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Article

Dispute Resolution in Islamic Banking Contracts through Alternative Dispute Resolution

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Abstract

Dispute resolution has become a critical issue in Islamic banking due to the increasing complexity of Sharia-compliant financial contracts and the growing volume of commercial transactions. This study examines the role of Alternative Dispute Resolution (ADR) in resolving disputes arising from Islamic banking contracts by analyzing its legal foundation, institutional framework, procedural effectiveness, and conformity with Islamic legal principles. The research employed a qualitative normative legal approach using statutory, conceptual, case, and comparative approaches. Data were collected through an extensive review of statutory regulations, judicial decisions, and scholarly literature concerning Islamic banking dispute resolution in Indonesia and selected international jurisdictions. The findings indicate that ADR mechanisms, particularly negotiation, mediation, and arbitration, provide effective alternatives to litigation by promoting procedural efficiency, confidentiality, legal certainty, and the preservation of long-term commercial relationships. The study further reveals that the successful implementation of ADR depends on harmonized legal regulations, institutional capacity, professional expertise, standardized contractual clauses, and public awareness. Based on these findings, this study proposes an integrated ADR framework that applies negotiation, mediation, arbitration, and litigation in a sequential process according to the complexity of disputes. The proposed framework strengthens legal certainty while ensuring compliance with Sharia principles and supporting the sustainable development of the Islamic banking industry.

Keywords: alternative dispute resolution; islamic banking contracts; arbitration; mediation; sharia dispute resolution.

Introduction

The rapid development of the Islamic banking industry has significantly transformed the global financial landscape over the past two decades. Islamic financial institutions have expanded beyond Muslim-majority countries into international markets, offering financial products that comply with Sharia principles while meeting the diverse needs of modern economic activities. This expansion has increased the volume and complexity of contractual relationships between Islamic banks and their customers. Financing contracts such as murabahah, mudharabah, musyarakah, ijarah, and istisna involve distinct legal characteristics that differentiate them from conventional banking agreements. Consequently, disputes arising from these contracts require settlement mechanisms that not only ensure legal certainty but also uphold the ethical and religious principles underlying Islamic commercial law. Conventional litigation often fails to accommodate

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these unique characteristics because judges may rely primarily on civil law principles without adequately considering Sharia doctrines governing contractual obligations. Therefore, dispute resolution in Islamic banking has become an increasingly important issue for scholars, policymakers, and practitioners seeking to maintain public confidence in Islamic financial institutions (Al-Shibli, 2018; White, 2020).

The increasing number of Islamic banking transactions has inevitably been accompanied by a growing diversity of disputes involving financing defaults, contractual interpretation, profit-sharing arrangements, collateral execution, and the fulfillment of rights and obligations under Sharia contracts. Unlike conventional commercial disputes, conflicts in Islamic banking involve dual legal dimensions, namely compliance with national legislation and adherence to Islamic legal principles. These dual dimensions require dispute settlement mechanisms capable of balancing legal certainty, procedural fairness, commercial efficiency, and Sharia compliance. If disputes are resolved solely through conventional litigation, the resulting decisions may not fully reflect the contractual intentions of the parties or the substantive values embedded in Islamic commercial jurisprudence. As a result, many jurisdictions have increasingly recognized Alternative Dispute Resolution (ADR) as a more appropriate mechanism for resolving Islamic banking disputes because it promotes flexibility, confidentiality, efficiency, and mutually acceptable outcomes while preserving business relationships (Kholid, 2018).

Alternative Dispute Resolution has become one of the most significant developments in contemporary Islamic financial law. ADR encompasses several mechanisms, including negotiation, mediation, conciliation, adjudication, and arbitration, each offering different procedural characteristics depending on the nature of the dispute. These mechanisms are consistent with the Islamic concepts of shulh (amicable settlement) and tahkim (arbitration), both of which have long been recognized in classical Islamic jurisprudence as effective means of resolving conflicts peacefully. Rather than emphasizing adversarial litigation, Islamic law encourages disputing parties to pursue consensus and reconciliation whenever possible. Such an approach reflects the broader objectives of maqasid al-shariah, particularly the protection of wealth (hifz al-mal), justice (al-'adl), and social harmony. Consequently, ADR is not merely an alternative procedural mechanism but also represents the practical implementation of Islamic legal values within contemporary financial transactions (Herawan & Athoillah, 2024; Fariana & Nugrahanti, 2022).

