463 (Neth.), in Karen Mills, *Judicial Attitudes to Enforcement of Arbitral Awards and other Judicial Involvement in Arbitration in Indonesia*, 68 ARB. 106 (2002) (Article 463 of the RV provides that Indonesia will not enforce foreign court judgments).

38. Mulyana & Jan K. Schaefer, *Indonesia's New Arbitration Law: Salient Features and Aberrations in the Application*, 2002 INT'L A.L.R. 41 [hereinafter Mulyana & Schaefer, *Salient Features*]. This uncertainty stemmed from Indonesia's ostensible abandonment of the RV, which originally applied to legal matters that affected Europeans in Indonesia. *Id.* After abandoning the RV, only the procedural rules pertaining to arbitration that applied to indigenous Indonesians remained in force. *Id.* As a result, Articles 615-651 of the RV continued to govern arbitration in Indonesia *de facto*. *Id.*

39. Mills, *supra* note 26, at 193; see *APEC Guide to Arbitration*, *supra* note 25 (Indonesia ratified the New York Convention subject to two reservations:

Civil Code's standing interpretation was irreconcilable with that treaty's pro-enforcement obligations.⁴⁰ Indonesia's ratification of the Convention created high expectations among foreign investors, who believed the action signified a turning point for enforcing foreign arbitral awards there.⁴¹

However, in the decade following ratification, local courts remained reluctant to enforce foreign arbitral awards against Indonesian nationals. In the 1984 *Navigation Maritime Bulgare v. P.T. Nizwar* case, for example, the Indonesian Supreme Court's decision put the New York Convention's applicability into serious doubt.⁴² In *Bulgare*, the Court declared that foreign arbitral awards remained unenforceable in Indonesia because the government had failed to pass implementing regulations explaining to courts how they were to apply the New York Convention.⁴³ Arbitration scholars around the world denounced this ruling because it clearly contradicted the terms of the New York Convention, which requires contracting States to "recognize as binding and enforce" foreign

"(i) arbitration awards that can be executed in Indonesia must relate to commercial disputes; and (ii) recognition of awards had to be on the basis of reciprocity, i.e. rendered in a country which together with Indonesia, is a party to an international convention regarding implementation of foreign arbitral awards").

40. See *id.* (comparing the Code of Civil Procedure's mandate that foreign-rendered arbitration awards cannot be enforced in Indonesia with Article III of the New York Convention, "which provides that every Contracting State must recognise [sic] and enforce awards rendered in other Contracting States without imposing substantially more onerous conditions that are imposed upon recognition or enforcement of domestic awards").

41. Mulyana & Schaefer, *Salient Features*, *supra* note 38, at 61. However, the Indonesian Supreme Court soon thereafter refused to enforce a foreign award in *Navigation Maritime Bulgare*, thus making clear that despite signing the New York Convention, Indonesia was not ready to enforce all foreign awards. *Id.*

42. See Mahkamah Agung [Supreme Court], *20 August 1984, on file with author* (holding that although Indonesia had ratified the New York Convention, it was not yet bound by its provisions).

43. See SUP. CT. REG. 1 (1990) (Indon.), reprinted in INTERNATIONAL HANDBOOK ON COMMERCIAL ARBITRATION, Supp. 13 (J. Paulsson ed., 1992) [hereinafter 1990 REGULATION] (regulations should be promulgated concerning the enforcement procedure for foreign arbitral awards).

arbitral awards.⁴⁴ Thus, *Bulgare* did little to reassure foreign businesses that Indonesia would respect their contracts.

Not until 1990 did the Supreme Court issue the landmark Regulation No. 1 (“the Regulation”), establishing an implementing procedure for enforcing foreign awards.⁴⁵ Indonesian authorities praised the Regulation as a breakthrough, hoping it would restore investor confidence in the legal system.⁴⁶ Unfortunately, within a short time, it became obvious that both the New York Convention and Regulation No. 1 were failing to correct Indonesia’s enforcement problems. For instance, Regulation No. 1 neglected to set a time limit within which the Supreme Court would rule on applications for enforcement.⁴⁷ This omission often resulted in foreign arbitral awards being docketed along with the Court’s normal case-load, thus creating enormous delays.⁴⁸ Similarly, the Regulation provided no clear limits upon court intervention, an oversight that enabled local judges to derail international arbitrations involving Indonesian respondents.⁴⁹ Such flaws only served to deepen the recognized problem of rampant corruption within the Indonesian bench,⁵⁰ and “inroads were opened for the Indonesian courts to adversely interfere in international arbitrations.”⁵¹

44. New York Convention, *supra* note 2, at art. III.

45. See Duane J. Gingerich, *Indonesia to Enforce Foreign Arbitral Awards*, 12 E. ASIAN EXEC. REP., at 9 (nearly six years after the *Bulgare* decision, the Supreme Court finally issued long-awaited regulations to establish enforcement procedures).

46. *Id.* at 13.

47. Mills, *supra* note 37, at 107.

48. See Mills, *supra* note 26, at 194 (the Court acted on the first nine applications, received between 1991 and 1993, with reasonable speed, but the court did not issue any orders between 1994 and 2000, leaving seven applications pending).

49. Mulyana & Schaefer, *Critical Assessment*, *supra* note 33, at 40.

50. See Oliver Wright and Andi Zulfikar, *Indonesian Dispute Resolution*, April 2002 (suggesting that corruption within the Indonesian courts is reinforced by lawyers, judges, prosecutors, and the police), at http://www.dentonwildeapte.com/assets/I/IndonesianDisputeRes_Apr02.pdf (last visited Feb. 21, 2005). It is widely considered that the Indonesian courts are in a “sorry state” due to corruption. *Id.*

51. Mulyana & Schaefer, *Critical Assessment*, *supra* note 33, at 40.

Aside from these enforcement problems, Indonesia's legal reforms failed to respond to numerous other arbitration-related issues. For example, they did not codify any policy in favor of enforcing agreements to arbitrate, define the scope of party autonomy, or enumerate the grounds and procedures for challenging an arbitrator.⁵² Legislative silence on these and other pressing matters resulted in confusion among Indonesian justices; with no legislative solution to these issues throughout the mid-1990s, foreign expectations for an improved arbitration system quickly dissipated.⁵³

C. LAW NO. 30 OF 1999

In 1997, the looming economic crisis and the continuing uncertainty surrounding Indonesia's arbitration regime renewed calls for fundamental reform of the country's arbitration laws.⁵⁴ Local commentators pushed to "modernize" the arbitration regime, to make the prospect of doing business in Indonesia more palatable.⁵⁵ The result was the Law Concerning Arbitration and Alternative Dispute Resolution, No. 30 of 1999 (the "1999 Law" or "Law No. 30").⁵⁶ The Indonesian legislature designed this new law to repair the former system's ambiguities, particularly in connection with the enforcement of foreign arbitral awards.⁵⁷ In drafting the 1999 Law, Indonesia departed from its Southeast Asian neighbors, which chose

52. *Id.* at 41, 61-62.

53. *See* Mills, *supra* note 26, at 194 (noting that because the Supreme Court has failed to act on an application since mid-1994 and the first order under the Regulation was later nullified by the Supreme Court, Indonesia earned "a negative reputation in arbitration circles").

54. *See* Mulyana & Schaefer, *Critical Assessment*, *supra* note 33, at 40 (suggesting that the impetus for arbitration reform in Indonesia came from the International Monetary Fund, which took the position that reform would make Indonesia a more investment-friendly environment and that it would provide a workable solution until the country's court system could be modernized).

55. *See id.* (noting that as the country attempted to attract investment, "the suitability of Indonesia's framework for arbitration was scrutinized by foreign investors and modernization was recommended").

56. Law No. 30 of 1999 (Indon.), *reprinted in* 17 MEALEY'S INT'L ARB. REP. A-1 (2002) [hereinafter Law No. 30].

57. Mulyana & Schaefer, *Critical Assessment*, *supra* note 33, at 40.

to adopt the UNCITRAL Model Law on International Commercial Arbitration (the "Model Law").⁵⁸ Instead, the legislature created an independent set of rules applicable to national and international arbitration, different from both the Model Law and the previous legal framework.⁵⁹ The law is founded on civil law notions that arbitration is an out-of-court process for settling private disputes.⁶⁰

Chapters I through IV of Law No. 30 deal with general principles and the procedures to be followed by arbitrators absent party agreement.⁶¹ Chapters V, VI, and VII deal with the making of awards, recognition and enforcement of awards, and annulment of awards, respectively.⁶²

Chapter VI of Law No. 30 first provides for the enforcement of domestic arbitral awards. To be enforceable, an award must be "delivered and registered by the arbitrator or his attorney-in-fact to the Clerk of the District Court" within thirty days of the date the award was "pronounced."⁶³ If the requirements for registering the award are not met, Article 59(4) provides that "the arbitral award shall not be enforceable."⁶⁴ The second part of Chapter VI provides for the enforcement of international arbitral awards. The competent authority to enforce the foreign award is the District Court of Central

58. *See Status of Conventions, supra* note 3, at sec. II.10 (listing the states that have enacted legislation based on the UNCITRAL Model Law, including Hong Kong, Macau, Thailand, Japan, South Korea, and Singapore).

59. Mulyana & Schaefer, *Critical Assessment, supra* note 33, at 40-41.

60. *Id.* at 41.

61. *See generally* Law No. 30, *supra* note 56 (defining key terms within the law, and providing an overview of how to initiate arbitration proceedings).

62. *See generally id.* chs. V-VII (providing guidelines for the rendering of arbitration awards and for post-award procedures). Articles 3 and 11 of the new law clearly exclude local courts from ruling on the merits of arbitrable disputes, stating that the District Court "shall have no jurisdiction to try disputes between parties bound by an arbitration agreement" and "shall reject and not interfere in the resolution of a dispute which has been determined to be resolved through arbitration." *Id.* arts. 3, 11.

