
Foreword

Most human beings place a very high value on security of income and work: we all seek the comfort of recourse to some form of support if calamitous events occur, such as work injury, ill health, or poverty in old age. It is important to reflect these human priorities in national policy objectives. In Indonesia, these issues have been debated for several decades, going back to the 1960s when the various national development plans laid out a vision of sharing the gains from rapid economic growth with the wider population. The ideas have taken root and were enshrined in an amendment to the Constitution in 2002. But the institutions for social security remain rudimentary, if not at a crossroad.

In terms of ideas, or rather ideals, Indonesia's National Social Security System Law of 2004 represents a social aspiration—namely, to provide all Indonesians with coverage under a comprehensive system of insurance and assistance spanning pensions, work injury, health insurance, old-age savings, and death benefit. The challenge is to transform this aspiration into a framework that judiciously and fairly embodies the principles of assistance for the needy and insurance for those who are able to pay. To be sustainable, the system, as a whole, must be cost effective, with the collected contributions sufficient to pay promised benefits. The precise combination of insurance and assistance will reflect, of course, the social values and goals of nation and society.

As the studies in this report detail, the existing social-security-related programs are costly and provide only limited protection to those covered. There are also issues related to their governance and management. Together, these features pose formidable challenges to the successful implementation of the National Social Security System Law. Relatively low-income levels and labor productivity constrain contribution rates and argue for redistributive policies. Yet such policies would place possibly intolerable pressures on the budget while preventing the emergence of a sustainable social security system. The administrative capacity for managing an integrated system needs to be built as does a public accountability mechanism that will ensure transparency in the management of the system.

These remain difficult issues. From this perspective, this report seeks to illuminate the nature of the challenges in terms of the expected fiscal costs of alternative arrangements assuming a variety of macroeconomic, indexing, and demographic scenarios. The report also suggests how existing schemes could be integrated under the National Social Security System Law. The goal is not to offer settled answers to all the issues, but rather to support the informed debate needed to establish a key national institution—one that has profound implications for intergenerational equity and fiscal balance.

The Asian Development Bank (ADB) has supported social security reform in Indonesia through technical assistance and adjustment loans since 1999. In continuation of this support, the studies in this report were prepared by the Southeast Asia Department of ADB under the supervision of Jaseem Ahmed, Director, Governance, Finance and Trade Division (SEGF). The Task Leader was Michiel Van der Auwera, Social Security Specialist (SEGF), who is also a co-author of some of the studies. The bulk of the analysis, and all of the fiscal and actuarial work, was carried out by Mitchell Wiener, Consultant. A major role was also played by the Indonesia Resident Mission of ADB, especially by Ramesh Subramaniam, who supported the SEGF team through his extensive knowledge of Indonesia and this sector. Sukanya Wignaraja edited the report in its entirety. I am grateful for the secretarial assistance provided by Jenelyn Mendez.

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Executive Summary

Introduction

The Government of Indonesia faces a challenging period in reforming its national social security system. Currently, social security is provided through a series of programs that have developed separately from each other. The Asian financial crisis that hit the region in 1997 revealed the weaknesses of the existing system, leaving a large part of the population unprotected and providing only limited protection to those who were covered.

In response to the crisis, legislative reforms have been introduced to be better prepared in the future. In 2002, the Government of Indonesia amended the Constitution regarding the extension of social security to the entire population. The 1945 Constitution (Second Amendment) Article 28H, Subsection 3, states: "Every person shall have the right to social security in order to develop oneself as a dignified human being", and Article 34, Subsection 2, states: "The state shall develop a social security system for all the people and shall empower the vulnerable and poor people in accordance with human dignity".

On 19 October 2004, Indonesia enacted the National Social Security System Law (*Sistem Jaminan Sosial Nasional/ SJSN law*). This law will create a social security system covering all Indonesian workers and their dependents in both the formal and informal economy. Implementation of this law will be a major challenge. These programs will affect all Indonesians, involve multiple government ministries and institutions, create new permanent fiscal obligations for the State budget, and require the strengthening of existing institutions and IT systems.

