Civil Service and Military Pension Reforms in

Indonesia, Malaysia and Singapore

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Preliminary Draft: January 10, 2011

DO NOT CITE

Paper prepared for workshop on Civil Service and military Pension Arrangements in selected countries of the Asia Pacific, Hitotsubashi Centre Tokyo, January, 20-21, 2011

I. Rationale for Civil Service and Military Pension Reform

The 2008 Global Crisis and demographic trends in Indonesia, Malaysia, and Singapore has increased the urgency of reforming their pension systems for enhancing financial, fiscal, and economic sustainability over a long period, and mitigating possible adverse economic impacts. As national and international mobility of labor becomes more pronounced, the implications of superior pension benefits for civil servants and the military personnel as compared to private sector workers merit review.

The civil service and military pensions in these countries have been among the least transparent, their governance structure exhibit conflict of interest, with the beneficiaries designing, implementing, and assessing their own pension benefits. Moreover, as the pension expenditure is a statutory expenditure, it has the first claim over future government revenue as well. This suggests that regardless of the future performance of the economy and the capacity of tax payer to bear the pension expenditure of civil servants and the military, the pension benefits to them will continue. The risk therefore is not borne by the beneficiaries (civil servants and military personnel).

The risk therefore is not borne by the beneficiaries (civil servants and military personnel). This raises the issue of equitable sharing of risk within a given generation and amongst generations. Investment management of civil service and military pension funds is undertaken separately from that of the private sector employees. There is therefore merit in examining these pension systems for addressing the issues raised by the above characteristics.

This paper is organized as follows. Section II provides an overviews of the pension arrangements for civil servants and military personnel in all three countries. Section III offers broad reform directions that apply to all sample countries, and followed by specific policy recommendations for each country.

II. Civil Servants and Military Pension Arrangements: An Overview

(Insert Figure 1)

Indonesia

The Civil Service pensions governed under law 11 of 1969. Pensions are for life, and cover survivors as well. The pensionable age is 56(50 with 20 years of service). Civil servants also are provided Life and endowment Insurance (known as THT). It pays lump-sums at death or termination. Under labor Law 13, there is also statutory termination of payments.

PT Taspen is a non -licensed and unregulated state insurance company that underwrites the THT program. The MOF of Indonesia has outsourced to PT Tapsen administration of the Civil Service Pension Program. But PT Tapsen has no financial responsibility for the program. As a result, PT Tapsen's financial statements reflect Its core activities, with Civil Service Pension activities relegated to the notes. The contribution rate is 4.75 percent by the members; the rest by the government as an employer.

The employee contributions are however accumulated in a PT Tapsen account, with no clear financing plan. In effect, therefore, government bears 100 percent of the civil service pension costs. As there is no pre-funding, these expenditures are met from budget. Guerard (2010) estimates that the total cost of pensions for the civil servants to the government are equivalent to 28.4% of the pensionable wage. The percentage is lower if full wage, including fringe benefits, is considered.

The accrual rate for pensions is 2.5%, with a maximum of 75%.The 2010 Budget of Indonesia(Table VI.17,Page 67) indicates actual pension expenditure of 0.74 percent of GDP in 2009; and projects 0.01 percent of GDP for 2010.This is a moderate amount, and is likely to be sustainable. The total coverage of civil servants pension as at December 2009 is estimated at 4.52 million, of which 45.6 percent are women (Table 1).

56.2 percent of men, and 54.9 percent of women are in the 36-50 age group. This suggests considerable future pension liabilities, given current provisions. The Decentralization law of 2000 has transferred responsibility of Civil Servants employed at lower levels to these jurisdictions. But liabilities for pensions at decentralized levels are unclear. If it is at a lower level, wide divergences in pension benefits may occur, and this may have broader fiscal, civil service efficiency and other implications.