63. *See id.* at art. 59(1) (mandating that the arbitrator deliver the original or an authentic copy of the arbitral award).

64. *Id.* at art. 59(4).

Jakarta,⁶⁵ and the award will be recognized and enforceable if the following conditions are met: 1) the award was rendered in a country that is bound with Indonesia to recognize and enforce international arbitration awards; 2) the dispute is commercial in nature; 3) the award does not violate *ordre public*; 4) the Chairman of the District Court of Central Jakarta issues an exequatur [an authorization of execution]; and 5) where Indonesia is a party to the dispute, the Supreme Court of the Republic of Indonesia issues the exequatur.⁶⁶

Articles 70 and 71 of Chapter VII provide for the annulment of arbitral awards. Chapter VII makes no visible distinction between domestic and international awards. The text of Article 70 provides:

[W]ith regard to an arbitral award, the parties may submit an application for annulment if the award allegedly contains any of the following elements:

a) letter(s) or document(s) submitted in the examination proceedings, after the award was rendered, was (were) admitted as forged or declared as forgeries; b) after the award was rendered, documents which are dispositive were discovered, which were concealed by the opposing party; or c) the award was a result of fraud committed by one of the parties during the examination of the dispute.⁶⁷

Thus, the grounds for challenging awards under the 1999 Law are significantly narrower than those contained in the Model Law.⁶⁸ Article 70 does not appear to allow courts to vacate awards where the arbitrators have exceeded their powers, or where there is a violation of Indonesian public policy. Article 71 requires that the moving party submit an application for annulment within thirty days of having had

65. *See id.* at art. 65 (declaring the District Court of Central Jakarta to be the “relevant authority for the recognition and the enforcement of International Arbitral Awards”).

66. *See* Law No. 30, *supra* note 56, art. 66 (once the Supreme Court issues the exequatur, it delegates authority to the District Court of Central Jakarta to execute it).

67. *Id.* at art. 70.

68. *See* Sebastian Pompe and Marie-Christine van Waes, *Arbitration in Indonesia*, in *INTERNATIONAL COMMERCIAL ARBITRATION IN ASIA*, at 3-19 (Philip J. McConaughay ed., 2002) (distinguishing other modern arbitration laws, which include provisions for recourse by the losing party, such as set aside provisions, from the Law No. 30, which does not).

the award registered with the Clerk of the District Court, but curiously sets no deadline for registering the award.⁶⁹

Law No. 30 does incorporate certain key principles of the Model Law, such as limited court involvement and finality of awards;⁷⁰ however, some central aspects of the Model Law are missing, such as the doctrine of *Kompetenz-Kompetenz* (the arbitrator's power to rule upon the extent of his own jurisdiction).⁷¹ In addition, many of the 1999 Law's procedural provisions appear to be mandatory, constraining the parties' ability to construct a dispute resolution system that best suits their needs.⁷²

Like many Indonesian statutes, the 1999 Law is accompanied by a non-binding "Elucidation," designed to guide courts when putting the text into practice.⁷³ Frequently, these explanations create as many problems as they solve.⁷⁴ On the one hand, the Elucidation extols the virtues of arbitration and calls for "fundamental changes to the Civil Procedures Regulation... both philosophically and substantively."⁷⁵ At the same time, the Elucidation raises serious doubts that Article 70 of the 1999 Law provides exhaustive grounds for annulment. It states that annulment is possible for several reasons: "*inter alia*," forged documents, withholding of material documents, and fraud on the parties.⁷⁶ The phrase "*inter alia*" may have been a flourish of

69. Law No. 30, *supra* note 56, art. 71.

70. Mulyana & Schaefer, *Critical Assessment*, *supra* note 33, at 41.

71. *Id.* at 51. Because of this lacuna, disputes concerning an arbitrator's jurisdiction often end up in Indonesian courts, creating unnecessary judicial involvement by judges who "lack expertise in international commercial matters and have a shattered reputation." *Id.*

72. *Id.* at 57. For example, it is unclear whether the arbitrators should honor the parties' choice of law if it lacks a substantial connection to the contract. *Id.*

73. Pompe and van Waes, *supra* note 68, at 2, 3.

74. See, e.g., *Karaha Bodas Co. v. Perusahaan Pertambangan Minyak Dan Gas Bumi Negara*, 313 F.3d 70, 87 (2d Cir. 2002).

75. *Elucidation to Law of the Republic of Indonesia Number 30 of 1999*, reprinted in 17 MEALEY'S INT'L ARB. REP. A-8, A-9 (2002).

76. See *Perusahaan Pertambangan Minyak Dan Gas Bumi Negara (Pertamina) v. Karaha Bodas Co.*, No. 86/PDT.G/2002/PN.JKT.PST, Judgment, at 23 (English translation on file with author) [hereinafter *Indonesian Case, Judgment*] ("grounds on which to base a petition for the annulment of an arbitral award are, among

overly legal language, but as illustrated in the *Karaha Bodas* case, described below, the Jakarta District Court seized upon these words to depart completely from Article 70.⁷⁷

Since Indonesia adopted the 1999 Law, arbitration-related proceedings have revealed that Indonesia's courts are still finding it difficult to resist interfering in some cases, leading observers to wonder whether conditions have changed at all. In a 2000 case, for example, a Jakarta court ignored a clearly binding arbitration clause on grounds that the dispute was purely legal, and that arbitration should only be used to decide technical or "expert" matters.⁷⁸ Further, when the main contract's validity was questioned, the court decided that it had jurisdiction over the merits of the dispute on grounds that the arbitration clause was part of the main contract; and since the main contract was invalid, the arbitration clause therein must also be null.⁷⁹

Perhaps the most notorious—and certainly the most complicated—arbitration matter to test the viability of the 1999 Law is the case of *Karaha Bodas Company, L.L.C. v. Perusahaan Pertambangan Minyak Dan Gas Bumi Negara* ("*Karaha Bodas v. Pertamina*"). The *Karaha Bodas* case revealed that the problems with Indonesian arbitration law lay as much with the Indonesian courts as with the 1999 Law.

II. *KARAH BODAS V. PERTAMINA*

A. THE *KARAH BODAS* PROJECT

Three parties and two contracts lie at the root of the *Karaha Bodas* case. KBC is a Cayman Islands company primarily owned by Florida Power and Light⁸⁰ and Caithness Energy,⁸¹ two of America's most

others, as stipulated in Article 70").

77. *Id.*

78. *See id.* at 12 (explaining that the arbitral decision should be nullified because it failed to apply Indonesian Law to resolve the dispute).

79. *See id.* at 7 (finding the agreement's arbitration clause inoperative and incapable of being performed because the agreement itself is null and void).

80. FPL Group, *About Us*, at http://www.fplgroup.com/about/contents/about_us.shtml (last visited Feb. 21, 2005).

important energy producers and distributors.⁸² Pertamina is Indonesia's national gas and oil company;⁸³ PLN is its national electric company.⁸⁴ In November 1994, KBC and Pertamina entered into a joint operation contract ("JOC") that granted KBC geothermal development rights in a West Java, Indonesia project.⁸⁵ KBC and Pertamina also signed an energy sales contract ("ESC") with PLN in which PLN agreed to purchase from Pertamina the electrical energy produced at the Karaha Bodas geothermal facility.⁸⁶

In September 1997, President Soeharto responded to the looming Asian financial crisis⁸⁷ by issuing a decree suspending the KBC project.⁸⁸ When KBC protested, Soeharto reversed his decision and

81. Caithness Energy, L.L.C., *About Us*, at <http://www.caithnessenergy.com/about.html> (last visited Feb. 21, 2005).

82. *Karaha Bodas Co. v. Perusahaan Pertambangan Minyak Dan Bumi Negara*, 190 F. Supp. 2d 936, 939 (S.D. Tex. 2001) [hereinafter *Karaha Bodas III*].

83. PT Pertamina (Persero), *Company's History*, at <http://www.pertamina.com/englishversion/companyprofile/history.html> (last visited Feb. 21, 2005); see PT Pertamina (Persero), *Company in Brief* (noting that Pertamina has recently become a Limited Liability Corporation, although it is still state-owned) at <http://www.pertamina.com/englishversion/companyprofile/brief.html> (last visited Feb. 21, 2005). Pertamina's move to a limited liability enterprise was promulgated by the passage of Law No. 22/2001 in November 2001 and subsequent Government Regulation No. 31 in September 2003. *Id.*

84. PT PLN (Persero), *Company Profile*, at http://www.pln.co.id/english/company_profile_energy.asp (last visited Feb. 21, 2005).

85. *Karaha Bodas III*, 190 F. Supp. 2d at 939-40; see *Exclusive Right on Geothermal Resources Lifted*, JAKARTA POST, Aug. 4, 2000.

86. *Karaha Bodas III*, 190 F. Supp. 2d at 940. See generally E. ALLAN FARNSWORTH, FARNSWORTH ON CONTRACTS § 2.15 (2d ed. 1998) (providing an overview of output and requirement contracts).

87. Embassy of the United States of America, Jakarta, Indonesia, *Chronology of the Crisis* [hereinafter *Crisis Chronology*] at <http://www.usembassyjakarta.org/econ/crisis.html> (last visited Feb. 21, 2005); see Meydiatama Suryodiningrat, *APEC Analysts Predict Slower Growth for RI*, JAKARTA POST, Nov. 24, 1997, available at 1997 WL 13541112.

