Volume 6 Number 2, July 2024: pp. 109-120.
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p-ISSN: 1978-5186 E-ISSN: 2723-2603
http://jurnal.fh.unila.ac.id/index.php/lajil

ISDS Reform UNCITRAL: Implications For Indonesian Investment Policy

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Submitted:March 28, 2024; Reviewed:October 5, 2024; Accepted: December 20, 2024

Article Info

Keywords:
Investment; dispute settlement; UNCITRAL model law

DOI: 10.25041/lajil.v6i2.3422

Abstract

The United Nations Commission on International Trade Law (UNCITRAL) Working Group III (WG III) has been meeting intensively to formulate comprehensive reforms to Investor-State Dispute Settlement (ISDS) based on emerging criticisms. In July 2017, UNCITRAL established Working Group III with a mandate to identify and evaluate ISDS-related concerns, consider the need or desirability of reforms, and develop relevant solutions. Some of the issues that have been identified in relation to the current ISDS mechanism include lack of consistency and predictability of arbitral awards by ISDS forums, lack of independence and impartiality of arbitrators, cost and duration of proceedings, and third-party financing. The WG III forum has formulated several options to address these issues: 1) establishment of a court mechanism, 2) appointment of arbitrators and adjudicators, 3) parties' involvement and control, 4) dispute prevention and mitigation: strengthening dispute prevention and mitigation mechanisms, 5) cost management and third-party financing transparency: efforts to manage costs and related procedures, as well as transparency in third-party financing. The findings indicate that Indonesia actively participates in WG III by advocating for balanced reforms that safeguard state sovereignty and public interest while addressing investor rights. Key recommendations include enhancing transparency and leveraging regional alliances to strengthen Indonesia's position in international investment frameworks.

A. Introduction

Dispute settlement is an important aspect of the international investment field. Most international investment treaty (IIA) frameworks require the inclusion of a dispute resolution mechanism if a dispute arises in the implementation of an investment between parties to the treaty. However, in the context of IIA, a unique legal relationship is created. While international regulation typically governs the relationship between states, the IIA legal framework also governs the relationship between states and investors (investor-state). Traditionally, dispute resolution under international law concerns disputes between states. However, the emergence of private enterprise in the commercial activities undertaken by individuals and companies

engaged in international trade and/or investment has created a dispute resolution mechanism involving two different types of distinct legal subjects.[1]

The ISDS dispute resolution concept serves as a form of investor protection, allowing private companies based in other countries to sue a state in an arbitration body, such as in cases of bankruptcy. This mechanism focuses on resolving business disputes while ensuring the confidentiality of the litigation process. Its rationale lies in the vulnerability of investors when dealing with states that possess absolute power to regulate domestic affairs. However, it is important to note that investment activities often intersect with public interests.

Over time, criticism has emerged over conventional investment dispute resolution forums, such as ICSID and UNCITRAL, which are often viewed as originating from host countries. In Indonesia, for example, experts have raised concerns about these mechanisms, which are perceived as frequently unfavorable to Indonesia's position. Since joining the International Center for Settlement of Investment Disputes (ICSID) more than 50 years ago, Indonesia has been sued seven times, with the arbitral tribunal criticized for failing to reflect the principles of fairness, efficiency, and completeness expected in arbitration. Furthermore, Rouli Anita Velentina has highlighted that ICSID arbitration practices are inconsistent with the values enshrined in Indonesia's constitution, particularly the theory of dignified justice reflected in the second precept of Pancasila. Some experts have even advocated for Indonesia to withdraw from ICSID.