Indonesia has established a comprehensive legal framework governing dispute resolution in Islamic banking. Law Number 21 of 2008 concerning Islamic Banking recognizes various mechanisms for resolving disputes arising from Sharia banking activities. Furthermore, Law Number 30 of 1999 concerning Arbitration and Alternative Dispute Resolution provides a broader legal basis for implementing non-litigation dispute settlement. A significant milestone in this legal development was the Constitutional Court Decision Number 93/PUU-X/2012, which clarified the jurisdiction over Islamic banking disputes and strengthened legal certainty regarding the authority of religious courts and alternative dispute resolution institutions. Following this decision, institutions such as the National Sharia Arbitration Board (BASYARNAS) and the Indonesian Alternative Institution for Banking Dispute Resolution (LAPSPI) have gained increasing importance in facilitating efficient and specialized dispute settlement. These institutions are expected to resolve disputes through procedures that reflect both national legal requirements and Sharia principles while minimizing lengthy litigation processes (Ramadhan et al., 2024; Marlina & Maknun, 2022; Mahpudin & Khisni, 2018; Harahap et al., 2016).

Although the Indonesian regulatory framework has provided multiple dispute resolution pathways, practical implementation continues to face several challenges. Previous studies have highlighted issues related to overlapping institutional authority, inconsistencies in dispute settlement clauses, limited public awareness regarding ADR mechanisms, and variations in judicial interpretation concerning Islamic commercial contracts. Other scholars have also emphasized that legal certainty remains an important concern following the Constitutional Court decision because parties frequently include multiple dispute resolution forums within a single contractual clause, potentially creating jurisdictional ambiguity. Furthermore, institutional capacity, professional expertise, and harmonization between national procedural law and Islamic legal principles remain important factors affecting the effectiveness of dispute resolution in Islamic banking. These challenges indicate that strengthening Alternative Dispute Resolution requires not only adequate legal regulation but also institutional development, professional competency, and greater integration between modern dispute resolution practices and the normative values of Islamic jurisprudence (Hasima, 2020; Budiastanti, 2020; Umam et al., 2024; Purnomo et al., 2024).

Beyond Indonesia, numerous jurisdictions have adopted Alternative Dispute Resolution (ADR) as a strategic instrument for resolving disputes arising from Islamic banking and finance. Malaysia is widely recognized for developing an integrated legal framework that combines statutory regulation, specialized arbitration institutions, and Sharia advisory bodies to ensure consistency between commercial practices and Islamic legal principles. Similarly, Dubai has strengthened its dispute resolution system by promoting arbitration and specialized financial tribunals that accommodate the distinctive characteristics of Islamic financial contracts. In Sri Lanka, arbitration has also been recognized as a practical alternative because it offers confidentiality, lower procedural costs, and greater flexibility than conventional court proceedings. Meanwhile, studies conducted in non-Muslim jurisdictions demonstrate that the successful resolution of Islamic finance disputes depends largely on harmonizing domestic legal systems with internationally accepted arbitration principles while maintaining compliance with Sharia requirements. These international experiences illustrate that effective dispute resolution requires not only appropriate legal provisions but also institutional specialization, procedural flexibility, and professional expertise capable of addressing the unique nature of Islamic financial transactions (Nafees & Ayub, 2016; Kawamura, 2017; Amjad & Riaz, 2023; Blanke, 2020).

The growing body of literature has substantially contributed to understanding dispute resolution mechanisms in Islamic banking. Previous studies have examined arbitration as the primary mechanism for resolving Sharia banking disputes, emphasizing its advantages in maintaining confidentiality, reducing procedural complexity, and providing binding decisions that respect contractual autonomy (Kholid, 2018; Al-Shibli, 2018). Other scholars have focused on mediation and amicable settlement based on the concept of shulh, arguing that consensus-oriented dispute resolution reflects the ethical foundations of Islamic commercial law while preserving long-term business relationships (Herawan & Athoillah, 2024; Fariana & Nugrahanti, 2022; Mashudi, 2024). Additional studies have explored the institutional roles of BASYARNAS and LAPSPI, highlighting their contribution to strengthening non-litigation dispute resolution within Indonesia's Islamic banking sector (Ramadhan et al., 2024). Furthermore, comparative legal research has examined the experiences of several countries to identify best practices in integrating arbitration with Islamic legal principles and national legal systems (White, 2020; Kawamura, 2017).