88. See *Crisis Chronology*, *supra* note 87 (the Indonesian president suspended the Karaha Bodas Company ("KBC") project in order to alleviate budgetary pressures in light of growing debt); see also *Karaha Bodas III*, 190 F. Supp. 2d at 940 (KBC continued its production schedule because Pertamina and PLN insisted that the suspension was temporary, even though the presidential decree indefinitely postponed the project).

reinstated the project in November 1997.⁸⁹ Finally, on January 10, 1998, a third decree postponed the project for good.⁹⁰ After the third Presidential Decree, KBC notified Pertamina and PLN on April 30, 1998 that the government's actions "constituted an event of *Force Majeure*" under both contracts, ceased operations, and served the parties with notice of its intent to initiate arbitration.⁹¹

Clauses in each contract provided that the three parties would arbitrate disputes arising out of the contracts in Geneva, Switzerland, under the United Nations Commission on International Trade Law Arbitration Rules ("UNCITRAL Rules").⁹² Both contracts also provided for the parties' selection of arbitrators within thirty days of the initiation of arbitration by one of the parties.⁹³ The contracts added the proviso that if either party failed to appoint its arbitrator within thirty days, the Secretary General of the International Centre for Settlement of Investment Disputes ("ICSID")⁹⁴ would appoint an arbitrator upon any party's request.⁹⁵ While the JOC provided that each party would appoint an arbitrator, the ESC stated that KBC and Pertamina would jointly appoint an arbitrator, with PLN appointing

89. *Karaha Bodas III*, 190 F. Supp. 2d at 940.

90. *Id.* See *Crisis Chronology*, *supra* note 87.

91. *Karaha Bodas III*, 190 F. Supp. 2d at 940; see generally Jennifer M. Bund, Note and Comment, *Force Majeure Clauses: Drafting Advice for the CISG Practitioner*, 17 J.L. & COM. 381, 399-401 (1998).

92. *Karaha Bodas Co. v. Perusahaan Pertambangan Minyak Dan Gas Bumi Negara*, 364 F.3d 274, 282 n.7 (5th Cir. 2004) [hereinafter *Karaha Bodas IV*].

93. *Id.*

94. World Bank Group, *About ICSID*, at <http://www.worldbank.org/icsid/about/main.htm> (last visited Feb. 21, 2005). The Convention on the Settlement of Investment Disputes Between States and Nationals of Other States created the International Centre for Settlement of Investment Disputes ("ICSID") and both Indonesia and the United States ratified the Convention. *Id.* See World Bank Group, *List of Contracting States* (Indonesia ratified the Convention in 1968 and the United States ratified the Convention in 1966), available at <http://www.worldbank.org/icsid/constate/c-states-en.htm> (last visited Feb. 21, 2005).

95. *Karaha Bodas IV*, 364 F.3d at 282 n.7.

the other arbitrator.⁹⁶ Both the JOC and the ESC provided that Indonesian laws would govern each agreement.⁹⁷

KBC appointed Professor Piero Bernardini to the arbitration panel,⁹⁸ but Pertamina failed to name an arbitrator within thirty days.⁹⁹ KBC notified ICSID and requested appointment of a second arbitrator.¹⁰⁰ The ICSID Secretary General did not receive any objections from Pertamina,¹⁰¹ and proceeded to appoint Dr. Ahmed El-Kosheri to the arbitral panel on July 15, 1998.¹⁰² The two arbitrators subsequently appointed Yves Derains to serve as panel Chairman.¹⁰³

96. *See id.* (“PLN on one hand, and [KBC] and Pertamina on the other hand, will each appoint one arbitrator . . .”).

97. *Id.* at 291 n.30. *See* discussion *infra* Part III.C (reviewing Pertamina’s contention that the application of Indonesian law includes the country’s procedural law, in addition to the uncontested application of Indonesian substantive law).

98. *Karaha Bodas III*, 190 F. Supp. 2d at 941 n.2.

99. *Id.* at 940.

100. *Id.* at 940-41.

101. *Id.* at 941.

102. *Id.* *See* Press Release 92/04, International Court of Justice, Questions of Interpretation and Application of the 1971 Montreal Convention Arising from the Aerial Incident at Lockerbie (Mar. 24, 1992) (describing Dr. El-Kosheri as an eminent Egyptian attorney and arbitrator, who is well-known in international arbitration circles for his voluminous writings on international arbitration in the developing world and his rulings in several important investment arbitrations), available at <http://www.icj-cij.org/icjwww/ipresscom/1991-1995/ipr9204.html> (last visited Feb. 21, 2005). Dr. El-Kosheri was Vice Chairman of the ICC’s International Court of Arbitration when the ICSID appointed him as the second arbitrator. *Karaha Bodas III*, 190 F. Supp. 2d at 941 n.2.

103. *Karaha Bodas III*, 190 F. Supp. 2d at 941; *see also* International Council for Commercial Arbitration, *Officers, Members and Advisory Members* (noting that the Chairman of the arbitration, Yves Derains, is a former Secretary General of the International Court of Arbitration of the International Chamber of Commerce), available at http://www.arbitration-icca.org/officers_and_members.htm (last visited Feb. 21, 2005).

B. ARBITRATION PROCEEDINGS

Pertamina and PLN jointly submitted preliminary objections to the arbitral panel's jurisdiction.¹⁰⁴ On October 4, 1999, the arbitral panel issued a Preliminary Award, upholding the formation of the panel and ruling that KBC permissibly consolidated its JOC and ESC claims into a single arbitration hearing.¹⁰⁵ In its December 18, 2000 Final Award, the Tribunal held that Pertamina and PLN breached their contracts with KBC, because they had assumed the risk that government action would nullify the project.¹⁰⁶ The panel awarded about \$261 million in damages, including \$111 million in sunk costs and \$150 million in lost profits, plus 4% post-judgment interest.¹⁰⁷

C. LEGAL PROCEEDINGS

Pertamina sought to set aside the arbitrators' decision in the Swiss Supreme Court, pursuant to the law of the place of arbitration (Switzerland) and the New York Convention. The Swiss court declined to hear Pertamina's challenge, however, because of a procedural error in paying court fees on time.¹⁰⁸ After a motion for

104. See *Karaha Bodas III*, 190 F. Supp. 2d at 941 (PLN and Pertamina argued that the arbitration panel was improperly formed because the arbitrator nomination process did not conform to energy sales contract ("ESC") nomination provisions); see also *Karaha Bodas IV*, 364 F.3d at 284 (in addition to the arbitrator selection process, Pertamina objected to the consolidation of KBC's joint operation contract ("JOC") and ESC claims).

105. *Karaha Bodas III*, 190 F. Supp. 2d at 941.

106. See *Karaha Bodas IV*, 364 F.3d at 284-85 (the arbitrators interpreted the provision that PLN and Pertamina accept the risk of losses arising from "government related event[s]" to mean that the two companies were solely liable for Indonesian government actions that thwart performance of the ESC and/or JOC).

107. *Karaha Bodas III*, 190 F. Supp. 2d at 942; see also *Karaha Bodas IV*, 364 F.3d at 285; Louis T. Wells, *Double Dipping in Arbitration Awards? An Economist Questions Damages Awarded to Karaha Bodas Company in Indonesia* 19 *ARB. INT'L* 471, 471-81 (2003) [hereinafter *Double Dipping*] (arguing that damages for expenditure and lost profits are more appropriate in normal sales transactions, while lost profit damages are less appropriate in foreign direct investment cases).

108. See *Karaha Bodas Co. v. Perusahaan Pertambangan Minyak Dan Bumi Negara*, 264 F. Supp. 2d 470, 473 (S.D. Tex. 2002) [hereinafter *Karaha Bodas V*]

reconsideration was denied, the Swiss Supreme Court ultimately denied the appeal in August 2001.¹⁰⁹ Before the Swiss court had issued its final denial, KBC initiated legal proceedings worldwide to enforce the Final Award against Pertamina under the New York Convention.¹¹⁰ In February 2001, KBC sought enforcement of the award under Article V of the New York Convention in the United States District Court for the Southern District of Texas.¹¹¹ Pertamina opposed the enforcement of the award on the grounds that 1) the arbitral proceedings violated the parties' agreement;¹¹² 2) the arbitral panel deprived Pertamina of due process in the arbitration;¹¹³ and 3) enforcement would constitute a violation of public policy.¹¹⁴ On December 4, 2001, the district court issued a judgment confirming the award for enforcement under the New York Convention.¹¹⁵ The court upheld the agreement's legality,¹¹⁶ finding both the

(indicating that the arbitration took place in Switzerland and Pertamina's appeal to the Swiss Supreme Court was therefore "contemplated" by the New York Convention).

109. *Id.*

110. *Id.* In addition to enforcement actions in the United States, KBC actively pursued enforcement of the arbitral award in Canada, Hong Kong and Singapore.

111. *Id.*

112. *Karaha Bodas III*, 190 F. Supp. 2d at 945.

113. *Id.*

114. *Id.* at 945. See New York Convention, *supra* note 2, at art. V(2)(b) (stipulating that the laws of the country whose courts adjudicate the enforcement action determine whether or not the award violates public policy). Compare Hodayoon Arfazadeh, *In the Shadow of the Unruly Horse: International Arbitration and the Public Policy Exception*, 13 AM. REV. INT'L ARB. 43, 63-64 (2002) (asserting that the public policy exception to enforcement of international arbitration awards fosters international trade and individual rights), with *Report of the United Nations Commission on International Trade Law on the Work of its Eighteenth Session*, [1985] 16 Y.B. Int'l Trade L. Comm'n 36, U.N. Doc. A/CN.9/SER.A/1985 (a UNCITRAL proposal to eliminate the public policy exception from Article V of the New York Convention), available at <http://www.uncitral.org/english/yearbooks/yb-1985-e/vol16-p3-46-e.pdf> (last visited Feb. 21, 2005).

115. See *Karaha Bodas III*, 190 F. Supp. 2d at 957 (ruling that Pertamina failed to prove any of the defenses provided under the New York Convention, and denying Pertamina's request to conduct discovery).

