



## Arbitration as an Alternative for Resolving Investment Disputes in the North Sumatra Industrial Region: A Study of Business Actors and the Regional Government

### *Arbitrase sebagai Alternatif Penyelesaian Sengketa Investasi di Kawasan Industri Sumatera Utara: Studi terhadap Pelaku Usaha dan Pemerintah Daerah*

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##### **Abstract**

Increased investment in the North Sumatra industrial region brings both the potential for economic growth and the risk of disputes between business actors and the regional government. Dispute resolution through litigation is often considered inefficient due to the lengthy process, high costs, and limited technical understanding of the investment sector. This study aims to assess the effectiveness of arbitration as an alternative for resolving investment disputes in the region. Using a qualitative-descriptive approach, data was collected through in-depth interviews with business actors, regional government officials, and legal practitioners. The results indicate that although arbitration is recognized as a faster and more flexible mechanism, its utilization remains limited due to minimal publicity, the limited capacity of local arbitration institutions, and the lack of integration of arbitration clauses into regional investment contracts. This study recommends the development of regional policies that encourage the use of arbitration, increasing the capacity of regional legal resources, and strengthening cooperation between the government and business actors in drafting investment contracts that promote fair and efficient dispute resolution.

##### **Kata Kunci:**

Arbitrase;  
Penyelesaian  
Sengketa;  
Investasi;  
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Sumatera Utara

##### **Abstrak**

Peningkatan investasi di kawasan industri Sumatera Utara membawa potensi pertumbuhan ekonomi sekaligus risiko terjadinya sengketa antara pelaku usaha dan pemerintah daerah. Penyelesaian sengketa melalui jalur litigasi sering kali dianggap tidak efisien karena prosesnya yang panjang, biaya yang tinggi, serta keterbatasan pemahaman teknis terhadap sektor investasi. Penelitian ini bertujuan untuk menilai efektivitas arbitrase sebagai alternatif penyelesaian sengketa investasi di wilayah tersebut. Dengan menggunakan pendekatan kualitatif-deskriptif, data dikumpulkan melalui wawancara mendalam dengan pelaku usaha, pejabat pemerintah daerah, dan praktisi hukum. Hasil penelitian menunjukkan bahwa meskipun arbitrase diakui sebagai mekanisme yang lebih cepat dan fleksibel, pemanfaatannya masih terbatas akibat minimnya sosialisasi, keterbatasan kapasitas lembaga arbitrase di daerah, serta belum terintegrasi klausul arbitrase dalam

kontrak investasi daerah. Penelitian ini merekomendasikan pengembangan kebijakan daerah yang mendorong penggunaan arbitrase, peningkatan kapasitas sumber daya hukum daerah, serta penguatan kerja sama antara pemerintah dan pelaku usaha dalam penyusunan kontrak investasi yang mendorong penyelesaian sengketa secara adil dan efisien

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## INTRODUCTION

### Background of the Problem

North Sumatra is one of Indonesia's strategic provinces with significant potential for industrial and investment development. The presence of industrial areas such as the Medan Industrial Estate (KIM) and the Sei Mangkei Special Economic Zone (KEK) strengthens North Sumatra's position as a prime destination for national and international investment, particularly in the manufacturing, agro-industry, and energy sectors. Investment in this region is expected to drive regional economic growth, create jobs, and improve overall regional competitiveness (Malecki, 2017; Virjan et al., 2023; Kouskoura et al., 2024). However, with the increasing intensity of investment activity in the region, various potential disputes have emerged between businesses and local governments.

These disputes can stem from licensing issues, overlapping regulations, inconsistencies in the implementation of agreements, or differing interpretations of investment incentives (Drabek & Mavroidis, 2013; Roberts, 2013; Tienhaara, 2018). To date, such disputes have often been resolved through litigation, which is procedurally cumbersome, slow, and unresponsive to the dynamics of the business world. Lengthy and open court processes also often raise concerns among investors about legal uncertainty and the protection of their business interests.

In this context, arbitration is seen as a more efficient, expeditious, and flexible alternative dispute resolution (Nugraha & Riswadi, 2024; Saputra, 2024; Astri et al., 2025). The arbitration mechanism allows parties to resolve disputes privately by selecting an arbitrator who understands the technical characteristics of investment issues (Blythe, 2013). Indonesia itself has regulated arbitration through Law Number 30 of 1999 concerning Arbitration and Alternative Dispute Resolution (Fitrianingrum et al., 2016), but its application in the regional investment sector, particularly in North Sumatra, remains limited.

Stakeholders' lack of understanding of the arbitration mechanism, the limited capacity of local arbitration institutions, and the lack of integration of arbitration clauses into investment agreements are key challenges. This highlights the gap between the potential of arbitration as a modern dispute resolution instrument and the still-conventional practices on the ground.

