Asset-Liability Management of SJSN Social Security Funds

**Background**

PT Jamsostek will be transformed into BPJS Ketenagakerjaan on January 1, 2014 and will begin its operations administering the SJSN work accident, old age, pension and death programs no later than July 1, 2015. Participants in programs sponsored by PT TASPEN and PT ASABRI must join the SJSN employment programs by January 1, 2029.

In order to transform PT Jamsostek into BPJS Ketenagakerjaan, PT Jamsostek will be declared dissolved without liquidation and all assets and liabilities will be split between those that are the property of the government and those that are the property of participants. The assets belonging to participants will likely be transferred to the appropriate social security fund.

A detailed plan for separating these assets and satisfying the liabilities of PT Jamsostek to its program participants is needed. The BPJS Law requires the appointment of a public accounting firm to audit the closing statement of financial position of PT Jamsostek and the opening statement of financial position of BPJS Employment.

As stated in the BPJS Law, BPJS will manage its own assets and the assets of its Social Security Funds. This is a very different governance structure from PT Jamsostek, which does not separate its corporate assets and liabilities from the assets and liabilities of its program participants.

**BPJS Assets**

Under the BPJS Law, the assets of the Social Security Funds are legally separated from the BPJS assets. The BPJS administers the Social Security Funds, but the assets of each program are held in a separate fund at the state-owned enterprise custodian bank. BPJS assets come from several sources:

- Initial capital from the Government, which cannot exceed two trillion rupiah
- The assets transferred from the state-owned enterprises that currently administer the social security programs
- The investment yield of BPJS assets
- Operational fees collected from the Social Security Funds
- Other sources in accordance with statutory laws/regulations.

BPJS manages

Social Security Fund Assets

BPJS Assets

Transferred Asset

Operational Funds

Investment Yield

Initial Capital

Other Sources

BPJS assets can be used for:

- Operational costs of administering the Social Security programs
- Cost of procurement of goods and services to support Social Security program operations
- Costs to increase service capacity
- Investments in accordance with the statutory laws/regulations.
The sources of the Social Security Fund Assets are:

- Contributions from employers, workers and the government
- The investment yield of the Social Security Funds
- Each participant’s assets transferred from PT Jamsostek
- Other sources in accordance with the statutory laws/regulations.

BPJS Expenditures and Liabilities

BPJS expenditures consist of personnel costs, goods and materials and capital costs. The majority of expenditures is for personnel and consists of salaries and benefits for the Board of Commissioners, the Board of Directors, and employees. In addition, the BPJS must pay for routine operating costs such as utilities, telephones, rent or mortgage payments on buildings, supplies, etc. Capital expenditures are needed for such items as IT equipment, furniture and office machines.

BPJS liabilities are similar to those for any other corporation and consist of such standard items as accounts payable and the outstanding balance on loans. Benefit payments to program participants are not liabilities of the BPJS. They are the liabilities of the individual social insurance funds.
PT. Jamsostek has experience in managing health care, work accident, old age savings and death benefit programs, but has no experience in managing a defined benefit pension program. PT Jamsostek is also responsible for managing programs covering about 9 million formal sector workers, but BPJS Ketenagakerjaan will eventually need to manage programs covering 110 million workers in the formal and informal sectors. Consequently, significant changes in the organizational structure and business processes will be required to effectively and efficiently manage the SJSN employment programs.

Social Security Fund Expenditures and Liabilities

The main expenses of the social security funds is paying benefits under the four programs (work accident, old-age savings, pension and death benefit) to all participants and paying fees to BPJS Ketenagakerjaan for managing the funds. The liabilities of the social security funds at any point in time consist of the reserves necessary to assure program solvency and payment of claims when due. The size and characteristics of these liabilities differ significantly by fund. The primary types of reserves are:

• Claim reserves
• Unearned premium reserves
• Mathematical reserves

Claim reserves are liabilities for claims that have already been incurred but have not yet been paid. The claims process consists of three distinct steps. The claims must be reported to BPJS, the claims must then be approved or denied, and then the claim must be paid. There are three common types of claim reserves corresponding to each of these three steps:

• Open claim reserves. Reserves for claims that have already been received and approved but for which payment has not yet been made.
• Claims in course of settlement (ICOS). These are reserves for claims that have been submitted to the BPJS but have not yet been reviewed.
• Incurred but not reported claims (IBNR). These are reserves for claims that have been incurred but have not yet been reported to the BPJS. Since the type and amount of these claims cannot be known until they are actually submitted, this reserve must be estimated based on past experience.