116. See *id.* at 945, 949 (reasoning that the New York Convention's "pro-enforcement bias" requires the court to deny enforcement only where a procedural

composition of the arbitral panel¹¹⁷ and the consolidation of the JOC and ESC arbitration proceedings proper.¹¹⁸ The court also found that Pertamina received a fundamentally fair hearing,¹¹⁹ and that neither an award of lost profits¹²⁰ nor the fact (as Pertamina asserted) that compliance with the contracts would have contravened Indonesian law¹²¹ violated public policy.¹²² Pertamina subsequently appealed the

error substantially prejudiced the petitioner, and that Pertamina had failed to prove substantial prejudice). *See also* *Karaha Bodas Co. v. Perusahaan Pertambangan Minyak Dan Bumi Negara* [2003] 4 HKC 488, 496 [hereinafter *Karaha Bodas, Hong Kong Case*] (highlighting that the Hong Kong court's public policy analysis starts with a pro-enforcement bias). The district court agreed with the United States District Court for the District of Columbia that Article V(1)(d) of the New York Convention does not authorize courts to set aside arbitral awards based on minimal procedural violation. *Karaha Bodas III*, 190 F. Supp. 2d at 945.

117. *See Karaha Bodas III*, 190 F. Supp. 2d at 949 (finding that Pertamina did not prove arbitrator bias, conflict of interest, or lack of neutrality as required to demonstrate prejudice).

118. *See id.* at 946-47 (the highly integrated contracts made consolidation appropriate, and Pertamina failed to demonstrate a prejudicial loss of contract rights as a result of the consolidation).

119. *See id.* at 949-54 (neither the arbitral panel's failure to extend discovery nor its reversal of parts of the Preliminary Award violated Pertamina's due process rights, which included receiving adequate notice, an evidentiary hearing, and an impartial decision).

120. *See id.* at 954-57 (confirming that while Pertamina failed to prove that the "abuse of rights" doctrine is part of United States jurisprudence, Pertamina also provided no evidence refuting KBC's reasonable interest in asserting lost profits rights for compensatory purposes). *Compare id.* at 957 (quoting the proposition that limiting victims' awards to actual expenditure "transform[s] [the victim] into a lender, which is commercially intolerable when the party was at full risk for the amount of the investments made on the strength of the contract"), *with Double Dipping*, *supra* note 107, at 471-81 (disputing the validity of KBC's lost profits award as a fair means of compensatory damages).

121. *See Karaha Bodas III*, 190 F. Supp. 2d at 954-57 (reasoning that the Final Award merely obligated Pertamina to uphold its contractual assumption of the risk for "government related events," which is different than explicitly mandating defiance of Indonesian law).

122. *See id.* at 954, 957 (indicating that public policy violations require proof of results contrary to "basic notions of morality and justice," and that Pertamina had failed to meet this standard).

confirmation judgment to the United States Court of Appeals for the Fifth Circuit.¹²³

Nearly three months after the district court ordered the award enforceable under the Convention, Pertamina petitioned the District Court of Central Jakarta for both injunctive relief against KBC's enforcement actions and annulment of the Swiss Award.¹²⁴ In its challenge to the Indonesian court, Pertamina argued *inter alia* that the arbitral panel exceeded its authority by failing to apply Indonesian law;¹²⁵ that the panel failed to correctly interpret Indonesian law on the issue of *force majeure*;¹²⁶ that the award violated Indonesian public policy;¹²⁷ and that KBC failed to give Pertamina proper notice of the appointment of arbitrators.¹²⁸ In reply, KBC argued, *inter alia*, that the petition for annulment had no legal basis since the grounds for annulment under Indonesian law were not met; the annulment application was premature since the award had not been registered as required by Indonesian law; and Pertamina's claim was obscure and ambiguous because it was unclear whether Pertamina was requesting annulment of the JOC and ESC, or the Swiss Award itself.¹²⁹ On April 1, 2002 the Indonesian court issued

123. *Karaha Bodas V*, F. Supp. 2d at 473.

124. See *Perusahaan Pertambangan Minyak Dan Bumi Negara v. Karaha Bodas Co.*, Case No. 86/PDT.G/2002/PN.JKT.PST, Preliminary Award, April 2, 2002, Claimant's Arguments, ¶ 68 [hereinafter *Indonesian Case, Final Award*] (requesting that the Indonesian court fine KBC if it takes steps to enforce an arbitration award that Pertamina believes the court will annul once it has a chance to examine the case), available at <http://www.lfip.org/lawe506/documents/session14/e506kbjakartadctprelim.doc> (last visited Feb. 21, 2005) (on file with *American University International Law Review*).

125. *Id.* ¶¶ 11-14. *Contra Karaha Bodas IV*, 364 F.3d at 292 (holding that intermittent contractual references to Indonesian procedural rules cannot rebut the strong presumption that the procedural rules of the country hosting the arbitration proceedings control).

126. *Indonesian Case, Final Award*, Case No. 86/PDT.G/2002/PN.JKT.PST, ¶¶ 15-22.

127. *Id.* ¶¶ 22-28.

128. *Id.* ¶¶ 32-33.

129. See *Indonesian Case, Judgment*, 86/PDT.G/2002/PN.JKT.PST, at 12-20 (noting the factors Indonesian courts must consider before annulling an arbitral award).

an injunction in Pertamina's favor, barring KBC from attempting to enforce the arbitration award and imposing a \$500,000 per day penalty for any KBC non-compliance (the "Indonesian Injunction").¹³⁰

The Indonesian court issued the injunction shortly after the Texas district court had issued a temporary restraining order ("TRO") requiring Pertamina to withdraw its Indonesian court petition against KBC.¹³¹ On April 2, 2002, the Texas district court found Pertamina in contempt for failing to comply with the TRO,¹³² and again ordered Pertamina to withdraw its injunctive relief request from the Indonesian court.¹³³ Finally, on April 26, 2002, the district court granted KBC's Motion for Preliminary Injunction, and ordered Pertamina to refrain from taking action to prosecute or enforce the Indonesian Injunction.¹³⁴ The Preliminary Injunction, which superseded the previous TRO and contempt order, also forbade Pertamina from collecting money for KBC non-compliance with the Indonesian court's ruling.¹³⁵

In August 2002, the District Court of Central Jakarta rendered a final judgment after considering Pertamina's preliminary injunction arguments, KBC's arguments in response to the interim judgment, and the parties' additional arguments on the merits of the case.¹³⁶

130. *Id.* at 12.

131. *Karaha Bodas V*, 264 F. Supp. 2d at 473.

132. *Id.* at 474.

133. *Id.* at 474 n.3.

134. *Id.* at 483.

135. *Id.* Pertamina appealed the contempt order to the United States Court of Appeals for the Fifth Circuit. *Karaha Bodas I*, 335 F. 3d at 374. The appellate court ruled in Pertamina's favor, finding that international comity would be harmed by the district court's interference with the legal proceedings of a foreign sovereign, and that this concern outweighed the need to "prevent vexatious and oppressive foreign litigation" in this case. *Id.* at 366-74. See generally *5th Circuit Reverses, Vacates Preliminary Injunction in Pertamina*, MEALEY'S INT'L ARB. REP., June 2003, at 6, 6-10 (reviewing the main issues surrounding the appellate court's reversal, including the district court's authority to issue an injunction and whether Pertamina's appeal was moot).

136. See *Indonesian Case, Judgment*, at 1-21 (recounting the parties' contentions since Pertamina filed for an injunction and annulment in March 2002,

The court set aside the arbitral panel's awards,¹³⁷ reasoning that 1) the arbitral tribunal had exceeded its authority in failing to apply Indonesian law;¹³⁸ 2) the award violated Indonesian *ordre public*;¹³⁹ 3) the arbitral tribunal erred in its construction of the *force majeure* clause under Indonesian laws;¹⁴⁰ 4) the arbitral panel should not have consolidated the contract disputes;¹⁴¹ and 5) Indonesian law permits annulment.¹⁴² In so ruling, the court confirmed its provisional judgment of April 2, 2002, and concluded that the Final Award was null and void.¹⁴³ Ultimately, the Indonesian court's ruling merely delayed KBC's enforcement efforts.¹⁴⁴ In Hong Kong, Singapore, Canada, Texas, and New York, enforcing courts allowed KBC's execution on Pertamina's assets to proceed.¹⁴⁵

On March 23, 2004, the United States Court of Appeals for the Fifth Circuit affirmed the Texas district court's summary judgment decision enforcing the award.¹⁴⁶ Pertamina argued that the New York Convention accorded the Indonesian courts "primary jurisdiction"

and reviewing the parties' factual claims about the merits of the case).

137. *See id.* at 29-30 (declaring the holding immediately enforceable and ordering KBC to pay Pertamina's court fees).

138. *Id.* at 26.

139. *Id.* at 26-27.

140. *Id.* at 27-28. *See generally Crisis Chronology, supra* note 87 (recounting the circumstances contributing to Indonesia's economic climate in 1997).

141. *See Indonesian Case, Judgment* at 28 (arguing that ICSID should have appointed different arbitrators for the contract disputes because Pertamina and PLN had different interests).

142. *Id.*

143. *Id.* at 29.

144. *See, e.g., supra* notes 110-123 and accompanying text (recounting the United States federal court proceedings dedicated to resolving the litigants' dispute over the Indonesian court's injunction order).

145. *See, e.g., Karaha Bodas, Hong Kong Case*, 4 HKC at 497-504 (rejecting Pertamina's contention that the Indonesian court's annulment precludes enforcement because Swiss procedural law, not Indonesian law, applies).