North Sumatra Province is a strategic region on the national economic development map, particularly in the industrial and investment sectors. With abundant natural resources, continuously developing infrastructure, and a geographic location that supports access to domestic and international trade, this region is a magnet for investors, both domestic and international. The development of industrial estates, large-scale

plantations, mining, and renewable energy sectors demonstrates the dynamic acceleration of investment in various regencies and cities in North Sumatra. However, the rapid flow of investment is also overshadowed by the potential for various forms of disputes between investors and communities, local governments, or business partners. These disputes not only reflect differing interests but also serve as indicators of structural challenges in investment governance and law enforcement in the region. Some potential disputes include those concerning environmental permits and the sustainability of industrial projects, land acquisition and compensation conflicts, problems in the implementation of cooperation contracts between investors and local governments, and uncertainty in the implementation of fiscal policies and the provision of investment incentives.

This phenomenon demonstrates the need for an in-depth study of the legal, institutional, and social aspects surrounding the investment process in North Sumatra. Identifying and analyzing potential investment disputes is not only crucial as part of efforts to mitigate legal risks but also as a foundation for formulating fair, transparent, and sustainable policies. Therefore, discussions of these potential disputes need to be linked to the local context and national legal framework, particularly to promote effective dispute resolution through alternative approaches such as arbitration and mediation.

Therefore, this study aims to examine the potential and challenges of implementing arbitration as an alternative solution for investment disputes between businesses and local governments in strategic industrial areas in North Sumatra, specifically the Sei Mangkei Special Economic Zone (KIM) and Special Economic Zone (KEK). Through a qualitative approach, this study will explore the perceptions of businesses, local government officials, and legal practitioners regarding the effectiveness of arbitration in achieving legal certainty and a conducive investment climate at the regional level.

## Problem Identification

1. Ineffectiveness of Conventional Dispute Resolution: To what extent does the conventional litigation process fail to address the specific needs of the investment sector in North Sumatra, particularly concerning efficiency, cost, and technical expertise?
2. Underutilization of Arbitration: Despite its legal recognition and potential benefits, why does arbitration remain a largely untapped mechanism for resolving investment disputes between business actors and the regional government in North Sumatra?
3. Institutional and Regulatory Gaps: How do the absence of robust local arbitration infrastructure and the lack of supportive regional policies contribute to the perpetuation of legal uncertainty and hinder the creation of a favorable investment climate in the region?

## Research Question

Having meticulously delineated the core issues through a comprehensive problem identification process, this study is now poised to formulate its guiding inquiry. The critical examination of the existing gaps and contradictions naturally leads to the crystallization of the following primary research question, which will serve as the definitive lens for the entire investigation:

1. What are the primary factors contributing to the underutilization of arbitration as a dispute resolution mechanism for investment-related conflicts in North Sumatra's industrial regions?

2. How do the perceptions and legal literacy of business actors and regional government officials in North Sumatra shape their preferences for either litigation or arbitration in resolving investment disputes?
3. What strategic interventions, in terms of institutional development and regulatory reform, are necessary to enhance the effectiveness and adoption of arbitration for resolving investment disputes in North Sumatra?

### **Research Objective and Benefits**

Consequently, to provide a structured and actionable pathway for inquiry directly aligned with this central question, the present research aims to undertake a systematic investigation with the following interconnected objectives: to critically analyze the underlying mechanisms contributing to the identified problem, to empirically evaluate the proposed variables within their specific context, and to synthesize evidence-based conclusions that not only address the research question but also offer pragmatic insights for practical application and theoretical advancement.

Objectives:

1. To critically assess the effectiveness of the existing dispute resolution mechanisms, particularly litigation, in handling investment disputes within the industrial areas of North Sumatra.
2. To identify and analyze the structural, cultural, and institutional barriers that impede the widespread adoption of arbitration for resolving investment disputes in the region.
3. To formulate a set of policy recommendations and strategic guidelines for the regional government and stakeholders to foster a more conducive environment for the use of arbitration in investment disputes.

Benefits:

This research will provide valuable insights for the regional government of North Sumatra, enabling them to develop a more effective and investor-friendly legal framework for dispute resolution. For business actors and potential investors, this study will offer a clearer understanding of the legal landscape and the potential avenues for mitigating risks associated with disputes. Furthermore, the findings will contribute to the academic discourse on alternative dispute resolution in the context of regional development and investment in Indonesia.

### **THEORITICAL AND CONCEPTUAL FRAMEWORK**

The increasing complexity of investment activities in developing regions necessitates a re-evaluation of traditional dispute resolution mechanisms. The conventional litigation process, often characterized by its rigidity, protracted timelines, and public nature, is frequently ill-suited to the dynamic and commercially sensitive nature of investment disputes (Astri et al., 2025). This has led to a growing recognition of Alternative Dispute Resolution (ADR) mechanisms, with arbitration emerging as a particularly viable alternative. Arbitration offers a private, flexible, and efficient forum for resolving disputes, allowing parties to select arbitrators with specialized expertise in the subject matter of the dispute (Blythe, 2013). The principle of party autonomy, a cornerstone of arbitration, empowers the disputing parties to tailor the dispute resolution process to

their specific needs, thereby fostering a more collaborative and less adversarial environment (Sidik, 2024).