This criticism is also in line with worldwide criticism. Investors have filed more than 1,000 ISDS claims under 3,000 international investment treaties. More than half of all claims were filed in the last decade, and often the resulting awards involve monetary compensation of hundreds of millions of dollars or more.[2] In 2019, for example, Pakistan was ordered to pay US $6 billion in compensation to one foreign investor.[3]

In this regard, the agenda to reform the ISDS mechanism has intensified. Currently, the United Nations Commission on International Trade Law (UNCITRAL or Commission) Working Group III is intensely conducting meetings to seek comprehensive reform of ISDS based on various criticisms that are currently developing. It is anticipated that the work of WG III can be applied to all IIAs currently in force in the world, which currently number 3,000 documents.[4]

Several studies have discussed models in international investment dispute settlement. Syahrul Fauzul Kabir in his research entitled "Crisis and Reform: Dispute Settlement in Bilateral Investment Treaties in Third World Countries" analyzes the crisis of investment dispute settlement that befalls third world countries, prompting them to reform their BIT instruments.[5] This article lists the strategies of BIT dispute settlement reform in countries such as Brazil, India, Indonesia, and others, by adopting the principle *of exhaustion of local remedies* or *state-state dispute settlement* mechanisms. In his conclusion, Kabir mentioned that Indonesia has not fully anticipated the current ISDS legitimacy crisis and has the potential to suffer losses

[1] United Nations Conference on Trade and Development (UNCTAD). (2003). *Dispute Settlement: Investor-State*. Switzerland: United Nations

[2] Skovgaard Poulsen, L. N., & Gertz, G. Reforming the investment treaty regime. *Brookings*. (2021, March 17). Retrieved from https://www.brookings.edu/research/reforming-the-investment-treaty-regime/ (Accessed: March 4, 2022).

[3] Tethyan Copper Company Pty Limited Pakistan, ICSID Case No. ARB/12/1, Award, 12 July 2019.

[4] OHCHR, Contribution of the Secretariat of the United Nations Commission on International Trade Law (UNCITRAL) with regard to the open call for input for Working Group on Business and Human Rights' report on "Human Rights-compatible International Investment Agreements (IIAs)", 21 April 2021, https://www.ohchr.org/sites/default/files/Documents/Issues/Business/WG/Submissions/Others/UNCITRAL.pdf, akses tanggal 4 Maret 2022

[5] Syahrul Fauzul Kabir, "Krisis dan Reformasi: penyelesaian Sengketa dalam Perjanjian Investasi Bilateral di Negara Dunia Ketiga, Mimbar Hukum", Vol 33, No. 2 Tahun 2021https://doi.org/10.22437/ujh.6.1.151-187

in the event that investors file a lawsuit. An article entitled "Investment Court System as an Alternative to Foreign Investment Dispute Settlement" also outlines several criticisms of the current international investment dispute resolution mechanism. This article analyzes the investment court system (ICS) proposed by the European Union as another option for dispute resolution methods that can be used.[6]

This article will discuss the reform of the ISDS mechanism as a method of settlement of international investment disputes, especially in the UNCITRAL Working Group III forum. In the first part, the mechanism of dispute settlement in the field of international investment in the concept of ISDS will be outlined. The next section will address the development of dispute settlement mechanisms in the field of international investment in the efforts of investor-state dispute settlement reform in the UNCITRAL forum. The final section will focus on Indonesia's views on the development of dispute settlement mechanisms in the field of international investment in the efforts of *investor-state dispute settlement reform* in the UNCITRAL forum.

B. Analysis and Discussions

1. Investor-State Dispute Settlement (ISDS) Concept in International Investment

a. The Concept of Disputes in International Investment

Public dispute resolution mechanisms are regulated in Article 33 of the UN Charter which contains universal provisions on dispute resolution:

"The parties to a dispute which, if it continues, may jeopardize the maintenance of international peace and security, shall first seek settlement by negotiation, enquiry, by mediation, conciliation, arbitration, judicial settlement through regional bodies or arrangements, or by any other peaceful means of their own choosing."