146. *Karaha Bodas IV*, 364 F.3d at 310; *see also* Chuck Ragan, *Karaha Bodas Co LLC v. Perusahaan Pertambangan Minyak Dan Gas Bumi Negara Et Al*, 4 INT'L ARB. L. REV. N-37, N-43 (2004).

over the KBC arbitration,¹⁴⁷ empowering them to annul the award and precluding U.S. court enforcement of the award once so annulled.¹⁴⁸ According to Article V(1)(e) of the Convention, a court has primary jurisdiction when the court is located either at the place of arbitration, or in the country whose procedural law governs the arbitration proceedings.¹⁴⁹ Pertamina argued that Indonesian procedural law applied to its arbitration with KBC.¹⁵⁰ The Fifth Circuit rejected this position, relying upon the strong presumption that the law applicable to any arbitral procedure is the *lex arbitri*—the law of the arbitral situs, which in the KBC case was Switzerland.¹⁵¹ Occasional contractual references to certain Indonesian civil procedure rules were insufficient to rebut this presumption.¹⁵² The appellate court held that Switzerland had primary jurisdiction and the Indonesian courts only secondary jurisdiction over the proceedings.¹⁵³ The Fifth Circuit also found that Pertamina was judicially estopped from claiming Indonesian law was the applicable procedural law, because Pertamina had earlier relied on the procedural law of Switzerland, not least in bringing its first

147. *Id.* at 289-90. See *Arbitration – Enforcement of Award. Court Enforces New York Convention Award that Was Annulled by a Foreign Court of Secondary Jurisdiction*, 3 INT’L LITIG. & ARB. NEWSL., July 2004 (reviewing the appellate court’s opinion and noting how Pertamina’s contention that the Indonesian court had primary jurisdiction was a central focus in the case).

148. *Karaha Bodas IV*, 364 F.3d at 289-90.

149. New York Convention, *supra* note 2, at art. V; see *Karaha Bodas IV*, 364 F.3d at 289.

150. *Karaha Bodas IV*, 364 F.3d at 289-90.

151. *Id.* at 291-92.

152. See *id.* at 291 n.30-31 (reviewing several of the agreements’ references to Indonesian civil procedure rules, including Article 13.2 of the JOC and Section 8.2 of the ESC).

153. See *id.* at 294 (emphasizing that Switzerland is the only country with primary jurisdiction). Under Article V(1)(e) of the New York Convention it is theoretically possible that two countries may legally assert primary jurisdiction. *Id.* See generally New York Convention, *supra* note 2, at art. V (indicating that either a competent authority where the arbitrators rendered an award “or” a competent authority exercising jurisdiction under the laws governing the arbitration may set an award aside).

challenge of the award there.¹⁵⁴ Thus ended Pertamina's battle to block confirmation of the award in U.S. courts.¹⁵⁵

III. FLAWS IN THE INDONESIAN "ANNULMENT"

Pertamina's quest for annulment in Jakarta was not aimed at blocking enforcement in Indonesia—although this would certainly be one effect.¹⁵⁶ Rather, the hope was to delay or stop enforcement in other jurisdictions by operation of the New York Convention.¹⁵⁷ Pertamina's strategy was based on the fact that foreign awards can be refused by courts in signatory States under Article V of the Convention where an award has been set aside "by a competent authority of the country in which, or under the law of which, the award was made."¹⁵⁸ Pertamina argued that courts in the United States and elsewhere should not enforce the Swiss Award because the Jakarta district court had annulled it, and that this court was the competent authority of the country under the law of which the award was made.¹⁵⁹ Ultimately, this argument was roundly defeated, because of the serious flaws in the Jakarta Court's decision. First,

154. See *Karaha Bodas IV*, 364 F.3d at 293-94 (concluding that Pertamina's conduct meets the two qualifications of judicial estoppel—party positions that clearly contradict its prior positions and the court's acceptance of the past, inconsistent party position). The Fifth Circuit also affirmed the thrust of the district court's holdings, including finding that the arbitration panel properly consolidated the ESC and JOC disputes and that Pertamina received a fair hearing. *Id.* at 296-304.

155. In fact, the battle to enforce the award against Pertamina's assets continued for some time in the Federal District Court for the Southern District of New York, largely based upon the company's arguments that the Government of Indonesia actually owned the proceeds from Pertamina's production sharing agreements. *Karaha Bodas Co. v. Perusahaan Pertambangan Minyak Dan Bumi Negara*, 313 F.3d 70 (2d Cir. 2002).

156. See *Karaha Bodas V*, 264 F. Supp. 2d at 474 n.3 (explaining that the Indonesian Injunction issued by the Jakarta court purports to prohibit KBC from taking actions to enforce the Swiss Award in any jurisdiction).

157. See New York Convention, *supra* note 2, at art. V (detailing grounds for supporting a refusal to recognize and enforce an award).

158. *Id.* at art. V(1)(e).

159. See discussion *infra* Part III.C (describing the extensive legal proceedings and Pertamina's various legal assertions).

Indonesia was not a “primary jurisdiction” authorized under the Convention to vacate the award.¹⁶⁰ Second, the “annulment” departed sharply from the provisions of Law No. 30.¹⁶¹

A. INDONESIA WAS NOT A “COMPETENT AUTHORITY” TO VACATE THE SWISS ARBITRAL AWARD

It seems eminently clear that the Indonesian court was not the proper location in which to lodge an annulment of the Swiss award.¹⁶² The Indonesian court made two initial errors with regard to the applicability and interpretation of the New York Convention. First, while the Jakarta district court could have applied the Convention to an *enforcement* proceeding in Indonesia,¹⁶³ the Convention has no place in an action to vacate an award.¹⁶⁴ Second, even assuming the Convention governs annulment proceedings, the court erred in concluding that the Indonesian court is a “competent authority” to vacate the Swiss Award under the Convention.¹⁶⁵

There are only two articles in the Convention that refer to annulment of an arbitral award—Articles V(1)(e) and VI.¹⁶⁶ The text of Article V(1)(e) refers to annulment by a “competent authority of the country in which, or the country under the law of which, the award was made;”¹⁶⁷ and Article VI provides:

160. See discussion *infra* Part IV.A (explaining why Indonesia is not a “competent authority” to vacate the Swiss arbitral award).

161. See discussion *infra* Part IV.B (detailing reasons why the “annulment” departed from Indonesia’s Law No. 30).

162. See discussion *infra* Part IV.A (discussing the New York Convention articles applicable to annulment actions and Indonesia’s improper “annulment” of the Swiss arbitral award).

163. See New York Convention, *supra* note 2, at art. I(1) (the Convention applies to awards made in a territory other than in the territory where the enforcement of the award is sought).

164. *Karaha Bodas V*, 264 F. Supp. 2d at 481. Under the New York Convention, a country’s courts may only annul an award if it was issued there, or if it was issued under the country’s arbitral law. *Id.* at 482.

165. See *id.* at 482 (confirming that both the physical and legal situs of the award was Switzerland, not Indonesia).

166. New York Convention, *supra* note 2, arts. V(1)(e), VI.

167. *Id.* at art. V(1)(e).

[I]f an application for the setting aside or suspension of the award has been made to a competent authority referred to in Article V(1)(e), the authority before which the award is sought to be relied upon may, if it considers it proper, adjourn the decision on the enforcement of the award.¹⁶⁸

It is clear that Articles V and VI distinguish between two sets of courts: 1) the country of origin's courts, which have "primary" jurisdiction; and 2) the enforcement courts, where the respondent's assets are located, which have "secondary" jurisdiction.¹⁶⁹ Thus, according to Articles V and VI, the same award may either be a domestic award in the country in which, or under the laws of which it was made, or a foreign award in any other country.¹⁷⁰ Although the Convention recognizes these "two faces" of an arbitral award, its provisions distinguish between foreign and domestic awards, applying only to the former.¹⁷¹ In fact, "the New York Convention does not apply to actions seeking to set aside an award; it is limited to actions seeking to enforce a foreign award."¹⁷² As such, in the case between Pertamina and KBC, Pertamina's application for annulment with the Indonesian courts should not have been considered to fall under the New York Convention at all.¹⁷³ The Swiss Award was

168. *Id.* at art. VI.

169. *See, e.g.,* V.S. Deshpande, *Jurisdiction Over 'Foreign' and 'Domestic' Awards in the New York Convention, 1958*, 7 *ARB. INT'L* 123, 126 (1991) (distinguishing between the powers of these two sets of courts). The courts of the country of origin can set the award aside, while enforcement courts may only refuse to enforce the award in their jurisdiction. *Id.*

170. *See id.* at 127 (cautioning that some awards issued within the state of enforcement may not be considered domestic under local law, and might consequently be enforced as foreign awards).

171. *Id.* at 126-27.

172. *See* Albert Jan van den Berg, *Court Decisions on the New York Convention, Consolidated Commentary, Vols. XIII-XIV*, 14 *Y.B. COM. ARB.* 595 (1989) (providing instances in which courts held that the Convention only applies in enforcement actions).

173. *See id.* (explaining that under the New York Convention the only courts competent to set aside an award are those of the country in which the award was made, or those of the country under the law of which the award was made).

certainly a foreign award, but the Convention simply has nothing directly to say about annulment applications.¹⁷⁴

The Jakarta court's second mistake—accepting jurisdiction to vacate the Swiss Award—arose out of a misapprehension of the distinction between the two types of court authority referred to in Articles V and VI of the Convention.¹⁷⁵ Article V(1)(e) suggests that the court of origin has the power to vacate the award under its domestic arbitration laws, a competence again recognized in Article VI.¹⁷⁶ The enforcement court, meanwhile, cannot set aside the award; it can only *refuse enforcement* if the party meets the requirements set forth in Article V.¹⁷⁷ In fact, “the courts have affirmed the principle that, according to the Convention, the courts of the country in which, or under the law of which, the award was made, are exclusively competent to decide on an action for setting aside the award.”¹⁷⁸ Thus, regarding the power to set aside an award, it is clear that there are two possible “competent authorities” within the meaning of Article V(1)(e).¹⁷⁹ The first is a court in the territory where the arbitrators rendered the award.¹⁸⁰ In the case at hand, it was the Swiss Supreme Court that had authority to vacate the award, since it was

174. See Christopher R. Drahozal, *Enforcing Vacated International Arbitration Awards: An Economic Approach*, 11 AM. REV. INT'L ARB. 451, 455 (2000).