Until the system proposed under the SJSN law is implemented, it is fair to say that Indonesia does not have a real social security system, although a number of workers are covered by health and old-age programs. The coverage, however, is very limited and, most of the time, the schemes do not deliver a sufficient level of income protection or quality of services.

Current social security system in Indonesia

The provision of social security is a shared responsibility between the State, employers, individuals, and families. In Indonesia, as in most other Asian countries, there is a strong reliance on the extended family and the community to provide support in case of illness, loss of income, or other unforeseen events. About two thirds of the population work in the informal sector and rely almost entirely on these informal mechanisms.

For the private sector, there is a strong reliance on employer's liability provisions and, to a lesser extent, on social insurance programs organized on a public and/or private basis. Private sector employers pay between 21% and 27% of the total cost of employees on social security programs, severance pay, and private health insurance. In exchange, private sector workers receive limited protection, especially in old age. This is because the lump sum payments that are provided by the severance pay and the old-age savings benefit are consumed early on and do not provide any form of financial security in retirement.

The public sector can fall back on an integrated package of benefits. While the level of protection provided under the public sector pension scheme is high, the concerns are of a different nature. The government allocates close to 5% of the central government budget to finance social security programs for the civil servants, a share that is increasing every year. One of the main concerns is the unfunded pension liability that was already accrued and is growing every year. On 1 January 2000, the unfunded liability of the public servants' pensions program was estimated at Indonesian rupiah (Rp)342 trillion.

The social health insurance programs for both civil servants and private sector workers are perceived as providing poor-quality services, resulting in members paying out-of-pocket for health services outside the system. In the case of private sector workers, many opt out and purchase private health insurance. Askeskin, the health

insurance program for the poor and near-poor, does make a difference for the target group, but still has considerable problems with targeting and with the quality of service delivery. In addition, it is underfunded on per capita basis.

Overall, social security coverage is rather limited. Only about 12% of the total workforce is entitled to pension and/or old-age benefits, while about 40% of the population is currently entitled to health insurance, covering formal sector workers under compulsory health programs and poor informal sector workers under the Askeskin program.

The social security institutions managing these programs face problems in almost all operational areas, including poor compliance; expensive and ineffective administration; poor governance structure lacking transparency, accountability, and focus on members' interests; complex and ineffective supervisory structure; and poor member service.

The SJSN Law

The SJSN law is a framework law. It outlines the basic structure of the reformed social security system, but does not specify details. Major strategic policy options, amounts of benefits, and contribution rates still need to be determined by regulations. The SJSN law provides for coverage of the entire Indonesian population with five separate programs: (i) pensions, (ii) old-age savings, (iii) health insurance, (iv) employment injury, and (v) death benefit. All these programs are to be administered by the four existing social security institutions. In addition, the law provides for the creation of a SJSN Council as the policy-making body responsible for running the SJSN system. There is a different contribution structure for formal and informal sector workers, with the government paying for the poor.

The ADB project prepared an initial fiscal analysis based on reasonable assumptions to illustrate the order of magnitude of program costs. In the case of pensions, the assumptions are that the pensioner would be entitled to a flat-rate pension equivalent to Rp200,000 per month in 2007, from age 60 onwards, with wage indexing following the retirement. In case of old-age savings, the contribution is set at 5.7% of income. The health program follows the benefit package for civil servants.

The total cost of these three programs is projected to grow from 2.88% of gross domestic product (GDP) in 2010 to 11.02% of GDP in 2070. The primary factors affecting the increase in costs as percentage of GDP are (i) the 15 years qualifying period for pensions, meaning that pensions will only be paid from 2022 onwards; (ii) the gradual phasing in of the health care costs; and (iii) the population aging

that will affect both the number of pensioners and the cost of health care. The government contribution for the poor and the financially disabled is projected to grow from 0.53% in 2010 to 3% in 2070.