There are two dimensions to international investment disputes. The first is disputes between host states and investors from other countries as parties to foreign investment contracts. The second dimension involves states parties to IIAs. In a short settlement of the first dispute, the steps that can be taken are through the investor-state dispute settlement (ISDS).[7] ISDS mechanisms may include (i) negotiation, (ii) consultation, (iii) competent national courts, (iv) ICSID arbitration, (v) ad hoc arbitration with UNCITRAL, or (vi) other ad hoc arbitration tribunals agreed by the parties.[8]

In Indonesia, regulations related to foreign investment dispute settlement are regulated in Article 32 of Law No. 25/2007 on Capital Investment (UUPM):

1) In the event of a dispute in the field of investment between the government and an investor, the parties shall first resolve the dispute through deliberation and consensus.
2) In the event that dispute settlement as referred to in paragraph (1) is not reached, such dispute settlement may be conducted through arbitration or alternative dispute resolution or court in accordance with the provisions of laws and regulations.
3) In the event of a dispute in the field of investment between the government and domestic investors, the parties may settle the dispute through arbitration based on the agreement of the parties, and if the settlement of the dispute through arbitration is not agreed upon, the settlement of the dispute will be carried out in court.
4) In the event of a dispute in the field of investment between the government and a foreign investor, the parties will resolve the dispute through international arbitration which must be agreed by the parties.

[6] Fatma Muthia Kinanti & Garuda Wiko, "Investment Court System sebagai Alternatif Penyelesaian Sengketa Penanaman Modal Asing, Arena Hukum": Jurnal Ilmu Hukum, Vol. 16 No. 2, Agustus 2023
[7] *Ibid.*
[8] *Ibid.*

b. Definition of International Investment Agreement (IIA)

International investment agreements can be defined as agreements with the purpose of connecting investment borders for the promotion of foreign investment, protection and liberalization of investment itself. IIA also offer companies and individuals from the contracting side increased security and certainty in international law when investing or doing business in the country of the other party to the agreement. The reduced investment potential of IIAs is intended to encourage a company or individual to invest in a country that is a signatory to the IIA. In this case, it is important to note that dispute resolution between the foreign party and the host is not only in the host's domestic courts but international arbitration.

Types of IIA include:

1) Bilateral investment agreements

According to UNCTAD, a bilateral investment treaty (BIT) is an agreement between two countries for the mutual encouragement, promotion, and protection of investment in their respective territories by companies based in both countries. Over time, BIT has primarily focused on matters related to investment protection and public policy, such as safety, health, and others, which usually start with a general description of the treaty and its scope.[9] BIT resolves issues regarding the admission and establishment of foreign investment as well as standards of treatment. It also deals with investment damage, determine the amount and compensation to investors in the event of adverse state action, and decide the level of protection and compensation in situations of unrest or war. BIT usually also includes a state dispute settlement clause. It establishes the term of the agreement, outlining when the agreement is extended and terminated, and to what extent investments prior to the conclusion and ratification of the agreement are covered.[10] According to UNCTAD, as of 2021, there were 2,844 BIT agreements signed worldwide with a total of 2,290 BITs in force.

2) Preferential trade and investment agreements

These agreements, abbreviated to PTIAs, are larger economic agreements in support of international trade and shipping related to cross-border production. These can be economic integration agreements, FTAs, EPAs, and other similar agreements. Only a small section of about one or two chapters covers foreign investment in PTIAs. PTIAs also deal with trade in goods and services, tariff and non-tariff barriers, customs procedures, sector-specific provisions, competition, IPR, and others. PTIAs have a major goal in terms of trade and investment liberalization. One of the most important agreements in PTIAs is NAFTA, a treaty that addresses a wide range of issues, one of which is cross-border trade between Canada, Mexico, and the United States.[11]

A distinctive feature of BITs and PTIAs are standard clauses on the protection and treatment of foreign investment that usually address the issues of fair treatment, full protection and security, national treatment and most favored nation treatment.[12]

Most IIAs regulate cross-border transfers of funds, but investment promotion provisions are not often formally raised within these agreements, and when they are, they are not binding. Still, increased protection is formally offered, which will encourage cross-border

[9] Moon, W. J, Essential Security Interest in International Investment Agreements. Journal of International Economic Law, 15(2) 481-502, (2012).