In the context of investment, the legal framework governing arbitration plays a pivotal role in shaping its effectiveness. In Indonesia, Law No. 30 of 1999 concerning Arbitration and Alternative Dispute Resolution provides the legal foundation for the use of arbitration in resolving commercial disputes (Fitrianingrum et al., 2016). This law not only recognizes the validity of arbitration agreements but also underscores the final and binding nature of arbitral awards, thereby ensuring their enforceability. However, the mere existence of a national legal framework is often insufficient to guarantee the effective implementation of arbitration at the regional level. The successful integration of arbitration into the local legal culture requires a supportive ecosystem, including the presence of credible arbitration institutions, a sufficient pool of qualified arbitrators, and a judiciary that respects and enforces arbitral awards (Universitas Medan Area, 2023).

The concept of legal culture, which encompasses the attitudes, beliefs, and values of a society towards law and legal institutions, is crucial for understanding the adoption of arbitration. In many jurisdictions, a deeply entrenched litigious culture can pose a significant barrier to the acceptance of ADR mechanisms (Saputra, 2024). Overcoming this requires a concerted effort to raise awareness and build capacity among legal practitioners, business actors, and government officials. The role of the judiciary is particularly critical in this regard. A judiciary that is supportive of arbitration and consistently enforces arbitral awards can play a vital role in building trust and confidence in the arbitral process (Sinaga, 2023).

Furthermore, the theory of institutionalism provides a useful lens for analyzing the challenges and opportunities for promoting arbitration in North Sumatra. From an institutional perspective, the absence of a well-functioning local arbitration center can be seen as a major impediment to the growth of arbitration (Losari & Ewing-Chow, 2015). The reliance on national or international arbitration institutions, while a viable option for large-scale disputes, can be prohibitively expensive and inconvenient for smaller, regional disputes. Therefore, the development of local arbitration infrastructure is a critical step towards making arbitration more accessible and affordable for a wider range of business actors.

Finally, the concept of good governance is central to creating a favorable investment climate. A key aspect of good governance is the provision of a fair, transparent, and efficient system for resolving disputes. By embracing arbitration, regional governments can signal their commitment to upholding the rule of law and protecting the rights of investors (Ajuwan, 2024). This, in turn, can enhance the region's attractiveness as an investment destination and contribute to its long-term economic development. The integration of arbitration clauses into regional investment contracts and the development of policies that encourage the use of ADR are concrete steps that regional governments can take to promote good governance and foster a more predictable and stable legal environment for investment (Gulzar, 2024).

## METHODOLOGY

This research uses a qualitative approach with descriptive-analytical methods, aiming to gain an in-depth understanding of the dynamics of investment dispute resolution between business actors and local governments in the industrial areas of North Sumatra. This approach was chosen because it is appropriate for contextually exploring the social realities, perceptions, and practices related to the application of arbitration as an alternative dispute resolution at the regional level.

The research locations focused on two strategic industrial areas: the Medan Industrial Estate (KIM) located in Medan City and Deli Serdang Regency, and the Sei Mangkei Special Economic Zone (KEK) in Simalungun Regency. These two areas were chosen because they are investment centers that involve intensive interaction between the local government and the private sector, and serve as important indicators of the investment climate in North Sumatra in general.

Data collection was conducted through a combination of primary and secondary sources. Primary data were obtained through in-depth interviews with various key informants, including business actors operating within the industrial areas, local government officials involved in investment management and supervision, and legal practitioners with experience in dispute resolution through arbitration or other alternatives. Interviews were conducted semi-structured to allow for further exploration of information emerging throughout the process.

In addition, secondary data was obtained from various official documents, such as relevant laws and regulations, investment contracts, annual reports from regional investment agencies, and scientific literature on arbitration and investment dispute resolution. These documents were used to strengthen and enrich the interview findings and provide a relevant legal and theoretical framework. All collected data was analyzed qualitatively using thematic analysis (Castleberry & Nolen, 2018). This process began with data reduction to select information relevant to the research focus, then categorized the findings based on key themes such as perceptions of arbitration, institutional barriers, contractual practices, and opportunities for regulatory strengthening. Next, interpretation was conducted to draw meaning and relationships between themes, and draw conclusions that comprehensively answer the research questions.

To maintain the validity and reliability of the data, triangulation of sources and methods was conducted by comparing interview results, legal documents, and limited observations of field dynamics (Natow, 2020). This technique was used to ensure consistency of findings and avoid bias in drawing conclusions (Drucker et al., 2016). This narrative approach is expected to fully describe the empirical conditions and normative structures that influence the use of arbitration in resolving investment disputes in the industrial region of North Sumatra.

## RESULT AND DISCUSSION

### Potential Arbitration Disputes in North Sumatra's Industrial Areas

#### *Disputes Related to Environmental Permits and the Sustainability of Industrial Projects*

In North Sumatra, many industrial projects are located adjacent to forest areas, watersheds, and settlements of indigenous or local communities. The issuance of environmental permits is often a point of contention between investors, civil society, and local governments. For example, in the construction of palm oil mills or smelters in upstream areas, objections often arise from residents or NGOs due to concerns about environmental pollution and ecosystem damage. These conflicts usually stem from minimal public consultation processes or non-transparent environmental impact analysis (AMDAL) documents (Talitha, 2025). These disputes can escalate if local governments are perceived to be siding with investors and ignoring community voices. The legitimacy of environmental permits, public participation, socio-ecological impacts, and the role of environmental oversight agencies such as the Environment Agency (DLH) and the Ministry of Environment and Forestry (KLHK) are also important factors.

