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Legal Protection of International Business Transactions in the Era of Free Trade

(A Normative–Empirical and Comparative Analysis of Indonesia and Global Practices)

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Abstract

The era of free trade has significantly accelerated the cross-border flow of goods, services, capital, and technology. This dynamic simultaneously intensifies legal risks arising from differences in legal systems, asymmetries in bargaining power, and the limited institutional capacity of developing countries. This article analyzes the forms, mechanisms, and effectiveness of legal protection in international business transactions through a normative–empirical and comparative approach between Indonesia and global practices. The study employs a normative juridical method using statutory, conceptual, and comparative approaches, enriched by empirical data drawn from reports of international trade institutions and cross-border dispute resolution practices. The findings reveal that effective legal protection rests on the harmonization of contractual norms, the adoption of global legal instruments (CISG, UNIDROIT, UNCITRAL), prudent contract design, and credible international arbitration mechanisms. Indonesia continues to face challenges in legal harmonization, low levels of legal literacy among business actors, and a legal system reputation that has yet to become internationally competitive. This article recommends the adoption of global legal instruments, the strengthening of national judicial and arbitral institutions, and the empowerment of business actors as protective strategies within the free trade regime.

Keywords: international business transactions; free trade; legal protection; international contracts; arbitration.

1. Introduction

1.1. Introduce the Problem

Free trade constitutes a defining characteristic of the contemporary global economy. Through the regime of the World Trade Organization (WTO), as well as bilateral and regional free trade agreements (FTAs, RCEP, CEPA), states open their markets and progressively reduce both tariff

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and non-tariff barriers. As a consequence, cross-border business transactions have expanded rapidly in the form of exports and imports, technology licensing, joint ventures, international franchising, and foreign direct investment.

This process of economic globalization not only generates opportunities but also gives rise to increasingly complex legal risks. Cross-border transactions bring together parties subject to different legal systems, diverse business cultures, and unequal economic power. In this context, international business contracts no longer function merely as instruments of economic exchange; they have become the primary devices of legal protection.

Business actors from developing countries often occupy a weaker bargaining position in comparison to their counterparts from developed states. They tend to accept unilaterally determined clauses on the applicable law (*choice of law*) and dispute resolution forum (*choice of forum*). As a result, when disputes arise, the cost of accessing justice escalates, while the prospects of obtaining substantive justice diminish. Indonesia faces a structural paradox: market openness has increased significantly, yet the level of legal protection afforded to domestic business actors has not evolved in proportion to the risks they confront.

The growing number of cross-border disputes further reinforces the urgency of this issue. Statistics from international arbitral institutions demonstrate an escalating trend in commercial and investment cases across jurisdictions. This indicates that free trade proceeds in tandem with an intensification of legal conflict. In the absence of an adequate protective design, economic openness risks widening disparities between large and small business actors, as well as between developed and developing countries.

1.2. Research Questions

(1) What are the forms and mechanisms of legal protection in international business transactions in the era of free trade?
(2) To what extent does Indonesia's legal framework correspond with global practices in providing such protection?

1.3. Objectives and Contribution

This article aims to analyze mechanisms of legal protection through a normative–empirical and comparative perspective, while offering a conceptual contribution by viewing law as economic infrastructure. Practically, it proposes policy recommendations to strengthen Indonesia’s position within the free trade regime.

2. Literature Review

2.1. Legal Protection from the Perspective of Law and Economics

From a *law and economics* perspective, the existence of legal protection constitutes a fundamental prerequisite for the efficient functioning of markets. North (2019) emphasizes that strong legal institutions are capable of reducing transaction costs and enhancing trust among

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economic actors. In the absence of adequate legal guarantees, business actors face high levels of uncertainty, which discourages them from engaging in investment or cross-border trade. Accordingly, legal protection serves as an *enabling framework* that facilitates and sustains global economic growth.

At the international level, legal protection in business transactions is manifested through a set of relatively standardized norms, principles, and dispute resolution mechanisms. However, due to the absence of a fully supranational global authority, this system of protection remains fragmented and is heavily dependent on the willingness of states to adopt and implement international legal instruments (Berman, 2012). This condition creates particular challenges for developing countries, which often possess more limited regulatory and institutional capacities.

2.2. Legal Certainty in International Contracts

Contracts constitute the primary instrument in international business transactions. In a cross-border context, a contract not only reflects the private agreement of the parties but also serves as a point of convergence for multiple legal regimes. Schwenzer et al. (2019) observe that international contracts function as a "normative bridge" between different legal systems. Consequently, legal certainty becomes a fundamental necessity.

