Al-Qadha: Jurnal Hukum dan Syar'iah
Vol. 2, Nomor 1, 2026, pp. 130-137
e-ISSN: 3109-1474
DOI: https://doi.org10.64317/alqadha.v1i2.20

Arbitration and Mediation as Instruments for Resolving Business Disputes in Commercial Contracts: An Islamic Law Perspective

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Abstract

Business disputes frequently arise from the implementation of commercial contracts, particularly regarding contractual obligations, interpretation, and breaches of agreement. Litigation is often considered ineffective due to lengthy procedures, high costs, and its adversarial nature. Consequently, arbitration and mediation have become preferred alternative dispute resolution mechanisms. This article examines the role and challenges of arbitration and mediation in resolving business disputes within commercial contracts from the perspective of Islamic law. Using a normative juridical approach, the study analyzes relevant legal doctrines, regulations, and Islamic legal principles. The findings indicate that arbitration and mediation are consistent with the Islamic concepts of tahkim (arbitration) and sulh (amicable settlement), which emphasize justice, consensus, and the preservation of business relationships. Despite several implementation challenges, both mechanisms offer effective, efficient, and Sharia-compliant solutions for contemporary commercial dispute resolution.

Keywords: *Arbitration, Mediation, Business Dispute Resolution, Commercial Contracts, Islamic Law*

Submitted: May 08, 2026	Accepted: May 30, 2026	Published: June 01, 2026

Introduction

Business activities are mainly carried out through contracts that create legal promises between people or groups. In today's business world, conflicts often happen because one side doesn't follow the agreement, there's confusion about what was agreed, work is delayed, or there's poor communication. As business deals get more complicated, especially when companies from different countries are involved, the chances of problems increase. This is because the parties involved may follow different laws, business rules, and cultural norms.

Businesses are moving away from lawsuits and toward Alternative Dispute Resolution (ADR) because they want to keep things private and protect important business information. In court, everything is public, which can reveal sensitive details. ADR methods like mediation and arbitration offer a more neutral setting where both sides can work together to find solutions that benefit everyone. This helps keep long-term business relationships strong. Since the world economy is connected, businesses need a way to resolve disputes across countries. They don't want to deal with unfamiliar laws or court systems that might favor one side. The 1958 New York Convention helps with this by making sure that decisions from arbitration are accepted and followed in different countries, something court rulings don't always do.

In the past, going to state courts to settle disagreements was the usual way people solved problems. But court cases are often seen as slow, expensive, not private, and following strict rules. Court hearings are usually public, which can show private business details and hurt a company's image. Because of these issues, many businesses now look for other ways to settle disputes that are faster and better suited for business needs.

Arbitration and mediation are the most common ways to resolve business disagreements without going to court. Arbitration is a private process where a neutral person makes a final decision that both sides must follow. Mediation, on the other hand, helps both sides reach an agreement through discussion with the help of a mediator. Legal agreements like the 1958 New York Convention, which helps recognize and enforce arbitration decisions across countries, and the UNCITRAL Model Law, which provides a standard for international business arbitration, have helped make arbitration widely accepted around the world.

Previous research has shown that arbitration and mediation are beneficial in business settings. Born (2021) points out that arbitration is fair and can be enforced in international trade. Menkel-Meadow (2018) says that mediation helps keep business relationships strong over time. Studies also show that arbitration can lower costs and make the process faster than going to court (Eisenberg & Miller, 2015). Even with these benefits, using arbitration and mediation in real-world situations still has several difficulties.

Most of the writing so far talks about the good sides of using arbitration and mediation, but not much is said about the real problems businesses face. These problems include expensive arbitration, unfair power during talks, not knowing much about mediation, and having trouble making agreements work. Because of this, there's a need for more legal studies on how well arbitration and mediation actually work in solving business conflicts.