### *Disputes Related to Land Acquisition and Compensation*

Land acquisition for the development of industrial estates, ports, or investment-supporting infrastructure (such as coal-fired power plants or industrial toll roads) frequently leads to conflict in North Sumatra. These disputes often arise from differing perceptions of land ownership status, compensation rates that do not meet residents' expectations, or the involvement of intermediaries (land brokers) who disadvantage one party. In some cases, indigenous communities or local farmers reject land release because they feel they have not been given fair negotiation opportunities. These disputes become complex if the government issues HGU or HGB on land that is still disputed by customary law (Aprido & Fatimah, 2023). This includes land rights, compensation negotiations, conflicts between customary and formal law, and the involvement of the National Land Agency (BPN), local governments, and investors.

### *Disputes Related to Cooperation Contracts between Investors and Local Governments*

Industrial areas in North Sumatra often involve cooperation schemes between private investors and local governments (public-private partnerships) in the form of utilization of regional assets, the establishment of jointly owned regionally-owned enterprises (BUMD), or the management of economic zones. Potential disputes arise when there is an imbalance in responsibilities and profit sharing, or when a contractual clause is violated by one of the parties (Artono, 2018). For example, an investor delays the construction of a promised facility, even though the government has facilitated licensing. Or, conversely, a local government unilaterally changes spatial planning policies, hindering project operations. Enforcement of contractual clauses, dispute resolution mechanisms (including arbitration clauses), and transparency of public-private agreements are crucial.

### *Disputes Related to Fiscal Policy and Investment Incentives*

Investors entering the industrial areas of North Sumatra are usually promised various fiscal incentives, such as exemptions from local taxes and levies, or eased imports of heavy equipment and raw materials. However, sudden changes in regulations or fiscal policies at the regional or central levels often trigger tensions. For example, if a local government revokes tax incentives due to fiscal pressure or a Supreme Audit Agency (BPK) audit, investors may feel unilaterally disadvantaged (Atmaja et al., 2023). This can also occur if there are differences in interpretation between investors and tax authorities regarding the applicable incentives. Legal certainty regarding incentives, harmonization of central and regional fiscal policies, and clarity of initial contracts or supporting investment regulations are crucial. The North Sumatra industrial region, as a developing and investment-friendly region, holds significant potential for investment disputes if governance is not implemented transparently and accountably. The four types of disputes mentioned above demonstrate the critical role of arbitration institutions, mediation mechanisms, and adherence to contractual and environmental law principles in maintaining a healthy and sustainable investment climate.

## **Understanding and Perceptions of Arbitration**

Interviews indicate that most business owners in the Medan Industrial Estate (KIM) and the Sei Mangkei Special Economic Zone (SEZ) have a basic understanding of arbitration as a form of alternative dispute resolution (ADR). They acknowledge that arbitration offers advantages in terms of speed, confidentiality, and efficiency compared to court

litigation. However, this understanding remains largely normative and has not yet been translated into concrete contractual practices.

Interviews with business owners in the Medan Industrial Estate and the Sei Mangkei Special Economic Zone indicate that their understanding of arbitration is conceptual but has not yet reached the practical aspects. A legal manager at an agrichemical company in the Sei Mangkei Special Economic Zone stated: "We know arbitration is faster and more neutral, but so far, when problems arise, they are usually resolved through informal meetings or directly in court, because we don't know where to go for arbitration." Meanwhile, an official from the Simalungun Regency Investment Office stated: "Arbitration seems like a major or inter-state matter. At the regional level, we still believe the best resolution is through communication or regular courts." This statement indicates a gap in perception between national legal norms that accommodate arbitration and the reality of understanding at the local level. Among local governments, understanding of arbitration mechanisms remains very limited. Some officials believe that disputes with investors must be resolved through formal legal channels, as they involve state administrative and financial responsibilities. This demonstrates a gap in understanding between the business world and the bureaucracy regarding the role of arbitration as a constructive solution.

### Practices of Drafting Arbitration Clauses in Investment Contracts

Research found that most investment cooperation agreements in the KIM and SEZ Sei Mangkei do not explicitly include arbitration clauses as a dispute resolution mechanism. In many cases, contracts only specify resolution through deliberation or through the local district court. This demonstrates a lack of attention to contractual design that supports alternative and efficient dispute resolution. Of the ten investment agreement documents analyzed, only two included arbitration clauses, and even then, they referred to arbitration institutions outside North Sumatra, such as BANI Jakarta. The remainder contained only general provisions regarding settlement through deliberation or district court.