[10] United Nations Conference on Trade and Development (UNCTAD).Bilateral Investment Treaties 1995-2006: Trends in Investment Rule making. New York and Geneva. (2007). (p. 34)

[11] Perjanjian Perdagangan Bebas Amerika Utara (NAFTA). (n.d.). SICE-Situs Web Sistem Informasi Perdagangan Internasional.

[12] Dolzer, R., & Schreuer, C, "Principles of International Investment Law". Oxford University Press, (2008).

investment and have a positive impact on developing countries. BITs and PTIAs include investment dispute resolution provisions, which give investors the right to bring claims before international arbitration tribunals.

2. Investment-State Dispute Settlement (ISDS) Reform in Uncitral Working Group III 1

a. Background of ISDS Reform

The number of ISDS disputes oriented towards conventional arbitration has risen sharply. Based on UNCTAD data, the total number of ISDS cases was more than doubled, rising from under 600 in 2013 to 1,332 by the end of 2023. In 2023 alone, 60 new ISDS cases were initiated, although the actual numbers were likely to be higher due to some arbitrations being confidential.[13] The increase in the number of claims is in line with the increase in capital flows within the framework of foreign investment globally. Despite this increase, foreign investment flows experienced a significant decline in 2020 by up to 35% as a result of the global financial crisis that occurred due to lockdown policies in response to the COVID-19 pandemic.[14] However, when viewed at a macro level, the increase in foreign investment capital flows can be seen from the trend in 1960, where global foreign investment capital flows were "only" US$ 60 billion, while in 2013 this amount increased rapidly to US$ 25 billion.[15] This trend underscores the growing need for a robust ISDS reform to address the complexities of modern foreign investment flows.

Investors from countries that export large amounts of capital are the most frequent litigants. Forty-six percent of global investment flows come from Europe. Data in 2014 showed[16] that half of the arbitration claims filed came from European investors. In addition, the United States was the country that contributed the largest foreign capital at 24% of global capital. The likelihood of filing claims through ISDS is highest among investors from the United States.[17] Most of the defendants in these cases are countries whose governments play a major role in their economic systems and sectors that are considered essential. A quarter of the claims come from the oil and gas and mining sectors.[18] Disputes also typically involve host countries with weak legal systems.[19]

The increase in the number of ISDS claims parallels the growing debate over the implementation of the ISDS process itself. Indonesia as one of the host countries of several foreign investments, for example, has been voicing such criticism since 2013 following Indonesia's defeats at the forum. This reached its peak in 2014 when Indonesia, along with South Africa, announced to let some of its BITs expire on the grounds that the ISDS provisions were no longer relevant to its domestic regulations.[20] Other countries, especially developing countries, took a similar stance, including Ecuador and Venezuela. The main points of concern in this controversy are the attitude of investors towards host country policies and that ISDS often overrides domestic law and prioritizes investors over the public

[13] United Nations Conference on Trade and Development (UNCTAD), IIA Issues Note: International Investment Agreements, #3, November 2024.
[14] United Nations Conference on Trade and Development (UNCTAD). (2021). *World Investment Report, 2021: Investing in Sustainable Recovery*. Geneva: UNCTAD.
[15] Miller, S., & Hicks, G. N, *Investor-State Dispute Settlement: A Reality Check*. Washington, D.C: CSIS, (2015).
[16] *Ibid.*
[17] *Ibid*.
[18] *Ibid*.k;
[19] *Ibid*.
[20] Bland, B., & Donnan, S. Indonesia to terminate more than 60 bilateral investment treaties. *Financial Times.* (2014, March 26). Retrieved from http://www.ft.com/intl/cms/s/0/3755c1b2-b4e2-11e3-af92-00144feabdc0.html#axzz3NK0O7u6u.