Legal certainty in international contracts is generally ensured through several principal mechanisms, namely:

1. Choice of law clauses, which determine the national law or specific legal regime governing the contract.
2. Choice of forum clauses, which designate the institution or jurisdiction responsible for dispute resolution.
3. Standardization of contractual clauses, which adopts global practices and international best practices.

In international practice, parties tend to select legal systems perceived as neutral, stable, and business-friendly, such as English law or the law of the State of New York. This tendency reflects the existence of an implicit hierarchy among legal systems in the global market (Carr & Stone, 2018). States with a reputation for weak legal systems often occupy a lower bargaining position, resulting in their national laws being rarely chosen as the governing law.

For Indonesia, this situation reveals a structural challenge. Although national civil law provides a basic contractual framework, in international contractual practice Indonesian business actors frequently must accept the application of foreign law. This condition limits the scope of national legal protection for the interests of domestic business actors.

2.3. Lex Mercatoria and the Harmonization of Commercial Law

In response to the fragmentation of national legal systems, the international business community has developed what is known as *lex mercatoria*—a body of transnational principles, customs, and practices of international trade. *Lex mercatoria* is understood as a modern "law of

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merchants" that is flexible, pragmatic, and relatively neutral with respect to the interests of any particular state (Berman, 2012).

Instruments such as the *UNIDROIT Principles of International Commercial Contracts* and the *UNCITRAL Model Law* represent formal manifestations of efforts to harmonize international commercial law. These principles are not always directly binding; however, they are frequently invoked by contracting parties and relied upon by arbitral tribunals in resolving disputes.

The principal functions of such harmonization are to:

- Reduce uncertainty arising from differences among legal systems;
- Provide minimum standards of protection for the parties; and
- Create a *level playing field* in cross-border transactions.

Within the context of free trade, legal harmonization becomes increasingly significant, as the flow of transactions involves actors from highly diverse legal backgrounds. In the absence of a shared normative framework, the risk of legal conflict would increase substantially.

2.4. CISG and the Regime of International Trade Law

One of the most significant instruments in international business transactions is the *United Nations Convention on Contracts for the International Sale of Goods* (CISG). This Convention aims to unify the rules governing international contracts for the sale of goods, thereby preventing parties from being entangled in conflicts arising from divergent national legal systems. As of 2024, the CISG has been ratified by more than 95 countries, including the majority of developed states (UNCITRAL, 2024).

The CISG provides legal protection through:

- The standardization of the rights and obligations of sellers and buyers;
- The regulation of breach of contract and remedies, including damages; and
- The incorporation of the principle of good faith in international trade.

However, Indonesia has not yet ratified the CISG. As a result, Indonesian business actors often remain outside a legal regime that has effectively become the default framework in global trade. In practice, export–import contracts involving Indonesian parties are frequently subject to the CISG, either because their trading partners originate from CISG member states or because the contractual clauses explicitly adopt it. This situation reveals a gap between the national legal framework and global commercial practice.

At the macro level, the World Trade Organization (WTO) establishes an international trade law regime governing relations among states. Principles such as *most-favoured nation*, *national treatment*, and the prohibition of non-tariff barriers constitute the normative foundations of free trade (WTO, 2023). Although the WTO does not directly regulate private contracts, the existence of this regime significantly shapes the structure and dynamics of international business transactions.

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2.5. International Arbitration as an Instrument of Protection

In the realm of international business, international arbitration has become the principal mechanism for dispute resolution. The advantages of arbitration lie in its flexibility, confidentiality, the expertise of arbitrators, and its cross-border enforceability under the 1958 New York Convention. More than 170 countries, including Indonesia, are parties to this Convention (Born, 2021).

Institutions such as the ICC, SIAC, LCIA, and ICSID provide relatively neutral forums for the resolution of cross-border business disputes. In many international contracts, arbitration clauses are almost invariably included as standard provisions. This practice demonstrates that, in reality, legal protection does not rely solely on national courts but increasingly on private, transnational mechanisms.

For developing countries, international arbitration presents a dual character. On the one hand, it offers access to a fair and professional forum. On the other hand, the high costs and procedural complexity often impose a significant burden on small and medium-sized enterprises. Moreover, in investment disputes, the Investor–State Dispute Settlement (ISDS) mechanism is frequently perceived as an instrument that affords greater protection to foreign investors than to host states (Sornarajah, 2021).

3. Research Method

This study employs a normative juridical approach enriched with empirical and comparative analysis. The normative approach is conducted through:

1. Statute approach, by examining national regulations and international instruments relevant to international business transactions.
2. Conceptual approach, to analyze the concepts of legal protection, international contracts, *lex mercatoria*, and free trade from the perspectives of legal and economic theory.
3. Comparative approach, by comparing Indonesia's legal framework with global practices in major trading jurisdictions.