**Table 1.** Distribution of Dispute Resolution Clauses in Investment Contracts (n=10)

Types of Settlement	Contract Amount	Percentage
Consultation + Court	6	60%
Consultation Only	2	20%
Arbitration (BANI Jakarta)	2	20%
Local Arbitration	0	0%

Source: Document analysis results, 2025

The lack of arbitration clauses is due to a lack of legal assistance in contract drafting, as well as the absence of regional regulations requiring or encouraging the use of ADR within an investment framework (Gulzar, 2024). The primary reason for the absence of arbitration clauses is related to the lack of professional legal assistance during the contract drafting stage, as well as the absence of regional policies encouraging the standardization of ADR-based investment agreements. As a result, when disputes arise, parties are often confused about determining a neutral and expeditious resolution forum.

### *Institutional and Regulatory Barriers*

From an institutional perspective, the lack of an arbitration center or independent mediation forum at the provincial level poses a serious obstacle to the implementation of arbitration in the regions. Businesses wishing to use arbitration generally have to refer to Jakarta-based institutions such as BANI (Indonesian National Arbitration Board).

This raises efficiency issues, particularly in terms of costs and logistics. Institutionally, North Sumatra does not yet have a credible regional arbitration forum that is widely recognized by investors. In fact, Law Number 30 of 1999 concerning Arbitration and Alternative Dispute Resolution, Article 1, point (1), clearly states that arbitration can be conducted by a private institution based on the agreement of the parties (Larosa et al., 2023).

However, in practice, reliance on national arbitration institutions in Jakarta discourages businesses in North Sumatra from choosing this mechanism, due to the cost and inefficiency of distance. This is reinforced by the statement of a legal consultant who stated: "There is not a single arbitration institution operating in Medan at full capacity. Our clients ultimately prefer the courts, even though they know the process is lengthy." Regional regulations have not been progressive enough in adopting arbitration-based dispute resolution principles. Regional investment work plans and policies still focus on facilitating investment entry, but do not adequately regulate effective and preventative dispute resolution mechanisms. Some regional regulations do not even address technical contractual issues, including dispute resolution clauses.

Business actors expressed their hope that local governments would be more proactive in creating an investor-friendly investment legal ecosystem, including providing a means for expeditious and impartial dispute resolution. They also hope that investment contract drafting will be facilitated by professional legal personnel who understand arbitration principles and dispute resolution clauses. Business actors expressed the need for regional investment contract guidelines that standardly include the option of arbitration as a dispute resolution forum. This aligns with the OECD Investment Policy Review's recommendations, which encourage regions to develop local legal instruments that support business security.

Several informants from government agencies acknowledged the need for training on arbitration mechanisms and drafting dispute resolution clauses. An official from the North Sumatra Industry Agency said: "We need training on ADR, because so far we have focused more on investment promotion and have not addressed the technical aspects of contracts." Meanwhile, local governments are emerging with a renewed awareness of the importance of creating regulations that adapt to the needs of the business world. Several informants from government agencies expressed the need to develop regional investment contract guidelines that accommodate the use of arbitration, as well as training relevant officials on ADR mechanisms.

### **Arbitration as a Solution and Challenges**

The findings above indicate that although arbitration is recognized as an ideal dispute resolution mechanism in the investment context, its use in the industrial region of North Sumatra still faces structural and cultural barriers. Theoretically, arbitration offers advantages in terms of efficiency, neutrality, and flexibility. However, its practical application requires institutional infrastructure, competent human resources, and regulatory support for a non-litigative approach. In a regional context, strengthening local arbitration institutions and reforming regional investment regulations are crucial steps. Local governments can act as facilitators by establishing dispute resolution units under the Investment Office or by collaborating with national arbitration institutions to establish regional branches (Losari & Ewing-Chow, 2015). This way, arbitration can be more firmly institutionalized in local investment practices.

Legally, Law No. 30 of 1999 provides strong legitimacy for dispute resolution through arbitration (Al et al., 2024). Article 3 states that a court has no authority to examine disputes that have been agreed to be resolved through arbitration. This demonstrates

that the existence of an arbitration clause in a contract constitutes a binding and exclusive legal basis. However, the absence of regional technical regulations governing a standard model for arbitration clauses and the absence of a local arbitration forum hamper the optimal implementation of this norm. This demonstrates that the implementation of arbitration as a dispute resolution instrument at the regional level still requires harmonization between central policy and local readiness.

### **Potential for Arbitration Application in North Sumatra's Strategic Industrial Zones**

The Medan Industrial Zone (KIM) and the Sei Mangkei Special Economic Zone (KEK) are two important nodes in the growing national industrial network in North Sumatra. Supported by infrastructure such as ports, railways, and their proximity to the Kuala Tanjung international port, these two areas are designed to attract substantial investment in manufacturing, palm oil processing, logistics, and basic chemicals. In this context, the legal relationship between business actors (both national and foreign) and the regional government and regional-owned enterprise (BUMD) managing the area is becoming increasingly complex and prone to conflict.

The Sei Mangkei Special Economic Zone (SEZ), which focuses on the downstream palm oil and basic chemical industries, is a national strategic project with a partnership scheme between the private sector and state-owned enterprises (BUMN)/PTPN III as the area manager (Sinurat et al., 2019). During its implementation, there were delays in the construction of supporting infrastructure, such as connectivity to Kuala Tanjung Port and logistics facilities, resulting in losses for investors due to the inability to operate according to planned production schedules.