interest.[21] Criticism has also been directed at the underlying value of ISDS itself, which privileges investors and is therefore feared to be used as a tool to intimidate states. Finally, many experts consider that the dispute settlement provisions in BITs sufficiently contain an exhaustion of local remedies mechanism.[22]

In July 2017, efforts to reform the conventional ISDS mechanism were made through UNCITRAL's WG III which was mandated to:[23]

1) Identify and review concerns related to ISDS
2) Consider whether ISDS reform is necessary or desirable
3) Develop relevant solutions

3. Profile of the UNCITRAL Working Group on Investor-State Dispute Settlement (ISDS) Reform

In July 2017, UNCITRAL gave WG III the mandate to reform ISDS. The rationale for the appointment was WG III's considerable reach and experience with negotiating legal instruments in the field of international dispute settlement.[24]

The UNCITRAL forum seems to be the right body to provide a multilateral forum to discuss investment dispute resolution issues in an inclusive and transparent manner, where the interests of both states and other stakeholders can be considered. It is worth noting that UNCITRAL has successfully taken the first step towards ISDS reform with the development of transparency standards.

In 2014, the Rules on Transparency in Treaty-based Investor-State Arbitration (Rules on Transparency) came into force in April 2014. These rules govern "the public interest involved in [ISDS] arbitration proceedings". UNCITRAL subsequently established a convention designed to facilitate the application of the rules to over 3,000 investment treaties concluded prior to the entry into force of the Convention on Transparency in Treaty-based Investor-State Arbitration (the Mauritius Convention on Transparency). In essence, the Mauritius Convention on Transparency organizes the substantive transparency standards contained in the Rules on Transparency into separate treaty regimes into a single multilateral instrument.

Following the treaty adoption process, the question arose is whether the Mauritius Convention on Transparency could provide a useful model for possible further reforms in the field of ISDS. In 2016, a research paper was submitted to UNCITRAL proposing an approach similar to that pursued in the case of the Mauritius Convention on Transparency, which would allow the reform of complex international investment treaty regimes to be simplified through a single multilateral instrument.[25]

4. Development of ISDS Reform in the UNCITRAL Working Group III

WG III forum has conducted various recorded meetings in Vienna since 2017. The official website indicates that the ISDS reform process by WG III is still underway. As of

[21] Scott Miller, Gregory N. Hicks, *Op Cit.*

[22] Chi, M, Privileging Domestic Remedies in International Investment Dispute Settlement. *Proceedings of the Annual Meeting (American Society of International Law)*, 107, 26 , (2013)..

[23] IISD. (2017, July). *UNCITRAL and Reform of Investment Dispute Settlement*. Retrieved from https://www.iisd.org/projects/uncitral-and-reform-investment-dispute-settlement

[24] "Report of the United Nations Commission on International Trade Law", 50th Sess. (3-21 July 2017) General Assembly, 72nd Sess. Supplement No. 17, UN Doc. A/72/17, para. 264.

[25] "Report of the United Nations Commission on International Trade Law", 48th Sess. (29 June-16 July 2015) General Assembly, 70th Sess., UN Doc. A/70/17, para. 268. See also "Settlement of commercial disputes: presentation of a research paper on the Mauritius Convention on Transparency in Treaty-based Investor-State Arbitration as a possible model for further reforms of investor-State dispute settlement, Note by the Secretariat" UNCITRAL, 49th Sess. (New York, 27 June-15 July 2016) UN Doc. A/CVN/9/890 (24 May 2016).

January 2023, WG III entered its 44th session of ISDS reform efforts. From the 34th to 37th sessions, WG III conducted work on possible ISDS reforms. The deliberations and decisions of the group from the 34th to 37th sessions are set out in documents A/CN.9/930/Rev.1 and its Addendum, /CN.9/935, A/CN.9/964 and A/CN.9/970, respectively. At these sessions, WG III identified and discussed issues regarding ISDS and considered that reforms were necessary given the problems identified.