Despite these valuable contributions, several research gaps remain evident. First, many previous studies examine only one ADR mechanism, such as arbitration or mediation, without providing a comprehensive evaluation of the full spectrum of available dispute resolution methods, including negotiation, conciliation, adjudication, mediation, and arbitration. Second, existing research frequently focuses on regulatory interpretation or institutional authority while giving relatively limited attention to comparing the effectiveness of different ADR mechanisms according to the characteristics of specific Islamic banking contracts. Third, comparative discussions concerning international practices are often presented separately from analyses of Indonesia's legal framework, resulting in limited integration between domestic regulatory developments and global experiences. Finally, only a small number of studies attempt to synthesize legal theory, Islamic jurisprudence, institutional practice, and comparative evidence into a unified analytical framework that may guide future dispute resolution policies. Consequently, there remains an important opportunity to develop a more comprehensive understanding of ADR as an integrated dispute resolution system for Islamic banking contracts rather than merely as a collection of independent procedural mechanisms (Hasima, 2020; Budiastanti, 2020; Umam et al., 2024; Yanova, 2025).

The novelty of this study lies in its comprehensive analysis of Alternative Dispute Resolution as an integrated framework for resolving disputes arising from Islamic banking contracts. Unlike previous studies that concentrate primarily on arbitration, mediation, or specific legal institutions, this research systematically examines the legal foundations, institutional structures, procedural characteristics, and practical effectiveness of all major ADR mechanisms within a single analytical framework. Moreover, the study combines national legal regulations, classical Islamic dispute resolution principles, and comparative international experiences to evaluate how each ADR mechanism contributes to legal certainty, procedural efficiency, confidentiality, fairness, and Sharia compliance. This integrated perspective is expected to enrich the existing literature by providing a broader conceptual understanding of dispute resolution that accommodates both legal and religious dimensions of Islamic banking.

Based on these considerations, this study addresses three principal research questions. First, how is Alternative Dispute Resolution regulated within the legal framework governing Islamic banking contracts? Second, how effective are various ADR mechanisms in resolving disputes arising from Islamic banking contracts while ensuring legal certainty and compliance with Sharia principles? Third, what conceptual model of Alternative Dispute Resolution can be developed to strengthen dispute settlement in Islamic banking contracts by integrating legal effectiveness, institutional capacity, and Islamic legal values? Addressing these questions is expected to contribute both theoretically and practically by expanding academic discourse on Islamic banking dispute resolution and by providing recommendations for policymakers, financial institutions, legal practitioners, arbitrators, mediators, and other stakeholders involved in the continuous development of Islamic financial dispute resolution systems.

Methods

This study employed a qualitative normative legal research design to examine the implementation of Alternative Dispute Resolution (ADR) in resolving disputes arising from Islamic banking contracts. Normative legal research was selected because the primary objective of the study was to analyze legal norms, statutory regulations, legal doctrines, judicial decisions, and scholarly perspectives governing dispute resolution within the Islamic banking sector rather than to measure empirical behavior or collect statistical data. This approach enables a comprehensive examination of the legal framework regulating Islamic banking contracts while evaluating the compatibility of existing dispute resolution mechanisms with the principles of Islamic law and modern commercial dispute resolution. A qualitative research paradigm was adopted to facilitate an in-depth interpretation of legal concepts, institutional practices, and theoretical developments related to ADR in Islamic banking.

The research employed four complementary legal approaches to provide a comprehensive analysis. The first was the statutory approach, which examined the legal instruments governing dispute resolution in Islamic banking. Particular attention was given to Law Number 21 of 2008 concerning Islamic Banking, Law Number 30 of 1999 concerning Arbitration and Alternative Dispute Resolution, and Constitutional Court Decision Number 93/PUU-X/2012, all of which constitute the principal legal foundation for resolving disputes arising from Sharia banking contracts in Indonesia. These legal sources were analyzed to identify the legal authority, institutional jurisdiction, and procedural mechanisms available for dispute settlement.

The second approach was the conceptual approach, which explored the theoretical foundations of Alternative Dispute Resolution from both contemporary legal scholarship and classical Islamic jurisprudence. This approach examined the concepts of negotiation, mediation, conciliation, adjudication, and arbitration alongside the Islamic principles of shulh and tahkim. The conceptual analysis also considered broader legal principles, including legal certainty, procedural justice, efficiency, confidentiality, party autonomy, and the objectives of Islamic law (maqasid al-shariah). By integrating these theoretical perspectives, the study established an analytical framework for evaluating the effectiveness of ADR mechanisms within Islamic banking contracts.

The third approach was the case approach, which analyzed the legal implications of Constitutional Court Decision Number 93/PUU-X/2012 and other relevant legal developments influencing dispute resolution in Indonesia. Particular attention was directed toward the interpretation of dispute settlement clauses, the allocation of jurisdiction between Religious Courts and arbitration institutions, and the evolving role of specialized dispute resolution bodies such as the National Sharia Arbitration Board (BASYARNAS) and the Indonesian Alternative Institution for Banking Dispute Resolution (LAPSPI). This approach facilitated an assessment of how judicial interpretation has shaped the implementation of ADR within the national legal system.