The civil servants investment portfolio comprises estimated balances with PT Taspen(which remain unutilized for paying pensions). The total assets at end 2008 were RP19.65 trillion (0.036 percent of GDP; 0.56 percent of annual benefits)(Guerard, 2010). The return on invested assets in 2008 was 9.12 percent, lower than the inflation rate of 11.1 percent; and about the same as yield on Central Bank Certificates (9.2percent) (Guerard, 2010). Law No 40 of 2004 (Known as SJSN Law) envisages five different mandatory social insurance programs covering the entire population. The programs involve Pensions, Old -Age savings, Health, Workers Compensation, and Death Benefits. It provides a framework, but leaves financing and other details for a later stage. The Pensions will also be based on Social Insurance principles, and will be DB type, based on final pay. If implemented, current differential treatment between Civil Servants and military on the one hand, and the private sector workers on the other would narrow drastically or disappear all together. The 2004 Law has not yet been implemented, though limited progress in initiating the process has been observed. But there however does not seem to be urgency in implementing it.

The Draft White Paper by Weiner (2009) suggests a defined benefit pension equal to 0.5 percent of final pay per year of contribution, providing a replacement ratio of 20 percent for 40 year career. The retirement age was to increase to 60, and then gradually to 65 by the year 2047. These suggestions are yet to be accepted.

Table 1-Distribution of Civil Servants in 2009

Table 1

Distribution of Civil Servants by Age Group and Sex December 2009					
Age Group	Males	%	Females	%	Total
18 - 20	1,264	0.1	1,166	0.1	2,430
21 - 25	71,794	2.9	100,065	4.8	171,859
26 - 30	202,561	8.3	252,296	12.2	454,857
31 - 35	251,927	10.3	261,641	12.8	516,468
36 - 40	343,813	14.0	326,510	15.8	670,323
41 - 45	491,118	20.0	415,495	20,1	906,613
46 - 50	544,325	22,2	392,258	19.0	936,583
51 - 55	438,773	1.9	228,403	11.0	667,176
56 - 60	105,507	4.3	86,602	4.2	192,109
61 - 65	3,894	0.2	1,434	0.1	5,328
65+	293	0	66	0	359
	-				
Total	2,455,269	100	2,068,936	100	4,524,205

Source: As cited in Guérard (2011). The original source is National Civil Service Agency; *www.**bkn**.go.id/*

Table 2

Civil Service Investment Portfolio

Civil Service Pensions Investment Portfolio End of 2008		
Type	Rp million	%
Term Deposits	7,691,730	39.14%
Bonds	11,114,868	56.55%
Direct investments	50,610	0.26%
Deposits on call	2,101	0.01%
Cash	113	0.00%
Balance	793,900	4.04%
Total	19,653,322	100.00%

Guérard (2010)

Malaysia:

Civil Service Pension Scheme: The civil servants are members of a DB (Defined Benefit) pension scheme financed from the annual government budget. In 2008, there were

1.24 million civil servants in Malaysia, equivalent to 11 percent of the labour force, and 4 percent of the total population (Ong and Hamid, 2010). They report that the total number of pensioners in 2008, including those receiving survivors pensions, was 0.51 million, equivalent to 41.1 percent of the civil servants; and pension costs were RM 8.4 billion, equivalent to 1.2 percent of 2008 Gross National income (GNI).

The current retirement age is 58 years, clearly too low for the life expectancy at 60, which as noted in Section II, was 17.2 years for males, and 19.6 years for females in 2005. The demographic profile and life expectancy of the civil servants may differ from the population averages, and this will need to be considered in design and in assessing financial and fiscal sustainability of civil service pension schemes.

A minimum of 10 years of service is required to be eligible. The pension benefit levels vary between 20 and 60 percent of last drawn basic pay (which excludes allowances), depending on the length of service. There is provision for survivors' pension; and for those who get injured or meet death during service. The pension benefits are not indexed to prices, but are revised periodically when salary revision of existing civil servants is undertaken. Civil servants are currently not required to contribute for their pension benefits.