SJSN Implementation Issues

The SJSN law describes a new concept for social security in Indonesia. For fiscal and administrative reasons, it will take a considerable period of time to fully introduce the new social security structure. Coverage must be gradually expanded in a way that is fiscally affordable. In addition the legal structure, administrative systems, health care infrastructure, and institutions necessary to manage the SJSN system are not yet in place. Indonesia also needs to change the legal structure of the existing social insurance administrators and improve overall governance to protect the interests of fund members.

The improvement of the existing system and the gradual implementation of SJSN is a long-term process, covering different phases. The first phase, taking place during the initial years of reform, includes the policy debate and the preparation of the system design. During the second phase, taking place over the medium term, the focus is on institutional development, capacity building, and construction of new administrative systems. In the long run, SJSN coverage can be gradually extended to the entire population. Based on worldwide experiences, this phase lasts the longest and can take up to 25 years for full implementation.

The first step in any social security reform is to fix the current system before making other changes. The four existing social security institutions—PT Jamsostek, PT Taspen, PT Asabri, and PT Askes—are the foundation of the current system and retain a critical role under SJSN. If these institutions are weak, the current system will continue to function poorly and the new system will not function well either. The legal structure of the four administrators has to be changed from *perseros* (for-profit entities responsible to their shareholders [the government]) into trust funds (not-for-profit entities managing the funds in the best interest of the participants). The overall governance structure of the administrators needs to be improved, including a more effective regulatory and supervisory structure.

In order to introduce the new SJSN, the SJSN Council will have to be created, and the role of the existing social security institutions in the new setting will have to be determined. The law does not provide the required details needed to evaluate the fiscal costs of any of the proposed programs. The benefit programs and contribution levels

will have to be determined based on fiscal projections. In addition, other strategic policy options will have to be specified. As the last step in the process, the regulations and decrees will have to be drafted, reflecting the decisions reached during the preparatory design period. All reform will need to be clearly communicated to the different groups involved, so that the benefits and administrative structure of the new system are fully understood and appreciated.

The project prepared an SJSN implementation road map as a guideline for the Government of Indonesia to sequence the actions to reform the existing social security system and to gradually introduce SJSN. The road map requires discussions with the government in order that it can be further refined and adjusted to the institutional and political reality.

Conclusion

SJSN is a progressive law providing the entire Indonesian population with social protection through social security funds. It is a complex undertaking that will have a significant impact on every Indonesian. It will also affect a wide range

of government ministries and institutions and will create significant coordination challenges. It is essential to involve all stakeholders and build maximum possible consensus on how to move forward.

Experience from other countries shows that one of the keys to successful social security reform is political support from the highest levels and the presence of a reform champion to lead and sustain the effort on a daily basis. In Indonesia, the key first steps for successful SJSN design and implementation include

- creation of the SJSN Council,
- appointment of a coordinator in the Ministry of Finance and other key ministries, and
- identification of a champion to lead reform on a daily basis.

We look forward to assisting the government with the design of SJSN that will truly meet the needs of all Indonesians at an acceptable cost and developing a road map for staged implementation of the reformed system.

Table of Contents

Foreword	iii
Executive Summary	v
Abbreviations	xi
Design, Fiscal Analysis, and Implementation of the National Social Security System	1
I. Introduction	3
II. Current Social Security System in Indonesia	4
III. Trends Affecting Social Security	11
IV. The SJSN Law	12
V. SJSN Harmonization Issues	16
VI. SJSN Implementation Steps and Timeline	22
VII. Conclusion	25
Assessment of Fiscal Cost of Social-Security-Related Programs in Indonesia	29
I. Introduction	31
II. Update of Indonesia's economic situation	31
III. Overview of existing social-security-related programs	32
IV. Cost of existing social-security-related programs	36
V. Financial performance of the pension funds	40
VI. Fiscal analysis of Existing Pension Programs	42
VII. Fiscal Management of Pension Programs: An International Perspective	44
VIII. National Health Insurance System	51
IX. Indonesia's Decision Process and Road map for Reform	55
Estimated Cost of Pensions, Old-Age Savings, and Health Insurance under the National Social Security System Law	59
I. Introduction	61
II. Population and Labor Force Projections	62
III. Pension Program	65
IV. Old-Age (Savings) Benefit	69
V. Severance Pay Program	73
VI. Health Insurance Program	74
VII. Summary	78
Governance Assessment of the Social Security Organizations in Indonesia	79
I. Introduction	81
II. Existing Institutional Structure	82
III. Alternative Institutional Structures	91
IV. Stakeholder Assessment	93
V. Good Governance for Pension Plans	99
VI. Governance of the Asset Management Process	101
VII. Special Governance Issues for Public Plans	102
VIII. The Governance Structure	103
IX. Fiscal Management of Defined Contribution Pension Programs	108
X. Fiscal Management of Defined Benefit Pension Programs	115