Some of the problems that have been identified in relation to the existing ISDS mechanism are:

1) Lack of consistency, coherence, predictability and correctness of arbitral awards by ISDS forums. WG III uncovered inconsistent and unjustifiable interpretations by ISDS tribunals of provisions in investment treaties and other relevant principles of international law. There is also a lack of a framework for filing proceedings in accordance with investment treaties, regulations, legal instruments or agreements that provide access to international dispute settlement mechanisms. The existing legal framework also lacks a mechanism to address (*inconsistencies*) and incorrectness of awards.
2) WG III also highlighted issues related to arbitrators and other decision-makers, such as mediators, judges, and others. The lack of independence and impartiality of arbitrators and policy makers acting in the existing ISDS mechanism is in line with the criticisms raised by most developing countries. In addition, WG III also pointed out a number of considerations that should be included in the ISDS reform process, including:
   - Effective and transparent *(disclosure)* or recusal mechanisms
   - Diversity in the background of arbitrators in the ISDS mechanism because currently arbitrators from Western countries are predominant
   - Mechanism for establishing an ISDS tribunal
3) Cost and duration of ISDS proceedings including issues of allocation of arbitral tribunal fees and security of costs
4) Third-party financing which remains unclear in terms of rules and practices in ISDS

WG III also discussed several other related issues, such as mechanisms other than arbitration for resolving investment disputes including dispute prevention methods, *exhaustion of local remedies*,[26] third-party involvement, counterclaims, *regulatory chill*,[27] and calculation of damages claims.

At the 38th session of the WG III meeting from 14 to 18 October, 2019, the options for ISDS reform mechanisms were formulated, which are summarized as follows:

1) Both ad hoc and institutional multilateral court mechanisms

- WG III proposed the option of establishing a multilateral advisory center. This follows the model of the Advisory Center on WTO Law (ACWL). Under the proposal, the advisory center is tasked with providing legal advice on investment law before a dispute arises and acting as an advisor when a dispute occurs. It can also provide assistance to countries in terms of capacity building and *best practices*. It is also directed to provide support and assistance to (*least developing countries*/*LDC)* in preparing for international investment-related disputes and to provide legal advice and advocacy.
- WG III found that most investment arbitration provisions lack quality control procedures aimed at enabling a review before the award is read out. Therefore, the option offered is the establishment of a review mechanism. This mechanism refers to the existing procedure at the International Court of Arbitration of the International Chamber of Commerce (ICC). This mechanism allows the parties to submit written

[26] The use of domestic dispute resolution methods before the parties brings the dispute to an international forum.
[27] The reluctance of the state to make/change public policy based on "fear" of the threat of demands from investors that could potentially sacrifice public interests.

comments to the arbitral tribunal before the award is executed. It also proposes the establishment of an appeal mechanism. In this case the mechanism would take the form of a higher judicial body, tasked with ensuring consistency in the interpretation of bilateral investment treaty provisions and correcting errors in awards that have a significant impact on the public interest.

- WG III also proposed the option of establishing an investment court consisting of a first instance and an appellate court. This court would have full-time judges and two tiers. The first tier would assess disputes and conduct fact-finding and relevant law. The appellate court would be in charge of receiving appeals from the decisions of the court of first instance.

2) Methods and ethics of appointment of arbitrators and adjudicators

- WG III provided options on mechanisms for the selection, appointment and removal of ISDS tribunal members. Some approaches to the establishment of the mechanism include the provision of a mechanism for the appointment of arbitrators by the parties, the establishment of a list of arbitrators or adjudicators and a body that has the authority to appoint arbitrators or adjudicators. This option will also be influenced by the option of establishing first instance and appellate investment tribunals.
- Establishment of a *code of conduct* for ISDS panel members that addresses issues of independence and impartiality, as well as other professional ethical standards.

