

Indonesia Regulation on Wage Structure and Scale

Indonesia recently introduced a regulation on formulating, implementing, and communicating wage structure and scale. Its focus on pay transparency is expected to spur a number of new compensation and pay differentiation strategies for banks.

Ministry of Manpower, Indonesia has recently introduced a regulation on wage structure, and scale. The regulation (Minister Regulation No. 1/2017) – requires **all firms in Indonesia** to formulate, implement, and inform a wage structure and scale for all their employees by 23 October, 2017.

While the deadline for implementing this regulation is near, banks in Indonesia are seeking further clarity and guidance on how to best comply with this regulation. In this article we cover in brief what the regulation is about and, more importantly, what impact we are seeing on the ground.

Definitions & Considerations

The wage structure pertains to the hierarchy of grades in an organization. The scale pertains to the nominal pay range for each of these grades (typically in a minimum - maximum format).

As per existing labour laws, both the structure and the scale should be formulated by each firm based on the grade, position, years of experience, education, and competence of the workers. When formulating the wage structure and scale, the employment capacity of the firm, including financial capacity to hire, should also be taken into account. The lowest of wages in the wage structure and scale should be higher than the regional minimum wage applicable to the domicile of the employer. All employees in different cities should be paid more than the minimum wage of the respective city / province (UMK / UMP).

Prevalence

While regulations have always encouraged firms to have a formal wage structure and well defined pay ranges for each grade, firms typically exist across the spectrum – including those who have a well-defined grade structure and corresponding pay ranges, those who have a grading structure but no well-defined pay bands per grades, and those who have no formal grading structure. With this regulation, all firms will be required to formulate a clear wage structure and scale to communicate to employees.

The Communication Aspect

Where this regulation really breaks new ground is the requirement of firms to communicate the employee's grade and the pay range applicable for that grade. An employee should only receive information pertaining to his or her own grade and scale. It is unclear how this communication will take place and how the regulator will enforce and audit this aspect.

Apart from communicating to each employee his or her grade and scale, firms are also required to disclose the entire wage structure and scale to the Ministry of Manpower during the following instances:

- Ratification, approval, or renewal of company regulation
- Registration, extension, and renewal of the collective work agreement

Company regulation and collective work agreements are two commonly used legal documents in Indonesia that define the employer-employee relationship. These must be registered with the Ministry of Manpower and must be periodically renewed and / or extended.

Penalties

Any business that fails to comply with its obligations under this regulation will be penalized with administrative sanctions. The penalties will be determined based on the criteria set forth under Minister of Manpower Regulation No. 20 of 2016, and range from written warnings to restrictions on business activities.

Initial Assessment & Closing Thoughts

The biggest question for banks in Indonesia is how firms should to communicate the wage grade and range to employees. By giving employees this information in writing, there is a risk that the employee may share this information, knowingly or by accident, with those from other grades. However, communicating it verbally will be difficult to audit and prove.

There is concern that this level of disclosure may open up other conversations with employees once they see where they lie on the pay range of their grade, potentially impacting a bank's pay differentiation strategy.

An unintended consequence of this could cause firms to start changing their pay-mix more frequently, paying out a larger percentage in bonuses and commissions so that they remain competitive on a total compensation basis. We are continuing to work with local and regional banks in Indonesia on their response to this regulation, and we should all have more clarity once everyone returns from the Hari Raya festivities!

Authors Contact Information

Saurabh Mittal

Associate Partner
Aon Hewitt | Talent, Rewards & Performance
+62 212 985 8594
saurabh.mittal@aonhewitt.com

Ruchir Agarwal

Manager, South East Asia
McLagan
Aon Hewitt | Talent, Rewards & Performance
+65 6313 7050
ruchir.agarwal@mclagan.com

About McLagan

McLagan provides tailored talent, rewards, and performance expertise to financial services firms across the globe. Since 1966, we have partnered with the largest and smallest financial services firms to help them make data-driven decisions to hire, retain, and engage the top talent for keeping the global economy running. Our compensation surveys are the most comprehensive, in-depth source of rewards data covering over 150 countries from more than 2,500 clients. Our consultants work with hundreds of firms annually to design total rewards programs and benchmark financial performance for boards of directors, executives, employees, and sales professionals. McLagan is a part of Aon plc (NYSE: AON). For more information, please visit mclagan.aon.com.

About Aon

Aon plc (NYSE:AON) is a leading global professional services firm providing a broad range of risk, retirement and health solutions. Our 50,000 colleagues in 120 countries empower results for clients by using proprietary data and analytics to deliver insights that reduce volatility and improve performance.

For further information on our capabilities and to learn how we empower results for clients, please visit <http://aon.mediaroom.com>.

This article provides general information for reference purposes only. Readers should not use this article as a replacement for legal, tax, accounting, or consulting advice that is specific to the facts and circumstances of their business. We encourage readers to consult with appropriate advisors before acting on any of the information contained in this article.

The contents of this article may not be reused, reprinted or redistributed without the expressed written consent of McLagan. To use information in this article, please [write to our team](#).

© 2017 Aon plc. All rights reserve