In addition to pensions, civil servants are also eligible for gratuity payment, whose amount varies with the number of years of service. Some government agencies give in addition an additional lump sum payment known as "Golden Hand Shake". The civil servants are also entitled to cash payment in lieu of leave, for a maximum of 150 days. So there is considerable lump-sum payment made available to retiring civil servants, in addition to pensions.

Until 1991 annual allocation from the budget was provided for the pension expenditure of civil servants. This practice was modified when the Pension Trust Fund Act 1991 was introduced. An initial allocation of RM 500 million was made by the Federal government. In 2007, This Act was replaced by the Retirement Fund Act of 2007 (Act 662 of 2007).

There are three main sources of income for this fund. First, the Federal government provides 5 percent of its annual emolument budget to finance pensions of its employees. The lower levels of government contribute 17.5 percent of the salaries of their pensionable employees to this fund. The accumulated funds are currently invested within Malaysia in a diversified portfolio comprising equities, Malaysian government securities, and corporate debt (Ong and Hamid, 2010). The third source therefore is the investment income generated from the accumulated balances in the Retirement Fund. These amounted to RM 60 billion as of September 30, 2009, equivalent to about 9 percent of 2009 GDP. Actuarial studies however have not been made available to ascertain whether the contributions plus investment income are sufficient to meet future pension liabilities. The extent to which current civil service pensions and other retirement benefits will impact on fiscal consolidation (fiscal policy consistency with macroeconomic sustainability) and fiscal flexibility (ability to reallocate budgetary resources towards growth and equity enhancing directions) also cannot be ascertained.

Armed Forces Fund (LTAT): LTAT was established in August 1972 by an Act of Parliament. It is mandatory for military personnel below commissioned officers. It is a DC scheme, with contribution rate of 10 percent of monthly salary by employees, and 15 percent by the government as employer. It has disability and survivors' benefit features if the events occur during service. The full withdrawal age is 50 years. Those who are entitled to pensions, can withdraw only their contributions; the rest can withdraw the entire amount. There is also provision of housing purchase once during service. The details of membership are not available, but as at end 2008, the accumulated balances were RM 7.2 billion, equivalent to 1.0 percent of GDP.

Table 3

Singapore:

Civil Service and Armed Forces Pension Arrangements[1]

Table 3a: Singapore Civil Service		
	2004	2009
Total Number of Civil Servants	61,516	74,201
Male (percent)	44.4	43.7
Female (percent)	45.6	46.3
Share in Resident Labor Force	0.04	0.02

Prior to 1986 eligible civil servants were covered under the Pension Scheme[2] financed by the Government. In 1973, the civil servants were given an option to transfer from the Pension Scheme to the CPF, but relatively few chose to do so. The attempt in 1986 to transfer the civil servants to the CPF was effective as it was combined with the discontinuation of the Pension Scheme for most civil servants. A relatively small number of key civil servants and office holders were permitted to be on the pension scheme. Their details however are not publicly available.

[1] Data on balances, and rate of returns for Pension Fund and Saver Fund were calculated based on the Account General's Financial Statements for the Financial Year 2004-2005, Government of Singapore.
[2] The Pension Scheme's Fund is governed by The Pension Fund Act (Cap. 224A, 1996 Revised Edition) and is administered by the Ministry of Finance.

Most civil servants employed after 1986 are covered by the CPF[3]. Non-pensionable civil servants have the same contribution rates, and wage ceiling as Singaporean citizens and permanent residents employed in the private sector. Pensionable civil servants however have lower contribution rates, but a higher wage ceiling of $6000 is applied to their contributions. These rates for both pensionable and non-pensionable civil servants are provided in Table 3

Pensionable civil servants on reaching retirement can choose between a) full pension calculated at 1/600 x Annual Pensionable Salary x Completed Months of Service; b) a lump sum payment based on full annual pension x 14.2; c) a combination of a lump sum payment and reduced pension for 12.5 years, after which the monthly pension is restored to the full pension. The Pension Fund Act stipulates that the maximum replacement rate to not exceed two-thirds of the highest pensionable emoluments paid to the civil servant. Under option a) above after completing 30 years of service the pension would be 60%; the 2/3 maximum is attained after 33 1/3 years of service. Effectively Civil servants although nominally participating in the CPF DC scheme as other workers are being guaranteed a high DB floor, the best of two formulas.