x Preparatory Studies on National Social Security System in Indonesia

XI.	International Examples	116
XII.	Strengthening Pension Regulation	121
XIII.	Summary	122

Abbreviations

ADB	–	Asian Development Bank
APBN	–	State Budget (Anggaran Pendapatan Belanja Negara)
Asabri	–	Pension Scheme for the Armed Forces (Asuransi Angkatan Bersenjata Republik Indonesia)
Askes	–	Indonesia Health Insurance (Asuransi Kesehatan Indonesia)
Askeskin	–	Health Care Scheme for the Poor (Asuransi Kesehatan untuk Keluarga Miskin)
Bapepam LK	–	Capital Market Supervisory Agency and Financial Institutions
BI	–	Central bank (Bank Indonesia)
BLU	–	non-profit organization (Bayan Layanan Umum)
BPJS	–	Social Security Administrative Body (Badan Penyelenggara Jaminan Sosial)
CMPM	–	Cost per member per month
CPF	–	Central Provident Fund
CPP	–	Canada Pension Plan
CPPIB	–	Canada Pension Plan Investment Board
DJSN	–	National Social Security Council (Dewan Jaminan Sosial Nasional)
DPLK	–	Financial Institution Pension Fund (Dana Pensiun Lembaga Keuangan)
DPPK	–	Occupational Employer Pension Fund (Dana Pensiun Pencari Kerja)
EPF	–	Employee Provident Fund
EPS	–	Employee Pension Scheme
GMOP	–	General Meeting of Participants
GPF	–	Government Pension Fund
HMO	–	Health Maintenance Organization
ILO	–	International Labour Organization
Jamsostek	–	Private Sector Social Security System (Jaminan Sosial Tenaga Kerja)
JHT	–	Jamsostek Old-Age Program (Jaminan Hari Tua)
JKK	–	Jamsostek Employment Injury Program (Jaminan Kecelakaan Kerja)
JKM	–	Jamsostek Death Grant Program (Jaminan Kematian)
JPK	–	Basic health care package (Jaminan Pemeliharaan Kesehatan)
JPKM	–	Community Health Maintenance Protection (Jaminan Pemeliharaan Kesehatan Masyarakat)
JPS	–	Social Safety Net Program (Jaringan Pengaman Sosial)
MOF	–	Ministry of Finance
MOH	–	Ministry of Health

MOM	–	Ministry of Manpower
MPFA	–	Mandatory provident fund authority
MSA	–	Ministry of State Apparatus
MSOE	–	Ministry of State-Owned Enterprises
NBFI	–	Non-bank financial institutions
NPS	–	New Pension Scheme
OAP	–	Old-age pension
OJK	–	Financial Services Authority (Otoritas Jasa Keuangan)
Persero (PT)	–	State-owned limited liability company (Perseoran Terbatas)
PKPS-BBM	–	Compensation for Fuel Subsidy Reduction Programs (Program Kompensasi Pengurangan Subsidi Bahan Bakar)
PMPM	–	Premium per member per month
PPI	–	Investment management guidelines (Pedoman Pelaksanaan Investasi)
ROI	–	Rate of return
SJSN	–	National Social Security System (Sistem Jaminan Sosial Nasional)
SSO	–	Social Security Office
Taspen	–	Pension Scheme for Civil Servants (Tabungan dan Asuransi Pegawai Negeri)
THT	–	Taspen Old-Age Savings Program (Tabungan Hari Tua)
TSP	–	Thrift Savings Plan