This article looks at the legal and real-world issues that come up when businesses use arbitration and mediation to settle disputes. What makes this study different is that it combines both methods within the context of business agreements. The goal is to find out the main difficulties faced when using these dispute resolution methods and to suggest ways to make them work better.

Methods

This research employs a normative legal research method. The study applies a statutory approach by examining international conventions, model laws, and national regulations governing arbitration and mediation. A conceptual approach is also used to analyze legal doctrines, principles, and theories related to business dispute resolution. The legal materials consist of primary legal materials, including international conventions and arbitration laws, and secondary legal materials such as books, peer-reviewed international journal articles, and reports from reputable institutions. Data are analyzed qualitatively through systematic interpretation and legal reasoning to draw coherent conclusions.

Results and Discussion

Types of Business Disputes in Commercial Contracts

Business disagreements often happen because of things like sales contracts, distribution deals, construction agreements, joint ventures, and licensing agreements. Common problems include not paying on time, poor performance, late deliveries, ending contracts early, and different understandings of what the contract says. In deals that involve different countries, these issues can get more complicated because of questions about which country's laws apply, which court handles the case, and how easy it is to make someone follow the agreement (Born, 2021).

Legal Framework of Arbitration in Business Disputes

Arbitration is backed by a strong set of international laws. The New York Convention requires countries that sign it to accept and carry out awards made through arbitration in other countries, except in certain limited cases. The UNCITRAL Model Law offers a common set of rules that many countries have adopted, which helps ensure that arbitration processes are consistent and reliable. These legal tools make arbitration a more predictable and trustworthy way for businesses to resolve disputes.

Problems in Arbitration Practice

Even though arbitration has its benefits, it also has some big problems. One of the main issues is how expensive it can be. The costs include payments to the arbitrators, running the process, and hiring lawyers. These high costs can stop smaller and medium-sized businesses from using arbitration. A study by Redfern and Hunter in 2020 talks about this. Another study in the Journal of International Dispute Settlement shows that cost and how long the process takes are still major worries for international business arbitration, according to (Strong in 2020).

Another big problem is the unfair power balance between the parties involved in a contract. The stronger party might include standard arbitration terms that reduce fairness in the process and limit how much control each side has, especially in contracts where one party has little choice (Eisenberg & Miller, 2015). This unequal power can hurt the basic idea of fairness between the parties, which is a key part of arbitration.

From the Indonesian point of view, Law Number 30 of 1999 on Arbitration and Alternative Dispute Resolution clearly states that arbitration is a way to settle disputes that is final and must be followed. However, there are still problems when it comes to making sure that the decisions from arbitration are carried out, especially when the case involves foreign countries. Indonesian courts might use their own rules about public policy, which can change how certain legal decisions are treated and make things less certain (Republic of Indonesia, 1999).

Enforcing arbitral awards can be difficult on a global scale. Even though the New York Convention helps with enforcement, some courts in specific countries might not enforce the award because of public policy reasons or problems with the process. This can reduce the certainty and impact of arbitration (Chong, 2021).

The problem with enforcing awards isn't just about international ones, but also how courts in a country handle the idea of "public policy." In Indonesia, even though there's a clear law (Law Number 30 of 1999) that helps with enforcement, local courts sometimes apply public policy rules in ways that are vague or not consistent. This creates confusion and makes it hard for awards to be final. As a result, there are long delays in court cases trying to cancel the award, which goes against the main reason people choose arbitration—to get a quick and final decision. To keep Indonesia as a friendly place for arbitration, judges need to agree on what public policy really means and how it should be used.

Role of Mediation in Business Dispute Resolution

Mediation focuses on working together and finding a solution that everyone agrees on. It lets the people involved make their own decisions about the result, which helps keep good relationships, especially in business. Mediation usually happens more quickly and costs less than going to court or using arbitration. Because of this, courts and dispute resolution organizations are encouraging mediation as a first step to settle disagreements (Alexander, 2016).