As on 31st March 2005, (the latest year for which data are available) the Pension Fund had assets of $11.41 billion. The scheme is well funded with pension assets matching estimated actuarial liabilities of $11.40 billion. The Pension Fund is funded by income earned from its investments, occasional lump sum transfers from the Consolidated Revenue Account of the Government, and from monthly transfers. These are not necessarily related to civil service pension deficits. During 2004-2005, the fund earned $ 438.8 million (or 4.0 percent) from its investments. The GDP Deflator was 1.2 in 2005, thus the real rate of return on the pension fund was 2.8 percent. Data for a more detailed analysis of civil service pension scheme are not available.

Pension arrangements for the Armed Forces personnel are governed by the Saver Plan[4], a DC (Defined Contribution) scheme, established in 1998. The value of the accumulated pension benefits at the time of introduction were estimated and transferred into members' accounts. The Saver Fund is also funded by transfers from the Consolidated Revenue Account of the Government, contributions from personnel, and income earned from its investments. The contribution rate for the first six years of service is thirteen percent, after which it is increased to fifteen percent. Members have three options to invest their accumulated balances. The first option: *Stable*, fifty percent in cash and fifty percent in bonds; the second option *Balanced*: ten percent in cash, fifty percent in bonds, and forty percent in equities; and lastly *Dynamic:* Ten percent in cash, twenty percent in bonds, and seventy percent in equities. The default option is the *Balanced Plan.*

As of March 31, 2005 the Saver Fund had balances of $1.79 billion, and earned $42.5 million on the average balances between 2004 and 2005. After taking into account the

[3] The Pension Act stipulates that no civil servant employed after April 1, 1986 will be covered by the Pension Act except officers who are appointed to such schemes of service designated by the President.
[4] Renamed as the Saver Premium Fund in 2000.

investment adjustment of $42.91 million, the Saver Fund investments earned an implicit real return of 4.0 percent (5.2 in nominal terms). This is in contrast to the real rate earned on CPF balances of 2.0 percent, and 2.8 percent on balances in the Pension Fund during the same time period.

http://politics.sgforums.com/forums/10/topics/247199

Table4 -: Central Provident Fund contribution rates[1], 2010 (In effect from January 1, 2007)

For Private Sector, Non-Pensionable Civil Servants, Statutory Board Personnel, and Permanent Residents						
Employee Age	*Contribution By Employer*	*Contribution By Employee*	*Total Contribution*	*Credited Into*		
(years)	**(% of wage)**	**(% of wage)**	**(% of wage)**	**Ordinary Account** *(Housing and Others)*	**Special Account** *(Retirement)*	**Medisave Account** *(Health)*
	Upto Wage ceiling of $4500	**Upto Wage ceiling of $4500**	**Upto Wage ceiling of $4500**	**Share of contribution (%)**	**Share of contribution (%)**	**Share of contribution (%)**
35 & below	14.5	20	34.5	67	14	19
35 - 45	14.5	20	34.5	61	17	22
45 - 50	14.5	20	34.5	55	20	25
50 - 55	10.5	18	28.5	46	25	30
55 - 60	7.5	12.5	20.0	58	0	43
60 - 65	5.0	7.5	12.5	28	0	72
Above 65	5.0	5	10.0	10	0	90
For Pensionable Civil Servants						