175. See Deshpande, *supra* note 169, at 126.

176. *Id.*

177. See *id.* (contrasting the nature of a foreign award to that of a domestic award).

178. See van den Berg, *supra* note 172, at 595 (suggesting that once a competent court sets an award aside, this will preclude enforcement in other states). *But compare* Baker Marine (Nig.) Ltd. v. Chevron (Nig.) Ltd., 191 F.3d 194 (2d Cir. 1999) (vacatur at place of arbitration does not necessarily preclude enforcement elsewhere); see also Hamid Gharavi, *The International Effectiveness of the Annulment of an Arbitral Award* 106 (2002) (same); Albert Jan van den Berg, *Enforcement of Annulled Awards?*, 9(2) ICC Int'l Ct. of Arb. Bull., November 1998 at 15 (same).

179. See Deshpande, *supra* note 169, at 126 (confirming that an award may be set aside by the courts of the country in which, or under the laws of which, the arbitral award was made).

180. New York Convention, *supra* note 2, at art. V(1)(e).

rendered in Switzerland.¹⁸¹ In fact, it is well settled, in both theory and practice:

The competent authority [referred to in each Article] for entertaining the action of setting aside the award is virtually always the court of the country in which the award was made. The phrase 'or under the law of which' the award was made refers to the theoretical case that on the basis of an agreement of the parties the award is governed by an arbitration law which is different from the arbitration law of the country in which the award was made.¹⁸²

Nevertheless, the meaning of the language "or under the laws of which"¹⁸³ contained in Article V(1)(e) is ambiguous. The case law on the subject however, is now clear—the only place that the parties may lodge an application for annulment, apart from the courts in the territory in which the award was rendered, is the country whose *procedural* law applied to the arbitration proceedings.¹⁸⁴ Not only does United States case law support this view; various courts around the world have reached the same conclusion.¹⁸⁵

In *International Standard Electric Corp. v. Bidas Sociedad Anonima Petrolera Industrial y Commercial*,¹⁸⁶ the court directly confronted the language of Article V(1)(e)¹⁸⁷ The case involved a contract between an Argentinean (Bidas) and an American company ("ISEC"), which provided for arbitration in Mexico under the local Rules of Conciliation and Arbitration.¹⁸⁸ In addition, the parties resolved that New York state law would govern the agreement.¹⁸⁹ The parties arbitrated their dispute and the arbitration panel ultimately issued a final arbitral award in Mexico City against

181. *Karaha Bodas V*, 264 F. Supp. 2d at 473.

182. *International Standard Electric Corp. v. Bidas Sociedad Anonima Petrolera, Industrial y Comercial*, 745 F. Supp. 172, 177 (S.D.N.Y. 1990).

183. *Id.* at 91.

184. *Van den Berg*, *supra* note 172, at 595.

185. *See* discussion *infra* Part IV.A.

186. 745 F. Supp. 172 (S.D.N.Y. 1990).

187. *Id.* at 178.

188. *Id.* at 173.

189. *Id.* at 174.

ISEC.¹⁹⁰ Subsequently, ISEC petitioned the United States District Court to vacate the award, arguing that under the New York Convention, courts at both the arbitral situs and the country whose *substantive* law applied had jurisdiction to annul the award.¹⁹¹ The court referred to the “complex thicket of the procedural law of arbitration obtaining in the numerous and diverse jurisdictions of the dozens of nations in attendance at the time the Convention was being debated,” and held that the phrase “under the laws of which” in Article V(1)(e) referred to the *procedural* and not the substantive law of the arbitration.¹⁹² The court thus concluded that the Mexican courts were the only competent authorities to entertain an application for annulment.¹⁹³

The Sixth Circuit Court of Appeals has also held that the only courts that are competent to hear a motion to vacate a foreign arbitral award are those in the country in which the arbitration took place, or the courts of any country whose procedural law is specifically invoked in the contract.¹⁹⁴ This Court stated:

[r]esorting to the courts of the nation supplying the substantive law for the dispute does nothing to enhance the underlying principles of international arbitration because, under the terms of the New York Convention itself,

190. *Id.* at 175.

191. *Id.* at 175-76.

192. *International Standard Electric Corp. v. Bidas Sociedad Anonima Petrolera Industrial y Commericia*, 745 F. Supp. 172, 177 (S.D.N.Y. 1990).

193. *See id.* at 178 (declaring that because Mexico was both the location of the arbitration and country whose procedural law governed, only Mexican courts had jurisdiction to vacate the arbitral award); *see also* *Coutinho Caro & Co. U.S.A., Inc. v. Marcus Trading, Inc.*, Nos. 3:95CV2362 AWT, 3:96CV2218 AWT, 3:96CV2219 AWT, 2000 WL 435566, at *6-7 (D. Conn 2000) (finding the *International Standard Electric Corp.* analysis persuasive and concluding that only the courts of China had jurisdiction to vacate a CIETAC award rendered in China, despite the fact that United States law governed the merits of the dispute).

194. *See M&C Corp. v. Erwin Behr GMBH & Co.*, 87 F.3d 844, 848 (6th Cir. 1996) (following the decision in *International Standard Electric Corp.*). The arbitration was held in England, while Michigan law governed the contract disputes. *Id.* at 847-48.

judicial review of such an award is extremely limited and extends only to procedural aspects of the determination.¹⁹⁵

Courts in other countries have reached the same conclusion as those in the U.S. For example, the Supreme Court of India held that an award rendered in London, but subject to the procedural and substantive laws of India, was domestic, and thus that the Indian Arbitration Act of 1940 was the proper authority, not the Convention.¹⁹⁶ The Indian Supreme Court stated that only an Indian court had jurisdiction "to consider the validity or enforceability of the arbitral award at issue in this case."¹⁹⁷

Similarly, the Brussels Court of Appeals, in *S.A. Mines, Minerais et Metaux v. Mechema, Ltd.*,¹⁹⁸ rejected a petition to vacate an arbitral award rendered in Paris, France.¹⁹⁹ The arbitration agreement between the parties stated that the procedural rules for arbitration would be those set forth in the parties' contract.²⁰⁰ The arbitral panel held that because Paris was the arbitration venue, French arbitral law governed all matters not provided for in the contract's procedural rules.²⁰¹ In dismissing the application for annulment, the Brussels court noted the arbitrators' presumption that where the parties' agreement was silent, the law of the arbitral situs would govern the arbitral process.²⁰²

Likewise, the French Court of Cassation denied an application for vacatur when it determined that French procedural law did not apply

195. *Id.* at 848.

196. *Oil and National Gas Commission v. Western Company of North America, (India)* 13 Y.B. COM. ARB. 473, 475-76 (1988).

197. *Id.* at 482.

198. 7 Y.B. COM. ARB. 316 (1982).

199. *See id.* at 317 (denying S.A. Mines' application to set aside the award based on the reasoning that such an action may only be instituted in the country in which the award has been made).

200. *Id.* at 316.

201. *See id.* at 316-17 (in the absence of an agreement between the parties, it is generally accepted that the law of the country in which the arbitration occurs governs the arbitral procedure).

202. *Id.* at 317.

to an arbitration conducted in Brussels, Belgium.²⁰³ The French Supreme Court noted that the application for setting aside the award is only proper if it is a national award and made according to French procedural law.²⁰⁴ The court's decision rested on the fact that parties could not have intended French procedural law to apply to the arbitration because neither the parties nor the arbitral panel declared French procedural law to be applicable.²⁰⁵

With respect to a party choosing a procedural law that is different than that of the territory in which the arbitration proceedings occur, commentators have suggested that while the parties could theoretically choose a procedural law different from that of the arbitral situs,²⁰⁶ the parties must be clear in making such a selection.²⁰⁷ The assumption against a procedural law other than local law arises out of the rarity of such occurrences and the potential conflicts and complexities that could arise in such cases—particularly where the local law includes mandatory elements.²⁰⁸ In *Karaha Bodas*, Pertamina argued that certain waivers of Indonesian Civil Code provisions contained within the arbitration clause

203. See *Maatschappij voor Industriële Research en Ontwikkeling B.V. v. Henri Lièvreumont and M. Cominassi*, (Fr), May 25, 1983, 12 Y.B. COM. ARB. 480, 482 (1987) (dismissing an application to set aside an arbitration award, due to the inapplicability of French procedural law to the arbitration).

204. *Id.* at 481.

205. See *id.* (discussing the French Court of Appeal's inquiry into the will of the parties regarding the procedures and law applicable to their arbitration).

206. See, e.g., *REDFERN & HUNTER*, *supra* note 1, at 84 (noting that while choosing a different procedural law is theoretically possible, it is also potentially problematic).

207. See, e.g., *Karaha Bodas V*, 264 F. Supp. 2d at 481-82.

208. See *REDFERN & HUNTER*, *supra* note 1, at 84 (noting that such a choice would complicate arbitration because the arbitral tribunal would have to consider two sets of procedural laws—those chosen by the parties, and those of the territory in which the arbitration occurs that are mandatory in that territory). Furthermore, the courts in which recourse is sought might be reluctant to rule based on the procedural law of another nation. *Id.* See also, e.g., *S.A. Mines*, 7 Y.B. COM. ARB. 316 (1982), at 317 (quoting the arbitrators' observation that it is a generally accepted principle that the arbitral procedures of the country in which the arbitration takes place apply, absent an express agreement to the contrary by the parties).

constituted an implied election of Indonesian procedural law.²⁰⁹ It is clear, however, that despite the fact that the JOC and ESC each called for the application of Indonesian substantive law, Swiss law was the chosen *lex arbitri*.²¹⁰ This is not only because the award was rendered in Switzerland, but also because the parties did not make clear that Indonesian *arbitral* law was to apply.²¹¹ Evidence of the arbitral proceedings further supports this conclusion; Pertamina not only argued that Swiss law applied to the proceedings, but also repeatedly referred to Swiss law in presenting its arguments to the arbitral panel.²¹² Pertamina did not argue that Indonesian law applied to the proceedings either during the arbitration or in its appeal to the Swiss courts.²¹³ Furthermore, in Pertamina's attempt to persuade the Texas District Court to stay the enforcement proceeding pending the Swiss appeal, Pertamina contended that Swiss arbitration law applied and that the Swiss court had jurisdiction to hear the challenge.²¹⁴

The Indonesian court, therefore, improperly intervened in the case by applying the Convention to the annulment application filed by Pertamina. Furthermore, the Indonesian court wrongly decided that it was a "competent authority" to vacate the award.