3) Mechanisms for involvement and control of the parties in the interpretation of the agreement

To address the issue of inconsistent interpretation of investment treaties, WG III provided several options, such as including both unilateral and multilateral declarations of interpretation in each investment treaty, providing guidance to arbitral tribunals on terms or standards in treaties or adopting certain interpretations in treaty provisions, and establishing a joint committee on treaty interpretation.

4) Dispute prevention and mitigation

Some of the options proposed in WG III on this point include: strengthening dispute resolution mechanisms other than arbitration, such as ombudsman or mediation, *exhaustion of local remedies*, providing procedures to deal with (*frivolous claims*), allowing states to file counterclaims.

5) Cost management and related procedures

Some of the proposed options include: providing an *(expedited procedure)* for disputes with small and non-complex claim values, establishing principles or guidelines regarding the allocation and security of dispute resolution costs.

6) Financing from third parties

This option continues to be debated in the forum. While third-party financing mechanisms can be an effective way to ensure funds are available in the dispute resolution process, it is argued that this method can lead to conflicts of interest. Therefore, if it is used, there should be transparency regarding the identity of the funding provider to avoid any conflict of interest.

Currently, WG III is actively engaged in discussions and negotiations to implement the above options. In 2023, two meetings were held from March 27 to 31 in New York and from October 8 to 13 in Vienna.

At its 50th session in 2017, the Commission gave a broad mandate to Working Group III to examine possible reforms to investor-state dispute settlement (ISDS). Over the course of its 34th to 37th sessions, the Working Group identified and discussed various concerns related to ISDS, indicating that reforms are imperative in light of these concerns. From the 38th to 45th sessions, the Working Group detailed concrete solutions for ISDS reform.

Subsequently, at its 56th session in 2023, the Commission adopted a number of legal instruments, including the UNCITRAL Model Rules on Mediation for International Investment Disputes, the UNCITRAL Guidelines on Mediation for International Investment Disputes, and the UNCITRAL Code of Conduct for Arbitrators in the Settlement of International Investment Disputes, with accompanying commentary. The Commission has also, in effect, adopted the UNCITRAL Code of Conduct for Judges in International Investment Dispute Resolution and its accompanying commentary.

During the session, the Commission expressed satisfaction with the progress made by the Working Group and requested the group to continue its work effectively. The Commission also encouraged the Working Group to present a draft paper on the establishment of an international legal advisory center in the field of investment law, as well as a guidance paper on how to prevent and mitigate disputes, to be considered in 2024.

During this meeting, the concept of establishing an *advisory center on international investment law was* put forward. During the discussion, it was suggested that the Advisory Center should be established as an intergovernmental body, and that efforts should be made by the Working Group to draft a statute establishing its existence. It was also suggested that the Centre should be established as an independent organization separate from any existing organization, and that its establishment should not be linked to other elements of reform, especially the permanent mechanism.

5. Indonesia's view on ISDS Reform in UNCITRAL Working Group III Forum

Indonesia has highlighted conventional investment dispute resolution mechanisms that are often considered detrimental to Indonesia's position. For more than 50 years Indonesia has been a member of the *International Center for Settlement of Investment Disputes* (ICSID).[28] Indonesia has been sued seven times and the arbitration hearing is considered not to reflect the character of the arbitration hearing which should be fair, fast, efficient, economical, and complete.[29] In addition, Velentina mentioned that, in practice, ICSID arbitration is not in line with the values adopted in the Indonesian constitution, especially related to the theory of dignified justice in the second principle of Pancasila.[30] Some experts have even called on Indonesia to quit ICSID.[31]

As a developing country that is also the destination of foreign investment capital flows, Indonesia also criticizes the conventional ISDS mechanism. The central issue raised by Indonesia is the guarantee of policy space, especially for the investment destination country. This was triggered by several experiences of Indonesia being sued by investors over investment disputes, most recently by Churcill Mining in the ICSID forum. Indonesia even took concrete action by conducting a review of the ISDS system that has been included in several Indonesian BITs with partner countries.