The fourth approach was the comparative approach, which compared Indonesia's dispute resolution framework with practices implemented in other jurisdictions that have developed Islamic financial dispute resolution systems. Comparative analysis included experiences from Malaysia, Dubai, Sri Lanka, and selected non-Muslim jurisdictions that have incorporated arbitration and other ADR mechanisms into Islamic finance governance. Examining these jurisdictions provided valuable insights into institutional design, regulatory harmonization, procedural innovation, and best practices that may strengthen Indonesia's dispute resolution framework.

The study relied exclusively on secondary legal materials obtained through an extensive library research process. Primary legal materials consisted of statutory regulations, constitutional court decisions, and other official legal documents governing Islamic banking and Alternative Dispute Resolution. Secondary legal materials included peer-reviewed journal articles, academic books, book chapters, conference proceedings, dissertations, and authoritative scholarly publications discussing Islamic banking disputes, arbitration, mediation, negotiation, conciliation, judicial reform, legal certainty, and comparative Islamic finance dispute resolution. The literature selection prioritized publications with recognized academic credibility and relevance to the research objectives, while also incorporating both Indonesian and international studies to ensure a balanced and comprehensive review of existing knowledge.

Data collection was conducted through systematic document analysis. Relevant legal documents and academic publications were identified, classified, and organized according to their substantive contribution to the research questions. Each source was carefully reviewed to extract legal principles, institutional characteristics, procedural mechanisms, empirical observations, and scholarly arguments concerning Alternative Dispute Resolution in Islamic banking. The collected materials were subsequently grouped into thematic categories, including regulatory development, arbitration, mediation, negotiation, conciliation, institutional roles, comparative legal systems, judicial interpretation, and Sharia compliance. This systematic organization facilitated the integration of diverse legal perspectives into a coherent analytical framework.

The data were analyzed using qualitative legal analysis through several sequential stages. First, data reduction was undertaken to identify legal materials directly relevant to the research objectives while excluding information unrelated to dispute resolution in

Islamic banking contracts. Second, thematic classification was conducted to categorize legal sources according to specific ADR mechanisms, institutional arrangements, and legal principles. Third, normative interpretation was employed to examine the consistency between statutory regulations, judicial decisions, and Islamic legal doctrines governing dispute resolution. Fourth, comparative analysis was performed to identify similarities, differences, strengths, and limitations among dispute resolution frameworks implemented across different jurisdictions. Finally, conceptual synthesis was undertaken to integrate the findings into a comprehensive analytical model capable of explaining the role and effectiveness of Alternative Dispute Resolution in Islamic banking contracts.

To enhance the credibility and analytical rigor of the study, source triangulation was applied by comparing legal provisions, judicial decisions, and scholarly opinions from multiple authoritative references. The interpretation of legal norms was also cross-validated through comparative analysis involving domestic and international literature to minimize interpretative bias and strengthen the consistency of the findings. Rather than testing statistical hypotheses, the study emphasized analytical coherence, legal reasoning, and theoretical consistency as the principal criteria for establishing research validity. Through this methodological framework, the study provides a comprehensive legal analysis of Alternative Dispute Resolution in Islamic banking contracts while proposing an integrated conceptual perspective for strengthening dispute resolution practices in accordance with both national legal requirements and the fundamental principles of Islamic law.

Results and Discussion

The findings of this study indicate that Alternative Dispute Resolution (ADR) has become an increasingly important legal mechanism for resolving disputes arising from Islamic banking contracts. This development reflects the growing recognition that disputes involving Sharia-based financial transactions require settlement procedures that extend beyond the conventional litigation model. Unlike ordinary commercial contracts, Islamic banking agreements are governed simultaneously by national legal provisions and Islamic legal principles, creating a dual legal framework that demands specialized approaches to dispute resolution. Consequently, the effectiveness of dispute settlement depends not only on procedural compliance with statutory law but also on adherence to the ethical and contractual values embedded within Islamic jurisprudence. The analysis demonstrates that Indonesia has established a relatively comprehensive regulatory structure supporting ADR implementation, although several institutional and practical challenges continue to affect its effectiveness.