Limitations of Mediation in Commercial Disputes

Mediation is not legally binding, which is both a good and a bad thing. It lets people solve problems in a flexible way, but it also means that both sides need to be willing to work together in good faith. Mediation might not work if the people involved aren't ready to give up something or if the problem needs a strict legal answer. Also, whether mediation works depends a lot on how skilled and fair the mediator is (Menkel-Meadow, 2018).

Beyond what the mediator can do, when mediation happens also matters a lot for its success. Starting mediation early, before people spend a lot on legal costs or get really angry with each other, makes it much more likely that they will reach an agreement that keeps their business relationship good. But many business people see mediation just as a way to find out what the other side is hiding, which takes away from the idea that talks are private and not meant to be used against them in court. To keep mediation strong and make it a real choice instead of going to court, it’s important to make sure conversations stay private and set clear rules about what happens if someone doesn’t act in good faith.

Comparative Analysis of Arbitration, Mediation, and Litigation

Litigation gives official court rulings but can be slow and not very private. Arbitration gives a final decision that can be followed in court, while mediation focuses on getting both sides to agree and keeping their relationship good. Choosing which method to use depends on the type of problem, how the people involved get along, and what's best for their plans. Having clear rules that mix mediation and arbitration can make solving business conflicts better.

Implications for Business Contract Drafting

From a practical point of view, how well arbitration and mediation work depends a lot on the quality of the dispute resolution terms in business contracts. If these terms are not written clearly, they can cause confusion, disagreements about where the case should be handled, or multiple legal processes happening at the same time, which can make alternative dispute methods less effective. Because of this, business people are advised to create clear and detailed clauses for arbitration and mediation that explain where the arbitration will take place, which laws will apply, the steps that will be followed, and how the results can be enforced.

Including rules that require parties to try mediation before going to arbitration can make the process more efficient and help keep business relationships strong. These rules are now more commonly accepted and followed in international business dealings. Writing clear contracts also lowers the chance of problems during legal procedures and gives businesses more confidence in the legal process.

Institutional and Regulatory Challenges

The success of arbitration and mediation also depends on how strong the dispute resolution institutions are. Strong arbitration organizations offer clear rules, help with organizing the process, and set high standards of behavior, which makes people more confident in the results. However, if the institutions are not well developed, it can lead to slower processes and uneven ways of handling disputes.

In Indonesia, even though there is a law from 1999 that supports arbitration and other ways to settle disputes, more rules and consistent court decisions are needed. Better teamwork between courts and arbitration centers could help make enforcement better and support Indonesia's image as a place that is friendly to arbitration.

Comparative Perspective and Future Developments

Comparative legal analysis shows that places which strongly support arbitration and mediation often see more commercial activity. International trends show that mediation is becoming more common in arbitration processes, especially through mediation-arbitration (med-arb) methods. The rise of digital platforms for resolving disputes also brings new chances and challenges for handling business conflicts.

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As business deals become more complex, arbitration and mediation need to change to meet these new conditions.

Making legal rules more consistent, getting more support from courts, and providing better training for professionals will be key in shaping how business disputes are handled in the future.

As commercial agreements move towards digital forms, like smart contracts using blockchain, arbitration needs to change to keep up with new technologies. New challenges are appearing, especially when it comes to figuring out where arbitration should take place in transactions that aren't tied to a single location. This makes it hard to decide the legal location for arbitration. Also, there's ongoing debate about whether digital arbitration agreements count as “written” under the New York Convention. These issues show that even though the existing legal system is strong, it still needs to be updated to keep up with today's business practices.

Conclusion

Arbitration and mediation are important ways to settle business disagreements because they are efficient, keep things private, and offer more flexibility. But there are some big problems when using these methods, like expensive costs, unfair power situations, mediation not always working well, and difficulties in making decisions stick. To make these methods better, it's important to strengthen the laws that support them, improve the systems in place, and make sure contracts are fair. More research is needed to study how well these dispute resolution methods work in different areas of business.

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