This review includes the following actions:

1) discontinuing BITs that have expired
2) reviewing BITs that are still valid
3) making BIT models
4) renegotiation

[28] ICSID (International Centre for Settlement of Investment Disputes) is an international investment dispute resolution forum based on arbitration. For more information about ICSID, you can visit their official website at https://icsid.worldbank.org/.

[29] Humas FHUI, Indonesia Disarankan Mundur dari ICSID, law.ui.ac.id

[30] *Ibid*.

[31] [...], Guru Besar Hukum Minta Indonesia Keluar dari ICSID. *Hukum Online*, 17 Maret 2013. https://www.hukumonline.com/berita/baca/lt5145a99083b4d/guru-besar-hukum-minta-indonesia-keluar-dari-icsid/, diakses pada 20 Juni 2021.

In the negotiations at the WG III forum, Indonesia has taken an active stance and offered comments and inputs several times. Several issues related to ISDS, such as frivolous claims, regulatory chill, the existence of a parallel adjudication system, and the credibility of the arbitration system, were highlighted by the government of Indonesia. In this regard, Indonesia provides several options for reforming ISDS:

1) Provide more safeguards in both substantive and ISDS to fairly address investor rights and obligations
2) Allow investors to submit claims to international arbitration after *(exhaustion of local remedies)*
3) Require separate written consent as a requirement for investors to submit ISDS claims to international arbitration
4) Introduce mandatory mediation as an alternative dispute resolution before submitting disputes to ISDS

In the future, Indonesia should actively engage in the WG III reform process by advocating for a balanced ISDS framework that addresses both investor protection and the state's right to regulate in the public interest. Drawing from its own experiences, such as the Churchill Mining case, Indonesia can emphasize the importance of reforms that reduce frivolous claims, safeguard policy space, and align arbitration processes with national priorities.

Building alliances with other developing nations is crucial for amplifying Indonesia's voice in reform discussions. Collaboration can strengthen collective advocacy for fairer ISDS mechanisms that prioritize transparency and accountability, such as ensuring public access to proceedings and decisions. By taking these steps, Indonesia can play a leading role in shaping an ISDS system that supports equitable dispute resolution while preserving national sovereignty and public interests.

C. Conclusion

The ISDS reform initiative under UNCITRAL WG III responds to significant shortcomings in the current dispute resolution system, including issues of fairness, efficiency, and alignment with public interest. The reform agenda highlights the need for systemic changes, such as multilateral court mechanisms, transparency measures, and stronger safeguards for state sovereignty. For Indonesia, the conventional ISDS framework often undermines its regulatory authority, as seen in past arbitration cases. By taking an active role in WG III discussions and reviewing BIT provisions, Indonesia demonstrates its commitment to ensuring that ISDS reforms address the unique challenges faced by developing countries while safeguarding public interests.

To strengthen its position in the ISDS reform process, Indonesia should prioritize advocating for balanced reforms that address both investor protection and the state's right to regulate in the public interest. This includes pushing for mechanisms that align ISDS provisions with national development goals and constitutional principles. Strengthening domestic legal frameworks and institutional capacity is essential to ensure that Indonesia can manage disputes effectively within its own jurisdiction, reducing reliance on international arbitration.

Building regional alliances with other developing countries is equally important, as it allows Indonesia to amplify its voice in WG III negotiations and push for reforms that reflect shared challenges and priorities. Transparency and accountability should also be central to Indonesia's reform agenda, with a focus on enhancing public access to ISDS proceedings and introducing stricter disclosure requirements for arbitrators and third-party funders. Additionally, Indonesia should advocate for the exhaustion of local remedies before disputes escalate to international arbitration, promoting amicable and cost-effective resolutions.

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