The legal foundation for resolving disputes in Islamic banking contracts is primarily established through Law Number 21 of 2008 concerning Islamic Banking, which explicitly recognizes both litigation and non-litigation mechanisms. This legal framework is further reinforced by Law Number 30 of 1999 concerning Arbitration and Alternative Dispute Resolution, which provides general procedural rules governing arbitration, mediation, negotiation, conciliation, and other consensual dispute resolution mechanisms. Together, these legal instruments provide contracting parties with the autonomy to determine the most appropriate forum for resolving future disputes while promoting procedural flexibility and efficiency. The existence of these statutory provisions reflects Indonesia's commitment to accommodating the distinctive characteristics of Islamic financial transactions without isolating them from the broader national legal system (Marlina & Maknun, 2022; Ramadhan et al., 2024).

A major institutional development influencing Islamic banking dispute resolution was the Constitutional Court Decision Number 93/PUU-X/2012. The analysis shows that this decision significantly strengthened legal certainty by clarifying the jurisdiction over disputes arising from Islamic banking contracts. Before the decision, overlapping interpretations regarding the authority of Religious Courts, District Courts, and arbitration institutions frequently generated uncertainty among contracting parties. The Constitutional Court emphasized the central role of Religious Courts in resolving Islamic banking disputes while simultaneously maintaining the parties' contractual freedom to choose alternative dispute resolution mechanisms where permitted by law. This judicial clarification substantially reduced jurisdictional ambiguity and strengthened confidence in specialized dispute resolution institutions operating within Indonesia's Islamic financial system (Harahap et al., 2016; Mahpudin & Khisni, 2018; Hasima, 2020).

The findings further reveal that ADR aligns closely with the philosophical foundations of Islamic commercial law. Classical Islamic jurisprudence encourages disputing parties to resolve conflicts through peaceful settlement rather than adversarial litigation. The concepts of shulh and tahkim have historically functioned as mechanisms for preserving justice, protecting commercial relationships, and minimizing social conflict. These principles continue to influence contemporary Islamic banking by encouraging negotiation, mediation, and arbitration before judicial intervention becomes necessary. Rather than treating ADR merely as an optional procedural alternative, Islamic legal doctrine regards consensual dispute resolution as an integral component of commercial ethics that promotes cooperation, mutual respect, and equitable outcomes. Consequently, the implementation of ADR in Islamic banking reflects both legal pragmatism and religious obligation, creating a dispute resolution model that harmonizes procedural efficiency with moral responsibility (Herawan & Athoillah, 2024).

The analysis also demonstrates that arbitration remains the most prominent ADR mechanism within Islamic banking. Arbitration offers several advantages that are particularly relevant to Sharia financial contracts. First, arbitrators may possess specialized expertise in both commercial law and Islamic jurisprudence, enabling more accurate interpretation of complex financing contracts than conventional courts. Second, arbitration proceedings are confidential, protecting sensitive financial information and preserving institutional reputation. Third, arbitral awards are final and binding, thereby reducing prolonged legal uncertainty and facilitating faster enforcement of contractual obligations. These characteristics explain why arbitration has become the preferred dispute resolution mechanism in numerous Islamic finance jurisdictions, including Indonesia, Malaysia, and Sri Lanka (Kholid, 2018; Al-Shibli, 2018; Nafees & Ayub, 2016).

Nevertheless, the findings suggest that mediation has experienced increasing recognition as an equally valuable dispute resolution mechanism, particularly for disputes involving long-term contractual relationships. Unlike arbitration, which concludes with a binding decision imposed by arbitrators, mediation emphasizes collaborative dialogue facilitated by an independent mediator who assists parties in reaching a mutually acceptable agreement. This approach is highly compatible with the Islamic principle of islah, which prioritizes reconciliation and social harmony over adversarial competition. Mediation not only reduces procedural costs and settlement time but also preserves business relationships that are essential within Islamic banking, where repeated contractual interactions frequently occur between financial institutions and customers. Recent studies further indicate that mediation may improve voluntary compliance because negotiated settlements are generally perceived as fairer than externally imposed judgments. Consequently, mediation complements arbitration by providing a flexible dispute resolution mechanism suitable for disputes that require continuing commercial cooperation rather than definitive legal adjudication (Fariana & Nugrahanti, 2022; Mashudi, 2024; Ramadhani et al., 2021).

Overall, these findings demonstrate that Indonesia's legal framework has established a solid normative foundation for implementing Alternative Dispute Resolution in Islamic banking contracts. The combination of statutory regulation, judicial clarification, and Islamic legal principles has created multiple pathways for resolving disputes outside conventional litigation while maintaining legal certainty and Sharia compliance. However, the effectiveness of these mechanisms ultimately depends on institutional capacity, professional competence, and the willingness of contracting parties to utilize ADR as the primary avenue for dispute settlement. These practical dimensions provide the basis for evaluating the comparative effectiveness of individual ADR mechanisms, which is discussed in the following section.