One of the chemical companies serving as tenants in the area expressed objections because the local government was deemed to have failed to fulfill its initial commitments regarding infrastructure support and fiscal incentives (Davidson, 2021). However, this dispute did not escalate to arbitration because an arbitration clause was not included in the initial agreement. The final settlement was achieved through trilateral negotiations between the investor, the SEZ manager, and the provincial government. This case demonstrates the importance of arbitration clauses in contracts between investors and special area authorities such as SEZs. Without a standardized dispute resolution mechanism, negotiation efforts are ineffective if not supported by a strong and binding legal basis. One instrument with significant potential for effectively anticipating and resolving such conflicts is arbitration, a final and binding out-of-court dispute resolution mechanism (Simanjuntak & Hoessein, 2024). Arbitration has several advantages relevant to the needs of businesses in industrial areas, including:

- Speed and time efficiency,
- Confidentiality of disputes and contracts,
- Flexibility of the process, and
- The ability to appoint arbitrators with expertise in the relevant technical field or industry sector.

Amidst high expectations for legal certainty and investment protection, arbitration can be a mechanism that strengthens investor confidence and reduces reliance on conventional litigation processes, which are often lengthy and open to political or bureaucratic interference.

### *Challenges in Implementing Arbitration in Disputes between Business Actors and Regional Governments*

Despite its significant potential, the application of arbitration in the context of investment disputes in areas such as the KIM and the Sei Mangkei Special Economic Zone (KEK), is not without a number of challenges, including:

#### 1. Lack of Arbitration Clauses in Regional Government Contracts

Many cooperation contracts between business actors and regional governments or regionally-owned enterprises (BUMD) do not explicitly include an arbitration clause as a dispute resolution forum. This may be due to limited understanding or a lack of attention to legal mitigation aspects in the formulation of the agreement. Furthermore, there is a tendency for regional governments to prefer district courts because they are considered a "safer" forum from an institutional perspective.

#### 2. Low Arbitration Literacy Among Government Officials

Local governments, as one of the parties involved in investment projects, often do not fully understand the principles, benefits, and procedures of arbitration. Lack of training or exposure to arbitration practices makes government officials reluctant to incorporate this forum in agreement documents, despite the potential for efficiency and faster resolution.

#### 3. Unpreparedness of Local Arbitration Infrastructure

Although institutions such as BANI have branches in Medan, not all parties—especially local governments and local businesses—are accustomed to using local arbitration forums (Sidik, 2024). The preference for international arbitration can also create new dilemmas, particularly regarding costs and cross-jurisdictional procedures, which not all industry players in the KIM and Sei Mangkei Special Economic Zones (KEK) are prepared to navigate.

### *Challenges of Public Openness and Accountability*

As public institutions, local governments often face demands for transparency and accountability, which can conflict with the confidentiality of the arbitration process. This can raise concerns, both within the bureaucracy and within civil society, regarding public oversight of dispute resolution processes.

### *Implications for the Investment Climate and Regional Legal Governance*

The absence of an operational and reliable arbitration mechanism can prolong the investment dispute resolution process, create legal uncertainty, and ultimately damage the region's image as an investment destination (Ajuwan, 2024). Conversely, integrating arbitration into regional investment policies and cooperation agreements between local governments and investors can strengthen the competitiveness of strategic industrial areas such as the Medan Industrial Estate (KIM) and the Sei Mangkei Special Economic Zone (SEZ). This aligns with the principle of ease of doing business and Indonesia's commitment to investment protection through bilateral and multilateral agreements. Therefore, there is a need for:

- Strengthening the legal capacity of local governments,
- Standardization of arbitration clauses in investment contracts,

- Cooperation between local governments, BANI (National Acquisition Agency), and legal education institutions, and
- Promotion of non-litigation dispute resolution in regional investment policy documents.

One issue that has arisen in the Medan Industrial Estate (KIM) relates to disputes between business actors and the area management regarding the determination of utility tariffs, such as clean water supply, electricity, and other supporting infrastructure services. In recent years, several industry players have complained about the lack of transparency in the tariff-setting mechanism and the quality of services provided by the area management. For example, several companies experienced operational disruptions due to unstable water supplies, yet were still charged high tariffs.

In this case, the potential dispute could have been resolved through arbitration if the initial contract between the company and the area manager included a non-litigative dispute resolution clause. However, in practice, business actors tend to opt for informal negotiations or resort to district courts, which prolongs settlement times and creates legal uncertainty. This demonstrates the importance of formulating robust commercial contracts that incorporate arbitration mechanisms as part of industrial risk management (Rahman & Kumaraswamy, 2002). Utility disputes like this one contain contractual and governance dimensions of industrial services, which are highly suitable for resolution through arbitration due to their technical, repetitive, and long-term nature. By addressing these challenges, implementing arbitration in North Sumatra's strategic industrial area becomes not merely an option but a necessity to ensure the sustainability of sound, fair, and efficient investment.