B. THE INDONESIAN "ANNULMENT" VIOLATED LAW NO. 30

The Indonesian decision was also in error because the court premised its conclusions on a strained interpretation of Indonesian law. First, as explained above, Law No. 30 provides only three grounds for vacatur, none of which were satisfied in this instance.²¹⁵ Second, contrary to the Jakarta court's assertion and as already explained, the New York Convention does not supply "additional

209. *Karaha Bodas V*, 264 F. Supp. 2d at 481-82.

210. *Id.* at 482.

211. *Id.*

212. *Id.* n.13. Pertamina had also argued that under Swiss law the arbitral panel lacked jurisdiction, and that the arbitral panel did not have the power to consolidate the proceedings under Swiss law. *Id.*

213. *Id.*

214. *Karaha Bodas V*, 264 F. Supp. 2d at 482.

215. *See Indonesian Case, Judgment*, 86/PDT.G/2002/PN.JKT.PST, at 22-23 (listing the Court's reasons for annulling the final Swiss award).

grounds” upon which an award may be annulled; rather, it only provides bases for enforcement refusal.²¹⁶

Law No. 30 provides only three possible grounds for vacating an award in Indonesia.²¹⁷ Courts may vacate an award: (1) if there is proof that a party submitted false documents; (2) if the court finds that key documents were withheld from the other party to the arbitration; or (3) if one of the parties committed a fraudulent act during the arbitral proceedings.²¹⁸ KBC argued before the Indonesian court that Pertamina, in its application for annulment to the Indonesian Court, presented absolutely no evidence satisfying any of the three elements necessary to petition for annulment.²¹⁹ Indeed, Pertamina made no attempt to invoke any of the explicit grounds for vacatur contained in Law No. 30.²²⁰ The court stepped around this argument by relying upon the official Elucidation to Article 70 of Law No. 30, which states that the “grounds on which to base a petition for annulment of an arbitral award are, among others, as stipulated in Article 70.”²²¹ The Jakarta court held that “use of the phrase ‘among others’ instead of ‘namely’ implies that the law allows courts to apply legal grounds other than those specified in Article 70.”²²² The court then noted that because Indonesia ratified the Convention in 1981, Indonesian courts must directly apply its provisions. According to the Court, Pertamina was not restricted in its petition for annulment to Article 70 of Law No. 30, but could rely directly on Article V of the New York Convention itself.²²³ In so doing, the court confused the law applicable to the annulment of an

216. New York Convention, *supra* note 2, at art. VI; see *Karaha Bodas V*, 264 F. Supp. 2d at 477.

217. Law No. 30, *supra* note 56, art. 70.

218. *Id.*

219. *Indonesian Case, Judgment*, 86/PDT.G/2002/PN.JKT.PST, at 21-22.

220. See *id.* (holding that the legal basis for the claim can be found in the New York Convention and Law No. 30).

221. *Id.* at 23.

222. *Id.*

223. See *id.* at 27 (noting that the award should not be enforced because it contravened Article V(1)(b) of the New York Convention).

award under domestic law with that applicable to an enforcement action under the New York Convention.

A case where a U.S. court applied domestic law in an action to vacate an international award sheds light on the subject of the interaction between the Convention and domestic law applicable to annulment proceedings.²²⁴ In examining a request for vacatur of an award, the Second Circuit in *Yusuf Ahmed Alghanim & Sons W.L.L. v. Toys "R" Us, Inc.*²²⁵ read Article V(1)(e) to allow the application of domestic, U.S.-law grounds for vacatur to a non-domestic award rendered in the United States.²²⁶ The court stated that "there appears to be no dispute among [scholars and other signatories to the Convention] that an action to set aside an international arbitral award, as contemplated by Article V(1)(e), is controlled by the domestic law of the rendering state."²²⁷ The court further noted that "the award can be set aside in the country of origin²²⁸ on all grounds contained in the arbitration law of that country, including public policy of that country."²²⁹ The court concluded that "an action to set aside an award can be brought *only* under the domestic law of the arbitral forum, and can never be made under the Convention."²³⁰

As discussed above, none of the express grounds for relief under Indonesian arbitral law were satisfied, or even pleaded, in the *Karaha Bodas* case. Faced with this reality, the court construed the Convention's Article V grounds for refusal of enforcement as

224. *Yusuf Ahmed Alghanim & Sons W.L.L. v. Toys "R" Us, Inc.*, 126 F.3d 15, 20 (2d Cir. 1997).

225. 126 F.3d 15 (2d Cir. 1997)

226. *Id.* at 21. The Convention was applicable because the award was found to be "non-domestic," in that the dispute "involved two non-domestic parties and one U.S. corporation, and principally involved conduct and contract performance in the Middle East." *Id.* at 19.

227. *Id.* at 21.

228. *Id.* at 21 n.3.

229. *See id.* (noting that the grounds for setting aside the award under the Convention may include "all kinds of particularities of the arbitration law of the country of origin").

230. *Toys "R" Us, Inc.*, 126 F.3d at 21, 22, *citing* Case No. 2 ND 502180 (Feb. 1, 1980) (Aus), *excerpted in* 7 Y.B. COMM. ARB. 312, 313 (1982).

implied grounds for relief under Indonesian law. However, Pertamina's argument and the court's analysis fail to consider that even if the Convention could supplement domestic arbitration law, nothing would be added in terms of grounds for vacatur: no grounds for setting aside exist in the Convention.²³¹ The *Toys "R" Us* court recognized that Article V(1)(e) allowed the application of domestic law to vacate the award; and the court in fact used domestic law to consider the application for annulment. The Indonesian court, on the other hand, used domestic law to allow for the application of the New York Convention to consider the application for annulment of the Swiss Award. But while the New York Convention instructs domestic courts to annul an award based on its domestic law, it stops there.²³² The court's determination that the Convention applied to an action for annulment in Indonesia expanded an otherwise narrowly-phrased national arbitration law to provide for vacatur on far wider grounds.

The court's use of public policy as a ground for vacatur is one example of this expansion. Specifically, the Indonesian court considered Article V(2)(b) of the Convention,²³³ which states that courts may deny the enforcement of an arbitral award if enforcement would violate public policy of the place of enforcement.²³⁴ In addition to Article V(2)(b) of the Convention, the court referred to Indonesian Supreme Court Regulation No. 1 of 1999, which provides that "the enforcement of foreign arbitral awards in Indonesia imitatively applies to awards which do not violate public order in terms of all underlying principles of the legal system and society in

231. See *id.* at 22-23 (finding that "while it would have provided greater reliability to the enforcement of awards under the Convention had the available grounds been defined in some way, such action would have constituted meddling with national procedure for handling domestic awards, a subject beyond the competence of the Conference"), quoted in Leonard V. Quigley, *Accession by the United States to the United Nations Convention on the Recognition and Enforcement of Foreign Arbitral Awards*, 70 YALE L.J. 1049, 1070 (1961).

232. See W. Laurence Craig, *Some Trends and Developments in the Law and Practice of International Commercial Arbitration*, 30 TEX INT'L L.J. 1, 11.

233. *Indonesian Case, Judgment*, 86/PDT.G/2002/PN.JKT.PST at 27.

234. New York Convention, *supra* note 2, at art. V(2)(b).

Indonesia.”²³⁵ Thus, the court, in using the grounds for refusal of enforcement in place of those for annulment under Indonesian law, considered the issue of “whether recognition or enforcement would be in violation of public order.”²³⁶ The court ultimately concluded that “the [Swiss Award should] be denied of [sic] recognition and enforcement, since it is in violation of public order and the underlying principles of the people of Indonesia.”²³⁷

Even if Indonesian law allows for the possibility of extra-statutory grounds for vacatur,²³⁸ public policy does not appear to be such a ground.²³⁹ Indonesian law refers to public policy only with respect to *enforcement* actions, not *annulment* actions.²⁴⁰ In other words, the denial of recognition or enforcement based on public policy grounds may have been acceptable only if Pertamina or KBC had petitioned for recognition or enforcement of the Swiss Award before the court. It is clear, both from the Indonesian court’s reference to the Convention and its continuous use of the terms “enforcement and recognition” in its opinion, that the court confused the proceeding before it as one of enforcement or recognition, as opposed to what it really was—an annulment proceeding under domestic law.²⁴¹

235. *Indonesian Case, Judgment*, 86/PDT.G/2002/PN.JKT.PST, at 26-27.

236. *Id.* at 26.

237. *See id.* at 27 (specifying that the court’s decision that *ordre public* was violated rested on its conclusion that since the Presidential Decrees were “aimed to revive and overcome the country’s financial condition, which was in the midst of an economic and monetary crisis [and] such condition would be aggravated if the geothermal project were to be continued, and it would further exacerbate the Indonesian economy”).

238. Such is the case, for example, under U.S. law, where nearly all jurisdictions have accepted that awards may be set aside for “manifest disregard of law.” *See* Noah Rubins, *Manifest Disregard of Law and Vacatur of Arbitral Awards in the United States*, 12 AM. REV. INT’L ARB. 363 (2001) (explaining that U.S. courts apply additional non-statutory grounds for vacating of arbitration awards, the most recognized being “manifest disregard of law”).