Unearned premium reserves are reserves for contributions paid for coverage that has not yet been provided. For example, assume that a participant pays contributions for one year at a time at the beginning of each year. At the moment the contributions are paid, the social security fund has received an entire year of contributions, but it has not yet provided the coverage for any portion of the year. Consequently, the entire amount of the contribution must be set up as an unearned premium reserves and should not be considered as fund surplus. After two months have gone by, the social security fund has provided two months of coverage and still “owes” ten months of coverage. Consequently, an unearned premium reserves must be held for the other ten months of coverage that has not yet been provided.

Mathematical reserves arise whenever a social security program is fully or partially funded. This most commonly arises for defined benefit pension programs (where it is often referred to as a demographic reserve) and with whole life insurance. This type of reserve arises whenever an increasing pattern of required contributions is replaced by a level equivalent pattern of contributions. When this occurs, the contributions in the early years are higher than what is needed to pay expected claims and the contributions in the later years are insufficient to pay expected claims. The excess contributions in the early years must be saved and invested to cover the shortfalls in the later years.

Claim reserves will be required for all SJSN employment programs. These will be the primary reserves for the work accident and death benefit programs and will be relatively small. Since claims are paid quite quickly after claims are incurred, these reserves tend to be small and of short duration. Claim reserves for the old age savings program will be for payouts that have been approved but not yet paid. Since the lump sum payments under the old age savings program can be quite large, the reserve can also be significant. Claim reserves will usually be largest for the pension program because once a claim is approved, the reserve must cover all expected future monthly payments to the pensioner.

Mathematical reserves are the primary reserve for the pension and old age savings programs and can be very significant. The mathematical reserves for the old age savings program are equal to the total account balances of all active participants. For the pension program, the reserves represent the prefunding of future benefit payments. For new pension programs and pension programs for rapidly aging populations, these reserves are often quite high.
**Asset-Liability Management for BPJS**

From the explanation of the assets and liabilities of the BPJS, it seems the general regulations applicable to business capital are sufficient. The BPJS is not an insurance company and does not incur any insurance or investment risk at all. It merely administers the program for a fee. The BPJS doesn’t even face the direct risk of loss of customers, as it is a monopoly and contributions are mandatory. Consequently, the general business rules applicable to the manner in which capital can be invested should be applicable and sufficient.

**Asset-Liability Management for Social Security Funds**

The social insurance funds definitely need regulations on asset-liability management and investments. The regulations should state general principles and should also require that the assets be invested in accordance with fund liabilities and best international practice in asset-liability management. The regulations must allow the flexibility to appropriately adopt very different investment strategies for funds with different liability characteristics.

The type of assets held by a social security fund and the investment policy for those funds must be directly related to the nature of the fund’s liabilities. The assets should produce sufficient cash flow to finance expected benefit payments when due without creating a significant risk of having to sell plan assets at a loss in order to pay benefits.

For example, it would be inappropriate to buy 30-year bonds to back liabilities for health claims that will be paid in three months. If interest rates were to increase in the interim, the long bond would decline in value and would have to be sold at a significant loss in order to pay claims when due. Instead, a government bond maturing in three months would make more sense. Similarly, it would make sense to buy longer-term bonds for an old age savings plan where benefits may not be paid out until twenty years in the future and where the opportunity to earn higher rates of return exists.

Sophisticated techniques such as cash flow and duration matching and immunization exist to assure that benefits can be paid without incurring a high risk of asset losses and maximizing rates of return. These techniques should be taken into account when developing the investment policy guidelines for each of the social security funds.

The work accident program should be treated similarly to the health program, since normally about two-thirds of all claim payments are for health. Health claim reserves should be quite low and of short duration, so the investment policy and asset-liability management for the health fund is relatively simple. Reserves must be held for unpaid claims, claims in course of settlement (ICOS), incurred but not reported claims (IBNR) and unearned premium reserves. Assuming each health payment is treated as a separate claim, which is the practice in most countries, there should not be any claims that will be paid out over a long duration. Consequently, the regulations should require that assets be invested only in short-term, highly liquid and highly safe securities.

For the old age savings fund (and for the SJSN pension fund if it will be partially funded), a very different investment policy would be appropriate since most of the funds will not need to be paid out until many years in the future. Here the goal should be to maximize the rate of return within the risk levels appropriate for pension assets. Equities, longer-term bonds, securities backed by real assets and other assets with higher risk and rates of return might be appropriate.

While the actual technique for asset-liability management and the development of an appropriate investment policy statement and strategic asset allocation is beyond the scope of this policy note, it should be clear from this discussion that professional assistance from experts will be needed to develop appropriate regulations and investment policies.