### **Arbitration as a Win-Win Solution in Business Disputes: Strengthening the Role of Judicial Institutions and Academics**

On Wednesday, July 12, 2023, the Faculty of Law, University of Medan Area (FH UMA), held a legal seminar entitled "Execution of Arbitration Awards by Judicial Institutions in the Settlement of Business Disputes" at Campus I, Medan Estate (Universitas Medan Area, 2023). This event provided an important forum for academics, legal practitioners, and business people to discuss the dynamics and challenges of implementing arbitration awards in Indonesia. The seminar was also attended by judges from the Medan High Court, advocates, officials from the Medan Chamber of Commerce and Industry (KADIN), lecturers from various universities, and students.

Previously, on Wednesday, July 5, 2023, the Deputy Chief Justice of the Medan High Court, Dr. Herdi Agusten, SH, M.Hum., received a meeting from representatives of the Indonesian National Arbitration Board (BANI) Medan (Sinaga, 2023). The meeting took place in the office of the Deputy Chief Justice of the Medan High Court in a warm and collaborative atmosphere. This meeting was held as part of a series of events commemorating the 46th anniversary of BANI's founding. It also served as a crucial opportunity for consultation and coordination regarding the seminar "Execution of Arbitration Awards in North Sumatra," scheduled to be held at Campus I of the University of Medan Area (UMA). The meeting demonstrated synergy between the judiciary and arbitration institutions in an effort to strengthen the understanding and implementation of alternative dispute resolution, particularly arbitration, in North Sumatra.

Keynote speakers included the Chief Justice of the Medan High Court, Dr. Panusunan Harahap, SH, MH; the Chairman of the Indonesian National Association of Indonesian Legal Entities (BANI), Prof. Dr. Tan Kamello, SH, MS, FCBARB; the Chairman of the

Medan Chamber of Commerce and Industry (KADIN), Arman Chandra, SE, M.Pd; and Dr. Taufik Siregar, SH, M.Hum, a lecturer at the Faculty of Law, University of Muhammadiyah Malang (UMA). The seminar was further enriched by the signing of a memorandum of understanding (MoU) between UMA and the Medan High Court, the Indonesian National Accreditation Agency (BANI) Medan, and the Medan Chamber of Commerce and Industry (KADIN). This was followed by the signing of MoA by the Dean of the Faculty of Law, along with the leaders of these institutions. This signing demonstrated a shared commitment to strengthening synergy between academia, the judiciary, and the business world in resolving business disputes through arbitration (Universitas Medan Area, 2023).

In his remarks, UMA Rector, Prof. Dr. Dadan Ramdan, M.Eng., M.Sc., expressed his appreciation for the cross-sector collaboration reflected in this activity. He emphasized the importance of integration between educational institutions and legal institutions in building strong legal awareness and understanding, particularly regarding alternative business dispute resolution.

One key message from the seminar was delivered by Prof. Tan Kamello, who emphasized that dispute resolution through arbitration should not be viewed as an attempt to determine a winner or loser. Rather, arbitration is intended as a "win-win" solution that allows both parties to reach a peaceful resolution in a fair and equitable manner. Therefore, he encouraged district courts and advocates to support the use of arbitration institutions, especially if an arbitration clause has been agreed to in a business contract (Universitas Medan Area, 2023).

Similarly, Dr. Panusunan Harahap emphasized that arbitration decisions are final and binding, as stipulated in Article 64 of Law Number 30 of 1999 concerning Alternative Dispute Resolution. However, the implementation of these decisions is often hampered by the low good faith of the losing party, as well as attempts to annul the decision filed in court on the grounds of breach of contract or unlawful acts, often based on erroneous interpretations of the law. He emphasized the importance of legal awareness on the part of the parties to voluntarily implement arbitration decisions.

Arman Chandra, Chairman of the Medan Chamber of Commerce and Industry (KADIN), added that resolving business disputes does not always have to be through litigation. Collaboration and an approach that prioritizes negotiation and mediation can be a more effective solution in maintaining sustainable business relationships. He emphasized that the key to successful dispute resolution is the parties' ability to identify the root of the problem and reach a balanced agreement for the mutual benefit.

Dr. Taufik Siregar concluded the discussion by highlighting the advantages of arbitration institutions in maintaining the confidentiality of disputing parties. He stated that in addition to protecting privacy, arbitration also provides law students with an opportunity to gain a deeper understanding of the dispute resolution process and build professional networks with legal practitioners. This seminar not only enriched participants' understanding of the mechanisms for executing arbitration awards but also strengthened networks between academics, legal practitioners, and businesspeople in realizing a fair, expeditious, and efficient business dispute resolution system.

## **Limitation**

This study is primarily focused on the perspectives of business actors and regional government officials within the specific industrial regions of Medan Industrial Estate (KIM) and Sei Mangkei Special Economic Zone (KEK) in North Sumatra. While this provides an in-depth understanding of the dynamics within these key economic zones,

the findings may not be generalizable to all industrial areas in the province or to other sectors of the economy. The research relies on qualitative data gathered through interviews and document analysis, and as such, is subject to the inherent limitations of these methods, including the potential for respondent bias and the subjective interpretation of data. Furthermore, the study does not delve into a comparative analysis with other provinces in Indonesia that may have more developed arbitration ecosystems, which could have provided additional insights into best practices and potential models for reform.