	Upto Wage ceiling of $6000	Upto Wage ceiling of $6000	Upto Wage ceiling of $6000	Share of contribution (%)	Share of contribution (%)	Share of contribution (%)
35 & below	11.3	15.0	26.3	66	14	20
35 – 45	11.3	15.0	26.3	60	17	23
45 – 50	11.3	15.0	26.3	54	20	26
50 – 55	8.3	13.5	21.8	45	24	31
55 – 60	6.0	9.3	15.3	56	0	44
60 – 65	4.13	5.6	9.8	31	0	69
Above 65	4.13	3.8	7.9	10	0	90

Note: [1]The information in the above Table applies to employees with monthly wages above $750. The above contribution rates are for Singapore Permanent Resident (SPR) employees after their 3rd year of residence in Singapore. In 2010 Singapore Budget, The Government announced that the employer CPF contribution rate will increase by 1.0 %. This will be implemented in two stages. The first 0.5% increase will be implemented on 1 September 2010, and will be made into the Medisave Account (MA). The remaining 0.5% increase will be affected 6 months later on 1 March 2011, and will be made to the Special Account (SA).

Source: http://mycpf.cpf.gov.sg/Members/Gen-Info/Con-Rates/ContriRA, Accessed on March 9, 2010.

III. Key Issues and Reform Directions: (to be expanded)

- Governance
- Transparency, Accountability, Data Availability
- Fiscal Costs and Sustainability
- Impact on Fiscal Consolidation and Flexibility
- Labor Market Implications (particularly portability provisions, and their implications of inter-sectoral mobility of labour)
- Disparities between Private Sector employees on the one hand, and civil servants and the military on the other.

Common areas of reforms:

Improving governance structures: Independent experts in pensions should be on the Board of Trustees of Civil Service and Military Pension Funds. There should be an autonomous Statutory Board set up to administer the pension Funds.

Transparency and accountability need to be strengthened. For example , data on pensioners by various categories and the amount of pension received should be made routinely available.

The demographic data of the existing civil servants and of the pensioners should be routinely available. The actuarial and financial sustainability projections under different assumptions should be put on the website for public discussion.

The retirement age and the full pension age need to be increased, especially in Indonesia and Malaysia. The time path and other relevant aspects should be specified.

The arrangements for the civil servants and the military to share in the future pension risks need to be considered for more equitable treatment. Greater portability of pension benefits between public and Private sectors needs to be considered.

Specific country reforms:

Indonesia:

Provision for pension based on final pay needs to be reviewed. There is scope for reducing administrative costs. One possibility is to consolidate several administrative entities currently (MOF, Treasury, PT Taspen, National Civil Service Agency) involved in the civil service pensions. (Guerard, 2010). Address the anomaly that pension contributions to Pt Taspen are not used for that purpose. The pension accounting must be on accrual rather than on cash basis. To Implement 2004 SJSN Law, and Draft White Papers suggestions, develop transition steps

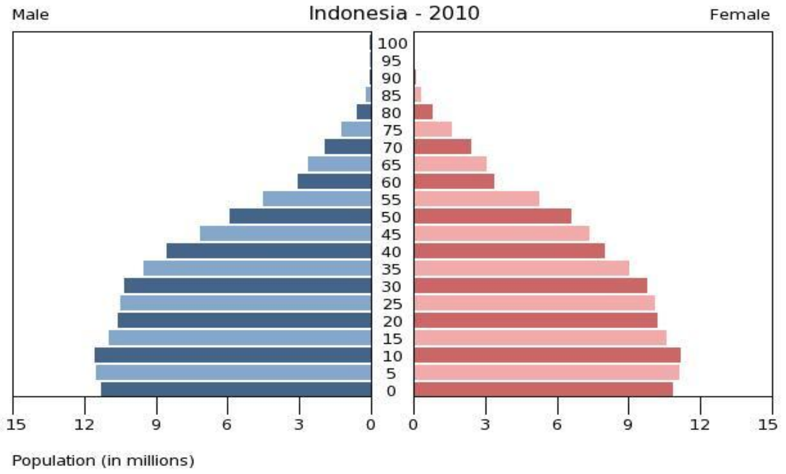
Malaysia:

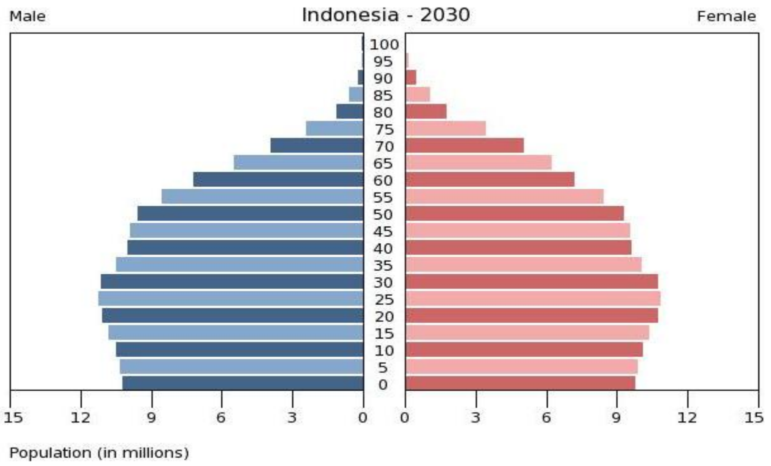
Consider introducing pension contribution by the employees. Make the investment policies and performance of the Civil service and Military pension funds transparent. Explore the possibility of reducing the divergence between pension arrangements for the civil servants and the military on the one hand, and the private sector employees on the other.

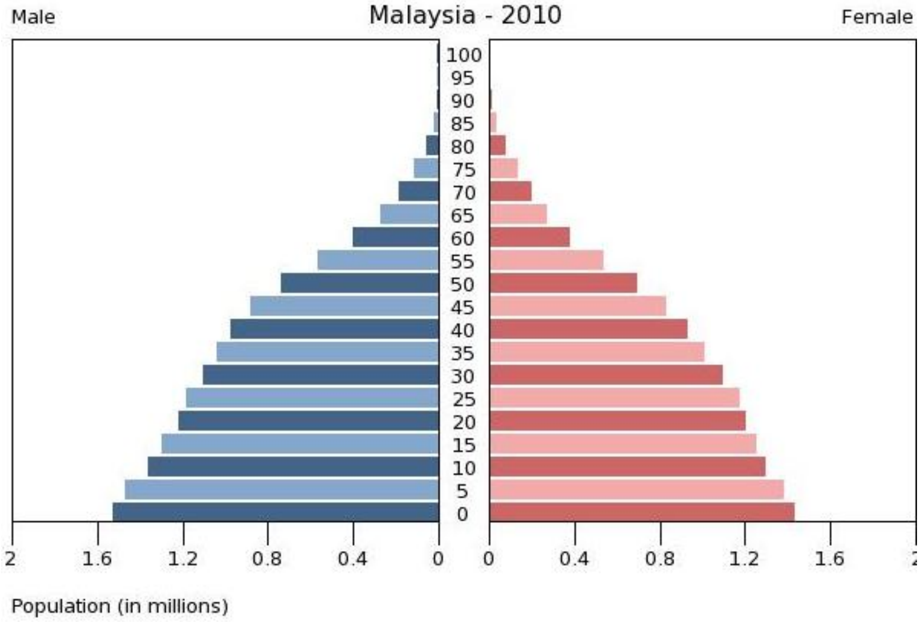
Singapore:

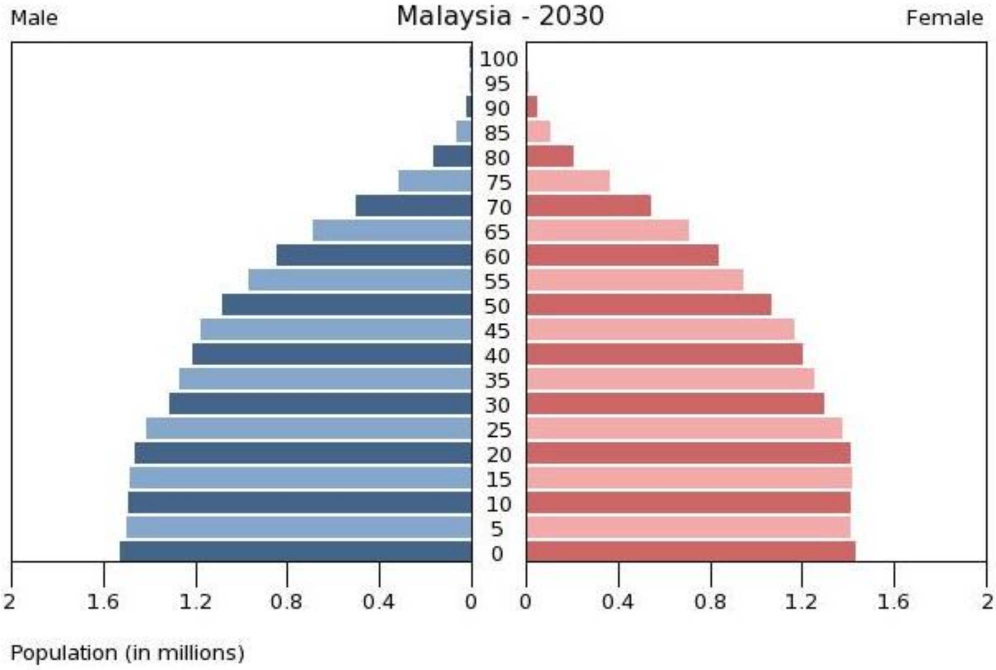
Data on number of pensioners; pension receipts and expenditure; and the demographic profile of the Civil Servants should be made publicly available. Data on the investment policies and performance of Civil Service and military pension funds should be made publicly available. Indexing provisions for Civil service pensions need to be strengthened.

Figure1: Demographic Profiles of Sample Countries.






Male
Malaysia - 2010
Female
100
95
90
85
80
75
70
65
60
55
50
45
40
35
30
25
20
15
10
5
0
2
1.6
1.2
0.8
0.4
0
0
0.4
0.8
1.2
1.6
Population (in millions)