239. *Toys “R” Us*, 126 F.3d at 23.

240. 1990 REGULATION, *supra* note 43 (noting that the Central Jakarta District Court is empowered to respond to matters dealing with the enforcement of foreign arbitral awards); *see also* Law No. 30, *supra* note 56, art. 66.

241. *Indonesian Case, Judgment*, 86/PDT.G/2002/PN.JKT.PST, at 28-29.

In drafting national arbitration laws, many nations have closely followed the provisions of the UNCITRAL Model Law on International Commercial Arbitration, in particular concerning the proper grounds for vacatur. As explained above, Indonesia chose a different route,²⁴² adopting significantly narrower grounds than those found in the UNCITRAL Model Law. The Indonesian legislature most likely took this approach to setting aside awards in Law No. 30 in an effort to compete with other jurisdictions as a center for international arbitration, since including only three limited bases for annulment (largely related to fraud on the arbitrators) could be seen to increase predictability and finality in international commercial disputes.²⁴³

Ironically, the *Karaha Bodas* decision suggests that Indonesia may have adopted an arbitration law with grounds for annulment (and enforcement, for that matter) that are *too* narrow to be of practical use. By allowing judicial review of awards only in rare circumstances of fraud, the 1999 Law effectively closes off a “safety valve” carefully preserved in the Model Law.²⁴⁴

In a country with a more developed judicial system, such tightly-circumscribed scope of review might well prove attractive to

242. See Drahozal, *supra* note 174, at 456 (noting that many national arbitration laws follow the UNCITRAL Model Law, which includes the New York grounds for non-enforcement of awards). The Model Law tracks New York Convention Article V’s list of grounds that permit courts to refuse enforcement of awards, with the exception of Article V(1)(e). *Id.* By doing so, in the countries that have adopted the Model Law, grounds for annulment are nearly the same as grounds for refusal of enforcement under the Convention. *Id.*

243. See *id.* at 458 (noting that countries compete for international arbitration business, thus implementing arbitration proceedings that may seem favourable to parties). Compare Samuel A. Hobold, *Opting Out of the U.S. Legal System: The Case for International Arbitration*, 10 INT’L L. PRACTICUM 43, 44 (1997) (stating that “[m]ost parties who elect to arbitrate rather than litigate do so because they want finality.”), and William H. Knull, III & Noah D. Rubins, *Betting the Farm on International Arbitration: Is it Time to Offer an Appeal Option?*, 11 AM. REV. INT’L ARB. 531, 536 (2000) (asserting that “for most parties to large-scale international arbitration, finality is at best a secondary advantage”).

244. See *supra* notes 160-161 and accompanying text (explaining the Model Law’s provisions on enforcement and annulment of awards).

contracting parties who value the finality of awards.²⁴⁵ But in a country such as Indonesia, historically hostile to international arbitration and with a judiciary notoriously vulnerable to outside influence, eliminating legitimate and precisely-tailored grounds for annulment or non-recognition may tempt judges to take the law into their own hands, as they did in *Karaha Bodas*.²⁴⁶ Adopting the Model Law provisions on recognition, enforcement, and annulment, which would include acceptance of public policy and excess of powers defenses, would at least reassure Indonesian courts that they can adhere closely to the statutory text without threatening fundamental national interests or enforcing awards rendered outside the scope of the parties' submission.²⁴⁷ It is unlikely that even the Model Law would have saved the *Karaha Bodas* award from an Indonesian vacatur, given the political sensitivity of the matter and the courts' determination to find for Pertamina at all costs. But the Jakarta court's departure from its legislative foundation may have set a precedent in Indonesia that undermines all the ostensible advances of the 1999 Law.

IV. RECENT INDONESIAN CASES

Since the Jakarta District Court heard the *Karaha Bodas* case, anecdotal evidence suggests that some progress is being made to standardize the review and enforcement of foreign arbitration awards. Research conducted at the Central Jakarta District Court in January 2002 indicates that for the period between September 2000 and December 2001, four foreign awards were registered, and all were subsequently approved for enforcement. To be sure, these

245. See generally Knull and Rubins, *supra* note 243, at 536-543 (discussing the importance and attraction of finality in international arbitration). It should not be assumed that all parties value finality above all else—studies indicate that many businesspeople fear arbitration precisely because of the lack of recourse against erroneous awards. *Id.*

246. See *supra* notes 87-132 and accompanying text (analyzing the Indonesian Court's decision to annul the Swiss award in the *Karaha Bodas* case).

247. See Knull & Rubins, *supra* note 243, at 544 (outlining the provisions on recognition, enforcement, and annulment of the Model law and the new York Convention and noting that most modern statutes correspond to these limited grounds for setting aside international awards).

arbitration awards appear to be relatively minor in size and of little political importance (unlike *Himpurna*²⁴⁸ and *Karaha Bodas*). These cases can serve as evidence that the Indonesian enforcement system is not wholly beyond repair.

In *PT. Wahana Adhireksa Wiraswasta v. Cocoa Merchants' Association of America, Inc.*, the Central District Court of Jakarta considered an award rendered on October 26, 1999, registered with the Court on July 18, 2001, and approved for enforcement in September 2001.²⁴⁹ The District issued a warning letter on September 5, 2000 to the respondent, instructing it to pay the award.

The London Court of International Arbitration ("LCIA") award in *Oceanis Shipping Limited v. Mrs. R. Adji A. Suryo Di Puro* was issued on November 4, 1998, and registered at the District Court on February 15, 2001. The court issued approval for enforcement a mere two months later.²⁵⁰ According to the District Court record, the claimant later enforced the award swiftly and successfully by obtaining a writ of confiscation and selling seized property by auction in August 2001.

An award of the Korean Commercial Arbitration Board was at issue in *Son, Han-Pil (representative of Dong San Machine Co.) v. Herman Tanuraharja*. Here, the claimant registered the award at the District Court in February 2001, and obtained approval for enforcement in April of the same year.²⁵¹ By September, the claimant had received a writ of confiscation against the Indonesian respondent.

Finally, in *Balmac International Inc. v. Firma Sinar Nusantara*, the claimant arrived in Jakarta with a November 2000 award issued by the Cocoa Merchants Association of America. The award was registered at the District Court on April 11, 2001. The Court was

248. *Himpurna California Energy Ltd. v. PT (Persero) Perusahaan Listrik Negara*, UNCITRAL Award of May 4, 1999, 14 MEALEY'S INT'L ARB. REP., A1 (Dec. 1999) (awarding Himpuna \$391,711,652).

249. Decree No. 143/2000/Eks., September 4, 2001.

250. Decree No. 35/2001/Eks, April 16, 2001.

251. Decree No. 025/2001/Eks, April 18, 2001.

even speedier in this case, confirming the award in May 2002.²⁵² On June 25, 2001, the District Court issued a confiscation writ for the award.²⁵³

It is encouraging that the District Court of Central Jakarta has been willing to approve all of the awards registered for enforcement and also to support their implementation. This may perhaps indicate a slowly changing attitude by the court, where traditionally it has tended to reject enforcement on the grounds that enforcement of foreign arbitral awards would disturb public order. It remains to be seen whether this pattern will continue where the respondent is an Indonesian State-owned company, or where the amount in dispute is as large as it was in *Karaha Bodas*.

CONCLUSION

Ultimately, the Jakarta District Court's alleged annulment of the *Karaha Bodas* award will do little service to Pertamina or to Indonesia as a whole. Pertamina, as an oil and gas company of global scale, can hardly stash its assets away within Indonesia's borders; its futile and ill-advised end-run around the New York Convention has only serviced to tarnish the company's reputation. As for Indonesia, there can be no doubt that it has squandered an opportunity to wipe the slate clean with Law No. 30. Although progress now seems underway to confirm and enforce arbitral awards according to the terms of the arbitration act, it may take a very long time to repair the reputational damage done to Indonesia's judiciary.

Adopting the UNCITRAL Model Law is by no means the only way to achieve a predictable arbitration regime that allows businesspeople to control political risk and get on with driving economic growth. But Law No. 30 suffers from serious weaknesses, and should be amended accordingly. Even if Law No. 30 were perfect, however, its implementation must always rely on a well-working, independent judiciary. This Indonesia still does not have. The *Himpurna* case showed that Jakarta is not an appropriate venue for international arbitration; *Karaha Bodas* proved that moving the

252. Decree No. 44/2001/Eks and No. 45/2001/Eks, May 1, 2001.

253. *Id.* at 1-2.

proceedings elsewhere may not help matters. There are those who believe that where there is oil and gas, Western investors and traders will come, regardless of the political risks. This is difficult to believe. At least for now, foreign business has choices as to where to place its capital. Unless Indonesia reforms its courts and its arbitration law, it may find itself losing out to the competition.

The Jakarta court's decision was arbitrary and illegitimate, and undermined stability and predictability by bending the law to fit Pertamina's interests.²⁵⁴ In future, Indonesian courts would be well-advised against giving any credibility or weight to the annulment decision in enforcement and vacatur cases under the Convention and Law No. 30. Even this is merely a superficial solution to a deeper problem, however. Even if courts disregard the *Karaha Bodas* annulment decision, a long-term solution is required to re-establish trust in Jakarta as an arbitral situs. Inadequacies in both the law and those that implement it must be addressed before the international business community will view Indonesia as a country committed to the impartial and fair resolution of international commercial disputes.²⁵⁵ The development and stability of the Indonesian economy may hang in the balance.²⁵⁶

254. See *supra* discussion Part IV A-B (providing the flaws of the Indonesian decision to annul the award in *Karaha Bodas* case).

255. Mulyana & Schaefer, *Critical Assessment*, *supra* note 33, at 66.

256. *Id.* at 49.