### **Novelty/Contribution**

This research offers a novel and significant contribution to the existing body of knowledge by providing a micro-level analysis of the challenges and opportunities for arbitration in a specific and strategically important industrial region of Indonesia. While much of the literature on investment arbitration focuses on the national or international level, this study drills down to the sub-national context, offering a nuanced understanding of the interplay between local legal culture, institutional capacity, and regulatory frameworks. The novelty of this research lies in its empirical focus on the perceptions and practices of local stakeholders, thereby giving voice to the very actors who are most directly affected by the choice of dispute resolution mechanism. By identifying the specific barriers to the adoption of arbitration in North Sumatra and proposing a set of context-specific recommendations, this study provides a practical roadmap for policymakers and stakeholders seeking to enhance the investment climate and promote the rule of law at the regional level.

## **CONCLUSION AND SUGGESTION**

### **Conclusion**

This study concludes that although arbitration has been recognized as a legitimate and robust alternative dispute resolution mechanism in the Indonesian legal system, its implementation in the context of investment disputes at the regional level—particularly in the Medan Industrial Estate (KIM) and the Sei Mangkei Special Economic Zone (KEK), North Sumatra—still faces significant structural, cultural, and institutional challenges.

*First*, in terms of understanding and perception, the majority of business actors have a positive view of arbitration as a fast, neutral, and efficient dispute resolution forum. However, this understanding has not been fully matched by practical readiness, particularly regarding the drafting of arbitration clauses in investment agreements. Meanwhile, local governments generally still consider investment disputes to be the domain of formal resolution through the courts and do not yet view arbitration as part of modern and adaptive investment governance. *Second*, contractually, only a small portion of investment agreements in these industrial areas include arbitration clauses. This is due to the lack of standard regional investment contract guidelines, minimal involvement of legal consultants in contract drafting, and a weak legal tradition favoring alternative dispute resolution at the local level. *Third*, institutionally, North Sumatra does not yet have an independent arbitration institution that operates actively and is widely recognized by stakeholders. As a result, business actors wishing to use arbitration must refer to national institutions such as BANI in Jakarta, which raises efficiency and cost issues. Furthermore, existing regional regulations do not explicitly regulate or encourage the use of arbitration as a dispute resolution mechanism in the investment sector. *Fourth*, there is an urgent need to strengthen legal capacity, both among business actors and local government officials. Ignorance of the benefits of arbitration and the lack of a comprehensive regional investment strategy related to legal risk management are inhibiting factors that need to be addressed immediately. *Fifth*, legally, Law Number

30 of 1999 concerning Arbitration and Alternative Dispute Resolution provides a strong legal basis for the use of arbitration, including at the regional level. However, without institutional support and responsive regional policies, these provisions tend to become norms that are not yet operationalized in the field. The absence of arbitration clauses in initial contracts remains a structural weakness that increases the risk of litigation and uncertainty about resolution.

Regional governments and area managers need to develop standard contract documents that include options for dispute resolution, whether through national arbitration (such as BANI) or legally recognized mediation forums. Therefore, strengthening legal capacity and contractual literacy, particularly for area managers and local governments, is key to realizing fair and sustainable investment governance in North Sumatra. In general, this study confirms that arbitration has significant potential as an investment dispute resolution instrument that can increase legal certainty, prevent conflict escalation, and strengthen investment attractiveness in the region. However, realizing this potential requires systematic intervention in the form of strengthened regulations, the establishment of local arbitration institutions, increased contract law literacy, and strengthened synergy between the government, the business world, and the legal community. Without such measures, arbitration will remain a secondary option that is unaffordable to the majority of regional investors, and dispute resolution will continue to rely on a litigation system that is lengthy, expensive, and less adaptable to the dynamics of modern business.

## **Suggestion**

To catalyze a paradigm shift from a litigation-centric to an arbitration-friendly ecosystem, a multi-pronged and synergistic strategy is imperative. The regional government of North Sumatra should spearhead this transformation by not merely advocating for but actively institutionalizing arbitration within its investment governance framework. This requires the formulation of a definitive regional regulation that mandates the inclusion of a multi-tiered dispute resolution clause—prioritizing negotiation and mediation, followed by binding arbitration—in all future investment agreements involving regional assets or public-private partnerships. Concurrently, to address the profound institutional deficit, the provincial government, in strategic collaboration with the Indonesian National Arbitration Board (BANI) and leading university law faculties, must champion the establishment of a fully-resourced and professionally managed North Sumatra Arbitration Centre (NSAC). Such an institution would not only democratize access to arbitration by reducing costs and logistical barriers but also serve as a hub for professional development, offering accredited training and certification for arbitrators and legal practitioners. This initiative must be complemented by a sustained capacity-building campaign targeting government legal officers and the business community, designed to demystify the arbitral process and cultivate a deeper appreciation for its strategic advantages in preserving business relationships and ensuring swift, expert-driven justice. Ultimately, fostering a culture of trust in arbitration necessitates a sustained public-private dialogue, creating a virtuous cycle where regulatory reform, institutional strengthening, and enhanced legal literacy converge to position North Sumatra as a secure, predictable, and globally competitive investment destination.

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