The empirical dimension is undertaken through the analysis of reports issued by the WTO, UNCTAD, ICC, and ICSID, as well as selected case studies of cross-border commercial and investment disputes. These data are utilized to assess how legal norms operate in practice.
The analytical technique is qualitative and deductive in nature. General norms and theories serve as the framework for evaluating concrete practices. The results of the analysis are subsequently synthesized to identify patterns, weaknesses, and opportunities for strengthening legal protection, particularly in the Indonesian context.

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4. Discussion

4.1. The Nature of Legal Protection in International Business Transactions

Legal protection in international transactions operates in both preventive and repressive dimensions. Preventive protection is realized through clear contract design, the determination of the applicable law (*choice of law*), and the selection of a dispute resolution forum (*choice of forum*). Repressive protection is manifested through mechanisms for enforcing rights once a dispute arises.

In global practice, parties tend to choose legal systems perceived as stable and business-friendly, such as English law or New York law. This preference reflects the economic function of law: legal systems are treated as economic assets. States with credible and predictable legal frameworks gain a competitive advantage in attracting international transactions.

For business actors from developing countries, this situation is inherently ambivalent. On the one hand, the selection of a neutral and reputable legal system provides certainty. On the other hand, the dominance of foreign law weakens normative sovereignty and increases transaction costs. The law thus becomes not merely a neutral framework, but also a strategic instrument that can reinforce structural asymmetries in international commerce.

4.2. Empirical Practices of Transactions and Disputes

In international trade in goods, the CISG serves as the primary reference. Many export–import contracts explicitly adopt the CISG. Because Indonesia has not acceded to this convention, Indonesian business actors are often contractually bound by the CISG without the support of a coherent national framework.

In the fields of services and technology, licensing agreements and joint venture contracts frequently contain clauses designating foreign law and international arbitration. Multinational corporations typically employ standardized global contracts that local partners are rarely in a position to renegotiate.

In dispute resolution, international arbitration dominates due to its flexibility, confidentiality, and the relative ease of cross-border enforcement. However, the costs of arbitration are comparatively high, rendering it inaccessible for small and medium-sized enterprises (SMEs). This inequality of access generates a *justice gap* within the free trade regime.

Investment cases such as *Churchill Mining v. Indonesia* illustrate the tension between investor protection and state sovereignty. Although Indonesia ultimately prevailed, the protracted proceedings and substantial costs demonstrate the structural risks inherent in the investment protection regime.

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4.3. Comparative Analysis: Indonesia and Global Practices

Leading trading jurisdictions such as the United Kingdom, the United States, and Singapore treat law as an instrument of competitiveness. They adopt global legal instruments, provide arbitration-friendly courts, and cultivate strong international reputations.
Singapore, for example, integrates legal policy into its national economic strategy. Its courts and arbitral institutions are designed as a global dispute hub. Law is positioned as economic infrastructure.

Indonesia, by contrast, continues to face regulatory fragmentation, inconsistency in judicial decisions, and limitations in institutional capacity. Although Indonesia has ratified the New York Convention, the practice of enforcing arbitral awards has not yet achieved full consistency. This condition affects perceptions of legal risk.

Moreover, the level of international legal literacy among domestic business actors remains relatively low. Many contracts are executed without a proper understanding of the implications of *choice of law* and *choice of forum* clauses. As a result, legal protection that exists normatively does not always operate effectively in empirical terms.

4.4. Law-and-Economics Implications

From a law-and-economics perspective, weak legal protection increases transaction costs. Legal uncertainty raises risk premiums, diminishes competitiveness, and constrains the participation of domestic actors in global value chains.

Conversely, the harmonization of norms and the establishment of credible institutions reduce transaction costs and expand market access. Legal protection is therefore not merely a juridical issue, but a structural factor in economic development.

5. Conclusion and Recommendations

5.1. Conclusion

Legal protection in international business transactions in the era of free trade rests upon the harmonization of norms, well-designed contracts, and credible cross-border dispute resolution mechanisms. Indonesia remains behind in terms of legal harmonization and institutional capacity, with the result that normative protection has not yet operated effectively at the empirical level.

5.2. Recommendations

1) Ratify the CISG and adopt global contractual standards;
2) Strengthen national courts and arbitral institutions to become business-friendly and enforcement-oriented;
3) Enhance the international legal literacy of business actors; and
4) Position legal protection as a central pillar of national economic policy.

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