The analysis demonstrates that the effectiveness of Alternative Dispute Resolution (ADR) in Islamic banking contracts cannot be assessed solely by examining the existence of legal regulations. Instead, effectiveness depends on the interaction between legal certainty, institutional capacity, procedural efficiency, Sharia compliance, and the willingness of disputing parties to pursue consensual settlement. The findings indicate that each ADR mechanism possesses distinctive procedural characteristics and practical advantages that make it suitable for different categories of disputes. Consequently, no single dispute resolution mechanism can be regarded as universally applicable for all Islamic banking conflicts. Rather, the selection of an appropriate mechanism should consider the complexity of the contractual relationship, the economic interests involved, the need for confidentiality, and the parties' intention to preserve future commercial cooperation.

Negotiation represents the most fundamental ADR mechanism because it allows disputing parties to communicate directly without third-party intervention. The findings suggest that negotiation is particularly effective during the early stages of contractual disputes involving payment delays, misunderstandings concerning contractual obligations, or disagreements regarding financing restructuring. Since negotiation is voluntary and informal, it minimizes procedural expenses while enabling both parties to maintain control over the outcome. From the perspective of Islamic commercial law, negotiation reflects the values of cooperation, mutual consent, and good faith that underpin contractual relationships. Although negotiation does not guarantee settlement, it often serves as an essential preliminary stage before disputes proceed to mediation or arbitration. The literature consistently emphasizes that early negotiation may significantly reduce the financial and reputational costs associated with prolonged legal proceedings while preserving trust between Islamic financial institutions and their customers (Herawan & Athoillah, 2024).

When direct negotiation fails to produce an agreement, mediation offers a more structured yet cooperative dispute resolution process. Unlike litigation, mediation encourages the parties to identify mutually beneficial solutions through facilitated dialogue rather than adversarial argumentation. The present analysis indicates that mediation is particularly appropriate for disputes involving long-term financing contracts, profit-sharing arrangements, and continuing business relationships where maintaining future cooperation remains commercially important. Mediators do not impose binding decisions but instead facilitate communication, clarify misunderstandings, and encourage compromise based on the interests of both parties. This characteristic closely corresponds with the Islamic concept of shulh, which prioritizes reconciliation and social harmony over confrontation. Furthermore, mediation generally requires less time and fewer financial resources than judicial proceedings, making it an attractive option for financial institutions seeking efficient dispute settlement while preserving customer relationships. Recent studies also suggest that mediated agreements achieve higher levels of voluntary compliance because the resulting settlements are jointly constructed rather than externally imposed (Fariana & Nugrahanti, 2022; Mashudi, 2024; Ramadhani et al., 2021).

Arbitration remains the most developed and institutionally recognized ADR mechanism within Islamic banking. The findings indicate that arbitration is particularly effective for disputes involving complex contractual interpretation, substantial financial claims, and technical issues requiring specialized expertise in both commercial law and Islamic jurisprudence. Unlike judges in ordinary commercial courts, arbitrators may be selected based on their knowledge of Islamic finance, enabling more accurate interpretation of Sharia-compliant contracts. Arbitration also provides procedural confidentiality, an important consideration for banking institutions seeking to protect sensitive commercial information and institutional reputation. In addition, arbitral awards possess final and binding legal force, thereby reducing prolonged uncertainty and limiting opportunities for repetitive litigation. These characteristics explain why arbitration has become a preferred mechanism for resolving Islamic banking disputes in Indonesia and many other jurisdictions that have developed specialized Islamic financial institutions (Kholid, 2018; Al-Shibli, 2018; Nafees & Ayub, 2016; White, 2020).

Despite these advantages, the findings also reveal several challenges affecting the practical implementation of ADR. One persistent issue concerns the limited public understanding of available dispute resolution mechanisms. Many customers remain unfamiliar with the legal consequences of ADR clauses included in Islamic banking contracts, resulting in a continued preference for litigation despite the availability of more efficient alternatives. Institutional capacity also varies considerably among dispute resolution providers. Specialized institutions such as BASYARNAS and LAPSPI have demonstrated significant potential in handling Islamic banking disputes; however, their effectiveness depends on the availability of qualified arbitrators, mediators, administrative support, and institutional resources. Previous studies further identify inconsistencies in contractual drafting, particularly where multiple dispute resolution forums are simultaneously designated within a single agreement. Such inconsistencies may generate jurisdictional uncertainty and delay dispute settlement despite the existence of clear statutory regulations (Ramadhan et al., 2024; Mahpudin & Khisni, 2018; Hasima, 2020; Umam et al., 2024).