Male
Malaysia - 2030
Female
100
95
90
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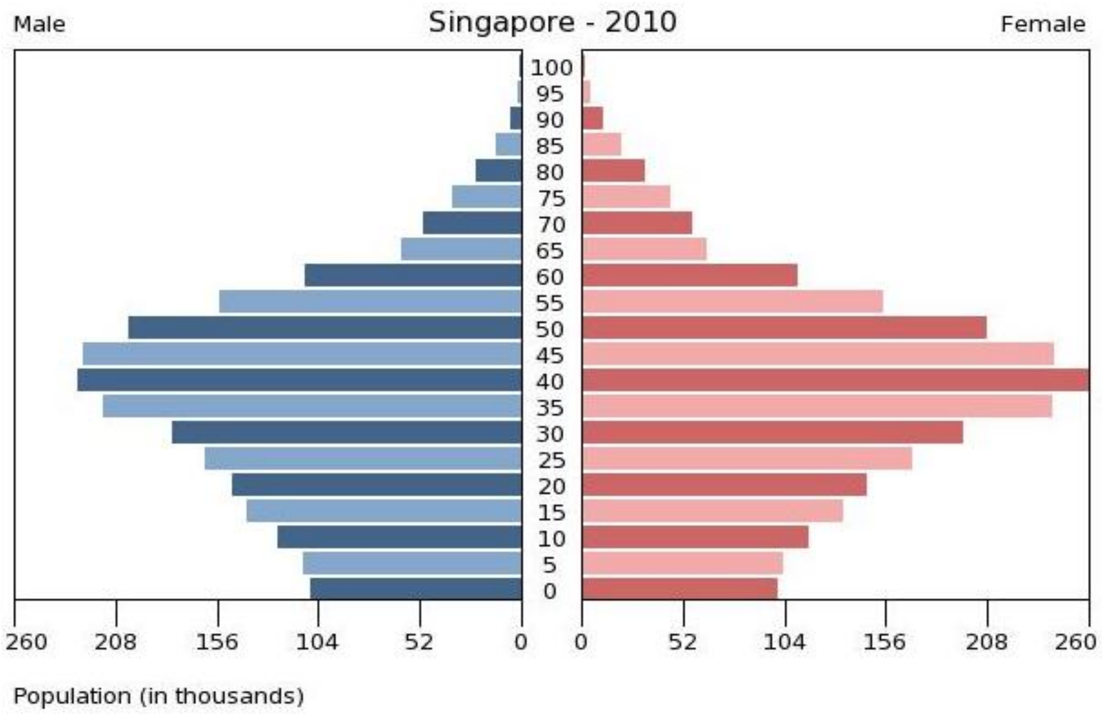
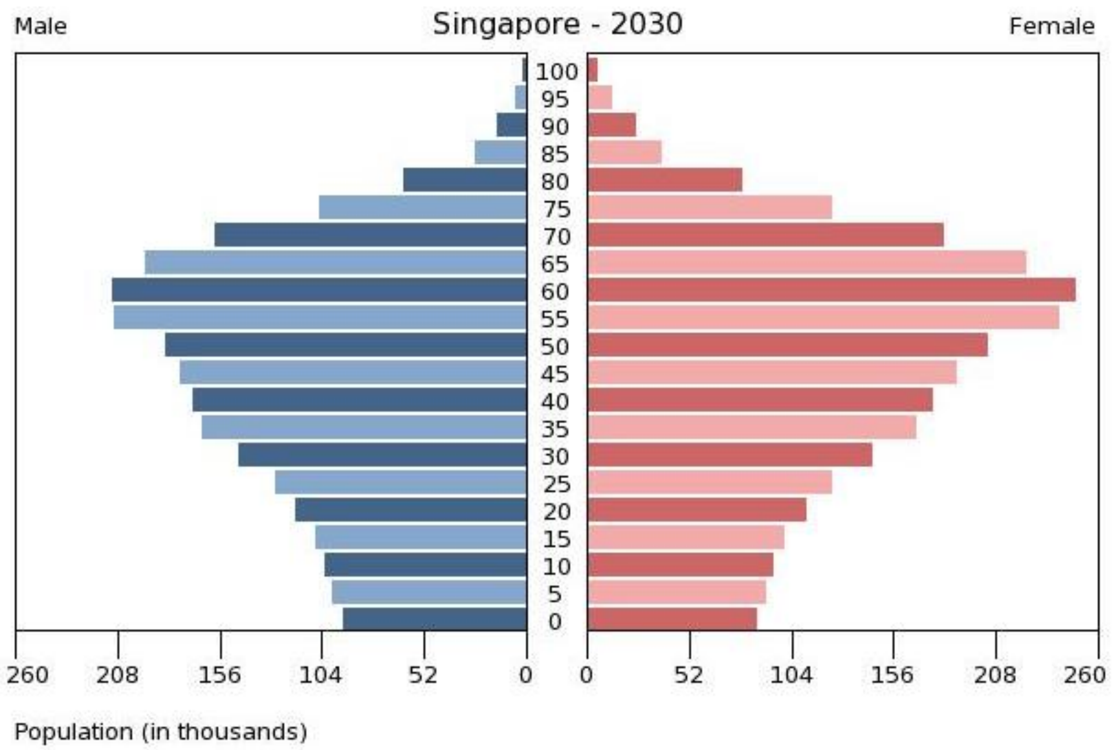
2
Population (in millions)





Source: http://www.census.gov/ipc/www/idb/country.php

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