Comparative analysis further strengthens these findings by demonstrating that successful implementation of ADR depends not only on legislative reform but also on institutional maturity and professional specialization. Malaysia has developed an integrated framework linking arbitration institutions, Sharia advisory bodies, and judicial supervision, thereby creating greater consistency in resolving Islamic finance disputes. Dubai similarly emphasizes institutional specialization through dedicated financial dispute resolution mechanisms that accommodate Islamic commercial transactions. In contrast, countries with less developed institutional frameworks often experience greater procedural uncertainty despite having statutory recognition of arbitration and mediation. These international experiences suggest that Indonesia's regulatory foundation is already relatively comprehensive, but continued institutional strengthening remains essential to improve procedural efficiency, professional competence, and public confidence in ADR. Consequently, the effectiveness of Alternative Dispute Resolution should be understood as the product of coordinated interaction between legal regulation, institutional development, professional expertise, and adherence to Islamic legal principles rather than the existence of legislation alone (Kawamura, 2017; Amjad & Riaz, 2023; Yanova, 2025; Purnomo et al., 2024).

Overall, the findings confirm that negotiation, mediation, and arbitration each contribute distinct strengths to the dispute resolution framework governing Islamic banking contracts. Their combined application provides a flexible and comprehensive system capable of accommodating diverse contractual disputes while maintaining legal certainty, commercial efficiency, and compliance with Sharia principles. Nevertheless, maximizing these benefits requires continuous regulatory refinement, institutional capacity building, standardized contractual drafting, and enhanced public awareness regarding the practical advantages of Alternative Dispute Resolution. These observations form the basis for developing an integrated conceptual model of ADR in Islamic banking, which is presented in the following section.

The findings of this study indicate that the future development of dispute resolution in Islamic banking should move beyond viewing Alternative Dispute

Resolution (ADR) as merely an alternative to litigation. Instead, ADR should be positioned as an integrated dispute resolution framework that combines legal certainty, institutional effectiveness, commercial efficiency, and compliance with Islamic legal principles. The analysis demonstrates that Islamic banking contracts possess unique legal and ethical characteristics that require dispute resolution mechanisms capable of accommodating contractual flexibility while maintaining justice and preserving long-term commercial relationships. Consequently, an integrated ADR framework provides a more appropriate response to the multidimensional nature of Islamic banking disputes than reliance on a single dispute resolution mechanism.

The proposed conceptual model developed from this study emphasizes a multi-tiered dispute resolution process in which each ADR mechanism functions according to the complexity and characteristics of the dispute. The first stage consists of direct negotiation between the contracting parties immediately after a dispute arises. Negotiation serves as the least formal mechanism and enables parties to clarify misunderstandings, renegotiate contractual obligations, or restructure financing arrangements without external intervention. If negotiation fails to produce an agreement, mediation becomes the second stage, allowing an independent mediator to facilitate communication and encourage mutually acceptable solutions while preserving business relationships. Should mediation also prove unsuccessful, arbitration becomes the final ADR mechanism, providing a legally binding decision delivered by arbitrators possessing expertise in both commercial law and Islamic jurisprudence. Litigation before the Religious Court should therefore function as the last available option when ADR mechanisms cannot effectively resolve the dispute or where statutory requirements necessitate judicial intervention. This sequential framework reflects both procedural efficiency and the Islamic legal preference for peaceful settlement before adversarial adjudication (Herawan & Athoillah, 2024; White, 2020).

The analysis further demonstrates that institutional collaboration constitutes a critical component of an effective ADR framework. Islamic banking dispute resolution should not rely solely on individual institutions operating independently but instead require systematic coordination among Islamic banks, BASYARNAS, LAPSPI, Religious Courts, financial regulators, and Sharia supervisory authorities. Each institution performs complementary rather than competing functions. Financial institutions should improve contractual drafting by incorporating clear and consistent ADR clauses that eliminate jurisdictional ambiguity. BASYARNAS should continue strengthening arbitration services through professional certification, procedural standardization, and enhanced administrative capacity. LAPSPI should expand mediation services capable of resolving disputes efficiently before arbitration becomes necessary. Religious Courts should maintain their supervisory judicial function while respecting valid ADR agreements concluded by contracting parties. Such institutional coordination would significantly strengthen legal certainty and reduce procedural duplication throughout the dispute resolution process (Ramadhan et al., 2024; Mahpudin & Khisni, 2018).

Another important finding concerns the need to strengthen professional competency among individuals directly involved in Islamic banking dispute resolution. Effective implementation of ADR depends not only on legal provisions but also on the availability of arbitrators, mediators, legal practitioners, and judges possessing interdisciplinary expertise. Professionals responsible for resolving Islamic banking disputes should demonstrate comprehensive knowledge of Islamic commercial jurisprudence, national banking regulations, commercial contract law, financial practices, and ADR procedures. The comparative analysis indicates that countries such as Malaysia have invested substantially in professional specialization through institutional training, certification systems, and close cooperation between legal and Sharia experts. Indonesia may benefit from adopting similar strategies by expanding professional education programs and strengthening institutional partnerships between universities, financial regulators, arbitration institutions, and Islamic banking practitioners. Improved professional competency would enhance both the quality and consistency of dispute resolution outcomes while increasing public confidence in ADR institutions (Kawamura, 2017; Nafees & Ayub, 2016).

The findings also reveal that greater public awareness represents an essential prerequisite for maximizing the effectiveness of Alternative Dispute Resolution. Although Indonesian legislation provides multiple avenues for resolving Islamic banking disputes, many customers remain unfamiliar with the legal consequences of ADR clauses or the procedural advantages offered by mediation and arbitration. This limited awareness often results in unnecessary litigation, increasing both financial costs and procedural delays. Islamic banking institutions should therefore strengthen customer education by clearly explaining dispute resolution provisions during contract formation, providing accessible information regarding available ADR mechanisms, and promoting dispute prevention through transparent communication. Public legal literacy concerning ADR would encourage informed contractual decision-making while reducing future jurisdictional disputes arising from misunderstanding of contractual provisions (Marlina & Maknun, 2022; Hasima, 2020; Budiastanti, 2020).

From a theoretical perspective, this study contributes to the literature by integrating modern Alternative Dispute Resolution theory with classical Islamic dispute resolution principles within a single analytical framework. Previous studies have generally examined arbitration, mediation, institutional authority, or comparative legal systems independently. In contrast, the present study demonstrates that these elements should be interpreted as interconnected components of a comprehensive dispute resolution system. The integration of negotiation, mediation, arbitration, institutional governance, statutory regulation, judicial interpretation, and Sharia principles provides a broader understanding of how Islamic banking disputes may be resolved effectively without sacrificing either legal certainty or religious legitimacy. This integrated perspective also supports the achievement of the objectives of maqasid al-shariah, particularly the protection of wealth, justice, contractual fairness, and social harmony, while simultaneously accommodating the practical demands of modern financial transactions (Yanova, 2025).

Overall, the findings confirm that Alternative Dispute Resolution constitutes the most appropriate framework for resolving disputes arising from Islamic banking contracts because it balances procedural efficiency, legal certainty, commercial practicality, and compliance with Islamic legal principles. Nevertheless, the long-term success of ADR depends upon continuous legal reform, institutional strengthening, professional capacity development, standardized contractual practices, and broader public understanding of non-litigation dispute resolution. By integrating these elements into a coherent and sequential framework, Islamic banking institutions will be better positioned to resolve disputes efficiently while maintaining public trust, protecting contractual relationships, and supporting the sustainable development of the Islamic financial sector. The proposed conceptual model therefore provides both a theoretical contribution to the academic discourse on Islamic banking dispute resolution and practical guidance for policymakers, regulators, dispute resolution institutions, and financial practitioners seeking to improve the effectiveness of ADR within contemporary Islamic banking systems.

Conclusion

This study demonstrates that Alternative Dispute Resolution (ADR) provides an effective and comprehensive framework for resolving disputes arising from Islamic banking contracts. The analysis shows that ADR mechanisms, including negotiation, mediation, and arbitration, offer greater procedural flexibility, efficiency, confidentiality, and preservation of commercial relationships than conventional litigation. These mechanisms are also consistent with the principles of Islamic law, particularly the values of justice, mutual agreement, reconciliation, and the protection of contractual rights. Indonesia has established a solid legal foundation for ADR through its statutory regulations and institutional framework, supported by specialized dispute resolution bodies that facilitate the settlement of Islamic banking disputes. However, the effectiveness of ADR depends not only on legal provisions but also on institutional capacity, professional competence, standardized contractual drafting, and public awareness of non-litigation dispute resolution mechanisms. The proposed integrated ADR model emphasizes a sequential process beginning with negotiation, followed by mediation, arbitration, and litigation only as a final option. Such an approach strengthens legal certainty while maintaining compliance with Sharia principles and promoting sustainable commercial relationships. Therefore, continuous regulatory improvement, institutional strengthening, and capacity building are essential to enhance the effectiveness of ADR and support the sustainable development of the Islamic banking industry.

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